

	PAPER NO: AC.62(12)	
Board/Committee:	Audit Committee	
Date:	30 October 2012	
Paper title:	Internal Controls – Annual review of effectiveness	
Author:	Richard Flatman, Executive Director of Finance	
Executive sponsor:	Richard Flatman, Executive Director of Finance	
Recommendation by the Executive:	The Executive recommends that the annual compliance statement is approved.	
Aspect of the Corporate Plan to which this will help deliver?	<ul style="list-style-type: none"> • Financial sustainability • Creating an environment in which excellence can thrive. 	
Matter previously considered by:	Audit Committee	Annually. Draft for 2011/12 reviewed at September Audit Committee.
Further approval required?	N/A	N/A
Communications – who should be made aware of the decision?	Included in statutory financial statements.	

Executive summary

This paper presents the annual review of effectiveness of the University's system of internal control and underpins the full compliance internal control statement in the annual report and accounts (a copy of which is included as Appendix 1). The statement relates to the period up to the date of approval of the financial statements.

A draft was presented to Committee for consideration at its September meeting. Various changes have been made to the detail within the report (highlighted in red) the most significant of which has been the receipt from HEFCE in October of their annual risk assessment of LSBU – confirming that we are “not at higher risk” at this time. However, nothing has arisen subsequent to review in September which alters the conclusion or our ability to issue a full compliance statement. The Committee, on the recommendation of the Executive, is asked to approve the report and the statement in Appendix 1.

Please refer to section 1 of the report for the summary/justification of the full compliance statement.

London South Bank University

System of Internal Controls

Annual Review of Effectiveness

Year ended 31 July 2012

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1. Executive Summary

This report documents the progress that has been made to our system of internal control and to our risk management processes over the past year. A copy of the proposed statement of full compliance for the year ended 31 July 2012 is enclosed as Appendix 1.

In making this statement, we are required to ensure that a number of key principles of effective risk management have been applied. These principles, together with an assessment of compliance by LSBU, are provided in the table below.

Effective risk management:

Requirement	Assessment
Covers all risks – governance, management, quality, reputation and financial.	✓
Produces a balanced portfolio of risk exposure.	✓
Is based on a clearly articulated policy and approach.	✓
Requires regular monitoring and review, giving rise to action where appropriate.	✓
Needs to be managed by an identified individual and involves the demonstrable commitment of governors, academics and officers.	✓
Is integrated into normal business processes and aligned to the strategic objectives of the organisation.	✓

In making this assessment and a full compliance statement for the period under review (for the year ended 31 July 2012 and up to the date of approval of the financial statements) the following assurance sources have been taken into account:

HEFCE

- LSBU is assessed by HEFCE as being “not at higher risk” at this stage. In making this assessment HEFCE has also concluded that LSBU is meeting the accountability obligations set out in the Financial Memorandum and other HEFCE guidance. This most recent assessment was received on 1 October 2012 and is based upon the accountability returns for 2010/11, including the revised financial forecasts submitted June 2012.

- ~~• As a result of changes in the timetable of reporting to HEFCE (in which the annual financial forecast was submitted in June 2012), LSBU is yet to receive its annual assessment of institutional risk for 2012. The most recent risk assessment, as reported by HEFCE in its letter to LSBU dated September 2011 (and as reported to Audit Committee at its meeting in September 2011) confirms that LSBU is “not at higher risk at this time”. The Executive is not aware of any issues which would currently change that rating~~
- HEFCE also carried out an assurance visit to LSBU on 12 July 2011, which is conducted every 5 years. The overall conclusion from the review was the highest assurance rating possible “*that, at this time we (HEFCE) are able to place reliance on the accountability information.*” No additional recommendations for improvement were included in the report.
- HEFCE have subsequently raised in their final assurance report some issues regarding the data amendments to the HESA fixed database. This is consistent with internal audit findings on data quality and an appropriate plan is in place to address these issues.

Internal audit

- The programme of internal audit work for the year ended 31 July 2012 was aligned to the corporate risk framework to provide assurance on the effectiveness of controls in key risk areas.
- A review of risk management was embedded within internal audit reviews for the year ended 31 July 2012. This was rated “medium risk”. Further detail is provided in section 4 of this report.
- The conclusions from internal audit work are discussed in more detail in section 5 of this report. With three specific exceptions where significant improvements are required, the internal audit opinion is that LSBU has adequate and effective arrangements in place. The volume and risk rating of recommendations made is indicative of an improvement in the overall control environment.

Internal governance

- The Corporate Risk Framework is aligned to the Corporate Plan, reviewed by the Executive on a monthly basis and updated regularly.
- Risk reports have been submitted to every meeting of the Board of Governors and the Audit Committee.
- In addition to risk reports, regular reports have been submitted to Audit committee/Board demonstrating progress on projects/actions related to key corporate risks.

- There has been one major breakdown in controls during the year which led to an erroneous payroll payment of £139k. The money has subsequently been recovered and appropriate disciplinary action taken.
- Regular [anti-fraud](#) updates/reports are provided to each meeting of the Audit Committee. No material issues have arisen in the period under review other than the payroll incident referred to above which was considered to be a typographical error rather than fraud/malicious intent and one which stemmed from the failure to apply agreed controls.
- No significant issues have arisen as a result of the University's external reporting processes.

2. Annual Review Process

To be able to make the statement on internal control set out in Appendix 1, Governors need to satisfy themselves that the risk management system is functioning effectively and in a manner that they have approved.

The two elements of effective monitoring are:

- An ongoing review process (for LSBU this takes the form of regular risk management reports to the Audit Committee and ongoing monitoring reports and consideration of risk issues by the Executive); and
- An annual assessment of the effectiveness of internal controls.

This paper documents the annual assessment undertaken. It considers issues dealt with in reports received during the year, together with any additional information necessary to ensure that Governors take account of all significant aspects of internal control for the year under review and up to the date of approval of the annual accounts.

3. Changes in the nature and extent of significant risks

The corporate risk framework has been subject to monthly review by the Executive and has been updated as appropriate. Significant changes were made in the year to combine risks where appropriate and to align the risk register with the University's new Corporate Plan 2011/14.

~~No new corporate risks were identified in year. OneTwo~~ risks relating to "Major staff strike" [and "control of staff costs"](#) have [yes](#) been downgraded to the local HR/[Finance](#) risk

registers respectively. Otherwise there have been no significant changes to the corporate risk register. Two additional risks were discussed at the detailed review by Governors of the corporate risk register at their recent Board meeting in October. These cover “reputational risk” and “staff disengagement”. Both matters will be considered by the Executive for potential inclusion in the corporate risk framework.

~~The current Corporate Risk summary framework is attached at Appendix 2.~~ The principal risks facing the University relate to student recruitment and the potential future loss of NHS income. These risks are discussed in more detail in the University’s financial statements.

4. Scope and quality of management’s ongoing monitoring of risks and the system of internal control

Risk Management is a standing item on every Executive agenda, and risk management and internal control are embedded into normal operating routines. Both are subject to regular management review and periodic audit review.

Every Corporate Risk has an Executive Risk Owner. Every member of the Executive is the Risk Champion for their area, and this is embedded into formal letters of delegated authority.

Risk management was the subject of a specific review within the internal audit programme for 2011/12 and was rated as “medium risk”. 4 medium risk recommendations were made and there were no critical or high risk findings. This compares favourably with previous risk reviews although there is still scope for further improvement, particularly regarding shared understanding of risk appetite.

5. Results of internal audit work for 2011/12

The University’s Internal Auditors for the period under review were PricewaterhouseCoopers LLP (PwC) and their opinion for 2011/12 is set out in their internal audit annual report.

The PwC opinion for 2011/12 is:

that LSBU has adequate and effective arrangements to address the risk that management’s objectives are not achieved in respect of:

- Risk management, control and governance, and

- Value for money arrangements

except for specific areas as noted below where significant improvements are required:

- Ensuring adequate arrangements are in place for bribery act compliance
- Ensuring that systems and processes are in place to ensure that HESA and HESES data returns are complete and accurate
- Discouraging staff from sharing user access credentials with other employees.

Whilst there were only a small number of outstanding recommendations at year end, there had been some delay in implementation in year and this is an area that we will work closely on in 2012/13.

Whilst specific issues have arisen in year, the [internal auditors have confirmed in their report that the](#) volume and risk rating assigned to recommendations is indicative of an improvement in the overall control environment.

6. Extent and frequency of communication to the Board (and other committees)

Regular reports on risk and control matters have been presented to the Board and its Committees throughout the year as set out below. These are in addition to the detailed papers at this meeting.

Board of Governors	Report	Purpose
3 October 2012	Key performance indicators	To note a progress report from the Vice Chancellor
	Corporate risk	Detailed review of the risk register by the Board
19 July 2012	Key performance indicators	To note a progress report from the Vice Chancellor
	Corporate risk	To note a report from the Executive Director of Finance
	Corporate projects	To note progress on the list of corporate projects from the Vice Chancellor
24 May 2012	Key Performance Indicators	To consider the Vice Chancellor's report and note developments

	Corporate risk	To consider a report from the Executive Director of Finance
	Corporate projects	To note progress on the list of corporate projects from the Vice Chancellor
08 March 2012	Corporate risk	To note and update report from the Executive Director of Finance
	Key performance indicators	To consider the Vice Chancellor's report and note developments
	Corporate projects	To note progress on the list of corporate projects from the Vice Chancellor
24 November 2011	Corporate risk	To note and update report from the Executive Director of Finance
	Key performance indicators	To consider the Vice Chancellor's report and note developments
	HESES/HESA data	To note report from the Pro Vice Chancellor Academic
	Annual report from Audit Committee	To note report from the Chair of Audit Committee
	Report from the Audit Committee on the accounts	To note report from the Chair of Audit Committee
	Annual report and financial statements for year ended 31 July 2011	To approve report from the Executive Director of Finance
	Report from the Policy and Resources Committee on the accounts	To note report from the Chair of Policy and Resources Committee
	External Audit key issues memorandum	To note report from the External Auditors (Grant Thornton)
	HEFCE annual accountability return	To note report from the Executive Director of Finance

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Audit Committee	Report	Purpose
27 September 2012	Internal Audit progress report 2011/12	To note report from internal auditors on audit areas for 2011/12
	Various Internal Audit Reports 2011/12	To note reports on various 2011/12 audit areas (including verbal update on continuous audit for Q4 2011/12)
	Draft annual report of the internal auditors	Consideration of the draft annual internal audit report
	Corporate risk report	To consider the report on corporate risks from the Executive Director of Finance
	Draft annual report on effectiveness of internal controls	To consider the report from the Executive Director of Finance
	HESA improvement project	To review the progress report
20 June 2012	Corporate risk report	To consider the report on corporate risks from the Executive Director of Finance
	Internal Audit progress report 2011/12	To note report from internal auditors on audit areas for 2011/12
	Various Internal Audit Reports 2011/12	To note reports on various 2011/12 audit areas
	Internal Audit plan 2012/13	To review report from internal auditors
	External audit plan for 2011/12	To approve report from external auditors
09 February 2012	Corporate risk report	To consider the report on corporate risks from the Executive Director of Finance
	Various Internal Audit Reports	To note reports on various 2011/12 audit areas
	Internal Audit Key Performance Indicators	To approve report from internal auditors
16 November 2011	Corporate risk report	To consider the report on corporate risks and mitigating actions
	Draft report and accounts for year ended 31 July 2011	To consider the report from the Executive Director of Finance
	Internal audit annual report	To note report from internal auditors

	Annual report on effectiveness of internal controls	To consider the report from the Executive Director of Finance
	Various Internal Audit Reports	To note reports on various 2011/12 audit areas
	Internal audit recommendations	To consider a progress report from the Executive Director of Finance
	Audit Committee Annual Report	To approve the Audit Committee Annual Report
21 September 2011	Corporate risk report	To consider the report on corporate risks and mitigating actions
	Internal Audit Plan 2011/12	To approve report from internal auditors
	Various Internal Audit Reports	To note reports on various 2010/11 audit areas
	External Audit Plan 2010/11	To approve report from external auditors
	HEFCE assurance report	To note a report from HEFCE

Policy and Resources	Report	Purpose
02 July 2012	Key performance indicators update	To consider the corporate plan KPIs progress report
01 May 2012	Key performance indicators update	To consider the corporate plan KPIs progress report
21 February 2012	Key performance indicators update	To consider the corporate plan KPIs progress report
10 November 2011	Key performance indicators update	To consider the corporate plan KPIs progress report
15 September 2011	Key performance indicators update	To consider the corporate plan KPIs progress report

In addition, the Audit Committee has reviewed the following reports before the accounts are signed:

- The financial statements, including the Statement of Internal Control
- final annual report of the internal auditors for the year ended 31 July 2012
- External auditor's Key Issues memorandum (KIM).

~~The Board will conduct a detailed review of the corporate risk register at its meeting in October.~~

7. Incidence of significant control failings or weaknesses during the year

One reportable incident arose relating to an erroneous payment of £139k in the payroll department. This has been the subject of a separate investigation conducted by the internal auditors, a copy of which has been sent to HEFCE. The incident was considered to be a typographical error rather than fraud/malicious intent and one which stemmed from the failure to apply agreed controls. Appropriate action has been taken in response.

8. Effectiveness of the University's external reporting processes

No significant issues have arisen as a result of the University's external reporting processes other than matters already covered within the Corporate Risk framework.

APPENDIX 1

Statement on Internal Control

As the governing body of London South Bank University, we have responsibility for ensuring that there is a process for maintaining a sound system of internal control that supports the achievement of policies, aims and objectives of the University, whilst safeguarding the public and other funds and assets for which we are responsible, in accordance with the responsibilities assigned to the governing body in the Memorandum and Articles of Association and the Financial Memorandum with HEFCE.

The system of internal control is designed to manage rather than eliminate the 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 linked to the achievement of institutional objectives and designed to identify the principal risks to the achievement of policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically. This process has been in place for the year ended 31 July 2012 and up to the date of approval of the financial statements, and accords with HEFCE guidance.

As the governing body, we have responsibility for reviewing the effectiveness of the system of internal control. The following processes have been established:

- We meet a minimum of four times a year to consider the plans and strategic direction of the institution;
- The approach to internal control is risk based, including a regular evaluation of the likelihood and impact of risks becoming a reality;
- The Audit Committee provide oversight of the risk management process and comments on its effectiveness;
- We receive periodic reports from the chair of the Audit Committee concerning internal control and we require regular reports from managers on internal control activities and the steps they are taking to manage risks in their areas of responsibility, including progress reports on key projects;
- The Audit Committee receives regular quarterly reports from management;
- Internal audit is outsourced to an external provider. The Audit Committee receives regular reports from the internal auditor, which include their independent opinion on the adequacy and effectiveness of the institution's system of internal control, governance and risk management processes, together with recommendations for improvement;

- The internal audit programme has been aligned with the University's corporate risk register;
- An organisation-wide register of key corporate risks is maintained, together with individual risk registers for each faculty and department. Review procedures cover business, operational and compliance as well as financial risk;
- The executive team meets regularly to consider risk, assess the current exposure and keep up to date the record of key corporate risks facing the University;
- A network of risk champions exists to support risk management activity in all faculties and departments; Update training is provided as required to support delivery;
- Formal risk management and internal control procedures have been embedded within ongoing operations.

Our review of the effectiveness of the system of internal control is informed by internal audit, which operates to standards defined in the HEFCE Audit Code of Practice and which was last reviewed for effectiveness by the HEFCE Audit Service in July 2011. The internal auditors submit regular reports, which include their independent opinion on the adequacy and effectiveness of the institution's system of internal control, governance and risk management processes, with recommendations for improvement.

Our review of the effectiveness of the system of internal control is also informed by the work of the executive managers within the institution, who have responsibility for the development and maintenance of the internal control framework, and by comments made by the external auditors in their management letter and other reports.