



*Annual Report
&
Financial Accounts
2004-2005*



INVESTOR IN PEOPLE





Medical Supplies Agency

Annual Report & Financial Accounts

2004-2005

PRESENTED TO THE HOUSE OF COMMONS PURSUANT TO SECTION 7 OF THE
GOVERNMENT RESOURCES AND ACCOUNTS ACT 2000

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STATEMENT BY MEDICAL SUPPLIES AGENCY CHIEF EXECUTIVE

MR STEPHEN SMITH

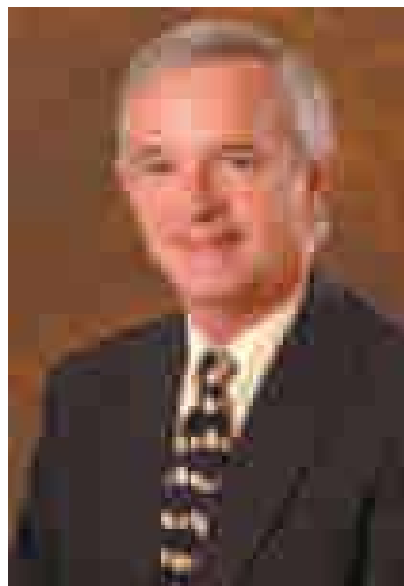
In last year's report, I referred to the very high levels of commitment of all the staff, within MSA Headquarters and the Medical Distribution Centres both in the UK and overseas, to deliver the highest standards of service to our customers. I also commented on the staffs' dedication and determination to get the work done to achieve that.

This year's performance, the last for the Medical Supplies Agency, has underlined the validity of that statement. The Agency has delivered an even higher level of service than was achieved last year including the support to ongoing operations in the Gulf, Afghanistan and Bosnia, and urgent operational support required following Hurricane Ivan in the Caribbean, and the Far East Tsunami. At the same time the demands of day-to-day supplies for peacetime primary and secondary healthcare have continued.

Throughout the year, the priority was on ensuring those high levels of service were maintained and improved. However, at the same time, following Ministerial Approval in the summer of 2004, the Agency underwent a fundamental restructuring in organisational and business terms, leading to its transformation into the Medical Supplies Integrated Project Team on 1 April 2005. This is covered in more detail in the body of the report. However the headline objectives were as follows. First, to exit the business of medical supplies storage and distribution. Second, to move to commercial best practices of direct delivery by a number of strategic suppliers to UK based medical centres utilising electronic ordering, invoicing and payment. Third, to integrate the operational activity even more strongly into the Defence Logistics Supply Chain; and finally to close the warehousing and distribution centres leading to a reduction in size of the organisation by some 60%.

That these objectives have all been achieved, managed by the workforce, is testament to their loyalty, dedication, and determination. This programme of change has been profound for most if not all of the staff, in respect of their careers and future employment, requiring redeployments, transfers and redundancy schemes, all of which had to be very sensitively and carefully managed. This inevitably created uncertainty and for many staff sadness to see the end of the Agency. However no one allowed their personal feelings and concerns to impact the performance of the Agency, or the impetus of the change programme. I consider myself very fortunate and honoured to be the last Chief Executive responsible for the Agency and such a remarkable workforce.

I am sure that these high standards of innovation, dedication and determination to succeed will continue as the Medical Supplies Integrated Project Team forms up on 1 April, maintaining the highest levels of support for our service personnel, wherever they are stationed and deployed.



CONTENTS

| | | |
|-------------------|---|-----------|
| Section 1: | Aims and Objectives | 3 |
| Section 2: | Review of Activity | 5 |
| Section 3: | Performance against 2004/2005 Key Targets | 12 |
| Section 4: | Future Strategy | 19 |
| Section 5: | Accounts for the Year Ending 31 March 2005 | 20 |

Section 1

AIMS and OBJECTIVES

The Medical Supplies Agency (MSA) is a Business Unit within the Defence Supply Chain (Def SC) of the Defence Logistics Organisation (DLO).

AIM

The aim of the MSA is to ensure the cost-effective and timely provision of medical, dental and veterinary materiel, blood and blood products, technical and medical logistic support and trained personnel to the UK Armed Forces worldwide in War, Operations Other Than War, and Peace.

BUSINESS STATISTICS

The Agency encompasses the MSA Headquarters and the Blood Supply Depot (BSD) at Ludgershall and 14 Medical Distribution Centres (MDCs) located throughout the UK and Overseas.

The Agency's average number of staff during the year was 26 military and 279 civilian personnel. The professional skills mix within the Agency includes Logisticians, Financiers, Commercial Officers, Pharmacists, Laboratory, Medical Supply and Combat Medical Technicians.

The Agency has responsibility for the provision of medical materiel to nearly 2,000 individual locations worldwide with approaching 400,000 issues per annum being made from a live inventory of nearly 30,000 items. This range includes items as diverse as a simple remedy for a minor illness to complex equipment such as a portable intensive care system used in aeromed evacuation. The BSD received 20,965 blood samples for Mass Grouping and distributed 4,100 units of blood and 198 units of fresh frozen plasma in 04/05. In addition, the Agency responds to emergency situations by maintaining around-the-clock capability to provide lifesaving products and technical support.

MISSION

The mission of the MSA is to deliver medical materiel in order to sustain UK military capability.



Urgent Medical Supplies en route to HMS Richmond

OUTPUT

The Agency's primary outputs are as follows:

- Maintain operational and non-operational support through the provision and delivery of medical supplies including modules and kits to customers in the UK and overseas.
- Provide Medical Countermeasures capability to UK Armed Forces worldwide and develop and license new and improved Medical Countermeasures.
- For the MSA Change Programme, achieve all milestones in each of the 7 key process areas as follows:
 - Stakeholder and Customer Management
 - Operational Support
 - Strategic Partnering
 - Supply Chain Management
 - Business Resource Management
 - Medical Countermeasures Management
 - Blood Supply and Training Management

BUSINESS OBJECTIVES

The principal business objective is:

- To fulfil all operational tasks placed on the Agency, on time and within budget.

The supporting business objectives are:

- To provide medical materiel of a specified quality within the overall materiel policy through an agreed standard of service to customers of the Agency in the most efficient manner.
- To establish a fully integrated Tri-Service structure based on best management practice and effective staff training arrangements.
- To implement the business systems necessary to meet the Accounts Direction, provide the cost of outputs and monitor the performance of the Agency.



Medical Services in the front line

Section 2

ANNUAL REVIEW OF ACTIVITY

This has been another extremely busy year for the MSA. The Agency has had to combine the day to day activities of providing medical items and equipment to operations and meeting normal replenishment and peacetime requirements, alongside the implementation of the MSA Change Programme. The Agency met all the challenges, due to the enormous effort made by all the staff. This was particularly noteworthy bearing in mind that it was the last year of operation as an Agency. The year-end would also mean a significant change in the careers and lives of many Agency staff facing job changes and for some, redundancy. Success against the specific Key Targets, reported in Section 3, confirms the outstanding performance that has been achieved throughout this year.

Detail of the work underlying the achievements in meeting the Key Targets follows.

MSA Change Programme

Implementation of the MSA Change Programme was a dominant theme of the last year and represented a significant challenge for every member of the Agency. Against the overall aim of delivering the same or better service levels at a lower cost, the principal elements of the Change Programme were as follows:

- To exploit proven commercial supply chain solutions to allow direct delivery to non-deployed customers, allowing the closure of the UK Medical Distribution Centres (MDCs).
- To rationalise the supplier base and drive 10% out of procurement costs by entering into prime vendor contracts with key suppliers.
- To empower our customers and reduce the administrative overhead by enabling e-commerce ordering direct from medical and dental centres.
- To establish a small operational customer support and module build facility at the existing Defence Storage and Distribution Agency (DSDA) site at Donnington.
- To reduce the workforce by 60%.
- To assume the responsibility for medical equipment management from the Workshop Support Services Integrated Project Team and to create the capability for procurement and through-life management of equipment in accordance with the principles of Smart Acquisition.
- To exploit the potential for synergy with the Defence Science and Technology Laboratory (Dstl) by relocating our Medical Countermeasures Team to Porton Down.
- To close the Ludgershall headquarters and main warehouse site and move the organisation to the existing DLO facility at Andover.
- To disestablish the Medical Supplies Agency and reform as the Medical Supplies Integrated Project Team (Med S IPT).

Work began with the establishment of a baseline for change which, following successful outline submissions to Ministers, was used as the framework for formal consultation with Trades Union at both national and local level, beginning in April 2004. Throughout this process our emphasis was on openness and honesty, and we were most grateful to the staff side for their constructive and helpful engagement throughout.

Completion of the first phase of TU consultation allowed us, in June 2004, to make a second and final submission to Ministers laying out the detail of the changes and, following their approval to continue, to enter into a second phase of TU consultation which, began in July 2004. This time the emphasis was on the methods of implementing the proposed changes and we were again grateful to the staff side for their positive and pragmatic contributions.

Final ministerial approval for implementation allowed us to move forward in two critical enabling areas: negotiation of the prime vendor contracts for direct delivery; and management of the reductions in staffing levels. Work in the first of these areas led to the award of contracts in our two biggest areas of activity (primary healthcare and dental products) in March 2005 and, at the time of writing, the direct delivery solutions are working well. Unfortunately the associated move to e-commerce has not progressed as quickly as the Agency had hoped, due to various software problems arising with 'Purchase to Payment', (P2P), the DLO e-commerce package. However successful modifications have been carried out and further robust testing should see the initial e-commerce transactions for the dental

ranges in May 2005, and, subject to satisfactory performance, the transfer of the main part of the medical inventory to follow from July 2005.

Head of Supply Management Division receiving her CDL Commendation reflecting her personal contribution to the Transformation Programme



In managing staff reductions, great emphasis was placed on managing the redundancy and placement programmes with as much care and sensitivity for the individuals involved as was possible. This is described in more detail later in Section 2, under Staff Matters.

Closure of the UK MDCs (and transfer to local command of overseas MDCs) was achieved through a rolling programme running from August 2004 to March 2005, with UK MDC work initially being drawn back to the main warehouse at Ludgershall before the switch over to direct delivery in March 2005. Simultaneously, negotiations with DSDA were conducted to arrange for the establishment of the operational medical capability at Donnington and the associated works, to enable the creation of a licensed facility. This facility went live in March 2005 and the transfer of the final module components from Ludgershall will continue into the summer of 2005.

The physical relocation of staff to Andover, where the new Medical Supplies Integrated Project Team would form up on 1 April 2005, was completed very successfully during December 2004. Likewise the move of the Medical Countermeasures team to Porton Down to become more closely integrated with Dstl project support staff, which went very smoothly. The culminating point for the Change Programme was the closure ceremony for the Ludgershall site on 31 March 2005, during which we were delighted to invite back a number of ex-MSA employees still resident in the Ludgershall area.

A major plank in the Change Programme was the emphasis placed on stakeholder engagement. The MSA Change Road Show was taken out to give regional customer presentations across the UK and in Germany, touching in all over 500 stakeholders. In addition, two-monthly newsletters were widely distributed, a virtual working group web site was provided for sharing information and posting questions, and the Executive Steering Group (comprising 1* level representatives from all stakeholders) continued to meet quarterly.

Overall coordination of the Change Programme was achieved through the Transformation Programme Board, attended at Management Board level and chaired by the Deputy Chief Executive. Progress on the Change Programme was regularly reported at 2* level within the DLO to Director General Defence (Supply Chain). The MSA Change Programme was identified as one of the DLO's 'Truly Transformational' projects which allowed the Joint Executive 2* Board to receive monthly updates and provide oversight.

Taken as a whole, the Change Programme has been a great success. Implementation has run to time, levels of service to stakeholders have been maintained and we are on track to achieve the annual savings in the region of £15M that had been identified. Managing and implementing the Change Programme has placed a huge additional burden on every member of the MSA team and it is greatly to their credit that the organisation has moved so far in such a short period of time. Successful implementation of the Change Programme has given the organisation great confidence and provides the ideal springboard into a future of continuous improvement.

Support to Operations

Support to operations has remained the Agency's highest priority and is managed by the Operations Division. As in previous years, the MSA has continued to provide Medical Logistic support to UK troops deployed on operational commitments worldwide. OP TELIC in Iraq and OP HERRICK in Afghanistan have continued to generate high levels of work for MSA throughout the year.

In addition to routine support to these and other mature operations, Operations Division staff have responded to several short notice requests for medical assistance in support of tasks that arose in the Ivory Coast, the Balkans and elsewhere. In particular, the MSA provided much needed assistance following the Asian Tsunami. Members of staff were recalled during the Christmas and New Year leave

period, at extremely short notice, to build and dispatch disaster relief medical supplies. This task was achieved seamlessly and ensured that the deployed medical teams were provided with the requisite materiel and equipment to successfully carry out their operational task without detriment to the overall Humanitarian Assistance mission. Such short notice tasks highlight the versatility of the organisation and its ability to quickly react to abnormal surges in operational tempo, in support to the military task, even at the most unsociable hours.

Concurrently, and in addition to the preparations necessary in anticipation of the MSA Change Programme Implementation, the Agency continued to provide Medical Logistic support for Military Training and minor exercises, and Major Air Shows including recovery and reconstitution of medical assets.

As reflected above, as part of the Change Programme, all this work was carried out against a backdrop of a move of operational activities and materiel to DSDA, Donnington. In anticipation of the transfer of responsibility for building and maintaining medical modules together with equipment and consumables storage, Operations Division out-loaded 2,500 pallets of medical materiel to the Medical Logistics Operations Centre (MedLOC), at Donnington during the latter part of FY04/05.



An Air Transit Isolator (ATR)

Medical Countermeasures Integrated Project Team

The Medical Countermeasures Integrated Project Team (MedCM IPT) is responsible for Chemical, Biological, Radiological and Nuclear Medical Counter-Measures (CBRN MedCM).

It manages the range of in-service MedCMs, such as anthrax vaccine and nerve agent antidotes. These products are specialist in nature, and the Ministry of Defence is the Product Licence holder for a number of them. The team works closely with customers, industry and regulatory authorities to ensure the availability of safe and effective products. The MedCM IPT also works closely with other government departments, especially the Department of Health and its agencies, to enhance national capabilities and make efficient use of available resources.

As a whole-life IPT, it is also responsible for the MedCM Development Programme, for which Director Equipment Capability (CBRN) is the MOD customer. To execute this programme, the MedCM IPT works very closely with the Dstl MedCM Project Office, benefiting from co-location with them on Dstl's site at Porton Down. There are also a number of collaborative projects being pursued with allies, and this brings significant gearing to the projects, as well as enhancing future interoperability.

Clinical and Professional Services Division (CPSD)

The Clinical and Professional Services Division (CPSD) provide a range of specialist pharmacy services to a wide range of customers.

In Jun 04, CPSD commenced liaison with Director Defence Medical Services Department (DMSD) and the 18 Defence Consultant Advisers to review and agree a definitive list of current & obsolete operational medical modules. By Sep 04, the work was completed and from an original list of 514 modules a reduced list of 261 was agreed to be the definitive list of current modules to be managed. This rationalisation considerably reduced the size of a further task, carried out in Aug 04, by CPSD to 'cleanse' the medical materiel data for the transfer from MSA's own inventory management system (MMM) to the DLO Corporate Stores System (SS3). This transfer was an integral part of the Change Programme implementation. It involved compiling & scanning the data and where necessary amending descriptions of in excess of 8,000 items in a period of two months. Each item detail was checked to ensure that there was consistency and no ambiguity in the descriptions.

In addition CPSD provided expertise to enable a complete review of the Medical Equipment Table for Ships Afloat (METSA), designed and proposed new Vascular Modules in the light of lessons learnt from Op TELIC, and provided the information to enable a complete review of the Maxillo/Facial modules. They have also enabled the RAF to produce Patient Group Directions (PGDs), which are now published on the RAF website, while Naval PGDs are also being assessed. In an update of the Safety Alert Broadcast System (SABS), CPSD involved all the stakeholders in enabling the rollout of Safety Alerts via the e-mail system from MSA, with a validated feedback system. Finally CPSD led activity to improve the Temperature Controlled Supply Chain and advice in the Contracts process to ensure suppliers will appreciate the complexities of shipping pharmaceuticals overseas.

Wholesale Dealers Licence (WDL) and Wholesale Dealers (Import) Licence (WI)

The following sites were inspected by the Medicines and Healthcare products Regulatory Agency (MHRA) and were re-accredited with the Wholesale Dealers Licence:

In the UK: Donnington MDC
 Porton Down

Overseas: Akrotiri, Cyprus
 Dulmen, Germany

The new MedLOC was given an initial inspection by the MHRA in March, in preparation for issue of its own WDL.

In addition the MSA's Responsible Person carried out inspections of the sites at Brunei, Aldershot, Catterick, Colchester, Greenock, Haslar, Northern Ireland, Plymouth, and Ludgershall.

Transfer of Workshop Support Services Medical and Dental (WSS Med & Dent) team into the Agency

This engineering based team of 25 provide equipment support advice, policy and publications for all tri-service Medical, Dental and Veterinary equipment.

Mobile Transportable Surgical Facility

(JSP 473 defines Medical, Dental and Veterinary equipment as that equipment which is mechanical, electrical, electro-mechanical and electronic and includes all types of medical gas regulators and gas driven equipment).

The team also provide Contract Repair, Spares, Equipment Care Inspections, Health



Monitoring Test Equipment, and identify and facilitate training requirements. It also provides all-encompassing support for the Modular Transportable Surgical Facility.

On 4 October WSS Med & Dent joined the MSA as the Clinical Engineering Team with the primary task of delivering medical, dental and veterinary material/capability in a whole life manner based on the CADMID/CADMIT cycle, utilising best Project Management practice and SMART Acquisition principles. This is necessary as the capital cost of equipment generally represents only 20% of the Whole Life Costs (WLC) and will bring the procurement of Medical equipment in-line with the procurement of all other military equipment.



The formal transfer of WSS Med and Dent to MSA

MSA Information Technology (IT)

The Change Programme required significant IT changes in switching to DLO Corporate IT systems and as a result, considerable in depth planning. The run down of the MSA MMM system and the transfer of data to SS3, and the preparations for the use of the e-commerce system (P2P), raised a series of challenges. None were insuperable, and the large majority of these have been overcome but some remain, to be addressed by the Med S IPT. The training required for the new systems has placed increased demands upon staff resources, but as elsewhere in MSA the staff took on the additional work with enthusiasm and determination.

Staff Matters

As already mentioned in this review, much effort was expended in ensuring the people issues were properly and rigorously addressed during the last year of Agency operations. The Agency ensured that Management Board members visited each of the remote sites to talk the workforce through the Change Programme Implementation process and to answer questions, regarding redeployments, transfers and redundancy. Throughout, a Human Resources Working Group, with TU participation, led on implementation and matters of detail. The Agency also received excellent support throughout from Civilian Personnel Managers, across MOD.

In concert with the run-down and closure of the Storage and Distribution facilities at MSA HQ Ludgershall and Medical and Distribution Centres in 2004, as part of the Change Programme, two key staff initiatives were conducted throughout the Agency. These were the Skills Enhancement and Re-skilling Programmes, to assist and prepare those members of staff who would be facing redundancy to improve their skills, thereby increasing their chances of attaining other employment.

The Skills Enhancement Programme was started at the beginning of the MSA Change Programme and was designed to equip staff facing redundancy with the essential skills for work outside the MoD. This programme, funded by the Learning and Skills Council, with tuition being provided by Salisbury College, has been extremely successful with staff gaining the confidence to face the changes ahead of them. 16 industrial and non-industrial members of the warehouse staff who undertook training to attain NVQs at various levels covering, Warehouse Operations, Administration and Management achieved

the set levels, with the NVQ courses run and assessed by PROTOCOL. A further 16 who undertook the Learning & Skills Enhancement courses in English and Mathematics exceeded their own expectations, leading some to carry on to the next levels of learning.

In recognition of the MSA efforts in encouraging and developing staff, the Agency was awarded regional Joint Winner for the Essential Skills for Life under the Employer Training Awards 2005. At the award ceremony in March 05, the MSA Training Team proudly accepted the award on behalf of CE and MSA.

The MSA Training Team, with the Chief Executive and trainer from Salisbury College, with the Essential Skills for Life Award

The Re-skilling Programme run for staff facing redundancy or early release/retirement has also been very successful. It was directed by the MOD Outplacement Service (MODOPS) and was offered to those staff to be released under redundancy terms. Locally based consultants were based at all MSA sites, who were sensitive to local concerns and aware of the marketplace. Staff were offered support to help them decide what they wanted to do next. They were then advised and guided on how to move within their chosen career, or how to start a successful business and, in some cases, taken through the thought processes for an active retirement. This advice was given to group sessions where appropriate and in



one-to-one meetings for personal requirements. Special seminars were arranged for briefings on all aspects of financial planning and other local requests. The MSA continued to support and maintain the on-site training centre at Ludgershall containing e-learning facilities, which staff used to full capacity, and provided the necessary accommodation for the group discussions or one-to-one meetings with the MODOPS representative.

The take-up of the service varied across the country with the smaller sites being more proactive but the overwhelming response from the individuals who attended these sessions was that they were delighted with the help and felt much more capable of progressing forward as a result. Many of the staff had been with the Agency for a long time and had little appreciation of private sector recruitment - they were nervous of the process but after receiving the MODOPS support felt considerably more confident and better equipped. MODOPS are continuing to contact the staff that have left and are monitoring their progress to find alternative work. The programme will continue throughout the closure period for the small number of staff remaining at the Ludgershall site.

Investors in People

The Agency successfully completed the tasks required of it, to support the DLO preparations to achieve IiP recognition.

A member of staff receiving her Commendation from the Chief Executive for her contribution to the Agency Programme



Health and Safety (H&S) Week

The annual H & S week was held during October 04. The event was organised and run by the Warehouse H & S Advisor. The event consisted of presentations, talks and demonstrations covering the following aspects of H & S:

- Chemical Awareness.
- Environmental Protection
- DSE Self Assessment
- First Aid
- Common causes of accidents
- Stress
- Office Safety

The event was extremely well attended and successful in underlining to all staff the necessity of H & S in the work place.

Christmas Event

The Christmas event in December 2004 included a Carol service, Christmas luncheon and raffle. Although this was the last of what had over the years become a major event, it proved to be a great success and morale booster for everyone, much to the credit of the organisers, the Entertainment Committee, before the closure of the Agency at the end of March 2005.

Closure Event

On 31 March 2005, a closure ceremony marking the end of business of the MSA was held at the Ludgershall site, which had been the home of Army and then Defence Medical Supplies for 60 years. It was attended by DG Def(SC) and marked by a short presentation by the Chief Executive following which a buffet was provided to the Ludgershall based staff, and ex-members of MSA living locally, personally funded by the MSA Management Board.

Section 3

MSA PERFORMANCE AGAINST 2004/2005 KEY TARGETS

The Agency's Key targets (KTs) focus on the delivery of services to meet the customers' routine and operational requirements as well as assessing the Agency's efficiency and the value it adds to the MOD. The KT's are the main way in which the Agency's performance is evaluated and assessed by the MOD, Framework Team, Cabinet Office and parliament.

MSA Key Targets were included in the MSA Business Plan 04/05, constantly monitored and updated on a monthly basis for the MSA Management Board, and the updates were made available for view by customers through the MSA web site on the MOD Intranet.

Key Target 1

Meeting Operational Medical Equipment and Materiel Requirements

To build and deliver, to schedule and within budget, all modules on the Operational Build programme as agreed with our key customer, the Defence Medical Services Department (DMSD), and to meet all authorised operational requirements for equipment, medical consumables and blood products. Also to meet unplanned requests from DMSD based on operational need.

Rationale

This target measures key output of support to operations, through the delivery of:

- a. Medical capability, in the form of equipment and materiel modules. The build programme is agreed annually with DMSD staffs following a full costing exercise and once tasked the Agency aims to deliver to strict time requirements within previously agreed cost ceilings. Unfortunately, funding shortfalls within DMSD have significantly limited the programme in recent years.
- b. Authorised equipment, medical consumables and blood products to meet the ongoing requirements of operational commanders.
- c. Ad-hoc requests for modules. The Agency has responded to, and met, all ad-hoc requests for modules.

Measurement

The Agency aims to meet the full requirement of the module, except where items are obsolete and no replacement has been identified by the appropriate Defence Consultant Adviser through DMSD.

A table showing the last two years performance against Key Target 1 are shown below:

| Key Target 1 Results | 2003/04 |
|--|----------------|
| No of modules in planned Build Programme | 0 ¹ |
| No of planned modules completed | 0 ¹ |
| No of unplanned modules completed | 1739 |
| Total No of modules completed | 1739 |
| Achievement % | N/A |
| Target % | 100 |

| Key Target 1 Results | 2004/05 |
|--|----------------|
| No of modules in planned Build Programme | 0 ¹ |
| No of planned modules completed | 0 ¹ |
| No of unplanned modules completed | 1015 |
| Total No of modules completed | 1015 |
| Achievement % | N/A |
| Target % | 100 |

This target is to provide 100% Support to Operations and remains MSA's and in future the Med S IPT's highest priority. Measurement is based on % achievement of the build programme - the total number of modules completed, planned and unplanned compared against the original number of modules requested.

In respect of meeting all urgent operational requirements, this target was met. Specific urgent demands included delivering medical supplies to relief effort following Hurricane Ivan, providing materiel for Spearhead Lead Element in planned evacuation of Ivory Coast and supporting the Tsunami relief effort on New Year's Day. Despite meeting all urgent operational requirements, the status as at 31 Mar 05 was not achieved in respect of a planned build programme, as one had not been provided. However, the MSA achieved 100% in respect of the unplanned module build.

¹ Due to lack of adequate funding there was no formal Build Programme in Financial Year 2003/04 and 2004/05, therefore the achievement against this key target was not reported.

Key Target 2

Meeting the Medical Equipment and Materiel Requirements for the in-year Exercise and Training Programme

To build and deliver, to schedule and within budget, all modules on the Exercise and Training Build Programme as agreed with DMSD, and to meet all authorised requirements for equipment, medical consumables and blood products.

Rationale

The rationale for this Key Target is similar to that for Key Target 1. It measures output through the delivery of:

- a. Medical capability, in the form of equipment and materiel modules. The build programme is agreed annually with DMSD staffs following a full costing exercise and once tasked the Agency aims to deliver to strict time requirements within previously agreed cost ceilings. Unfortunately, funding shortfalls within DMSD have significantly limited the programme in recent years.
- b. Authorised equipment, medical consumables and blood products to meet the ongoing requirements of units deployed on exercises and training.
- c. Ad-hoc tasking from DMSD.

The objective to deliver complete modules is as in Key Target 1 above and is subject to the same caveat.

Measurement

A table showing the last two years performance and the forecast for Financial Year 2003/04 against Key Target 2 is shown below:

| Key Target 2 Results | 2003/04 |
|---|---------|
| No of loans in planned Build Programme | 1078 |
| No of planned loans completed to date | 762 |
| No of unplanned loans completed to date | 212 |
| Total No of loans completed to date | 974 |
| Achievement % to date | 90.35 |
| Target % | 100 |

| Key Target 2 Results | 2004/05 |
|---|---------|
| No of loans in planned Build Programme | 1 |
| No of planned loans completed to date | 1 |
| No of unplanned loans completed to date | 81 |
| Total No of loans completed to date | 82 |
| Achievement % to date | 100 |
| Target % | 100 |

Measurement is based on % achievement of the build programme - the total number of loan modules assembled, planned and unplanned compared against the original number of loan modules requested. The status as at 31 Mar 05 was achieved.

Key Target 3

Meeting Customer Requirements

To meet demands for non-operational customers in UK and overseas as follows:

- a. **Urgent (Priority Code 5)**
 - **Cat B consumables – ready for despatch same day as receipt of demand.**
 - **Cat E equipment – within 24 hours initial contact made with supplier and customer informed when delivery will be despatched.**
 - **Cat E equipment delivered via Ludgershall despatched same day.**
- b. **Routine (Priority Code 9 – 16)**
 - **Cat B consumables – ready for despatch within four working days.**
 - **Cat E equipment – within 3 days initial contact made with supplier and customer informed when delivery will be despatched.**
 - **Cat E equipment delivered via Ludgershall despatched within 3 days.**

Target 95% achievement applies to a. and b.

Note: Target for Cat B consumables relates to items held in stock or readily available from Trade.

Rationale

This key target measures the MSA's speed of response to demands from authorised customers of medical consumables and equipment used in primary and secondary care, both in the UK and overseas. It measures the time to receive, process, pick and prepare stock for dispatch in accordance with JSP 336 Standard Priority Codes (SPCs). The distribution of stock from the depot to the customer is outside of direct MSA control. The measure allows demanding units to have a high level of confidence in availability of important medical consumables, reduces waste of short shelf life medical consumables and contributes to a reduced need for unit holdings of valuable stock.

Measurement

Measurement of this target is difficult because of the absence of an electronic demand and payment system. We therefore have to rely on measurement of performance against stock ready for despatch to users, and regular contacts with our customers through the customer relationship management process. Full measurement of this process will be possible through the Purchase to Payment (P2P) e-commerce system, which is planned, will be introduced as part of the MSA Change Programme.

Categories

Items procured within Category B (Cat B) covers medical stores, supplies and equipment which are in common use and which are purchased for stock at the Medical Supplies Agency, supplied on a dues out basis or by trade direct means if circumstances require.

Items in this category include: drugs and biological preparations; surgical dressing materials; medical, surgical and pathological instruments; laboratory supplies; medical and dental x-ray supplies; hospital and surgical clothing supplies; opticians instruments; equipment and supplies; veterinary supplies: all War Maintenance Reserve (WMR) stocks.

The definition of Cat B consumables includes stock readily available from trade. Previous targets excluded non-stocked items.

Items procured within Category E (Cat E) covers medical supplies, which are procured either by properly authorised central contracts or local arrangements.

Items in this category cover medical stores such as; laboratory equipment; medical and dental equipment; speech therapy equipment and supplies; artificial limbs; occupational therapy equipment; psychiatric testing material; hearing aids; spectacles; surgical appliances and footwear and veterinary equipment. It also covers equipment maintenance services provided by Contractors. Broadly speaking 'CAT E' items are non-consumable and/or require in-life support management; some training aids are also included (i.e. Resusci-Anne). The demanding unit must have budgetary authority before demanding such items from MSA since purchase is charged to the demanding units budgetary UIN.

FY 03/04

Performance against Key Target 3 for FY 03/04 is shown below (as defined in the old MSA Charter – 1 day, 3 day, Urgent and Routine system):

Top 250 items

Percentage of demands satisfied within MSA Charter Response Time:

| Year | Urgent | Target 95% | Routine | Target 95% |
|-------------|---------------|-------------------|----------------|-------------------|
| 2003/04 | 92 | Not Achieved | 94 | Not Achieved |

Percentage of demands satisfied within follow up (5 days):

| Year | Urgent | Target 97% | Routine | Target 97% |
|-------------|---------------|-------------------|----------------|-------------------|
| 2003/04 | 96 | Not Achieved | 94 | Not Achieved |

Overall Performance

Percentage of demands satisfied within MSA Charter Response Time:

| Year | Urgent | Target 90% | Routine | Target 90% |
|-------------|---------------|-------------------|----------------|-------------------|
| 2003/04 | 89 | Not Achieved | 92 | Achieved |

Percentage of demands satisfied within follow up (5 Days):

| Year | Urgent | Target 97% | Routine | Target 97% |
|-------------|---------------|-------------------|----------------|-------------------|
| 2003/04 | 94 | Not Achieved | 94 | Not Achieved |

Key Target 3 measures performance against customer demands. During the period of failure Ludgershall were required to manage an additional £16m build programme, which put pressure on the existing resources within the Supply Management Division and the Warehouse. This additional activity was not considered when measuring Key Target 3 for Financial Year 2003/04.

FY 04/05

The measurement for Financial Year (FY) 2004/05 Key Target 3 was reviewed because the Agency, as part of the Defence Logistics Organisation, was required to comply with the Defence Supply Chain standard. Performance against Key Target 3 for FY 04/05 is shown below (as defined in the reviewed target):

Percentage of urgent and routine demands met for non-operational customers in UK and overseas:

| Year | Urgent | Target 95% | Routine | Target 95% |
|-------------|---------------|-------------------|----------------|-------------------|
| 2004/05 | 95% | Achieved | 97% | Achieved |

This target was achieved at the end of the year. However, at the half-year position, as at Sep 04, the status was identified as a serious weakness for urgent demands. At that time, between 70% - 80% of the target for urgent demands was being met. This was due to a combination of factors - staff losses and shortages, re-skilling and training arising from the MSA Change Programme. However, the loss in performance was not raised as an issue by any of MSA's customers, but identified from the Agencies internal monitoring and reporting procedures. It was quickly recovered by staff re-deployment, task re-prioritisation and overtime. The target for urgent demands as measured on a monthly basis was met from Nov 04 onwards.

Key Target 4

MSA Change Programme

To work with our customers and stakeholders with the objective of delivering the key elements of the MSA Change Programme, which will deliver significant improvements in the effectiveness, and efficiency of the medical supply chain, contribute to CDL's strategic objectives, and improve delivery to our customers.

Rationale

The MSA Change Programme aims to build on the successful transfer of the MSA from Surgeon General's Department (SG's Dept) to DLO and develop the MSA into a true decider organisation. This objective is to deliver considerable improvements in customer service and a contribution to Chief of Defence Logistics' (CDL) Strategic Objective of a 20% reduction in output costs by Financial Year 2005/06, whilst maintaining, and where appropriate, improving the service to customers.

Measurement

The 31 Mar 05 marked the end of the MSA Change Programme in terms of its status as a DLO 'truly transformational' project, hence this target was achieved.

This reflects the successful delivery of all the work streams and objectives within the MSA Change Programme, which was completed apart from a very small number of activities, now regarded as normal business for the Medical Supplies IPT. These include the final stock removals from, and vacating the Ludgershall site, and the move of the Blood Supply capability of the Blood Supply Depot to Birmingham.

Section 4

FUTURE STRATEGY

As this report is the last of the Medical Supplies Agency, there is no future strategy for the Agency. However its successor, the Med S IPT does have a number of strategic goals, which are worth stating here. Completion of the MSA Change Programme signifies the start of a period of consolidation but also continuation of development of the IPT. Having obtained the confidence of staff to overcome challenges and embrace change, that momentum will be maintained. Work to re-engineer the equipment management and governance areas of the organisation better to be able to cope with the demands of Smart Acquisition will continue. Likewise, the Med S IPT is taking an active and progressive role as a member of the Commodity Cluster of IPTs within the DLO. This is to identify the potential for further structural changes within the Cluster, and a root and branch review of working procedures to see what further enhancements and efficiencies are to be found. Continuous improvement in outputs is a fundamental component of the Med S IPT culture, arising from the MSA Change Programme.

Section 5

FINANCIAL STATEMENTS FOR THE YEAR ENDING 31 MARCH 2005

Foreword to the financial statements

Introduction

The Medical Supplies Agency was established on 1 March 1996 as a Tri-Service Agency and brought together the Defence Medical Equipment Depot, the Army Blood Supply Depot and Medical Distribution Centres, which had previously been managed on a Single Service basis. The Agency ceases to exist on 31 March 2005 when it is to be replaced by the Medical Supplies Integrated Project Team (Med S IPT), within the Director General Defence (Supply Chain). The owner of this Vote funded Agency until 31 March 2005 was DG Def (SC), with the Agency being an integral part of the Ministry of Defence. The DG Def (SC) reports to the Chief of Defence Logistics.

Principal activities

The Agency provides medical, dental and veterinary materiel, blood and blood products, technical and logistic support and trained personnel to the UK Armed Forces worldwide in War, Operations Other Than War (OOTW) and Peace.

Aims and objectives

The aim of the Agency is to ensure the cost-effective and timely provision of medical, dental and veterinary materiel, blood and blood products, technical and medical logistic support and trained personnel to the UK Armed Forces worldwide in War, Operations Other Than War (OOTW) and Peace.

The principal business objective is:

- To fulfil all operational tasks placed on the Agency, on time and within budget.

The supporting business objectives are:

- To provide medical materiel of a specified quality within the overall materiel policy through an agreed standard of service to customers of the Agency in the most efficient manner.
- To establish a fully integrated Tri-Service structure based on best management practice and effective staff arrangements.
- To implement the business systems necessary to meet the Accounts direction, provide the cost of outputs and monitor the performance of the Agency.

Composition of the Management Board during the year ended 31 March 2005

The Management Board assists the Chief Executive in the Management of the Agency. Members of the Board during the year ended 31 March 2005 were:

| | |
|---------------------|---|
| Mr Stephen Smith | Chief Executive |
| Gp Capt Andy Gell | Deputy Chief Executive |
| Cdr Tom McAuslin | Director of Operational Support |
| Mrs Felicity Belsey | Director of Management Services |
| Mr Bernard Mennell | Director of Medical Supply Chain – 1 April 2004 until 14 May 2004. |
| Mr Barry Newton | Director of Medical Supply Chain – 16 August 2004 to 31 March 2005. |

In the interim period between Mr Mennell's departure and Mr Newton's arrival, Cdr McAuslin covered both Operational Support and Supply Chain roles. The Agency does not have any Non-Executive Directors.

Mr Newton was appointed through MOD Civil Service standard procedures.

Remuneration of the board members and details of salary and pension entitlements are shown in Note 2.

Employment policies

The Agency's employment strategy is to employ and promote staff on the basis of individual merit in a non-discriminatory manner. The Agency abides by the existing formal legislation and the MOD Disabled and Equal Opportunity Policy. The Agency Management Board monitor the execution of the policies through the Agency Personnel and Training Section, ensuring staff awareness through Diversity and Disability sessions within induction and refresher training courses. Changes on policy are promulgated through Agency and special Core Briefs, cascaded through the line management chain, where personnel are also directed to centrally issued publications. Briefing is also specifically targeted at local TU representatives.

Staff involvement

Staff involvement is actively encouraged through the informal process of day-to-day line management, the publication of an Agency Core Brief and the formal procedures for appraisal of staff. The Agency has maintained Investors In People through re-accreditation.

Achievements

As well as working against Key Targets, the Agency achieved success against a number of objectives, the most notable of which are summarised below:

➤ Support to customers

This past year has seen a continuing improvement in the level of support provided to our customers and in the performance of the Agency in meeting customer requirements.

➤ Support to Operations

Support to Operations has remained the Agency's highest priority, with ongoing support to Ops Telic and Herrick continuing to require high levels of staff endeavour.

As well as the now routine operational activities, Operations Division staff have responded to several short notice demands, for life and limb saving equipment, including on New Year's Day 2005, provision of medical materiel to support the Asian Tsunami relief operation.

➤ **MSA Change Programme**

During the year the Agency's Change Programme, approved by Minister Armed Forces (AF), has been implemented. This has resulted in fundamental changes in the processes and procedures for the acquisition and delivery of medical materiel to the Armed Forces, enabling the Agency to exit the business of storage and distribution, thereby enabling significant reductions in operating costs and personnel, while aiming to improve levels of service.

➤ **People**

The main focus during the year has been to prepare staff for the changes introduced by the Change Programme, and in particular preparing those who were surplus to future requirements to be best placed for gaining employment elsewhere. To this end Learning Skills and Re-skilling programmes have been vigorously pursued and have been much appreciated by those affected. The HR Joint Working Group set up towards the end of the previous year, to address all HR aspects of the MSA Change Programme, has proved invaluable in maintaining good relationships between management, Unions and the workforce as a whole during this fundamental period of change.

➤ **Finance**

The internal compliance audit programme, inaugurated in 2003-2004, has been built on in 2004-2005 with reports on monthly audits presented to the Assurance Committee and action plans forwarded to the Management Board as appropriate.

Financial review

The net operating costs for year ending 31 March 2005 were £28,321 (£000s) (2003-04 £36,555 (£000s)).

Fulfilment of the Change Programme has generated some additional costs in 2004-2005 particularly on Other Administration Costs where the Agency is now providing for a future liability of £2,169 (£000s) for Early Departure Costs. Improvements to the building and information technology infrastructures within the Defence Storage and Distribution Agency, who will now be providing a much reduced storage facility dedicated solely to our deployable customers, have also had to be committed to.

However, 2004-2005 sees an overall drop in operating costs from 2003-2004, mainly attributable to both a much reduced requirement to write-off in year stock, particularly high in 2003-2004 for Medical Countermeasure items, and the need not to provide such a dramatic increase in our provision for the future write-off of stocks.

Total Net Assets at 31 March 2005 were £41,891 (£000s) (2003-04 £50,461 (£000s)). This drop is attributable to the reduction in the quantity of stocks held at our Ludgershall site, entirely planned in readiness for its complete closure during 2005-2006, offset by an increase in liabilities, specifically for early departure costs as mentioned above.

Key future developments in the activity of the Agency

As already stated, the Change Programme has enabled the Agency to exit from directly maintaining and managing the business of storage and distribution. Non-deployable customers will now receive their medical supplies deliveries direct from suppliers. Deployable customers will now receive their supplies from a much reduced storage and module build facility embedded within the Defence Storage and Distribution Agency (DSDA).

The Change Programme has resulted in an organisation significantly less than half the size of the Agency at the start of the reporting year, delivering the same outputs but utilising best commercial practices. This much smaller organisation and the ongoing closer integration into the Defence Supply Chain as part of the Defence Logistics Organisation Commodity Cluster, argued for the termination of agency status. This also reflected the fact that the Agency was originally created when in the Surgeon General's department where there was limited logistics knowledge or expertise. Furthermore all the generic benefits of Agency status, in terms of definition of clear targets, flexibility in decision making, accountability, and reporting and monitoring performance, are all inherent within the management and performance monitoring regime within the Defence Supply Chain and applied equally to all business units. Hence there was nothing to be lost by removing agency status, while there were some gains to be made through greater logistics integration and reductions in overheads. Based on these arguments, agreement to removal of agency status was given by Min AF with the concurrence of Ministers and HMT.

Recognising that 2004-2005 is the Agency's last year of existence, key future developments will therefore focus on the bedding down of new procedures and processes being adopted by its successor, the Medical Supplies Integrated Project Team (Med S IPT).

The IPT will also have to ensure that all customers enjoy the same high standards of service that they previously enjoyed with the Agency. This will inevitably require considerable monitoring and management of suppliers' performance by the new IPT.

At the same time, it will have to learn the disciplines of "through life management" and "whole life approach" as it looks to take on a greater role in deciding efficient and effective equipment solutions in accordance with the principles of "SMART" acquisition, as announced by recent Ministry of Defence Strategic Reviews.

Creditor payment policy

The Agency's bills, with the exception of some payments to suppliers by units locally and outside Great Britain, are paid through the Defence Bills Agency (DBA). Undeniably, an increase in the quantity of invoices received during 2004-2005 has meant that the Agency has sometimes struggled to certify and pass some invoices to DBA within the short timeframes achieved in previous years. However, on receipt at DBA, DBA has continued to meet its own high standards of performance paying 99.98% of all certified bills within 11 calendar days of receipt. Despite the drop in the Agency's own performance, no penalties have been invoked by suppliers under the Late Payment of Commercial Debts (Interest) Act 1998.

Auditors

The Accounts are audited by the Comptroller and Auditor General in accordance with section 7(3)(b) of the Government Resources and Accounts Act 2000.

The fee of £53,000 is in respect of statutory audit work only. The Auditors provided no other services.

A handwritten signature in black ink, appearing to read 'Stephen L Smith', written over a light grey rectangular background.

Mr S L Smith
Chief Executive
Medical Supplies Agency
6 July 2005

Statement of Agency and Chief Executive's responsibilities

Under Section 7(2) of the Resource Accounts Act 2000, Treasury has directed the Medical Supplies Agency to prepare a statement of accounts for each financial year, in the form and on the basis set out in the Resource Accounting Manual.

The financial statements are to be prepared on an accruals basis and must give a true and fair view of the state of the Agency's affairs at the year-end, and of its income, expenditure and cash flows for the financial year.

In preparing the financial statements the Agency is required to:

- observe the Accounts Direction issued by the Treasury, including 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 and financial reporting standards 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 Departmental Accounting Officer for the Ministry of Defence has appointed the Chief Executive of the Medical Supplies Agency as the Accounting Officer for the Agency. His relevant responsibilities as Accounting Officer, including his responsibility for the propriety and regularity of the public finances for which he is answerable and for the keeping of proper records are set out in the Accounting Officer's Memorandum, issued by the Treasury and published in "Government Accounting".

Statement on Internal Control

1. Scope of responsibility

As Chief Executive of the Medical Supplies Agency, I have responsibilities analogous to an Accounting Officer. These include responsibility for maintaining a sound system of internal control that supports the achievement of Agency policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Government Accounting and through my letters of delegation and designation.

The Agency is divided into 3 Directorates, an Integrated Project Team (IPT) and a Clinical & Professional Support Division. The Directorates are managed by a Director and the IPT by an IPT Leader, each with delegated responsibilities, who provide regular reports on performance to me as Chief Executive and who sit on the Agency Management Board.

As approved by Minister Armed Forces (AF) on 13th September 2004, the Agency is now divested of its Agency status with effect from 31st March 2005 and will transform into the Medical Supplies IPT (Med S IPT) on 1st April 2005.

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 Agency 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 the Agency for the year ended 31st March 2005 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

3. Capacity to handle risk

Risks within the Agency and from 1st April 2005, the Med S IPT, are captured, actioned and managed as follows:

- Change Programme risks have been owned and managed by the Agency's Change Programme Board, in accordance with the Defence Logistics Organisation's own Change Programme's Risk and Issue Management Strategy. Issues have been raised to the Agency's Management Board as necessary.
- Business level risks are mapped to the Business Plan key outputs and each has Business Owners and Managers. The Risk Register has been reviewed by the Agency's Management Board on a monthly basis, and will soon be upgraded to reflect the business needs and risks of the new IPT.
- Lower levels of risk are managed by individual department heads and work stream leaders.
- The Risk Register is managed in accordance with formal Departmental Guidance and all staff associated with risk management are fully competent in measuring their own area of risk.

Over the past year there has also been a series of workshops and consultancy with the Ministry of Defence's dedicated Internal Audit unit - Defence Internal Audit (DIA) - to review risk management within the Agency, including finalisation of the Risk Register.

4. The risk and control framework

Risk is identified in a number of ways including brainstorming, workshops and professional consultative advice. Risks are evaluated by the Assurance Committee and the Change Programme Board as to both likelihood and severity, and a suitable response to the risk is formulated based on the risk appetite of both the Agency and the customers.

Generic areas of risk priority in the Agency, and in future the Med S IPT, include the following:

- Change Programme
- Supply
- Personnel
- Regulatory
- Infrastructure
- Information Technology (IT)
- Professional
- Policy/Planning

As already stated, with the change of the Agency into the Med S IPT, these risks are to be reviewed.

The Agency's Business Risk Register has been reviewed regularly by the Assurance Committee and Management Board and has been formally signed off by the Assurance Committee at its last meeting. Each risk and associated Management Action Plan within the Agency Business Plan has had a business risk owner who is a member of the Management Board. Each risk owner has in turn identified Risk Managers who have reviewed the risks regularly. It is intended to maintain this system within the new IPT. The Agency's Change Programme has had an additional risk register, which has been reviewed regularly at the Change Programme Board.

5. Review of effectiveness

As Chief Executive, with powers analogous to those of an Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the Agency 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. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Board; the Audit Committee and the Agency's Assurance Committee and a plan to address weaknesses and ensure continuous improvement of the system is in place.

- A Management Board that meets monthly to consider the plans and strategic direction of the Agency and to monitor progress against the Business Plan, Balanced Scorecard and Risk Register.
- An Assurance Committee that meets approximately bimonthly. An independent Chairperson chairs this. The members of the committee represent all areas of the Agency. The Assurance Committee is set up to review external and internal audits and advise on risks and control weaknesses. The Secretary ensures that the Management Board receive the minutes of the committee.
- The Agency Business Continuity Plan has been reviewed in year. Following the majority of staff moving to Andover, it is recognised a major revision will take place in the near future.
- A Safety, Health, Environment and Fire (SHEF) Committee that meets quarterly.
- A series of Medical Supplies Agency Standard Operating Procedures, that dictate procedures to be followed for key processes within the Agency, to strengthen Statutory and Ministry of Defence wide regulations. A programme of internal Compliance Audits has been operating for the past year and findings reported to the Assurance Committee and, if necessary, onto the Management Board in the form of a Management Action Plan.
- A bi-annual internal audit for the Wholesale Dealers licence, with external audit by the Medicines and Healthcare products Regulatory Agency (MHRA) every 3 years and weekly stock checks of controlled drugs carried out by Senior Management staff.
- An annual report on Assets & Inventory covering stocktaking and other stock account adjustments, to complement the formal return made to the Director General Defence Supply Chain's policies and in accordance with formal Departmental guidance, i.e. the Defence

Supply Chain Manual - Part C. A programme is also in place for Management Board members to hold regular snap stock takes over the year.

Where appropriate, these are to be replicated in the new IPT.

6. Significant internal control problems

In response to the Change Programme, many experienced and valued members of staff have sought voluntary transfers to other parts of the Ministry of Defence. This has threatened business continuity within most of the Agency's divisions but particularly in the Supply/Procurement area. This has been countered through the employment of a growing number of temporary staff but all carefully trained and monitored to ensure effectiveness.

A handwritten signature in black ink, appearing to read 'Stephen L. Smith', written in a cursive style.

**Mr S L Smith
Chief Executive
Medical Supplies Agency
6 July 2005**

The certificate and report of the Comptroller and Auditor General to the House of Commons

I certify that I have audited the financial statements on pages 11 to 29 under the Government Resources and Accounts Act 2000. These financial statements have been prepared under the historical cost convention as modified by the revaluation of certain fixed assets and the accounting policies set out on pages 14 to 16.

Respective responsibilities of the Agency, the Chief Executive and auditor

As described on page 5 the Agency and Chief Executive are responsible for the preparation of the financial statements in accordance with the Government Resources and Accounts Act 2000 and Treasury directions made thereunder and for ensuring the regularity of financial transactions. The Agency and Chief Executive are also responsible for the preparation of the other contents of the Annual Report. My responsibilities, as independent auditor, are established by statute and I have regard to the standards and guidance issued by the Auditing Practices Board and the ethical guidance applicable to the auditing profession.

I report my opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Government Resources and Accounts Act 2000 and Treasury directions made thereunder, and whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. I also report if, in my opinion, the Foreword is not consistent with the financial statements, if the Agency has not kept proper accounting records, or if I have not received all the information and explanations I require for my audit.

I read the other information contained in the Annual Report, and consider whether it is consistent with the audited financial statements. I consider the implications for my certificate if I become aware of any apparent misstatements or material inconsistencies with the financial statements.

I review whether the statement on pages 6 to 8 reflects the Agency's compliance with Treasury's guidance on the Statement on Internal Control. I report if it does not meet the requirements specified by the Treasury, or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered whether the Accounting Officer's Statement on Internal Control covers all risks and controls. I am also not required to form an opinion on the effectiveness of the Agency's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

I conducted my audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Agency and Chief Executive in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Agency'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 are free from material misstatement, whether caused by error or by fraud or other irregularity and that, in all material respects, the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I have also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In my opinion:

- The financial statements give a true and fair view of the state of affairs of the Medical Supplies Agency at 31 March 2005 and of the surplus, total recognised gains and losses and cash flows for the year then ended and have been properly prepared in accordance with the Government Resources and Accounts Act 2000 and directions made thereunder by the Treasury; and
- In all material respects, the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities, which govern them.

I have no observations to make on these financial statements.



John Bourn
Comptroller and Auditor General

Date: 11 July 2005

National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

OPERATING COST STATEMENT

For the year ending 31 March 2005

| OPERATING COSTS | Note | 2004/05 £'000 | 2003/04 £'000 <i>re-stated</i> ⁽¹⁾ |
|--------------------------------|-------------|--------------------------|--|
| Staff costs | 2 | 8,681 | 8,130 |
| Supplies and services consumed | 3 | 12,538 | 23,583 |
| Accommodation costs | 4 | 1,570 | 1,681 |
| Other administration costs | 5 | 6,278 | 3,652 |
| Gross operating costs | | 29,067 | 37,046 |
| Operating Income | 7 | (746) | (491) |
| Net operating costs | 19 | 28,321 | 36,555 |

STATEMENT OF RECOGNISED GAINS AND LOSSES

For the year ending 31 March 2005

| | Note | 2004/05 £'000 | 2003/04 £'000 |
|---|-------------|--------------------------|--------------------------|
| Unrealised net (gain)/loss on revaluation | 13 | 4,407 | (6,328) |
| Recognised Losses / (Gains) | | 4,407 | (6,328) |

The notes on pages 14 to 29 form an integral part of these financial statements.

⁽¹⁾ The prior year comparators for the other administration costs (note 5) and other operating income (note 7) have been restated by £423,121. This is to ensure that all costs and income are disclosed on a gross rather than net basis. Total net operating costs for 2003-04 remain unchanged at £36,555,252.

BALANCE SHEET
As at 31 March 2005

| | <u>Note</u> | 31 March 2005 | | 31 March 2004 | |
|--|-------------|----------------|----------------------|----------------|----------------------|
| | | £'000 | £'000 | £'000 | £'000 |
| Fixed assets | | | | | |
| Tangible assets | 8 | | 8,313 | | 9,089 |
| Current assets | | | | | |
| Stock/work in progress | 9 | 41,609 | | 49,962 | |
| Debtors due within one year | 10 & 21 | <u>2,971</u> | | <u>675</u> | |
| Total current assets | | 44,580 | | 50,637 | |
| Current liabilities | | | | | |
| Creditors: amounts falling due within one year | 11 & 21 | <u>(8,833)</u> | | <u>(9,265)</u> | |
| Net current assets | | | <u>35,747</u> | | <u>41,372</u> |
| Total assets less current liabilities | | | 44,060 | | 50,461 |
| Provisions for liabilities and charges | 12 | | (2,169) | | 0 |
| Net assets | | | <u>41,891</u> | | <u>50,461</u> |
| Taxpayers' equity | | | | | |
| Revaluation reserve | 13 | | 2,005 | | 6,464 |
| General Fund | 14 | | 39,886 | | 43,997 |
| | 15 | | <u>41,891</u> | | <u>50,461</u> |

The movement in Government Funds is set out at note 15 on page 26.

The notes on pages 34 to 50 form an integral part of these financial statements.



Mr S L Smith
Chief Executive
Medical Supplies Agency
6 July 2005

CASH FLOW STATEMENT

For the year ending 31 March 2005

| | <u>Note</u> | <u>2004/05</u> <u>£'000</u> | <u>2003/04</u> <u>£'000</u> |
|---|-------------|--------------------------------|--------------------------------|
| Net cash outflow from operating activities | 19 | 21,983 | 28,057 |
| Capital expenditure | | | |
| Payments to acquire tangible fixed assets | 8 | 91 | 2 |
| Net cash outflow before financing | | <u>22,074</u> | <u>28,059</u> |
| Financing | | | |
| Payments on Defence Resource Accounts | | 22,489 | 28,550 |
| Receipts on Defence Resource Accounts | | (415) | (491) |
| Voted expenditure appropriated in year | | <u>22,074</u> | <u>28,059</u> |
| Increase/(decrease) in cash | | <u>0</u> | <u>0</u> |

The notes on pages 34 to 50 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1: ACCOUNTING POLICIES

A. Basis of accounting

The financial statements for the Medical Supplies Agency have been prepared in accordance with the Resource Accounting Manual issued by HM Treasury. The financial statements have been prepared under the historical cost convention, modified to account for the revaluation of fixed assets and stocks to reflect their value to the business by reference to their current costs.

B. Value Added Tax

The Agency is not separately registered for Value Added Tax (VAT) as the Ministry of Defence accounts for VAT centrally. Following revision of the Departmental policy, input VAT on certain contracted out services is now recovered centrally through the MOD registration, consequently no debtor is included in the current year. All other input VAT is irrecoverable and is therefore included in the cost of the related expenditure or asset.

C. Income

Income comprises the value of services/supplies to other Government Departments, the wider public sector and the private sector. No value is attributed in the financial statements to services provided to other organisations within the Ministry of Defence. The funding of the Agency by the Ministry of Defence is shown in cash terms in the Cash Flow Statement.

The financial objective of the Agency is full cost recovery. The Agency has two separate charging regimes. The costs charged allow full recovery of costs for customers in different locations.

D. Notional charges

- 1) A notional charge for interest on capital is included in the Operating Cost Statement. This is calculated as 3.5% of the average value of total net assets in accordance with Ministry of Defence accounting policy.
- 2) Notional amounts are included in the Operating Cost Statement for charges in respect of services provided from other areas of the Ministry of Defence.

E. Fixed assets and depreciation

(1) Land and buildings, Non-dwellings

Where the Agency is the beneficial user of the Departmental Estate, such estate is treated as an asset of the Agency although legal ownership is vested in the Secretary of State for Defence.

Professional valuations of land and buildings are carried out at least once every 5 years. The last valuation was undertaken as at 1 April 2002 by the Valuation Office Agency and ATIS Real Weatheralls. This was undertaken on the basis of the value to the business model and was in accordance with the Royal Institution of Chartered Surveyors Appraisal and Valuation Manual. In accordance with the rolling programme of valuations agreed between the Ministry of Defence and the National Audit Office, new valuations are to be provided for 1 April 2005.

In the intervening years, land and buildings are re-valued using appropriate indices in accordance with MOD policy. Adjustments arising on revaluation are taken to a Revaluation Reserve. Permanent diminution in value is charged to the Operating Cost Statement to the extent that it is not covered by previous increases in values.

(2) Single Use Military Equipment (SUME)

The entire Agency's SUME is held on the Fixed Asset Register of the Equipment Support (Land) area of the MOD, and is communicated by them to the Agency. Fighting Equipment is capitalised where the useful life exceeds 1 year and the cost of acquisition and installation exceeds the Agency's capitalisation threshold. They are revalued annually using indices issued by the Corporate Financial Controller.

(3) Plant and Machinery and Information Technology (IT)

Plant and machinery assets, and Information Technology assets are capitalised where the useful life exceeds 1 year and the cost of acquisition and installation exceeds the Agency's capitalisation threshold. They are revalued annually using indices issued by the Corporate Financial Controller. Adjustments arising on revaluation are taken to a Revaluation Reserve. Permanent diminution in value is charged to the Operating Cost Statement to the extent that it is not covered by previous increases in values.

(4) Depreciation

Freehold land is not depreciated. Depreciation on all other fixed assets is calculated to write-off the cost or valuation of assets by equal instalments over their estimated useful lives, which are normally in the following ranges:

| Asset Category | Life |
|--------------------------------|-------------|
| Buildings, excluding dwellings | 15-50 years |
| Fighting Equipment | 5-40 years |
| Plant and machinery | 5-15 years |
| Information Technology | 5 years |

(5) Disposal of assets

The Agency does not receive any cash benefit for assets disposed of, any cash receipts being accounted for centrally by the Ministry of Defence.

(6) Capitalisation Threshold

Assets are capitalised by the Agency where the useful life exceeds one year and the cost of acquisition and installation is greater than £5,400 inclusive of VAT.

(7) Tangible Fixed Asset Transfers

In common with all Defence Agencies, tangible fixed assets are transferred to other parts of the MOD on a nil gain / nil loss basis. Under this accounting treatment, net asset transfers to other MOD bodies are transferred through the General Fund with no effect on the Operating Costs of the Agency.

F. Cash, Taxation and Social Security Liabilities

The Agency does not pay or receive money on its own account. Cash payments are made and receipts collected by the Ministry of Defence's central accounting organisations on behalf of the Agency. All transactions are brought to account by the Ministry of Defence and are disclosed in aggregate in the Cash Flow Statement.

As the Ministry of Defence charges the Agency during the year with the gross payments, inclusive of PAYE and National Insurance Contributions due to Agency employees, the Department is liable for the payment of any liabilities which may be due to the Inland Revenue or Department of Social Security at the balance sheet date, and these are not disclosed in the Agency's balance sheet.

G. Stocks

Stocks are stated at the lower of current replacement cost and net realisable value. Cost comprises purchase price and includes expenses incidental to acquisition. Current replacement cost represents the cumulative revaluation of stock using the latest cost of acquisition.

Net realisable value applies to stocks, which are not intended to be used or sold in the ordinary course of business. Where appropriate, provision is made for obsolete, surplus and defective stock.

H. Pension Costs

Staff are covered by the provisions of the Principal Civil Service Pension Schemes, the Armed Forces Pension Scheme, the NHS Pension Scheme and the UKAEA Principal Non Industrial Pension Scheme. Contributions are paid to the Paymaster General at rates determined from time to time by the Government Actuary and advised by the Treasury. These contributions were charged to the Agency as a cash cost for the period of these financial statements.

I. Research and Development Costs

These are costs incurred in the development of vaccines used as Medical Countermeasures. In accordance with MOD policy these costs are not capitalised as Intangible Assets, but are expensed to the OCS when incurred.

J. Operating Lease Commitments

Rental costs incurred under operating leases are charged to the Operating Cost Statement on a straight-line basis over the period of individual leases.

K. Provision for Liabilities and Charges

Provision for liabilities and charges under the criteria of FRS 12 and are based on realistic and prudent estimates of the expenditure required to settle future legal or constructive obligations that exist at the balance Sheet date. Our long term provisions are discounted to current prices by use of the HM Treasury's discount rate which is currently 3.5%.

2: STAFF COSTS AND NUMBERS

The Chief Executive received total emoluments, including bonus payments but excluding pension contributions, of £75,178. Mr Smith is a member of the UKAEA Principal Non Industrial Pension Scheme.

In line with new Departmental policy, contract staff numbers and costs are now included in this heading. Previous year comparative staff numbers have been adjusted for comparison purposes in table 1 below and the costs previously disclosed as professional fees are now included in table 2 below.

1. The average number of employees during the year was as follows:

| | 2004/05 | 2003/04 |
|----------------|------------|------------|
| | No. | No. |
| Military | 26 | 34 |
| Civil Service | 279 | 319 |
| Contract Staff | 36 | 27 |
| | <u>341</u> | <u>380</u> |

2. Staff costs can be analysed as follows:

| | 2004/05 | 2003/04 |
|-------------------------------|--------------|--------------|
| | £'000 | £'000 |
| Salaries and wages | 6,535 | 6,287 |
| Contract staff costs | 890 | 683 |
| Social Security costs (ERNIC) | 445 | 404 |
| Pension costs | 811 | 756 |
| | <u>8,681</u> | <u>8,130</u> |

3. The salary and pension entitlements of the most senior members of the Medical Supplies Agency are as follows:

| | <u>Salary Including Performance Pay £'000</u> | <u>Real increase in Pension and related lump sum £'000</u> | <u>Total Accrued Pension at 31/3/05 and related lump sum £'000</u> | <u>CETV at 31/3/04 £'000</u> | <u>CETV at 31/3/05 £'000</u> | <u>Real increase in CETV after adjustment for inflation and change in market investment factors £'000</u> | <u>Employer contribution to partnership pension account incl risk benefit cover £'000</u> |
|---|--|--|--|------------------------------|------------------------------|---|---|
| Mr S Smith Chief Executive | 75-80 | 0-2.5 plus 2.5-5.0 lump sum | 30-35 plus 100-105 lump sum | 421 | 434 | 12 | 0 |
| Gr Capt A Gell | 65-70 | 0-2.5 plus 5.0-7.5 lump sum | 20-25 plus 65-70 lump sum | 495 | 567 | 61 | 0 |
| Deputy Chief Executive | | | | | | | |
| Ms F Belsey Director Management Services | # Consent to disclosure withheld 65-70 | | | | | | |
| Cdr T McAuslin Director Operational Support | | 2.5-5.0 plus 12.5-15.0 lump sum | 20-25 plus 65-70 lump sum | 437 | 547 | 101 | 0 |
| Mr B Mennell Director Medical Supply Chain | # 10-15 | 0-2.5 plus 0-2.5 lump sum | 20-25 plus 55-60 lump sum | 345 | 353 | 2 | 0 |
| Mr B Newton Director Medical Supply Chain | # 20-25 | 0-2.5 plus 5.0-7.5 lump sum | 10-15 plus 35-40 lump sum | 134 | 164 | 22 | 0 |

opted to remain in PCSPS Classic scheme

Mr B Mennell was Director Medical Supply Chain until 14 May 2004 and was succeeded by Mr B Newton on 16 August 2004.

4. 'Salary' includes gross salary, performance pay or bonuses; overtime; reserved rights to London weighting or London allowances; recruitment and retention allowances; private office allowances and any other allowance to the extent that it is subject to UK taxation.

5. Pension benefits are provided through the Armed Forces Pension Scheme (AFPS), the Civil Service pension arrangements, the National Health Service Pension scheme (NHSPS) or the UKAEA Principal Non Industrial Superannuation Scheme (PNISS), as appropriate. All these schemes are unfunded multi-employer defined benefits schemes but MSA is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out at 31 March 2003 for PCSPS, 31 March 2001 for AFPS and 31 March 2001 for PNISS. Details can be found in the resource accounts for these schemes, which are published and laid before the House of Commons.

a) Armed Forces Pension Scheme (AFPS)

AFPS is a non-contributory defined benefit scheme that provides benefits at a normal retirement age of 55. Benefits in the scheme accrue unevenly throughout service and in addition a lump sum equivalent to three years' pension is payable on retirement.

b) Principal Civil Service Pension Scheme (PCSPS)

From 1 October 2002, civil servants may be in one of three statutory based 'final salary' defined benefit schemes (classic, premium and classic plus). The schemes are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under classic, premium and classic plus are increased annually in line with changes in the Retail Prices Index. New entrants after 1 October 2002 may choose between memberships of Premium or joining a good quality 'money purchase' stakeholder based arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at the rate of 1.5% of pensionable earnings for classic and 3.5% for premium and classic plus. Benefits in classic accrue at the rate of 1/80th of pensionable salary for each year of service. In addition a lump sum equivalent to three years' pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum (but members may give up or commute some of their pension to provide a lump sum). Classic plus is essentially a variation of premium, but with benefits in respect of service before 1 October 2002 calculated broadly as classic.

The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3% and 12.5% (depending on the age of the member) into a stakeholder pension product chosen by the employee. 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% of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8% of pensionable salary to cover the cost of centrally provided risk benefit cover (death in service and ill health retirement).

Further details about the Civil Service pension (CSP) arrangements can be found at the website www.civilservice-pensions.gov.uk.

c) United Kingdom Atomic Energy Authority (UKAEA) Principal Non Industrial Superannuation Scheme (PNISS)

UKAEA is responsible for the Principal Non Industrial Superannuation Scheme (PNISS), a defined benefit non-contributory scheme, which is closed to new members. All contributions are paid to and benefits paid by HM Government via the Consolidated Fund. The surpluses of contributions over benefits are deemed to have been invested in portfolios of notional

securities reflecting the investments of a sample of UK funded pension schemes. The most recent actuarial valuations show notional surpluses in the UKAEA sub-fund and UKAEA has followed the Government Actuary's recommendation that no employer contributions need to be paid for the period covered by these financial statements.

The table shown at 3 above shows the member's cash equivalent transfer value (CETV) accrued at the beginning and end of the reporting period. The real increase in CETV is 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.

A 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 the disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the CSP arrangements and for which the Civil Superannuation Vote has received a transfer payment commensurate to 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.

6. For 2004-05, employers' contributions of £810,534 (2003-04 £756,244) were payable at rates in the range 7 to 33.8 percent of pensionable pay, based on salary bands. Employer contributions for PCSPS are to be reviewed every four years following a full scheme valuation by the Government Actuary. Employer contributions for the AFPS have been reviewed during 2003-04. Employer contributions to PNISS, a defined benefit scheme that is closed to new members, for the period covered by these financial statements were not required following the most recent actuarial valuation. The contribution rates reflect benefits as they are accrued, not when the costs are actually incurred, and reflect past experience of the schemes.

3: SUPPLIES AND SERVICES CONSUMED

| | 2004/05 £'000 | 2003/04 £'000 <i>re-stated</i> <i>(1)</i> |
|---|------------------|--|
| Stock write off/(on) | 325 | 5,020 |
| Stock provisions | (608) | 7,385 |
| Operating leases: Plant, machinery & vehicles | 144 | 129 |
| IT maintenance, support and software | 1,391 | 924 |
| Depreciation on plant, machinery, vehicles and IT | 104 | 129 |
| Non medical materiel | 757 | 164 |
| Transport | 252 | 251 |
| Accommodation stores | 194 | 124 |
| Research and Development expenditure | 7,283 | 9,165 |
| Miscellaneous | 2,696 | 292 |
| | 12,538 | 23,583 |

⁽¹⁾ The prior year comparators for Transport costs and for the cost of Operating Leases: Plant machinery & vehicles have both been re-stated by £18,905. This more correctly reports the Agency's costs in hiring further vehicles beyond those already permanently assigned to it through long term operating leases. Total Supplies and Services Consumed costs for 2003-04 remain unchanged at £23,583,070.

4: ACCOMMODATION COSTS

| | 2004/05 £'000 | 2003/04 £'000 |
|---|------------------|------------------|
| Works maintenance | 441 | 664 |
| Depreciation of land and buildings | 479 | 445 |
| Rent and rates | 391 | 361 |
| Utilities (gas, water, fuel, electricity) | 210 | 163 |
| Telecommunications | 49 | 48 |
| | <u>1,570</u> | <u>1,681</u> |

5: OTHER ADMINISTRATION COSTS

| | 2004/05 £'000 | 2003/04 £'000 <i>re-stated</i> <i>(1)</i> |
|-------------------------------|------------------|--|
| Cost of capital charge | 1,711 | 1,780 |
| Administration | 16 | 43 |
| MOD central overhead | 363 | 658 |
| Professional fees | 414 | 306 |
| Training | 418 | 411 |
| Auditors fee | 53 | 51 |
| Permanent diminution in value | 202 | 1 |
| Fixed assets written off/(on) | (15) | (8) |
| Bad debt provision | 60 | (1) |
| Recruitment | 6 | 4 |
| Early departure costs | 2,255 | - |
| Miscellaneous | 795 | 407 |
| | <u>6,278</u> | <u>3,652</u> |

Contract staff numbers and costs are included in the staff costs heading.

⁽¹⁾ The prior year comparator for Miscellaneous administration costs has been restated by £423,121. This is to ensure that all costs are disclosed on a gross rather than net basis.

6: NOTIONAL COST ITEMS

The notional cost elements, also included under the headings of Staff Costs, Supplies and Services Consumed, Accommodation, and Other Administration Costs, are as follows:

| | 2004/05 £'000 | 2003/04 £'000 |
|---|--------------------------------|--------------------------------|
| Staff Costs | 167 | - |
| MOD central overhead | 363 | 658 |
| Rent and site utilities and other costs at host units | 411 | 412 |
| MOD military training | 246 | 279 |
| Audit fee | 53 | 51 |
| MOD civilian training | 115 | 90 |
| Plant, Machinery & Vehicle rentals | 144 | 129 |
| | <u>1,499</u> | <u>1,619</u> |

7: OPERATING INCOME

| | 2004/05 £'000 | 2003/04 £'000 |
|--|--------------------------------|--------------------------------|
| Revenue from supply of medical materials | 746 | 491 |
| Cost of medical materials supplied | (788) | (423) |
| Surplus / (deficit) from supply of medical materials | <u>(42)</u> | <u>68</u> |

Operating income is in respect of the supply of medical materials to specific overseas hospitals and other approved bodies both in the UK and overseas.

8: FIXED ASSETS

| | Land & Buildings Non-dwellings £'000 | Single Use Military Equipment £'000 | Plant and Machinery £'000 | Information Technology £'000 | Total £'000 |
|--------------------------|---|--|------------------------------|---------------------------------|----------------|
| Cost or valuation | | | | | |
| At 1 April 04 | 9,243 | 14 | 905 | 198 | 10,360 |
| Additions | 24 | - | 67 | - | 91 |
| Revaluations | 1,411 | - | 4 | - | 1,415 |
| Impairments | - | - | (300) | (20) | (320) |
| Write (off)/on | - | - | (36) | (19) | (55) |
| Disposals | - | - | - | - | - |
| Transfers | (1,188) | - | (132) | - | (1,320) |
| At 31 March 05 | 9,490 | 14 | 508 | 159 | 10,171 |
| Depreciation | | | | | |
| At 1 April 04 | 906 | 2 | 210 | 153 | 1,271 |
| Amount in current year | 479 | - | 92 | 12 | 583 |
| Revaluations | 236 | - | 2 | - | 238 |
| Impairments | - | - | (69) | (49) | (118) |
| Write (off)/on | - | - | (33) | (19) | (52) |
| Disposals | - | - | - | - | - |
| Transfers | (55) | - | (9) | - | (64) |
| At 31 March 05 | 1,566 | 2 | 193 | 97 | 1,858 |
| Net Book Value | | | | | |
| At 1 April 04 | 8,337 | 12 | 695 | 45 | 9,089 |
| At 31 March 05 | 7,924 | 12 | 315 | 62 | 8,313 |

Land and Buildings, Non-dwellings:

The last professional valuation was completed by the Valuation Office Agency and ATIS Real Weatheralls, members of the Royal Institution of Chartered Surveyors (RICS) and the Incorporated Society of Valuers (ISVA), in accordance with the RICS Appraisal and Valuation Manual on 1 April 2002. The valuation was based on existing use to the Agency.

On completion of the Agency's Change Programme during 2005-2006, all land and building assets will be transferred over to the Department's Defence Estates (DE) Unit on a no gain to DE, no loss to the Agency basis.

Plant & Machinery:

Some Plant & Machinery have now been re-valued in accordance with their open market value, reflecting their impending sale through the Defence Sales Agency. Others remain valued on their existing use basis given their expected transfer to other MOD Units during 2005-2006. Again, these will be completed on a no gain to the receiving unit, no loss to the Agency basis.

9: STOCKS & WORK IN PROGRESS

| | 2004/05 £'000 | 2003/04 £'000 |
|-----------------------------------|------------------|------------------|
| Medical materiel owned by the MSA | 40,722 | 49,594 |
| Work in progress | 887 | 368 |
| | <u>41,609</u> | <u>49,962</u> |

Work in Progress represents the valuation of partially complete modules of medical materiel.

10: DEBTORS

| | 2004/05 £'000 | 2003/04 £'000 |
|--------------------------------|------------------|------------------|
| Trade debtors | 543 | 308 |
| Prepayments and accrued income | 2,428 | 367 |
| | <u>2,971</u> | <u>675</u> |

11: CREDITORS - AMOUNTS FALLING DUE WITHIN ONE YEAR

| | 2004/05 £'000 | 2003/04 £'000 |
|------------------|------------------|------------------|
| Trade creditors | 3,432 | 4,579 |
| Accrued expenses | 5,401 | 4,686 |
| | <u>8,833</u> | <u>9,265</u> |

12: PROVISION FOR LIABILITIES AND CHARGES

| | Early Departur e Costs £'000 | Total £'000 |
|--|---------------------------------------|----------------|
| At 1 April | 0 | 0 |
| Charged (credited) to the Operating Cost Statement | 2,169 | 2,169 |
| At 31 March | <u>2,169</u> | <u>2,169</u> |

Early departure Costs:

This provision relates to the additional costs of benefits, paid annually between the dates of early departure and normal retirement, to employees who have left the Ministry of Defence early as a result of the Agency's Change Programme.

13: REVALUATION RESERVE

| | 2004/05 | 2003/04 |
|--|---------------------|---------------------|
| | £'000 | £'000 |
| Revaluation reserve at 1 April | <u>6,464</u> | <u>149</u> |
| Revaluation depreciation on fixed assets | (238) | (19) |
| Revaluation in year on fixed assets | 1,415 | 377 |
| Revaluation in year on stocks | (5,454) | 5,971 |
| Transfers | <u>(130)</u> | <u>(1)</u> |
| | (4,407) | 6,328 |
| Realised element transferred to General Fund | (52) | (13) |
| Revaluation reserve at 31 March | <u>2,005</u> | <u>6,464</u> |

The revaluation reserve in respect of stocks arises from the application of Agency policy requiring stocks to be valued at the lower of current replacement cost and net realisable value

14: GENERAL FUND

Reconciliation of net operating costs to changes in the General Fund

| | 2004/05 | 2003/04 |
|--|----------------------|----------------------|
| | £'000 | £'000 |
| Net Voted Expenditure | 22,074 | 28,059 |
| Notional costs | 3,210 | 3,399 |
| Realised element of the revaluation reserve | 52 | 13 |
| Inter management group transfers of fixed assets | (1,126) | (6) |
| Less: | | |
| Net expenditure for the year in respect of the Agency operations | (28,321) | (36,555) |
| Net increase/(decrease) in General Fund | <u>(4,111)</u> | <u>(5,090)</u> |
| General Fund at 1 April | 43,997 | 49,087 |
| General Fund at 31 March | <u>39,886</u> | <u>43,997</u> |

15: RECONCILIATION OF MOVEMENT IN GOVERNMENT FUNDS

| | 2004/05 £'000 | 2003/04 £'000 |
|--------------------------------------|------------------|------------------|
| At 1 April | 50,461 | 49,236 |
| Revaluation Reserve movement in year | (4,459) | 6,315 |
| General Fund movement in year | (4,111) | (5,090) |
| Total movement in year | (8,570) | 1,225 |
| At 31 March | 41,891 | 50,461 |

16: RELATED PARTY TRANSACTIONS

The Medical Supplies Agency is an Executive Agency of the Ministry of Defence.

The Ministry of Defence is regarded as a related party. During the period 1 April 2004 to 31 March 2005, the Medical Supplies Agency has had various material transactions with the Ministry of Defence. It has also had a small number of transactions with the Defence Science and Technology Laboratory Trading Fund for which the Ministry of Defence is also regarded as the parent Department.

In addition, the Agency has had a number of material transactions with two other Government Departments, the Foreign and Commonwealth Office (F&CO) and the Department of Health (DH). This has specifically been with the Falkland Islands Government and the Health Protection Agency, parented by the F&CO and DH respectively.

During the year none of the senior and other key management staff, or other related parties, has undertaken any material transactions with the Medical Supplies Agency.

17: CAPITAL COMMITMENTS AND CONTINGENT LIABILITIES

There are no capital commitments for which no provision has been made in these financial statements.

There are no contingent liabilities.

18: DERIVATIVES AND OTHER 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 largely non-trading nature of its activities and the way in which government Agencies are financed, the Agency 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.

Financial assets and liabilities are generated by day-to-day operational activities and are not held to change the risks facing the Agency in undertaking its activities, or for trading. The fair values of all the Agency's financial assets and liabilities approximate to their book values. In line with FRS 13, short-term debtors and creditors (those which mature or become payable within 12 months from the balance sheet date) have been excluded from these disclosures (except for those relating to currency risk).

Interest rate risk

The Agency has no financial assets and liabilities on which interest is earned or paid, and is therefore not exposed to significant interest rate risk.

Currency risk

The Agency does not hold assets or liabilities denominated in a foreign currency, and income and expenditure denominated in a foreign currency is negligible. The Agency is therefore not exposed to significant currency risk.

The Ministry of Defence, through whose Resource Account the Agency is financed, enters into forward purchase contracts annually with the Bank of England to cover the majority of its foreign exchange requirements for the following year. The details of the outstanding foreign currency contracts are given in its Departmental Resource Account.

Liquidity risk

The Agency is not exposed to significant liquidity risk, as the liquidity requirements are met by financing from the Ministry of Defence Resource Account, and it has no borrowing facilities. The Department's resource requirements are voted annually by Parliament.

19: RECONCILIATION OF NET OPERATING COST TO NET CASH FLOWS

| | 2004/05 £'000 | 2003/04 £'000 |
|--|------------------|------------------|
| Net Expenditure from operating activities | 28,321 | 36,555 |
| Adjustments for non cash transactions | | |
| Depreciation | (583) | (574) |
| Fixed assets and stock written on/(off) | (310) | (5,012) |
| Fixed asset impairments | (202) | (1) |
| Stock provisions | 608 | (7,385) |
| Cost of capital | (1,711) | (1,780) |
| Movements on provisions | - | 1 |
| Notional costs | (1,499) | (1,619) |
| Movements in net current assets: | | |
| Increase/(Decrease) in stocks/work in progress | (3,200) | 10,185 |
| Increase/(Decrease) in debtors | 2,296 | (1,229) |
| (Increase)/Decrease in creditors | 432 | (1,084) |
| Movement in Provisions for Liabilities and Charges | (2,169) | - |
| Net Cash Outflow from operating activities | 21,983 | 28,057 |

20: OBLIGATIONS UNDER OPERATING LEASES

| | 2004/05 £'000 | 2003/04 £'000 |
|--|------------------|------------------|
| Plant, Machinery & Vehicles | | |
| Payments due under leases expiring: | | |
| Within one year | 105 | - |
| Between two and five years | 3 | 15 |
| Over five years | - | 130 |
| | 108 | 145 |

21: INTRA-GOVERNMENT BALANCES

| | Debtors: amounts falling due within one year £'000 | Creditors: amounts falling due within one year £'000 |
|---|--|--|
| Balances with other central government bodies | 489 | 0 |
| Balances with local authorities | 96 | 3 |
| Balances with NHS Trusts | 0 | 0 |
| Balances with public corporations and trading funds | 2,143 | 3,044 |
| Balances with bodies external to government | 243 | 5,786 |
| At 31 March 2005 | 2,971 | 8,833 |
| Balances with other central government bodies | 297 | 1,225 |
| Balances with local authorities | 0 | 1 |
| Balances with NHS Trusts | 0 | 2 |
| Balances with public corporations and trading funds | 12 | 3,420 |
| Balances with bodies external to government | 366 | 4,617 |
| At 31 March 2004 | 675 | 9,265 |

22: POST BALANCE SHEET EVENTS

The Parliamentary Under Secretary of State and the Minister of State for the Armed Forces announced that with effect from 1 April 2005 the Medical Supplies Agency would cease to have Agency status. As a result, the Treasury Direction to produce an annual report and accounts for Parliament will no longer apply, making this the last report to Parliament on the work of the Agency. These accounts have been prepared on a going concern basis, as the functions of the Agency will continue to be in operation for the foreseeable future through its successor, the Medical Supplies Integrated Project Team (Med S IPT) and through a small storage and distribution facility serving its operationally deployable customers within the Defence Storage & Distribution Agency (DSDA). Both the Med S IPT and DSDA will prepare future annual resource accounts as part of the Defence Resource Account.

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