

Current Questions for Higher Education Audit Committees

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Given the challenging environment surrounding the higher education sector at present, the role of the Audit Committee is more important than ever in discharging its responsibilities supporting the governing body. These responsibilities as defined in the financial memorandum lie largely around ensuring adequate and effective risk management, control, and governance arrangements, as well as value for money.

In view of this we have compiled a series of questions around key issues we see facing the sector and ideas on how Audit Committees can best engage with these topics.

How aligned is the audit committee agenda to the University's risks?

Higher education is in a period of substantial change, with universities having to adapt quickly to changes in government policy. As a consequence the nature of the risks faced by universities is also changing quickly.

Risk should be at the centre of the audit committee's agenda, and in such a fast changing environment that means continually being aware of how the risk pattern is changing and getting appropriate assurance that management is responding appropriately to emerging risks.

How effectively does the University's annual report reflect the business risks

The Financial Reporting Review Panel recently (February 2011) issued a press release expressing concern about how UK companies are reporting the principal risks and uncertainties that they face. They raised concerns that disclosures often: do not focus on principal risks; are described too generally not relating to the company's circumstances; are inconsistent with other information in the annual report and do not go on to describe how the risks are managed.

The accounting SORP in higher education also requires universities to report their principal risks within the Operating and Financial Review. In light of the FRRP's comments the Audit Committee may wish to consider how the University's risks are disclosed.

Do you know where your assurance is coming from?

A key challenge for all governors is understanding the ever-changing risk profile of the institution, but also ensuring that the necessary assurances over risk are being obtained. It is therefore important for all Audit Committee members to actively engage in discussions around risk and the completeness in coverage of assurance.

Good practice in the current climate is to develop a risk and assurance map which allows members to view the relative levels of assurance and their source over key risk areas.

Does the audit committee's scope extend to subsidiaries and overseas activities?

Many universities have a network of subsidiary companies, and more and more are developing overseas operations. There have been numerous cases over many years of control, governance and tax issues in subsidiaries and overseas operations in higher education.

Audit committees should understand whether their role extends to gaining assurance over these areas, and if so how it is assured over the governance and control arrangements in place.

Has the audit committee evaluated its own effectiveness?

The recent financial memorandum for higher education reinforced the need for Governing Bodies to assess their own effectiveness. The same principle applies to University committees such as audit committees. Many now do this as part of their annual cycle of work.

To help improve their effectiveness, audit committees may wish to engage with their Governing Bodies and ask 'what are the risks that they would like the audit committee to focus on?'

Are you getting comfort over the University's financial sustainability?

The current financial climate and recent political reforms around HE funding and tuition fees have raised the profile of financial matters on institutional risk registers. As a result of these issues, it is increasingly difficult for institutions to make accurate forecasts, and particularly through the unknown factors around the effects on demand from tuition fee policies.

It is therefore important for Audit Committee members to understand the key drivers underpinning financial forecasts and receive appropriate levels of assurance around the financial sustainability of the HEI.

How reliable is your non-financial information?

The increased marketisation of higher education teaching will mean that student choice is informed by information on quality, such as course contact time and employment rates on completion. The Browne review asserts that “students will need access to high quality information...in order to make the best choices”.

It will be important that universities have the systems and processes to produce such information reliably. Audit committees should ensure that such systems are operating effectively, and is also being positioned appropriately externally.

Do you understand the key judgement areas in the financial statements?

Many universities may come under increased financial pressure over the years to come, placing greater scrutiny on their reported financial position.

It is important that audit committees are able to properly understand the important judgement areas in their financial statements which effect reported financial performance. This will enable them to understand whether approach being adopted is prudent, neutral or aggressive.

Judgemental areas include asset impairments, bad debt provisions, capitalisation decisions, recoverability of research work in progress, balance sheet credits, and deferred revenue judgements.

Do you understand how IFRS will affect the University's published financial position?

Increased volatility in income and expenditure and potential breaching of loan covenants are two potential issues that may arise as a result of the Accounting Standards Board's ("ASB") proposals to change accounting rules.

The ASB is currently consulting on a new three-tier accounting framework. Most universities will need to apply the second tier of accounting (based on IFRS for Small and Medium Entities) supplemented by a Public Benefit Entity Standard.

Some of the proposed accounting changes include carrying fixed assets at cost, and grants received being recognisable only where all conditions of funding have been met.

The ASB proposals require implementation for accounting periods beginning on or after 1 July 2013, and as such 2013/14 would be the first full year of IFRS. Comparatives for 2012/13 and an opening balance sheet as at 1 August 2012 will also need to be restated on an IFRS basis.

Are you at risk of losing senior people following recent pension tax changes?

Changes to the pension tax rules for high earners come into force from 1 April 2011. The changes could result in a large unforeseen personal tax bill payable many years before the pension benefit is received.

The rules affect individuals' personal tax positions, but can have an impact on the retention of senior people in a university if they choose to retire early to avoid the tax liability.

Remuneration committees will need to understand the impact and audit committees will need to understand what risks there may be as a consequence.

Does the University understand its bribery risk?

The Bribery Act is expected to come into force around May/June 2011 at the earliest. One of the most challenging elements of the Act is a new corporate offence of “failure to prevent” bribery by those who perform services on the University's behalf. In response, organisations need to show that they have “Adequate Procedures” in place to prevent corrupt practices. These include understanding where they may be at risk, having appropriate policies embedded across the organisation and properly understanding who they are doing business with.

Sensitive areas in universities include significant contracts, overseas operations (including the recruitment of overseas students), and relationships with donors.

Do you understand how your finance function maybe changing?

PwC recently surveyed finance directors in the higher education sector, asking them how they viewed the contribution of finance function across various important activities both now and in the future.

The clear message from the survey was a need to change where finance functions are spending their time, too much time being spent on compliance and control activities, with greater input needed into providing insight into the operations of their universities.

Audit committees both scrutinise finance functions and rely on them in carrying out their role. They should therefore understand how the finance function may be changing, and supporting them with delivering the benefits of those changes.

We will reflect further on this survey as we conduct our interim controls audit later in the year.

The full survey can be viewed at the PwC Public Sector Research Centre online at <http://www.psrc.pwc.com/>.

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