

London Metropolitan University

An Independent Review into the
circumstances and issues associated with
the clawback of significant funds in 2009

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1. Introduction

This Independent Review was established following the decision by the HEFCE Board in March 2009 to clawback £36.5million from London Metropolitan University (LMU) in respect of over claimed funding for 2005/6-2007/8 and notice of a reduction in funding for 2008/09 capped at £15 million. The situation raised considerable public and parliamentary interest and concern and following discussions between the University Board of Governors and HEFCE the following were proposed as terms of reference:

2. Terms of Reference of the Review

2.1 Purpose

The review will address the core issue of why the control and assurance processes failed to alert the LMU Board to the nature, scale and potential financial implications of non-compliant data returns to HEFCE and HESA over the period 2005/06 to 2007/08. In particular the review will explore in depth 4 key areas of control:

- management reporting on data and responsibility for its compilation into statutory returns;
- internal audit;
- funding Council Audit; and
- external audit; report findings and lessons to be learned by the LMU Board.

2.2 Timescale

The review to report to the Board on 30 September 2009. (Later changed to 18 November 2009)

2.3 Approach

The review to be assisted informed and advised by Sir David Melville who will ensure that the terms of reference have been fully met in the final report. The detailed work to be undertaken by Deloitte.

2.4 Scope

The review will specifically comment on the lessons to be learned in the following areas:

- The arrangements for compliance by both the Board and the Designated Officer with the terms of the Financial Memorandum and the Audit and Accountability Code.
- Internal management reporting arrangements and responsibilities in respect of data compilation analysis and submission of statutory returns
- Board and Committee structure, terms of reference and reporting arrangements and the information flow to the Board and Committees from Management.

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- Risk identification and management and the operation of the University Risk Committee and corresponding Risk monitoring at Governor level
 - Use and effectiveness of internal and external audit
 - Management of the contractual funding relationship with HEFCE

It was agreed in order to ensure independence that I should have authority to clarify and interpret my approach to the terms of reference. This I did as follows in a letter to Sir Alan Langlands, Chief Executive of HEFCE, dated 24 July 2009 and copied to the LMU Board and all LMU staff:

'As I and Deloitte embark upon the independent review of the events and failures which led to the clawback of significant funds from LMU, I felt it would be helpful to indicate to you how I intend to interpret the scope and terms of reference of the review.

I am clear that the purpose of the review is to consider all matters which led to these events and failures including the responsibilities of management, the Board and the audit committee.

In considering key areas of control, I will be reviewing all aspects relevant to data collection and funding; including the operation and integrity of the student record system and the processing of HESES and HESA returns as well as the role of internal, external and HEFCE audit and of the audit committee. It is clear that there are matters relating to the possible mismatch between the University's policies and HEFCE's funding requirements and these along with the operation of the relationship between the University and HEFCE will also be matter for the review and lessons to be learned.

More widely, I wish to make it clear from the outset that my report will be published and that it will if relevant include lessons to be learned for the whole of the HE sector.

I and the team from Deloitte will be conducting interviews with relevant staff, managers and Board members. I would also like to make it clear, by copy of this letter to all LMU staff, that I am open to written submissions from staff and am offering to meet with representatives of the recognised Trades Unions.

Copies of this letter go to Peter Anwyl, Chair of the Board of Governors; Alfred Morris; John McParland; Stephen Marston, BIS and Heather Bygrave, Deloitte.'

- 3.** This report is intended as an overview of the issues which have been identified by the detailed investigations carried out by the team from Deloitte who are reporting separately to the Board. Moreover it goes further in covering wider issues which arose in the course of interviews with present and past Members of the Board of Governors, present and past HEFCE Officers, present and past members of the University Executive and members of staff as well as the recognised Trades Unions. I have also been informed by conversations with Vice-Chancellors of other universities and a large number of written submissions from individual members of staff as well as those from the Trades Unions.

The report will first cover broad issues which underlie the failures at all levels during the relevant period and then go on to consider the specific responsibilities in relation to Government, HEFCE, the LMU Board and its Committees, the Vice-Chancellor and the Executive Group.

4. Overarching and Underlying Issues

It is clear that in terms of the history of universities in England, the level of clawback imposed on LMU is 'off the scale'. To put it into context, at the time it was imposed, at £36.5 million over three years it constituted almost one third of the total clawback from all HEIs since 2001/02. Of this total clawback only £23 million is attributable at least in part to incorrect reporting of non-completions on the part of all other institutions over this seven year period. Whilst there is evidence that the recent increase in the frequency of HEFCE audits has resulted in an increase in the number of HEIs experiencing clawback, none remotely approach the magnitude of that required of LMU.

The central issue at the heart of the LMU clawback is the HEFCE definition of 'funding completion' which requires that a student sits all of his or her examinations at the first opportunity or otherwise completes their assessments for the HEI to receive any funding for that student for the whole of the year in question. Put simply, in counting students in their data returns as eligible for funding LMU were applying a different definition based on successful progression to the next year of study. The discrepancy was huge, with the LMU measure indicating in 2006/7 a 3% non-completion rate whilst the HEFCE definition produced a figure of over 30%.

Throughout the period in question the quality of student data on the LMU system was very poor. There is well documented evidence in a series of audit reports from 2003 through to our own investigations, that the LMU student data system lacks integrity, is not properly documented and requires radical overhaul. It has been drawn to my attention that at the beginning of the period in question LMU were just recovering from serious industrial action which between Spring 2004 and Autumn 2005 had diverted management resources and prevented reform of the student record system. However little progress has been made since then.

A further part of the backdrop is the role of HEFCE in applying and clarifying their funding completion definition throughout the sector and their role in monitoring individual HEIs through audit.

There are however some important underlying issues within LMU relating to the style of management on the part of the Vice-Chancellor and Executive Group. These have come to light with some force in virtually all of the submissions from staff. They point to matters which will need urgently to be addressed by the new Vice-Chancellor when appointed, but also are in my view an important factor in explaining why LMU as a whole failed to deal with the issues in question.

In addition the relationship between the Governors of LMU and HEFCE has been difficult since the issues surrounding the clawback came to light.

- 5.** I am conscious of the considerable time and expense on the part of both the Funding Council and LMU which have gone into the investigation of these issues to date. My objective therefore is to attempt to draw a line under the matter to allow all parties to proceed with their much more important tasks. In order to do this I will attempt to answer two basic questions. These are 'Why did the position in relation to claw back reach such extreme level and where

did the responsibilities for this lie?' As indicated in 3. above I will consider each of the relevant bodies or individuals in turn.

6. Government

I am clear in my conclusion, that there is nothing in the overall supervision structure of the HE system by Government through the relevant Department that has had any responsibility or culpability in these matters. Moreover I do not feel that an extreme case such as this warrants any overall additional legislative measures. Whilst in common with some other post-92 London Universities, as a legal entity LMU is a registered company, I have found no evidence that this has had any impact, whether direct or indirect, on the matters of this report.

7. HEFCE

The involvement of HEFCE with LMU since its creation through merger in 2002 is extensive and detailed. It is fully documented and disclosed on the HEFCE website. The KPMG *'Review of lessons learned from the London Metropolitan University case'* commissioned by HEFCE and published in June 2009 points to the fact that the lack of credibility in student data identified in the audit processes (since 2003) could have triggered earlier detailed action.

I agree with this conclusion. Moreover it appears that despite course completion being a feature in the then audit approach the university was not interrogated on how they were defining funding eligibility. This despite LMU being subject to more audits than most institutions. These issues are being addressed in the current audit cycle, reduced from seven to five years since 2007 and supplemented by follow up audits where data errors are found. Despite the spotlight on completion issues, HEFCE continue to find a disappointingly high rate of error in the estimation and reporting of non-completions; and in 2009 they further compressed the audit cycle to three years, with completion by 2010-11. Hopefully, given the changes to the funding system from 2009/10 this will provide a full insight into the extent of this issue throughout the sector.

There is no doubt that the funding completion rule has been controversial since its introduction as a stratagem to reduce drop-out. There was widespread belief in the sector prior to 2004 that the rule was impractical and not applicable in its literal sense to HEIs with modular degree schemes and in particular to those with a strong widening participation ethos, many of whose students progress through university at an intermittent pace. More importantly it was also anecdotally believed that HEFCE did not apply the rule literally and therefore that there was leeway in the way HEIs might interpret their returns in the light of their own academic regulations on progression. I have found no documentary evidence for the origin of this belief, but it is clear that from 2004 onwards information was circulating in the sector on HEFCE's literal approach to the rule in audits and the Funding Council themselves found it necessary annually to update their guidance on this matter.

Many institutions took various forms of action to respond to this issue, including changes to their academic regulations, but it appears from the results of the current audit cycle that many

have still to come to terms with it. However, I am not aware of any other crucial funding rule which has been so difficult to apply and/or clarify and has had such a wide ranging effect on so many institutions. HEFCE therefore bear some responsibility for this, but this does not detract from the singularity of the responsibility of LMU to which I return below.

As noted above the relationship between HEFCE and the Board of Governors of LMU has soured since these matters came to light and I wish to address this issue here.

Once the extent of the funding clawback became clear in early 2008, a series of meetings took place between officers of HEFCE including the Chief Executive and members of the LMU Board including the Chair. These meetings focussed on the consequences of the £36.5 million clawback and the subsequent reduction in recurrent grant. Key areas for discussion were the timescale for the clawback and LMU's plan for 'recovery' in these difficult circumstances. Without exception, LMU members believed that some kind of arrangement was on the table by which HEFCE would refund a sum equal to or approaching the clawback sum once an LMU recovery plan was submitted and agreed. Equally clear is the view of all HEFCE officials present that although a recovery plan and restructuring support were discussed, no such deal was offered.

Although at the time no formal minutes of the meetings were made or agreed, the new Chief Executive of HEFCE has subsequently clarified to LMU in writing that any application for support for a recovery plan would have to be made through the Strategic Development Fund from which the largest grant to date has been £10 million plus a £10 million loan. Personal notes were kept by an officer on each side which differ widely and were not immediately shared. In addition HEFCE followed up meetings with letters but these did not address clearly the issue under contention.

A further problem in the relationship lies in the BDO report which HEFCE commissioned to investigate the funding and data issues. This report was intended to give an independent assessment, but it was marred by a dispute at its inception by it being carried out by a former lay member of the HEFCE Audit Committee. Whilst LMU accept the conclusions on data and funding issues in the report its independence and some of the commentary are still under dispute. I have interviewed nearly all of those involved in these meetings including the former Chief Executive of HEFCE. I am convinced that all are recalling in good faith but that this is an example of the two teams coming into the same meeting with different premises and leaving having drawn different conclusions on the implications of what was said.

This misunderstanding could have been obviated if HEFCE had produced a note of each meeting's conclusions for agreement immediately afterwards. I am surprised that this was not the practice of the Funding Council at that time, but am assured by the current Chief Executive that this is now standard procedure when such important issues are under discussion. As far as the BDO report is concerned whilst I believe it would have been advisable for HEFCE to use a completely independent individual for this work, it was unfortunate that LMU subsequently chose to threaten legal action over some aspects of the report, thus making more difficult good communications between them and the Funding Council at a crucial time in the process.

8. The Board of Governors

The Board of Governors of the University is ultimately responsible for all matters within the purview of the institution and in particular for matters relating to finance and/or where there is significant risk attached. This responsibility is heightened when such risks might threaten, as in this case, the very financial viability and existence of the University.

Whilst from our investigations it is clear that there was knowledge from as early as 2004 within the Institution that the HEFCE completion rule was not being applied at LMU the evidence that this was brought by management directly to the attention of either the Audit Committee or the Board of Governors is thin. The only specific mention of the funding completion rule was in a presentation to the Board of Governors by the Director of Finance in October 2005. However, this was as a single bullet point in a large presentation on a wide range of funding matters, delivered without particular emphasis and not featuring as part of the subsequent discussion.

It is, however, clear that the overall issue of high drop-out rates in the University and references to poor data returns in HEFCE audits were at an early stage brought to the attention of both the Audit Committee and the Board of Governors. It is, however, unfortunate that the Audit Committee appears to have failed to consider the HESES 03 and HESES 05 Audit Reports and to give proper attention to the detailed conclusions of other HEFCE Reports. Governors universally failed to follow-up these data issues or to draw conclusions that they might lead to significant problems for the University.

The fact that the Board of Governors did not have this information does not however, diminish their level of responsibility. It must be the case that the Board of Governors and the Audit Committee should take their share of corporate responsibility for a failure of this magnitude regardless of the detail of information provided by the Executive. Given what I say below regarding the important role played in this matter by the Vice-Chancellor of LMU the Board of Governors must consider whether the proper mechanisms were in place firstly to ensure a proper flow of information from the Executive and secondly adequately to conduct its role of providing supervision of the Vice-Chancellor.

Vice-Chancellors are often charismatic leaders and the case of LMU is no exception. Whilst it is important that they are allowed to manage, it is incumbent upon Boards of Governors to provide sufficient and effective challenge. In the light of what is now known about the management of LMU during this period as well as the disregard for Funding Council rules I can only conclude that this challenge and supervision by the Board of Governors in general was inadequate.

9. The Vice-Chancellor

It is beyond dispute that the Vice-Chancellor was fully aware of the existence of the HEFCE Funding Completion Rule and its potential consequences from September 2003 or earlier. There is clear evidence in the form of emails from third tier officers responsible for this area, that if HEFCE applied their definition literally 'the result will be disastrous'. Despite these detailed emails being sent to the V-C and most members of the Executive Group providing warnings and seeking guidance there is no evidence or recollection of responses. It also appears from minutes of meetings, that at no point did the V-C initiate discussions on this issue in the weekly Executive Group meetings or raise the issue in his meetings of the Board of Governors or his individual meetings with the Chair of Governors.

He has confirmed that he saw no reason for the University to change its practise since he firmly believed that HEFCE were not applying their funding completion rule in a literal sense and that the LMU approach that funding claims could be made on the basis of progression was valid. It appears that he took it upon himself to make this decision and it is clear that he was not challenged in this by his Executive Group colleagues. In this respect he was out of step with the actions of other V-Cs in the sector as they became aware of this issue in 2004. From all interviews with members of the Executive Group past and present, it appears that the V-C ensured that the Executive Group meetings were not a forum for discussion of such issues. This is a clear failure of senior management in the institution.

It is at this point that it is relevant to put this matter into context with the matters raised in submissions to this review from staff. I have received over 50 such submissions, from a wide range of staff, predominantly academics but also including some from support staff. They universally express their lack of surprise at the events that have unfolded. They attest to problems of student data quality for internal use over many years and provide many detailed examples of the difficulty of removing students from the record whom they know to have left or who never ever appeared. They generally describe a highly centralised and dictatorial Executive led by the Vice-Chancellor, which was incapable of listening to what was going on in the university, discouraged or ignored criticism and made decisions without consultation.

This total lack of collegiality is seen as having a dispiriting and demotivating effect on staff. Many staff who wrote to me expressed their strong support for the fundamental aims of LMU and were proud of its achievements, but they universally felt that their full potential and that of LMU were thwarted by this management style.

It is also worth noting a strongly held view amongst staff and students that student academic potential is not being realised by a *laissez-faire* attitude to problems of non-completion and a failure to provide much needed extra support for the many students admitted with modest educational backgrounds. Other universities with similar intake profiles have tackled these issues with some success, not accepting that such high non-completion rates are 'inevitable'. Rather they take the view that especially for such students it is in their interests and that of the institution to put significant and targeted resources into encouraging and supporting them towards a successful outcome.

The Vice-Chancellor failed to change policy on recording funding completions in any way and this coupled with over one third of students carrying modules forward led to the unique scale of the clawback at LMU.

I am satisfied that the particular management approach and its impact outlined above not only contributed to the original problems of data quality and funding completion but also failed to provide any mechanisms whereby staff could effectively provide corrections to the system. In addition they ensured that information reaching the Board of Governors was selective and failed to raise issues which might prove 'uncomfortable' for the Executive.

10. The Executive Group

As noted above the Executive Group are collectively viewed by staff as being part of the overall dictatorial and centralised management style led by the previous Vice-Chancellor. This is however indiscriminate and may be unfair to particular individuals. There is also much evidence that the prevailing style of management led to a 'silo' approach with little collective discussion. It must however be the case that they share collective and in some cases line management responsibility for the failings in relation to data quality. On the specific matter of funding completion those who received the emails referred to in section 9 above must bear responsibility for not ensuring that the issues when brought to their attention in 2004 were either discussed and addressed in the Executive Group or brought to the attention of the Board of Governors. As the University 'Risk Management Group' they failed to give timely and unequivocal advice to the Board of Governors regarding the risk associated with ignoring the HEFCE definition. Those interviewed indicate that at the time either they were unaware of it or they did not regard it as an important issue.

In addition and in particular:

The University Secretary has a specific responsibility for ensuring matters are brought to the attention of the Board and its committees and since 2006/7 had line management responsibility for the adequacy of student records;

The Director of Finance did not appear to relate the funding completion risk to its financial consequences nor to adequately highlight it as a risk in the 2005 presentation to the Board on funding issues;

The Deputy Vice-Chancellor – Academic, whilst focussing on the academic programme and standards did not relate high rates of module carry-forward to the funding completion issue and take appropriate steps in developing the university regulations to address this problem. In addition he had line management responsibility for student records between 2002/3 and 2005/6

Two previous Deputy Vice Chancellors, now retired had line management responsibility for planning and student numbers for the periods 2002-2005 and 2005-2007 respectively.

11. Conclusions

- In its returns to HEFCE, throughout the period 2005/6 – 2007/8, LMU consistently applied its own definition of funding completion rather than the Funding Council definition
- The unique level of the LMU clawback is attributable to a combination of ignoring the HEFCE definition and a failure to address very high levels of incomplete modules and student drop out
- The Vice-Chancellor and certain members of the Executive Group were fully aware of this from 2003 but no action was taken
- The Vice-Chancellor and the Executive Group failed to include this matter in the Risk Register
- The Vice-Chancellor, University Secretary and members of the Executive Group failed to clearly present this risk to the Board of Governors or to Board Committees
- From 2002 to the present day the LMU student data system has lacked integrity resulting in extensive data quality problems
- There is a need as a matter of urgency to implement the improvements detailed in the Deloitte report
- The Audit Committee and Board of Governors were fully aware of data quality issues and the long completion times and high drop-out rates of LMU students, but did not follow this up
- HEFCE could have followed up on data quality issues when they became apparent, as is their current practice. This may have identified the non-completion issues earlier. In addition a lack of clarity in the early application of their funding completion rule may have contributed to LMU's position but does not explain the extent of the clawback
- The Vice-Chancellor operated a management regime which was over-centralised, lacked collegiality and was incapable of reacting to clear internal and external warnings of risk on these matters. He must take the major responsibility and culpability for the outcome
- In the light of these events and the detailed findings in the Deloitte report, the Board of Governors needs to review its effectiveness and that of its committees and to consider in particular how it might have an improved flow of information from the Executive as well as the means to ensure comprehensive debate and appropriate challenge to the Executive
- The University needs to establish a robust process for compiling, updating and monitoring the risk register with clear responsibility in the Executive as well as in the Audit committee and the Board of Governors. The risk register must cover operational risks as well as risks associated with the strategic plan

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- Despite the fact that these issues were not explicitly brought to their attention, the Board of Governors and its Audit Committee are accountable for a financial failure of this magnitude and must take overall responsibility
 - Executive Group members and the University Secretary share responsibility for not ensuring that the funding completion issue was discussed, either through in some cases their line management responsibilities or for all in Executive Group meetings
 - In order to move forward, it is important for the Board of Governors and HEFCE to draw a line under past disputes and work together for the future good of the university
 - In due course, once a new Vice-Chancellor is in post, the Board of Governors may wish to consider the benefits of new leadership and refreshed membership of the Board and its Audit Committee

12. Acknowledgements

I am grateful to all who have provided me with valuable insights into the issues pertaining to this report and wish to acknowledge the openness and frankness of those past and present members of the Board of Governors, past and present members of the LMU Executive and other senior staff and past and present officers of HEFCE whom I have interviewed. I would also like to thank all of those staff of LMU and the recognised Trades Unions who have made helpful written submissions to the Review. In addition to those mentioned in the Deloitte report, I have interviewed Professor David Eastwood and Sir Alan Langlands, the previous and current Chief Executives of HEFCE respectively and Sir Roderick Floud, the former Vice-Chancellor of LMU. I have also benefited from discussions on current issues relating to funding completion with a number of Vice-Chancellors and Registrars in the HE sector.

13. Publication and Dissemination

It is my intention that this report will be published and widely circulated.

Whilst I have made no specific recommendations for the HE sector, I believe that there are lessons to be learned in relation to the governance and management of HEIs which have wider applicability.

David Melville

November 2009