Report
July **2017/08**

Memorandum of assurance and accountability between HEFCE and institutions

Terms and conditions for payment of HEFCE grants to higher education institutions

The memorandum of assurance and accountability between HEFCE and the institutions we fund sets out the terms and conditions for payment of HEFCE grants. This memorandum should be read in conjunction with the 'funding agreement' for each institution, which gives specific conditions, funds available and educational provision agreed in return for those funds. This document supersedes HEFCE 2016/12.

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HIGHER EDUCATION FUNDING COUNCIL FOR ENGLAND

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Of interest to those responsible for	Finance, Governance
Reference	2017/08
Publication date	July 2017
Enquiries to	MAAenquiries@hefce.ac.uk

Foreword

HEFCE is a non-departmental public body. This means that while our remit is currently set by the Secretary of State for Education, we are not part of any government department. This enables us to act as a broker between universities, colleges and the Government ensuring the appropriate institutional freedom for teaching, research and knowledge exchange.

The Government decides on the total public funding for higher education, and we distribute this funding fairly and transparently, according to agreed principles and criteria.

Under the Further and Higher Education Act 1992, which established HEFCE, the Secretary of State is not entitled to frame his conditions of grant to us by reference to specific institutions, or to particular courses of study or programmes of research, or to the criteria for the selection and appointment of academic staff or for the admission of students. This is designed to safeguard both institutional and academic autonomy, which are widely regarded as key factors in the success of English higher education. We strongly endorse these principles.

Higher education in England is made up of a diverse range of institutions of varying size and complexity. To give expression to the principle of autonomy, every institution is headed by a governing body which is unambiguously and collectively responsible for overseeing the institution's activities, determining its future direction, and fostering an environment in which the institutional mission is achieved and the potential of all students is realised. The governing body ensures compliance with the statutes, ordinances and provisions regulating the institution and its framework of governance. HEFCE funding is provided explicitly to the governing body as the institution's ultimate authority.

In addition to their responsibilities for good governance and financial stewardship, the leadership of institutions takes account of the interests of their students. Higher education is a partnership between students and the university or college that is delivering their courses or programmes of study. Universities and colleges have responsibilities with regard to their students, and take pride in the high quality of education they provide and the wider experience enjoyed by their students. Universities and colleges are also committed to the continuous improvement of learning and teaching, and the vast majority of students have a good relationship with the institution where they study.

As accounting officer, the chief executive of HEFCE has a personal responsibility to safeguard public funds and achieve value for money as set out in HM Treasury guidance, ‘Managing Public Money’. This includes responsibility for the public funds allocated by HEFCE to higher and further education institutions and other bodies for education, research, knowledge exchange and associated purposes.

The approach to accountability described above draws on the expertise and diligence of governors, the effective academic management of institutions and an established relationship of trust between HEFCE and universities and colleges in England which serves higher education extremely well.

HEFCE, in turn, has responsibilities to protect the collective student interest and to secure the wider public interest, particularly in relation to the funding of higher education.

In relation to the collective student interest, HEFCE remains legally responsible for making sure that the quality of learning and teaching is assessed in each university and college across England which it funds. We also assess the quality of research, enabling us to fund research selectively by supporting excellence wherever it is found, and promoting vibrant PhD and post-doctoral communities. HEFCE also has a role in respect of students by providing assurance about the financial sustainability of the universities and colleges where they are studying and the operation of policies that promote student opportunity and success. But a student’s primary relationship remains with his or her institution.

In relation to the wider public interest, HEFCE has a clear regulatory duty to ensure that universities and colleges in receipt of public funds provide value for money and are responsible in their use of these funds. We also ensure that the funding we distribute accurately reflects what is delivered. In addition, we act as the principal regulator for those universities and colleges that are exempt charities, advising the Charity Commission where appropriate. We aim to reduce the accountability burden on institutions by enabling other public bodies, wherever possible, to rely on our systems of oversight and assurance. We in turn seek to take assurance from institutions’ own systems of self-regulation and control.

The principle of institutional autonomy and the system of co-regulation on which it depends therefore relies on clear lines of accountability for the proper stewardship of public funds and on being able to demonstrate to Parliament and the public that, in the exceptional circumstance when something goes wrong, there is a clear mechanism to put it right. The purpose of the memorandum of assurance and accountability is to provide this clarity and assurance by defining the formal relationship between HEFCE, governing bodies and heads of institutions.

Professor Madeleine Atkins

Chief Executive

Higher Education Funding Council for England

Memorandum of assurance and accountability between HEFCE and institutions

Purpose of this document

1. The memorandum of assurance and accountability sets out the formal relationship, in the form of terms and conditions made under section 65 of the Further and Higher Education Act 1992, between HEFCE and the higher education institutions (HEIs) and further education colleges (FECs) that it funds, and their governing bodies and accountable officers. It reflects HEFCE's responsibility to provide annual assurances to Parliament that:

- funds provided to us are being used for the purposes for which they were given
- risk management, control and governance in the higher education (HE) sector are effective
- value for money is being achieved.

2. 'HEI' means the HEI including its **related undertakings**, as defined in Annex F, unless such undertakings are subject to a separate funding agreement directly with HEFCE, have been designated by the Secretary of State as institutions in the further education sector which have their own contract with the Education and Skills Funding Agency, or are schools as defined by section 4 of the Education Act 1996.

3. In addition HEFCE has to take account of the collective interest of students in how it operates. This memorandum of assurance and accountability has, therefore, been designed to address both the collective student interest and the public interest.

4. This memorandum of assurance and accountability is in two parts:

Part 1 sets institutional conditions of grant that apply to HEIs, but with specific conditions that also apply to FECs. Where requirements apply to both HEIs and FECs this is stated as 'HEIs and FECs'. Where the requirements only apply to HEIs, it is stated as 'HEIs'.

Part 2 sets conditions to specific grants that are paid to HEIs and FECs. It is issued each year as the 'funding agreement'.

References to the memorandum of assurance and accountability or the memorandum embrace both part 1 and part 2.

5. For those HEIs that are exempt charities the memorandum of assurance and accountability sets out the requirements for information to enable us to carry out our responsibilities as principal regulator under the terms of the Charities Act 2011. These responsibilities apply to all the funds and assets of HEIs that are exempt charities.

6. The memorandum of assurance and accountability sets out the mandatory requirements placed on HEIs and FECs as conditions of grant.

7. HEIs are bound by the requirements of their charter and statutes (or equivalent) and by the law relating to their charitable status. This document does not supersede those requirements but is intended to complement and reinforce them.

8. This document, including the Audit Code of Practice (Annex A), takes effect from 1 August 2017.

Linkage to Operating Framework and the register of HE providers

9. The memorandum of assurance and accountability applies to HEIs and FECs in receipt of grant funding from HEFCE. This forms part of a suite of accountability arrangements, covering both access to and continued operation in the HE sector, that provide coverage across all higher education providers which have one or more of the following features:

- its courses are validated by a listed body
- it has degree-awarding powers
- it has university or university college title
- its courses have been designated as eligible for access to student finances
- it has been designated as an HEI eligible to receive HEFCE grant funding.

10. These, and details of the register of HE providers, are set out in full in the Operating Framework[1]. This memorandum of assurance and accountability does not apply to alternative providers[2].

Requirements of other bodies

11. It is a condition of HEFCE grant that HEIs and FECs in receipt of HEFCE grant funding subscribe to the Quality Assurance Agency for Higher Education. It is also a condition of HEFCE grant that HEIs subscribe to and provide data or other information requested by the Higher Education Statistics Agency (HESA).

12. Under the Higher Education Act 2004 HEIs are required to subscribe to the Office of the Independent Adjudicator.

13. Non-compliance with regulatory requirements or requirements of other bodies, such as HESA or the Office of the Independent Adjudicator, may lead to a flag in the register of HE providers to alert current and prospective students and others to the non-compliance. Whether the non-compliance leads to a flag will depend on the circumstances and the impact of the non-compliance. There will be dialogue with the institution or institutions concerned to address the issues raised ahead of any decision to include a flag in the register, if that flag relates to compliance with the conditions in this memorandum. We expect the need for this escalated process to be extremely rare. Any such areas of non-compliance may also be taken into account by HEFCE in our assessment of risk, and there may be actions that flow from that assessment, as set out in our support strategy.

14. HEIs and FECs must ensure compliance with European Union state aid law in their own uses of HEFCE funding. In the case of any breach of state aid law we may be required to recover all or some funding, together with interest. HEFCE may also be required to withhold funding or aspects of funding to any institution which is subject to a state aid enquiry or which has an outstanding recovery notice against it.

Our responsibilities

15. HEFCE provides grant funding for the provision of education and the undertaking of research by those universities, institutions conducted by higher education corporations, and

[1] This can be found at www.hefce.ac.uk/reg/of/.
[2] Alternative providers are subject to separate conditions attached to designated courses (www.hefce.ac.uk/whatwedo/reg/desig/).

institutions of higher education designated as eligible to receive HEFCE grant funding (collectively referred to as 'higher education institutions' or 'HEIs') and FECs. HEFCE has lead responsibility for public accountability for HEIs.

16. As such we will endeavour to work with HEIs and others in the higher education sector to the highest standards of openness, integrity and consistency expected of public sector bodies. We recognise that universities, other HE providers and FECs are autonomous bodies and acknowledge that HEIs and FECs accept that they are accountable for the funding they receive. We will not ask for information that we already have, and as far as possible we will rely on data and information that HEIs and FECs have produced to meet their own needs. We will make regulation efficient and effective and seek to ensure that its benefits outweigh the costs to HEIs and FECs, ourselves and other parties.

17. We will respect commercial confidentiality within the constraints of the Freedom of Information Act 2000 and our own obligations to Parliament and under the framework document with our sponsor department.

18. Our grants to HEIs are to fund activities defined by the Further and Higher Education Act 1992. For HEIs these are:

- providing education and undertaking research
- providing facilities and undertaking activities that the HEI's governing body thinks are necessary or desirable for providing education or undertaking research.

19. We will review an HEI's annual accountability returns to us, and give to the accountable officer and governing body a confidential risk assessment. We will not normally make our risk assessments public until three years have elapsed. This period, based on advice from the Information Commissioner, gives an HEI that is designated 'at higher risk' time to reduce its risk classification.

20. We will make our risk assessments available within this three-year period, on an exceptional and confidential basis, to:

- other public funders and other regulators to enable those bodies to make their own assessments of risk, and
- the National Audit Office who may exceptionally need to discuss those assessments at the Public Accounts Committee or disclose them in a published report.

21. We must do this to minimise the risk to public funds distributed by those bodies or other regulatory remits they hold.

22. We will exceptionally make public a risk assessment at any stage if we have strong grounds for believing that it is in the collective student or the public interest to do so. We will only share or publish our risk assessments after having notified the accountable officer and governing body of the HEI concerned. When we assess an HEI to be 'at higher risk', we will engage with it in line with our institutional engagement and support strategy (see Annex B).

23. We define an HEI as 'at higher risk' when in our judgement, on the basis of all available evidence, it:

- faces threats to the sustainability of its operations, either now or in the medium term
- has serious problems relating to value for money, propriety or regularity (that is, whether funds are used for the purpose intended), or

- has materially ineffective risk management, control or corporate governance.

24. More detail on how HEFCE assesses institutional risk is given at Annex B, Table 2.

Responsibilities of universities and colleges to us and to students

25. HEIs are required to supply HEFCE with certain information about their viability and the way they operate, because we have:

- an oversight role for regulation of higher education
- responsibility and lead public accountability for HEIs designated to receive HEFCE grant funding
- a statutory duty to secure that provision is made for assessing the quality of education provided in institutions for whose activities we provide, or are considering providing, financial support
- responsibility to protect the collective student interest and the public interest
- responsibility as principal regulator of those HEIs that are exempt charities
- or any combination of the above.

Regularity and propriety

26. A condition of grant is that HEIs and FECs must use HEFCE funds only for activities that are eligible for funding under the Further and Higher Education Act 1992, as this is the intended purpose for which the funds have been provided by Parliament. When using these grants HEIs and FECs should ensure they apply proper processes that ensure effective accountability.

27. This condition also applies where the HEI passes on part of its HEFCE grant to another legally distinct entity for the provision of facilities or learning and teaching, or for research to be undertaken. In such cases, as set down in Section 65(3A) of the Further and Higher Education Act 1992, the HEI must obtain our consent before passing HEFCE funds to the connected institution. In these circumstances the HEI awarded the funding by HEFCE will be held accountable for those funds; and the HEI should therefore ensure adequate accountability arrangements are in place when it passes on such funding to another entity.

28. Members of HEI governing bodies and accountable officers should comply with the seven principles set out by the Committee on Standards in Public Life.

29. Governing bodies and accountable officers are accountable for their decisions and actions, and must submit themselves to whatever scrutiny is appropriate to their office. They should also be as open as possible about all the decisions and actions that they take that may affect funding provided by HEFCE. HEFCE will write to the new chair of each governing body of an HEI, on appointment, drawing attention to their own and their governing bodies' responsibilities under the memorandum of assurance and accountability.

Governing bodies

30. Members of governing bodies of HEIs have a set of legal responsibilities and other duties. Taken together, the responsibilities of members of a governing body and of the governing body as a whole are considerable, and must be met. The governing body of an HEI is collectively responsible and has ultimate responsibility that cannot be delegated for overseeing the HEI's activities, to determine its future direction, and to foster an environment in which the HEI's mission is achieved. In accordance with the HEI's own statutes and constitution, there should be effective arrangements for providing assurance to the governing body that the HEI:

a. Has a robust and comprehensive system of risk management, control and corporate governance. This should include the prevention and detection of corruption, fraud, bribery and irregularities.

b. Has regular, reliable, timely and adequate information to monitor performance and track the use of public funds.

c. Plans and manages its activities to remain sustainable and financially viable.

d. Informs us of any change in its circumstances which – in the judgement of the accountable officer and in agreement with the governing body – is a material change, including any significant developments that could impact on the mutual interests of the HEI and HEFCE.

e. Uses public funds for proper purposes and seeks to achieve value for money from public funds.

f. Delivers its charitable purpose for the public benefit.

g. Complies with the mandatory requirements relating to audit and financial reporting, set out in our Audit Code of Practice and in our annual accounts direction.

h. Sends us:

    i. The annual accountability returns.

    ii. Other information we may reasonably request to understand the HEI's risk status.

    iii. Any data requested on our behalf by HESA.

    iv. Information needed to enable us to act as principal charity regulator (exempt charities only).

i. Has effective arrangements for the management and quality assurance of data submitted to HESA, the Student Loans Company, HEFCE and other funding or regulatory bodies (HEFCE reserves the right to use and publish its own estimates of data, where we are not satisfied that the HEI or FEC data are fit for purpose. HEFCE also reserves the right not to publish data[3]). Responsibility for the quality of data used for internal decision-making and external reporting, which must be fit for purpose, rests with the HEI or FEC itself. Data submitted for funding and student number control purposes must comply with directions published by HEFCE; if in doubt an HEI or FEC should ask its HEFCE regional consultant to provide an authoritative, written ruling.

j. Has an effective framework – overseen by its senate, academic board or equivalent – to manage the quality of learning and teaching and to maintain academic standards.

k. Considers our assessment of its risk status, engages with us during the risk assessment process, and takes action to manage or mitigate the risks we agree upon.

[3] See the HEFCE website for the processes which we will follow to determine the action we will take in response to concerns about data quality relating to the National Student Survey ('Process for reporting concerns with NSS data' at www.hefce.ac.uk/lt/nss/) and information from the Key Information Set and Destinations of Leavers from Higher Education survey published on Unistats ('Process for handling concerns raised about Unistats data quality' at www.hefce.ac.uk/lt/unikis/).

Governing body members are also trustees

31. Where HEIs are charities, whether registered or exempt, members of their governing bodies are also trustees and have the responsibilities and potential liabilities that go with trustee status. They must apply the HEI's charitable assets for the charitable purposes of the HEI and not put them at undue risk. Members who act prudently, lawfully and in accordance with the governing instrument will not find themselves liable for their actions. However, in exceptional cases HEFCE will use its role as principal regulator to refer an issue to the Charity Commission, which may then investigate and take action against trustees who have not fulfilled their roles. Trustees need to be particularly careful to ensure that the charity has the means to meet its obligations when the HEI is entering into substantial contracts or financial commitments.

Accountable officer

32. The head of an HEI is first and foremost responsible for leadership of the academic affairs and executive management of the HEI. The appointment (or dismissal) of the head of an HEI is governed by employment law, and this is clearly the responsibility of the governing body. HEFCE has no role, rights or responsibilities in relation to the appointment (or dismissal) of the head of an HEI, and has no wish to change this position. We presume that in a case where a head of an HEI does not discharge his or her duties or acts improperly the governing body will take appropriate action.

33. Under this memorandum of assurance and accountability, the governing body is responsible for the use of public funds. To assist and enable it to discharge this responsibility and to provide clear accountability, the governing body will designate a senior officer, normally the head of the HEI, as the 'accountable officer': that is, the officer who reports to HEFCE on behalf of the HEI. On being notified by, or on behalf of, the governing body of a new accountable officer, HEFCE will write to that individual explaining what the responsibilities of an accountable officer involve.

34. The accountable officer is personally responsible to the governing body for ensuring compliance with the terms of this memorandum of assurance and accountability and for providing HEFCE with clear assurances to this effect.

35. The head of an HEI as the accountable officer is also required to report to HEFCE on behalf of the HEI in relation to the requirements set out in paragraph 30. In exceptional circumstances HEFCE may take the view that the accountable officer is failing to meet these responsibilities. Faced with this position HEFCE would be obliged to respond in a fair, reasonable and proportionate way.

36. If, in the judgement of the HEFCE chief executive, there is evidence of serious failure in relation to the oversight and management of public funds, (s)he will raise this as appropriate with the accountable officer concerned, the chair of the governing body or both; provide the relevant evidence; and seek and consider a response. Experience suggests that most difficulties can be resolved through this process.

37. In extremis, and after all due process has been exhausted, the HEFCE chief executive may conclude that the accountable officer is unable or unwilling to meet his or her responsibilities under this memorandum of assurance and accountability. HEFCE may then ask the governing body to appoint someone else to report to HEFCE on behalf of the HEI. In taking this action HEFCE will not seek to influence the employment relationship between the governing body and

the head of the HEI. The governing body is clearly entitled to maintain the head of the HEI in post. However, the governing body would then have to designate another senior officer as the accountable officer, and adjust the roles and responsibilities of the head of the HEI accordingly.

38. The HEI's accountable officer, the chair of the governing body or both may be required to appear before the Public Accounts Committee alongside the chief executive of HEFCE in his or her role as accounting officer, on matters relating to grants to the HEI.

39. In the event of a prolonged absence from work or a sudden departure by the accountable officer, the clerk to the HEI's governing body must ensure that HEFCE is made aware immediately of the identity of the interim accountable officer.

Provision of information to HEFCE

40. Our information requirements are set out in this memorandum of assurance and accountability and in guidance on accountability and other returns. It is a condition of grant that HEIs provide the requested accountability or other information. We keep these information requirements under review to ensure we only ask for the information we need.

41. HEIs also have an obligation to supply information to enable us to fulfil our role as principal regulator of HEIs as exempt charities under the Charities Act 2011. The information required for this is summarised at Annex E, and largely draws on existing returns that HEIs make to HEFCE.

42. HEFCE publishes an annual accounts direction, and HEIs and their external auditors must comply with it. The accounts direction states HEFCE's financial reporting requirements.

Provision of information for students

43. It is a condition of funding that institutions supply data requested by HEFCE or its agents to allow for provision of information to prospective and current students. For example institutions must provide Key Information Set data annually according to the published specification and timetable[4].

Quality of provision

44. HEFCE has a statutory duty to 'secure that provision is made for assessing the quality of education provided in HEIs and FECs for whose activities they provide, or are considering providing, financial support'[5]. In exercising this duty and in considering quality in the exercise of our other functions, we aim to ensure that students receive higher education provision of sufficient quality and that England's reputation for high-quality higher education is maintained.

45. We have published a 'Revised operating model for quality assessment (HEFCE 2016/03). This sets out the arrangements that will apply to all HEFCE-funded providers from 2017-18 and the transition arrangements during 2016-17. If an HEI or FEC does not meet the quality assessment requirements it will be expected to make any necessary improvements through the implementation of an agreed action plan. HEFCE will arrange regular meetings with the HEI or FEC to ensure that it provides HE of sufficient quality and is responsible in its use of public funds.

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[4] We are revising the Key Information Set data collection and the Unistats website, which may be renamed in 2017. This condition applies to the information institutions will be asked to provide for publication on the successor to the Unistats website.

[5] Further and Higher Education Act 1992, part II, section 70 www.legislation.gov.uk/ukpga/1992/13/section/70#commentary-c1106607.

Improvements will be expected and, in exceptional circumstances, sanctions may be applied. Our ultimate sanction is the withdrawal of some or all HEFCE funding.

Research integrity

46. Compliance with the concordat to support research integrity[6] is a condition of HEFCE grant for all HEIs eligible to receive our research funding. Each HEI is required to confirm in its annual assurance return that it complies with the concordat, particularly in relation to its recommendations for internal processes and guidance, and for staff training.

Sustainability of universities and colleges

47. HEIs should have a financial strategy that reflects their overall strategic plan, sets appropriate benchmarks and performance indicators, shows how resources are to be used, and how activities and infrastructure will be financed. This should include how the HEI assesses and reviews its own sustainability, including the use of sustainability assessments.

48. To remain sustainable and financially viable HEIs should also assess, take and manage risks in a balanced way that does not overly constrain freedom of action in the future.

49. We normally expect that an HEI will make a surplus in line with its financial strategy for sustainability, and thus that its unrestricted reserves will grow over time, all other things being equal. A series of deficits, even if covered by unrestricted reserves, might cause us concern, as could low levels of liquidity or increased financial commitments. In such cases we would expect to discuss financial performance and strategy with the HEI, to understand how sustainability is assessed and to be maintained and then, if appropriate, agree an action plan. We would expect financial strategies to include how the HEI intends to address pension scheme deficits, including participation in multi-employer pension scheme recovery plans.

50. HEIs must apply the following principles when entering into any financial commitments:

a. The risks and affordability of any new on- and off-balance sheet financial commitments must be properly considered.

b. Financial commitments must be consistent with the HEI's strategic plan, financial strategy and treasury management policy.

c. The source of any repayment of a financial commitment must be clearly identified and agreed by the governing body at the point of entering that commitment.

d. Planned financial commitments must represent value for money.

e. The risk of triggering immediate default through failure to meet a condition of a financial commitment should be monitored and actively managed.

51. The primary responsibility for assessing the affordability of, and risks around, financial commitments rests with HEIs' governing bodies. HEFCE's role is to assess whether any financial commitments entered into by an HEI present challenges to the HEI's sustainability that could impact adversely on the past and continuing public investment in an HEI, become a call on public funds, or adversely affect the collective student interest. An institution must get written permission from us before it agrees to any new financial commitments where its total financial

[6] See www.hefce.ac.uk/rsrch/integrity/.

commitments would increase to above six times its average adjusted net operating cash flow (ANOC) calculated from its latest July financial forecasts.

52. Annex C sets out how the ANOC-based financial commitments threshold is calculated, as well as the information we need to assess requests to increase financial commitments above the threshold. When we designate an institution as ‘at higher risk’ any increase in its financial commitments (regardless of the threshold) will require written permission in advance.

53. The threshold is not a limit, and should not deter an institution from increasing its financial commitments where appropriate. An institution should determine the level of its financial commitments that are both affordable and consistent with its financial strategy. In any case presented to us we ask the institution to demonstrate this, to show that the proposal represents good value, and to confirm the approval of its governing body. In responding to requests for consent we aim to be helpful and pragmatic, taking into account the circumstances of each proposal.

54. As part of ensuring its long-term viability, an HEI should know the full cost of its activities and use this information in making decisions. If it does not seek to recover the full cost, this should be the result of a clear policy set by the governing body and included in the financial strategy, and should not put the HEI in financial difficulty. We do not expect public funds to subsidise non-public activities.

55. The Financial Sustainability Strategy Group is overseeing the development of annual sustainability assurance reports (ASSUR). The Committee of University Chairs’ Higher Education Code of Governance mentions the ASSUR as an option available to the governing body to assure itself around institutional sustainability.

56. HEIs should manage their estate in a sustainable way, in line with an estates strategy and the requirements of HEFCE’s Capital Investment Framework. HEIs are required to have carbon management plans in accordance with guidance in HEFCE 2010/02[7], and performance against these plans is a factor in determining future capital allocations.

Material adverse events

57. The HEI’s accountable officer must report any material adverse change without delay – such as a significant and immediate threat to the HEI’s financial position, significant fraud[8], or impropriety or major accounting breakdown – to all of the following:

- the chair of the HEI’s audit committee
- the chair of the HEI’s governing body
- the HEI’s head of internal audit
- the external auditor
- the HEFCE chief executive.

Other significant events

58. The HEI’s accountable officer must also inform HEFCE about major changes in strategy, plans for major restructuring or merger with another institution or organisation.

[7] See www.hefce.ac.uk/pubs/year/2010/201002/.
[8] Defined as fraud of £25,000 or higher.

59. The governing body must inform HEFCE's assurance service without delay of the removal or resignation of the external or internal auditors before the end of the term of their appointment.

Equality and diversity

60. The Equality Act 2010 makes unlawful discrimination on the grounds of age, disability, gender reassignment, marriage or civil partnership, pregnancy or maternity, race, religion or belief, sex or sexual orientation. It introduced a public sector equality duty requiring HEIs and HEFCE to show due regard to the need to eliminate discrimination, advance equality of opportunity and foster good relations between protected groups.

61. This law applies to employment; education; the provision of goods, facilities and services; the management of premises; and the exercise of public functions. For the HE sector, the legislation applies to both staff and students, before, and during the relationship with the HEI, and for any dealings arising out of a past relationship.

62. HEFCE's Equality and Diversity Statement and Objectives (www.hefce.ac.uk/pubs/year/2016/201605/) set out the actions taken to meet the equality duty as a provider of public funds. Every HEI should, as a minimum, comply with the Equality Act's requirements, and HEFCE will monitor HEIs' progress with regard to equality and diversity.

Contributing to meeting policy objectives

63. We expect HEIs to consider how their actions affect our policy objectives for the higher education sector, as set out in our business plan[9].

64. All HEIs and FECs that are in receipt of HEFCE Student Opportunity funding from 2014-15 are required to provide a submission to HEFCE. For further details see www.hefce.ac.uk/sas/funding/.

Other requirements

65. HEIs are required to subscribe to Jisc's core network package from August 2017 to July 2018.

66. HEIs and FECs must ensure that their use of JANET and SuperJANET networks conform to acceptable practice and current legislation.

67. There is an Exchequer interest that has built up over time in HEIs in receipt of HEFCE capital funding. These HEIs entered into an agreement with HEFCE effective from 1 August 2006. These institutions and any others that have received capital funding since then are required to follow the conditions set at Annex D.

Payment of grant

68. Each year we determine how much money to allocate to each HEI or FEC. HEIs and FECs should use this money only for the purposes we are empowered to fund, as defined in the Further and Higher Education Act 1992 or other relevant legislation.

69. We may withhold or require an HEI or FEC to repay part or all of a grant if it does not comply with the conditions we attach to the grant or if it has been incorrectly over-funded. In cases where we require repayment we may charge interest, at 2 per cent above the Bank of England base rate, for the period before the HEI or FEC repays the funding to us.

[9] See www.hefce.ac.uk/about/plan/.

Institutional engagement, support and safeguarding actions

70. As a public sector funding body HEFCE must be confident that the bodies it funds have adequate and effective risk management, control and governance arrangements to protect the investment of public funding; and arrangements for delivering value for money (VFM) from public funds.

71. HEFCE's accountability framework has three main strands designed to give HEFCE the necessary confidence while minimising burden on the sector. The strands are:

- annual accountability returns
- HEFCE Assurance Reviews
- data assurance.

72. As far as possible the accountability process between HEFCE and HEIs is concentrated into an exchange of documents and dialogue during a specific period following the end of the financial year. We will confirm the specific content of this exchange each year and consult the sector on any major changes to the process. Our aim is to minimise our demands on HEIs, and as far as possible to rely on data and information that they have produced to meet their own needs.

Annual accountability returns

73. HEFCE takes assurance from a suite of accountability returns, including audited financial statements, financial forecasts and independent audit reports, which must be submitted to HEFCE by a specified date or dates. They provide HEFCE with a view of each HEI's risk management, control and governance, financial sustainability, arrangements for promoting VFM and managing and quality assuring data. By using information and assurances, much of which is needed for internal management and assurance purposes by the HEI, HEFCE is able to minimise its audit requirements and reduce burden. See paragraphs 78 to 80 on institutional engagement and support.

74. The annual accountability returns are analysed by HEFCE, which then carries out a risk assessment of each HEI. The risk assessment is reported to the governing body and accountable officer – see Table 2 of Annex B. For those we consider to be 'not at higher risk' (our experience to date suggests that this is the vast majority) there will be no need for further information or discussion of accountability until the following year's return, except in the case of an unanticipated change in circumstances. Sometimes we ask for more information to clarify uncertainties.

HEFCE Assurance Review

75. The HEFCE Assurance Review is a short site visit to HEIs to ensure that there are suitable accountability processes within each HEI to assure the validity of its annual accountability returns. This helps us validate the systems of self-regulation on which we rely.

Data assurance

76. HEIs and FECs are required to supply HEFCE with data to inform allocations of funding and for other purposes. The responsibility for the quality and accuracy of that data rests with the HEI or FEC. HEFCE relies on the institution's own data assurance processes where possible.

77. HEFCE monitors the reasonableness of data and undertakes verification, validation and reconciliation work between HESA data and other datasets. HEFCE may undertake audits at an HEI or FEC if it deems this necessary. Data audits will assess the strength of institutional systems and controls as well as assessing the accuracy of the data submissions.

Institutional engagement and support

78. When we assess an HEI as being 'at higher risk' we must respond appropriately, to protect the public and the collective student interest. Our institutional engagement and support strategy (see Annex B) describes the range of ways in which we might respond to help HEIs resolve difficulties and manage risks. We will always discuss our concerns with the HEI's accountable officer, and take his or her views and actions into account, before we formally make an 'at higher risk' designation. We will also try to reach agreement on what needs to be done. When we consider the HEI to be no longer at higher risk, we will write to its accountable officer and its governing body to confirm this.

79. Beyond the exchange of accountability information each year, we welcome the opportunity for regular and informal discussions with HEIs about their plans and developments. We believe this will help us to work together and reduce the risk of misunderstanding.

80. In response to requests from HEIs our annual risk letters also provide high level feedback to governing bodies on a number of quantitative measures and highlight any issues that we wish to bring to the HEI's attention but do not regard as sufficiently serious to warrant 'at higher risk' status.

Safeguarding actions

81. Our institutional engagement and support strategy, and risk assessment process, has been described in paragraphs 78 to 80 and is set out in detail at Annex B.

82. If an HEI fails to take any agreed action HEFCE will seek explanations and, if appropriate and justified, issue warnings to improve.

83. If the HEI still fails to address the risks and issues then the HEI will be informed that one or more of the safeguarding actions will be applied. This is very much a last resort and an action that we would not expect to take often.

84. The two safeguarding actions at HEFCE's disposal, which could be deployed if other routes to secure compliance are not successful, are:

a. **Financial** – through the recovery of grant funding or the denial of access to future grant funding, including access to specific grants or to discretionary funding, such as the Catalyst Fund. Ultimately HEFCE can withdraw funding entirely, should circumstances warrant such action.

b. **Informational** – through making public our concerns about an HEI where there are strong grounds to do so and where this is in the public or collective student interest (both current and prospective students, and past students where relevant). This could include an entry in the HEFCE register of HE providers.

85. In addition HEFCE may:

- provide advice to OFFA where there are issues around access

- provide advice to the Charity Commission where an HEI may have breached its charitable obligations
- provide advice to the Equality and Human Rights Commission where discrimination may have occurred.

86. The Agreement on institutional designation (updated in HEFCE Circular letter 03/2017, available online at www.hefce.ac.uk/pubs/year/2017/CL,032017/) has been developed with Universities UK, GuildHE and the Association of Colleges to ensure that accountability for public funds continues to be effective following the Government's reforms of the funding of higher education. The Agreement is effective until the new regulatory framework designed by the Office for Students is fully implemented. Any actions that HEFCE might take under that Agreement may also lead to actions under this memorandum.

Revision to memorandum of assurance and accountability

87. We will make material revisions to this document only after consulting the higher education sector or its representative bodies, as appropriate.

Annex A: Audit Code of Practice

Overview

1. In this Audit Code of Practice (the Code) the word ‘must’ denotes a mandatory requirement under the memorandum of assurance and accountability, whereas ‘should’ denotes our view of good practice.

2. The Code sets out what we require higher education institutions (HEIs) to have in place to provide themselves and us with adequate assurance on good governance, internal controls, the management of risk and achieving value for money (VFM). How these requirements are met is for HEIs to decide themselves.

Governing bodies of HEIs

3. The responsibilities of governing bodies are set out at paragraph 30 of the memorandum of assurance and accountability. Governing bodies are also responsible for the appointment and removal of external and internal auditors. Governing bodies are also responsible for appointing outsourced internal audit providers, on the advice of the Audit Committee, and for choosing to move between outsourced and insourced internal audit provision, also after taking advice from the Audit Committee. Staff appointments and terminations for insourced internal audit staff are a matter for management, with the Audit Committee advising on the appointment and termination of the Head of Internal Audit.

Audit committees in HEIs

4. Each HEI must have an audit committee which follows best practice in HE corporate governance. The audit committee is responsible for assuring the governing body about the adequacy and effectiveness of:

- risk management, control and governance
- VFM
- the management and quality assurance of data.

5. The Committee of University Chairs has published detailed guidance about audit committees (HEFCE 2008/06). This reflects best governance practice, and HEFCE expects HEIs to take account of such guidance in meeting the required standards (see paragraph 12 below) or explain why the guidance is not being applied and good practice is not being followed.

6. An audit committee can undertake whatever work[10] it considers necessary to fulfil its role. This should include assuring themselves about the effectiveness of their internal audit function and their external auditors. Audit committees will only be able to provide the necessary assurances if they are supported by suitably resourced internal audit and external audit functions, operating to recognised professional standards. They should also consider evidence based assurances from management.

7. Members of the audit committee must not have executive authority. Audit committees should include a minimum of three lay members of the governing body. Audit committee members should not be members of an HEI’s finance committee or its equivalent. This is

[10] As described in HEFCE 2008/06.

because it would create a potential conflict of interest when the audit committee is considering issues involving the finance committee. If an HEI's governing body determines that cross-representation involving one member is essential, this should be the subject of an explicit, recorded resolution, which sets out the rationale for such a decision – but it should not be an option for the chair of either committee or the chair of the governing body.

8. The committee must produce an annual report for the governing body and the accountable officer. The report must cover the financial year and include any significant issues up to the date of signing the report and its consideration of the financial statements for the year. The report must be presented to and reviewed by the governing body before the audited financial statements are signed.

9. The report must include the committee's opinion on the adequacy and effectiveness of the HEI's arrangements for:

- risk management, control and governance
- economy, efficiency and effectiveness (VFM)
- management and quality assurance of data submitted to the Higher Education Statistics Agency, the Student Loans Company, HEFCE and other bodies.

10. The final annual report to the governing body and the accountable officer must be shared with HEFCE each year.

Internal audit arrangements in HEIs

11. Internal audit is a vital element in good corporate governance since it provides governing bodies, audit committees and accountable officers with independent assurance about the adequacy and effectiveness of risk management, control and governance, and VFM.

12. Consequently each HEI must have a suitably resourced internal audit function which must comply with the professional standards of the Chartered Institute of Internal Auditors. Internal audit terms of reference must make clear that its scope encompasses all the HEI's activities, the whole of its risk management, control and governance, and any aspect of VFM delivery.

13. The internal audit service must produce an annual report which must relate to the financial year and include any significant issues, up to the date of preparing the report, which affect the opinions. It must be addressed to the governing body and the accountable officer and must be considered by the audit committee.

14. The report must include the internal auditor's opinions on the adequacy and effectiveness of the HEI's arrangements for:

- risk management, control and governance
- economy, efficiency and effectiveness (VFM).

15. The final annual report to the governing body must be shared with HEFCE each year.

16. The head of internal audit must have direct access to the HEI's accountable officer, the chair of the audit committee and, if necessary, the chair of the governing body.

17. Where internal audit is provided from an outside source, market testing should be undertaken at least every five years.

External audit arrangements in HEIs

18. External audit must provide an opinion to the governing body on whether funds (including public funds) have been applied for the intended purposes and on whether the financial statements provide a true and fair view of the financial results for the year. External audit must also form a view about whether an HEI is a going concern. External auditors of HEIs do not have a duty of care to HEFCE.

19. HEIs may ask external auditors to provide additional services. The audit committee must agree all significant matters with a bearing on the auditor's objectivity and independence. Additional work must not impair the independence of the external audit opinion.

20. HEIs must disclose separately, by way of a note to the financial statements, the fees paid to their external auditors for other services.

21. External auditors must issue a report (or reports, if more than one, covering different stages of the annual audit) to those charged with governance which records accounting issues and control deficiencies arising from the audit. HEFCE would expect any issues around the use of charitable assets for non-charitable purposes to be highlighted in such reports. The HEI's management must provide written responses to any recommendations made or issues raised. The report(s), including management response, is one of the annual accountability returns which must be submitted to HEFCE.

22. The report(s), with management responses, must be made available to the HEI's audit committee in time to inform the committee's annual report.

Audit report

23. The external auditors must report whether in all material respects:

a. The financial statements give a true and fair view of the state of the HEI's affairs, and of its income and expenditure, gains and losses, changes in reserves and cash flows for the year. They should take into account relevant statutory and other mandatory disclosure and accounting requirements, and HEFCE requirements.

b. The financial statements have been properly prepared in accordance with UK general accepted accounting principles and the 'Statement of recommended practice: Accounting for further and higher education', and relevant legislation.

c. Funds from whatever source administered by the HEI for specific purposes have been properly applied to those purposes and managed in accordance with relevant legislation.

d. Funds provided by HEFCE have been applied in accordance with the memorandum of assurance and accountability and any other terms and conditions attached to them.

e. The requirements of HEFCE's accounts direction have been met.

24. Auditors should have regard to the specific requirements of the memorandum of assurance and accountability such as compliance with those relating to increases in financial commitments thresholds, or other issues of non-compliance, in their management letters or reports, as set out in paragraph 21 above.

25. Market testing should be undertaken at least every seven years. One named individual partner in the firm is normally responsible for the HEI’s audit; he or she should not hold this position for more than ten consecutive years.

HEFCE access to auditors

26. HEFCE may wish to communicate with an HEI’s external or internal auditors, particularly in connection with a HEFCE Assurance Review and should have unrestricted access to do so. This will normally be arranged through the HEI’s accountable officer or representative. HEFCE will exchange letters where necessary with both parties to deal with confidentiality and the terms under which access is given.

Provision of audit services

27. Internal and external audit services must not be provided by the same firm or provider.

Auditors’ access to information

28. Internal and external auditors must have unrestricted access to information – including all records, assets, personnel and premises – and be authorised to obtain whatever information and explanations the head of internal audit service or the external auditor considers necessary.

Restriction on auditors’ liability

29. Where the internal audit service is provided through a contractual arrangement with an external provider, the provider may ask the HEI to agree to a restriction in the internal auditors’ liability arising from any default by the auditors. Normally such liability should be without limit. However, HEIs may negotiate a restriction in liability so long as the decision is made on an informed basis and the liability remains at such a level as to provide reasonable recourse for the HEI. The governing body, through the audit committee, must be specifically notified of any request for a liability restriction.

30. HEIs must not agree to any restriction in external auditors’ liability in respect of the external audit of their annual financial statements.

31. For other types of work performed by the external auditors, the provider may ask the HEI to agree to a restriction in the auditors’ liability arising from any default by the auditors. However, as with internal audit services, HEIs may negotiate a restriction in liability if the decision is made on an informed basis and the liability remains at such a level as to provide reasonable recourse to the HEI. The governing body, through the audit committee, should be notified of any liability restriction agreed.

Appointment, removal or resignation of internal and external auditors

32. Governing bodies are responsible for the appointment and removal of external and internal auditors. Where auditors cease to hold office for any reason, they should provide the governing body with either a statement of any circumstances connected with their removal which they consider should be brought to the governing body’s attention, or a statement that there are no such circumstances. Any such statements must also be sent to HEFCE by the accountable officer.

Annex B: Institutional engagement, support and safeguarding actions

Introduction

1. This annex sets out how we will engage with and support higher education institutions (HEIs) on matters relating to accountability and risk assessment. It also describes what will happen when, as a result of our assessment, we find there to be significant risks either to the organisation itself or to the collective student or public interest that HEFCE is charged to protect. Our risk assessment methodology is summarised in Table 2. The strategy applies to our work both as funder of higher education and as principal regulator on behalf of the Charity Commission.

2. The principles underlying our institutional engagement and support strategy are that we will:

- respect the independence of HEIs
- protect the collective interests of students, the public and the taxpayer
- maintain an open dialogue on matters of mutual interest
- seek to intervene only when necessary but we will do so vigorously, using the full extent of our powers, when we judge that an institution's management and governors are not effectively addressing risks to public funds and the collective interests of students
- be open with the HEI in our risk assessment and requirements and, if warranted, on student or public interest grounds, disclose our risk assessments publicly
- ensure our involvement is proportionate to the risks
- end our enhanced involvement as soon as possible.

3. In broad terms there are three levels at which HEFCE may engage with institutions:

- normal contact
- focused dialogue (in cases where we are supporting an institution's change or development or where we perceive there to be medium-term risks which, if not addressed, will put the institution at higher risk)
- support strategy (for institutions at higher risk or institutions which in HEFCE's view will be at higher risk if decisive action is not taken).

Each of these is dealt with in detail below.

Normal contact

4. As part of our routine engagement with institutions we will want to understand their mission, strategy and operational plans. This will help us to make appropriate responses to the needs of the institution and the higher education sector, and to gain assurance about matters that affect the delivery of our own objectives. There will often be a formal visit by the HEFCE institutional team to the institution in each year, sometimes in addition to more frequent and less formal exchange of information and views. It is also part of our normal contact to discuss an institution's accountability returns and give feedback, as part of the annual accountability returns exercise.

Focused dialogue

5. There are occasions when it is to the advantage of both HEFCE and institutions to explore issues in more detail. For example, an institution may wish to secure our support for particular plans, and we will want to understand how best to provide help to meet its development needs and fit with our wider objectives for the sector. Likewise, we may wish to discuss with an institution whether there are opportunities to improve its performance or work collaboratively with others. There will also be cases where an institution's risks are increasing because of strategic reasons, for instance, changes in student demand or increased competition, its performance or its internal control arrangements.; At such times HEFCE will seek to engage to try and ensure that the risks are appropriately addressed.

Support strategy

6. We have a risk assessment system covering all institutions. This draws on the information we routinely collect through the annual accountability returns exercise and on other information such as research and teaching quality assessments. Sometimes we will ask for more information to clarify our understanding. There are currently two risk categories: 'not at higher risk' (the vast majority of HEIs at any time) and 'at higher risk' (for a small number of institutions).

7. Through these annual returns or other contacts with an institution, there may be issues that require further discussion. All institutions face business and operating risks. The issue is therefore about managing risk, putting in place systems to identify, mitigate and report on risk. In many cases, as a result of further discussions, we will conclude quickly that there is no need for any further action.

8. When we have major concerns we need to intervene to protect the collective student interest and the wider public interest. We will firstly discuss these issues with senior management, specifically the accountable officer. We will seek a common understanding of the issues, clarify what actions have already been taken or are planned, and if necessary then agree an appropriate support strategy. Table 1 sets out the range of possible actions, though sometimes we will agree a different approach with an HEI.

9. The HEFCE associate director responsible for dealings with the HEI will lead our support activity, but a relevant senior manager – the HEFCE regional consultant or assurance consultant – will manage the day-to-day engagement. In exceptional cases, our chief executive will become involved. The process will be overseen by our audit committee and individual cases reported to the HEFCE Board. The role of the HEFCE audit committee is to advise on process, whereas the role of the HEFCE Board is, where required, to form a judgement.

10. If an institution does not address its problems to our satisfaction, it might be in the interest of current and prospective students and the public for us to disclose our risk assessment (see paragraph 84 of the main text), particularly if this relates to the institution's ability to meet our quality assessment requirements. We expect this to be a rare occurrence, because in our experience institutions generally do take appropriate action.

Table 1: HEFCE support strategy for HEIs 'at higher risk'

Possible HEFCE actions
Overall
We may require institutions to make changes as conditions of grant if we feel that risks to our

funding and the interests of students and the public are not being addressed. We will only do so after due consideration and consultation, and only on the basis of appropriate advice. Thus it will always be our intention to make only reasonable demands of institutions. The actions that we might take are escalatory, and we will not escalate our actions until we have exhausted prior stages in the engagement and support strategy. However, there may be circumstances where it is necessary to take action more urgently. If institutions do not comply with conditions of grant, then after we have exhausted the elements of the support arrangements, we will consider withdrawing grant in part or in full and making public our risk assessment. We see this as a last resort. In addition to the actions below we will consider any other action that we believe is necessary to support institutions at risk and protect the interests of the public, the taxpayer and the collective interest of students.
At governor and senior manager level we:
a. Will engage with senior management, including the accountable officer. b. Will assess the institution's compliance with the memorandum of assurance and accountability, including the requirement to have effective management and quality assurance arrangements over data supplied to the Higher Education Statistics Agency, the Student Loans Company, HEFCE and other funding bodies. c. Will inform the governing body of any change in risk assessment and seek commitments to improvement. We will notify other public funders, as appropriate, of any 'at higher risk' assessment, and exceptionally we will make such an assessment public at any time where we consider it to be the collective interest of students or the public to do so. d. Will engage directly with the chair of the governing body, the chair of the audit committee or both. e. Will engage with the whole governing body and, if necessary, take steps to ensure improvements are made to governance arrangements. f. May require observer status at governing body or audit committee meetings to enable us to assess whether our specific concerns are properly understood and are being addressed. This could be for individual meetings or over a period of time. Our observer will always be a senior HEFCE officer. g. May request the appointment of interim managers, where we consider the institution has insufficient capacity to address its risks properly.
Regarding information and audit we may:
a. Require or commission additional information, reports and data relating to the risks. b. Require that information and reports be audited. c. Request changes to internal or external audit arrangements. d. Undertake or commission audit investigations.
Regarding planning and strategy we may:

a.	Require or commission a recovery or action plan.
b.	Discuss possible changes to strategic plans and market positioning.
c.	Explore collaborative opportunities with other institutions.
Regarding funding we may:	
a.	Re-profile grant to assist an institution that has a cash flow difficulty.
b.	Consider the use or withdrawal of special funding.
c.	Attach special conditions to grant.
d.	Reduce or withdraw funding.
e.	Use our own estimates of data where we are not satisfied that information from the institution can be relied on.
As risks decline we will:	
a.	Inform the institution (and others who may have been notified of our risk assessment) about changes in our risk assessment.
b.	Remove special conditions of grant and other requirements.

Table 2: HEFCE institutional risk system

Introduction
HEFCE's management of risk obliges it to assess the risk to the collective interests of students and to public funds or the activities provided from those funds posed by institutions. We maintain an assessment of each HEI, which focuses on the three areas of risk identified in paragraph 23 of the memorandum of assurance and accountability: • institutional sustainability • value for money, propriety or regularity • risk management, control or governance.

Sources of information
We have a number of mechanisms and sources for enabling us to assess risk, including: a. **The annual accountability returns process** in which institutions submit a range of information and returns relating to financial performance and forecasts, student numbers, the use of funds and risk management, control and governance and sustainability assessments. b. **Our own institutional audit processes**, including data audits and cyclical assurance visits, which are designed to provide assurance on institutions' accountability returns. c. **The continuing dialogue that we have with each institution** about their changing priorities and strategies, and their reporting of material events. d. **Information from other sources** including public bodies that might potentially impact on our concerns with sustainability, among other issues. For example, we have memoranda of understanding with other funders of HEIs that commit us, on a confidential basis, to share information which could have a bearing on each other's assessments of the risk to funds. This furthers part of our commitment to minimise the accountability burden on institutions. e. **Indicators** that we monitor for the purpose of institutional risk and which, at times and in specific institutional cases, could have a bearing on our risk assessments. For example, the data used to underpin the operating model for quality assessment. f. **Information given to us through public interest disclosures** but only when substantiated in dialogue between us and the institutions concerned. g. **Other sources** of publicly available data.
Our risk assessment
Our assessment of the risk to **financial sustainability** is based on historical (two years) and forecast (four years) financial information supported by a narrative commentary. A number of indicators are employed as set out below. We perform assessments throughout the year on an ongoing basis and as necessary. We have internal benchmarks for each of these indicators which help us to flag concern. We also try to look beyond the snapshot position which the indicators represent to an institution's trends and how its performance compares with the sector and its peers. We feed back key parts of our financial assessment to each institution in our annual risk letter. The current indicators are: • surplus as percentage of total income • cash flow from operations as a percentage of total income • liquidity expressed in days

- affordability of financial commitments
- unrestricted reserves as percentage of total income
- staff costs as percentage of total income.

We develop and supplement these indicators over time and in response to individual cases.

Our assessment of risk relating to the **use of public funds** is concerned with all public funds being used for the purposes intended by Parliament (regularity), fraud and impropriety being prevented or dealt with effectively, and value for money (economy, efficiency and effectiveness) being pursued in the application of those funds. We do not normally audit these matters directly ourselves but derive information for our risk assessment from these sources:

a. The annual submission by HEIs of the reports of the governing body, audit committee, accountable officer and internal and external auditor.

b. Information and evidence from institutions themselves and other organisations and sources that indicate any material misuse of funds. From time to time we may receive information through these routes relating to any aspects of an institution's operations or provision that could cause us to reconsider our risk assessment. We would make such a judgement on a case-by-case basis having consulted with the institution concerned.

Our assessment of institutional **risk management, control and governance** is concerned with ensuring that public funds are being administered by well run corporations and that the collective interests of students are not at risk. In addition to information on finances and the use of funds, our own data and assurance audits enable us to corroborate institutional assurances. Overall, the regular sources of information for this risk assessment include:

- the annual accountability returns, including the governance and accountable officers' assurances
- the outputs of the institution's internal and external auditors
- information from other public bodies
- HEFCE's own audit and assurance work.

Risk notification

The work undertaken by HEFCE, augmented by information from other sources, enables us to make an annual risk assessment. For the majority of institutions this results in a letter from the HEFCE chief executive to the accountable officer, normally by the end of April advising that in HEFCE's judgement the institution is not at higher risk. We ask that all our risk letters be communicated to the governing body. For some institutions a second risk letter may be issued in the autumn following assessment of their financial forecast submissions.

In some cases, the HEFCE assessment letter notifying that an institution is not 'at higher risk' will be qualified by comments alerting the institution to concerns we have that need to be addressed and which, in some cases, if not addressed, may lead to a worsening of the institution's risk status. The comments can include a range of issues, including financial performance, future sustainability issues relating to the quality of the academic experience and student outcomes, strategic challenges and issues of non-compliance with accountability requirements. Some of these matters are more serious than others. We will endeavour in such cases to explain the issues fully, and we expect that our concerns will be considered and dealt with by the institution.

In a small number of cases, HEFCE's judgment will be that an institution is 'at higher risk'. This assessment is most likely to be made for financial reasons. Whatever the reason for the judgment, the process of making and communicating the judgment is very thorough and will be communicated to the institution concerned and the support strategy, as outlined at paragraphs 6 to 10 and Table 1 of this annex, will come into play.

Annex C: Approval of increases in financial commitments

Introduction

1. An institution must get prior written approval from us to increase its financial commitments before it agrees to any new financial commitment meeting either of the following criteria.

   a. Where total financial commitments (long-term and short-term) exceed six times its average adjusted net operating cash flow (ANOC) taken from the latest July forecasts (this is how the threshold is defined).

   b. Where it is assessed by us as being at higher risk.

Definitions

ANOC

2. ANOC is defined as:

- net cash flow from operating activities
- plus cash received from investment income
- plus cash received from endowments
- less cash paid on interest on borrowings
- less cash paid on interest element of finance leases.

Financial commitment

3. Financial commitments should be defined as those that are on balance sheet, in accordance with accounting standards.

4. Financial commitments include:

- all financial commitments, whether self-financing or not, drawn or undrawn
- finance leases
- service concession arrangements
- Private Finance Initiative arrangements which are accounted for as loans or finance leases in accordance with the requirements of Financial Reporting Standard 102
- repayable grants, such as from the HEFCE Catalyst Fund.

5. Pension fund liabilities, interest rate hedges (such as swaps) and all provisions should be excluded from financial commitments.

6. Where a university or college exceeds its financial commitments threshold in the future because of a decline in its ANOC, it need not apply for higher commitments to be approved. However, this is likely to lead to engagement with that institution about its ability to service its financial commitments.

Our response

7. We take a risk-based approach to each institution's application for higher financial commitments. This approach will determine whether the application is considered by the HEFCE Chief Executive or by the HEFCE Board. We will aim to respond to applications within 15 days of receiving the relevant information, although this period may be longer where approval by the HEFCE board is necessary (we will advise institutions when this is the case). We therefore

expect institutions to include their financial commitments plans as far as possible in their annual financial forecasts submissions, to enable HEFCE to review them at an early stage. Institutions are also advised to discuss their plans informally with HEFCE at an early stage. Where HEFCE approves the application for higher financial commitments, we will write to the institution setting out the revised commitment level. As part of this approval we may set out additional conditions which will need to be adhered to.

Information required

8. All applications for higher financial commitments must **be signed by the accountable officer**. In signing the application, the accountable officer is confirming that the institution's governing body has reviewed the terms and conditions of the financial commitment providing assurance over value for money, and has reviewed affordability and compliance with banking covenants under different scenarios (meaning that the proposed financial commitments have been stress tested). In addition we ask for confirmation that the student interest has been considered in any application.

9. We set out in Table 3 the information we require to consider a request for an increase in financial commitments. This addresses the issues on which we would expect the institution's own governing body to seek assurance before approving additional financial commitments. The main focus is on affordability and risk, not necessarily on the individual project.

Table 3: Information required by HEFCE to consider a request to increase financial commitments

Financial commitments
1. There should be a reasonable case for the new investment. Information required: a. A brief description of the new investment. b. An explanation of how it broadly fits with the institution's mission and strategic priorities. c. Confirmation that the institution has considered appropriate guidance on appraising investment decisions. d. A description of how the student interest will be taken into account.
2. The new financial commitments or refinancing arrangement (where these will result in an increase to financial commitments) should be consistent with the institution's financial strategy and represent good value for money. Information required: a. An explanation of why additional finance or refinancing is necessary and how this fits with the financial strategy. b. The forms of finance considered and the selection process and criteria. c. The net present value for each financing option, and a brief explanation of why the chosen method was selected.

3. Details of the new financial commitments. Information required: a. Details of the chosen option, including name of lender, value of new financial commitment, repayment period, basis of repayment and financial covenants. b. Terms and conditions of the financing (such as a copy of the offer letter) and an evaluation of the risks and uncertainties.
4. The new investment and financial commitments must be affordable. Information required: An update of the latest financial forecasts, to include the impact of the new investment and financial commitments, and demonstration that they are affordable. This update must include any other material changes in the institution's financial prospects, including guarantees to third parties.
5. The institution's governing body must have made an informed decision about the new investment and financial commitments. Information required: a. Details of when the governing body approved the new investment and financial commitments, and a minute of the decision reached. b. A summary of the information the governing body received in reaching its decision.
6. Details of the new commitment level. Information required: a. Details of existing financial commitments (including the lender, terms, interest rate and financial covenants) and of the new financial commitments. b. A calculation of the new commitment level required.

Annex D: Exchequer interest

Introduction

1. This annex reflects the agreed system for Exchequer interests, which provides accountability for public funding without imposing an undue administrative burden on institutions and enabling them to manage their estates flexibly (see HEFCE Circular letter 12/2006).

Requirements

2. Each higher education institution (HEI), having entered into an agreement with HEFCE effective on 1 August 2006 to enable the retrospective elements of a new system of accounting for Exchequer interests to be enacted, must follow the conditions set out below.

3. The Exchequer interest identified and agreed with HEFCE in that agreement formed the opening balance of a simple Exchequer interest register maintained by HEFCE. The register is adjusted immediately for the addition of capital grants received in the year, and annually for both of the following:

- indexation of the opening balance and all grants received in subsequent years
- writing down grants over the prescribed period.

4. The indexation rate used will be the GDP deflator published annually by the Treasury. This will take account of changes in value and ensure that the value of the Exchequer interest is not eroded through inflation.

5. All capital grants made by HEFCE after 1 August 2006 that create an Exchequer interest are entered onto the register, regardless of how they are treated for accounting purposes.

6. The opening Exchequer interest balance as at 1 August 2006 is written down over a 10-year period on a straight-line basis. All subsequent capital grants are written down annually over 15 years from the year of the grant in question, to recognise their consumption through the provision of education over that period.

7. The closing balance of the register as at 31 July 2007 and annually thereafter provides a single reportable sum for the Exchequer interest, and is confirmed annually with the institution by HEFCE.

8. As repayment of Exchequer interest only occurs in exceptional circumstances (see below), it does not need to be disclosed as a contingent liability in the institution’s annual accounts.

Circumstances in which the Exchequer interest becomes repayable

9. If either of the following remote events occurs, they will trigger immediate liability for the institution to repay to HEFCE the full amount of the Exchequer interest (as shown in the Exchequer interest register at that date). The institution will recognise HEFCE as an unsecured creditor until such repayment is made. If a liability to make repayment arises, HEFCE may agree to accept repayment of some other sum, or to delay repayment, at its absolute discretion, and such agreement may be on terms and conditions as HEFCE thinks fit.

10. The first trigger event will be if the institution becomes insolvent, including going into liquidation or administration, or if it dissolves or transfers its undertaking to some other body (for

example, by the exercise of the Secretary of State’s powers under the Education Reform Act 1988), or if it experiences any analogous event.

11. The second trigger event is if the institution ceases to be designated as eligible for HEFCE funding, or chooses to withdraw from its funding relationship with HEFCE.

12. If either of the triggers is activated, HEFCE has the right, but not the obligation, to request repayment. It has discretion to waive the requirement for repayment. In making this decision, HEFCE will consider the extent of any continuing public benefit arising from the use of previous HEFCE capital grants.

Annex E: Exempt charities

1. HEFCE is the principal regulator of those higher education institutions (HEIs) that are exempt charities. The benefit of HEFCE having this role is that we can utilise existing assurance processes, so minimising the burden on institutions as well as enhancing confidence.

2. This annex sets out our main requirements relating to annual and longer-term cyclical monitoring of HEIs that are exempt charities. They arise from our role as principal regulator of HEIs as charities (see www.hefce.ac.uk/whatwedo/reg/charityreg/ for more information).

3. In addition to the requirements set out here, from time to time we may need to ask for other information to enable us to deal with particular issues about HEIs as exempt charities. Our power to do so is set out in Section 79A of the Further and Higher Education Act 1992. In particular, our principal regulator role applies to entities that are exempt charity 'connected institutions' by virtue of Paragraph 28, Schedule 3, Charities Act 2011 (paragraph 28 connected institutions). Although we do not directly monitor those entities, we have the power to request information about them.

4. The information requirements of HEIs as exempt charities (see paragraphs 5 to 8 below) are similar to those of the Charity Commission for registered charities. However the collection and publication arrangements have been tailored to the sector, and reflect our responsibilities as the lead regulator of HEIs in respect of their accountability for public funds, and are largely embedded in our normal monitoring processes. For example, the Charity Commission publishes some of the information it collects on its own web-site; instead we require each HEI to publish information on its own site.

Information to be made readily available on HEIs' web-sites

5. HEIs that are exempt charities must maintain a page on their web-site to provide a gateway to the following information:

   a. The legal name and correspondence address of the HEI. The preferred name(s) used by the HEI should also be shown.

   b. The main constitutional document of the HEI (such as its Royal Charter, Memorandum and Articles, or Trust deed). This should be the latest version, but HEIs should provide earlier versions back to at least the one that was in force in 2009-10.

   c. The names of the trustees on 31 January each year, together with a list of **all** other charities (if any) of which each trustee is then also a trustee.

   d. The full audited consolidated financial statements for at least five years.

6. The 'gateway' web page should be easy to locate on the HEI's web-site and must be updated with the previous year's information no later than six months after the end of the previous academic year. HEIs must provide HEFCE with the up-to-date web address (URL) of the gateway page so that third parties can access it via our own web-site.

Information to be included in audited financial statements

7. The following information must be included in the HEI's audited financial statements and related reports:

   a. A statement about the HEI's charitable status and objectives.

b. A list of the trustees who served at any time during the financial year, and until the date the financial statements were formally approved.

c. A statement confirming whether the charity trustees have complied with their duty to have due regard to the guidance on public benefit published by the Charity Commission in exercising their powers or duties.

d. A report on how the trustees have delivered their charitable objectives for the public benefit over the financial year. This does not need to be part of a separate public benefit report but can included in the operating and financial review in other sections as appropriate. However it is presented, the public benefit reporting must cover the following:

  i. A review of the significant activities undertaken by the charity to carry out its charitable purposes for the public benefit.

  ii. Details of the charity's purposes and its strategic objectives.

  iii. Details of the strategies adopted and activities undertaken to achieve those purposes and objectives.

  iv. Details of the achievements of the charity by reference to the purposes and objectives that the trustees have set.

Further information on public benefit reporting can be found in the Charity Commission guidance (https://www.gov.uk/government/collections/charitable-purposes-and-public-benefit).

e. Provision in the notes to the financial statements information on payments to or on behalf of trustees, including:

  i. Payments to trustees for serving as trustees:

    1) The amount of all payments and other benefits to each (named) charity trustee who is not an employee of the HEI. Each payment should be disclosed to the nearest £1.

    2) Details of all waived entitlements to such payments and other benefits.

    3) The legal authority for such payments and reason for remuneration.

    4) If there are no such payments, an express statement to that effect.

  ii. Expenses paid to trustees:

    1) The total amount of expenses paid to or on behalf of the trustees as a whole, rounded to the nearest £1,000. (For trustees who are employees, this only applies to expenses when serving as trustees.)

    2) The nature of the various expenses.

    3) The number of trustees involved.

    4) If there are no such expenses, an express statement to that effect.

  It is not necessary to include routine expenditure on services provided for the trustees collectively, such as room hire or reasonable refreshments at meetings.

iii. Related party transactions involving trustees irrespective of whether or not they are undertaken on an arm's length basis:

1) The name of the transacting related party or parties.

2) A description of the relationship between the parties (including the interest of the related party or parties in the transaction).

3) A description of the transaction.

4) The amounts involved.

f. For each paragraph 28 (Charities Act 2011 Schedule 3) connected charity that has income in the year of £100,000 or more, the following:

i. Its name and charitable purpose.

ii. The opening balance, income and expenditure for the year, and closing balance.

g. For all other paragraph 28 charities, the following

i. An analysis into appropriate groups (for example prize funds, bursary or scholarship funds, research support funds) stating the number of entities in each group.

ii. For each group: the aggregate opening balances, income and expenditure for the year, and closing balances.

(Note: the terms 'opening balance' and 'closing balance' in paragraphs 7f and 7g should be interpreted as total reserves where the paragraph 28 charity is an operating charity.)

8. We may provide more detail about some of the above in the HEFCE accounts direction to HEIs, which is updated by an annual circular letter.

Reporting serious incidents

9. A serious incident is one which has resulted in, or could result in, a significant loss of funds or a significant risk to a charity's property, work, beneficiaries or reputation. For more guidance see www.hefce.ac.uk/reg/charityreg/sir/.

10. HEIs must report serious incidents to HEFCE at the time when they are identified. We have also included in HEFCE's annual assurance return a specific declaration that serious incidents have been appropriately reported to us. This declaration will be made on behalf of all trustees. It would be appropriate therefore for the trustees to be informed about incidents reported to HEFCE; however, we do not stipulate how this should be done.

11. Where HEIs report the loss of an HEI's assets through fraud, theft or other cause, we will consider an incident reported both as funder and as principal regulator.

12. In addition, and as principal regulator in the first instance, we expect HEIs to report the following serious incidents:

- donations of more than £25,000 from unknown donors or where the source cannot be verified
- abuse or mistreatment of a charitable beneficiary involved in activities of the HEI
- disqualification of a trustee

- known or alleged links (other than for bona fide academic reason) with proscribed organisations or terrorism; this applies to trustees, staff, students or anyone else associated with the HEI.

We would welcome a provisional report if it is likely that internal investigations may be time-consuming.

13. A report of a serious incident should be sent to the HEFCE chief executive. Our primary concern is to satisfy ourselves that the HEI has responded to the incident in an appropriate way, designed to protect the HEI as a charity. In order for us to do this, HEIs should provide as much information as possible to help us to decide if their response has been appropriate and what, if any, further action is planned. In particular we would expect the report to indicate:

- whether the incident has happened or is suspected
- when it occurred and who was involved
- the impact of the incident on the HEI, any beneficiary involved, or both
- what inquiries have been made and actions taken, including any reports to other regulators or the police
- what policies and procedures were in place that apply to the incident, whether they were followed and, if not, why
- whether the trustees have determined that policies and procedures need to be introduced or revised – and if so, how and by when.

14. In extreme cases, a serious incident report may lead us to invite the Charity Commission to consider opening a formal Inquiry under s46 of the Charities Act 2011.

15. We appreciate that information provided under the terms of paragraphs 10 and 11 may be of a sensitive nature, and we undertake to treat it with care. We ask for the information to fulfil our statutory obligations as principal regulator, and such obligations may require us to consult the Charity Commission to ensure that we deal with an issue in a manner consistent with the regulation of charities generally. As public authorities, both HEFCE and the Charity Commission are subject to the Freedom of Information Act. We will only disclose information to someone outside HEFCE or the Charity Commission in circumstances where we are legally obliged to do so. Further guidance about the way HEFCE applies the Freedom of Information Act and the Data Protection Act 1998 is available on our web-site.

16. Further guidance on these reporting requirements is available at www.hefce.ac.uk/reg/charityreg/sir/.

Annex F: Related undertakings

Institution

1. 'Institution' means the institution including its **related undertakings**, as defined in paragraphs 2 and 3, unless such undertakings are subject to a separate funding agreement directly with HEFCE, have been designated by the Secretary of State as institutions in the further education sector which have their own contract with the Education and Skills Funding Agency, or are schools as defined by section 4 of the Education Act 1996 or multi-academy trusts.

Related undertakings

2. An 'undertaking' includes a body corporate, a partnership, an unincorporated association or a trust. An undertaking will normally be regarded as a related undertaking of the institution if any of the following apply:

   a. The institution controls that undertaking.

   b. The institution and another undertaking or other undertakings related to the institution together control that undertaking.

   c. Another undertaking or other undertakings related to the institution control that undertaking.

   d. That undertaking is recognised by us as a 'connected institution', as defined by section 27 of the Teaching and Higher Education Act 1998.

   e. We consider that the sole purpose, or one of the main purposes, of registering students at that undertaking is to avoid or minimise regulation by HEFCE, to optimise funding or to manipulate data for regulatory or other purposes.

   f. We consider that the undertaking was established by or is operated for the primary benefit of the institution.

3. We may, at our discretion, decide to treat a related undertaking as a separate institution for funding, regulatory and other purposes if we consider that the undertaking has a separate historic identity from its parent institution.

4. For the purpose of paragraph 2, an undertaking is under the 'control' of another if any of the following apply[11]:

   a. That other holds or is entitled to acquire a majority of the shares in the undertaking.

   b. That other holds or is entitled to acquire a majority of the voting rights in the undertaking.

   c. That other has or is entitled to acquire the right to appoint or remove a majority of the board of directors or other governing body of the undertaking.

[11] The expressions 'voting rights in an undertaking', 'right to appoint or remove a majority of the directors', 'right to exercise a dominant influence' and 'control contract' have the meanings given in schedule 7 to the Companies Act 2006.

d. That other has or is entitled to acquire the right to exercise dominant influence over the undertaking by virtue of provisions contained in the undertaking’s articles of association or any other constitution, control contract, memorandum of understanding or other document regulating the undertaking or any other undertaking.

e. That other has or is entitled to acquire the right to a share of more than half the assets in the event of a winding up or in any other circumstances, or of more than half the income, of the undertaking.

f. Both are in common or overlapping ownership or are managed on a uniform basis or have a significant number of directors (or equivalent) or senior management in common.

g. That other has or is entitled to acquire the power, by any other means, to secure that the affairs of the undertaking are conducted in accordance with its wishes, or the undertaking is habitually conducted in accordance with the wishes of the other.

5. Where a school (as defined in paragraph 1) or multi-academy trust is under the control of the institution and delivers higher education (HE), the expectation is that HE students would be reported through the institution, but students not studying at HE level in school would be excluded.

6. Where a student union is under the control of the institution, it is excluded from the definition of related undertakings, except where it delivers higher education.

Annex G: Definitions and abbreviations

Accountable officer	Head of an institution responsible and accountable to HEFCE (and ultimately to Parliament) for ensuring that the institution uses HEFCE funds in ways that are consistent with the purposes for which those funds were given, and complies with the conditions attached to them. These include the conditions set out in the Further and Higher Education Act 1992 and in this memorandum of assurance and accountability.
Accounting officer (of HEFCE)	As accounting officer, the chief executive of HEFCE has a personal responsibility to safeguard public funds and achieve value for money as set out in HM Treasury guidance, 'Managing Public Money' and any subsequent guidance. This includes responsibility for the public funds allocated by HEFCE to higher and further education institutions and other bodies for education, research and associated purposes.
Annual accountability returns exercise	A streamlined accountability process between HEFCE and institutions, linked to an assessment of institutional risk, which comprises an exchange of documents and dialogue during a specific period each year.
Annual accounts direction	HEFCE publishes an annual accounts direction, which states HEFCE's financial reporting requirements. HEIs and their external auditors must comply with it. The most recent accounts direction was published as HEFCE Circular letter 27/2017.
ANOC	Adjusted net operating cash flow
ASSUR	Annual sustainability assurance reports.
EBITDA	Earnings before interest, taxes, depreciation and amortisation.
FEC	Further education college.
Governance Code of Practice	'Higher Education Code of Governance (see www.universitychairs.ac.uk/wp-content/uploads/2015/02/Code-Final.pdf)
Governing body	The university council, board of governors or other body ultimately responsible for the management and administration of the institution's revenue and property, and the conduct of its affairs.
HE	Higher education.
HEFCE	Higher Education Funding Council for England.
HEI	Higher education institution.
HESA	Higher Education Statistics Agency.
JANET	High-speed computer network supported by all the four higher and further education funding bodies, which links universities and colleges in the UK. SuperJANET is the enhanced network.

Key information Set	Key Information Sets are comparable sets of information about full- or part-time undergraduate courses, published on course web pages. All of the Key Information Sets are published on the Unistats web-site.
Operating Framework	The Operating Framework explains how higher education providers in England are held to account and regulated.
Register of HE providers	The HEFCE Register is a regulatory tool that provides information about how providers of higher education are regulated in England.
Regularity	Regularity is a public finance requirement for funds to be applied only to the extent and for the purposes authorised by Parliament.
Secretary of State	Secretary of State for Education.
SLC	Student Loans Company Limited.
the Code	HEFCE's Audit Code of Practice.
VFM	Value for money.

References to the **financial position**, **financial statements**, **financial commitments** or **borrowings** of the institution mean the consolidated financial position, financial statements, financial commitments or borrowing of the institution and its subsidiary undertakings, as defined in the Companies Act 1985 and revised by the Companies Act 1989 and 2006, and in accordance with generally accepted accounting principles.

Shall and **must** denote mandatory requirements, and **should** denotes our view of good practice.