February 2006/07
Core funding/operations
Outcomes of consultation

This report is for information only

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February 2006/**07**

Accountability for higher education institutions

Responses to the consultation

HIGHER EDUCATION FUNDING COUNCIL FOR ENGLAND

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Accountability for higher education institutions

Responses to the consultation

To	Heads of HEFCE-funded higher education institutions
Of interest to those responsible for	Senior management, Finance, Governance
Reference	2006/**07**
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Executive summary

Purpose

1. These are the results of the consultation on our plans for promoting better regulation for higher education institutions (HEIs) through a new streamlined accountability process linked to our assessment of institutional risk. We have called this process the 'single conversation'.

Key points

2. There was a high level of response from the sector to the consultation (HEFCE 2005/31) and strong support for most of our proposals.

3. We will run a pilot study in 2006 of the single conversation accountability process, with a common submission date of 30 November, before we roll it out to the whole sector in 2007.

4. We are working with a steering group of sector and stakeholder representatives to develop detailed proposals and implement the new accountability arrangements. We will consult the sector again on any further major changes.

Action required

5. This report is for information.

Introduction

6. In July 2005 we set out proposals to change the accountability process (see HEFCE 2005/31 ‘Accountability for higher education institutions’). The aim was to reduce the burden of regulation on institutions by placing greater reliance on their own systems of management and governance. The better these systems, the lighter would be the burden of providing assurance about the use of public funds. One key element of our proposals was the ‘single conversation’: concentrating the accountability process between HEFCE and HEIs as far as possible into an exchange of documents and dialogue during a specific period each year. At the same time we instigated a wide-ranging debate with the sector through regional seminars, presentations, and discussions with individual institutions and representative bodies. The consultation period closed on 30 November.

7. We had 108 responses, 98 of which were from HEIs, representing around three-quarters of the sector. Other respondents included sector representative bodies, audit firms and the National Audit Office. The overall tone of responses gives support to our approach. The consultation paper asked seven specific questions; Annex A lists these and summarises the responses. Many institutions took the opportunity to comment much more broadly on accountability issues and on their relationship with HEFCE and other stakeholders. We are encouraged by the range and quality of comments, which will make a major contribution to the development of our thinking.

8. The areas covered in the consultation are set out below.

The ‘single conversation’

9. Many institutions warmly welcome our proposals and see them as a contribution to better regulation and an improved dialogue with us. Many, indeed, view them as consistent with their own good management and governance. The great majority – around 80 per cent – said they foresaw no major difficulties in adopting the single conversation accountability process. Most indicated that significant changes would nonetheless be necessary to make this happen, the main ones being:

- amending committee meeting dates
- considering when to prepare (and, if necessary, revise) financial forecasts
- rescheduling activities and workload.

10. For some institutions, particularly small ones, the task of preparing information and interacting with HEFCE falls on only a few staff, and the compression of activity would cause difficulty at the busiest time in the financial and academic year. We will be sensitive to this and keep our information requests to a minimum. Some argued that shortened timescales would have an adverse effect on the quality of governance. These institutions may need support in making the necessary organisational and cultural changes.

11. Another important observation, often made even by institutions supporting the principle of the single conversation, was that the advantages of the change were not always obvious. While acknowledging the ways in which we have cut regulation in recent years, many institutions remained sceptical that these proposals would lead to a genuine reduction in the burden on them, or that the changes would deliver the promised 20 per cent reduction by 2007. The single conversation concentrates the accountability exchange into a short period each year, but as respondents often pointed out, this does not of itself reduce the administrative burden.

12. Our aim at this stage had been to set out the direction of travel and outline high-level principles, but many wanted much more detail. We will work on this with the steering group (see paragraphs 42 and 43 below) in the light of feedback from the sector. Our task over the medium term, in developing our proposals, will be to ensure that there are real savings to institutions and that these are clearly explained.

13. The single conversation allows us to collect financial statements and financial forecasts together. We argued that all parties – HEIs, their governing bodies and ourselves – would find it helpful to consider past financial performance and future financial prospects at the same time. Many

institutions, but not all, appear to have accepted this, though some pointed out that the compression of workload would make it difficult to prepare or revise forecasts in the autumn.

14. In the consultation document we set out suggested elements of the single conversation, covering financial, audit-related, planning and performance information. Some institutions felt this list was too long and that we should reconsider the number of returns; others wanted a guarantee that we would not add requirements at a later date, and cited the new sustainability framework as an example of 'regulatory creep' (see HEFCE Circular letter 28/2005). Conversely, others were concerned that further de-regulation might undermine public confidence in the sector and lead to greater political intervention.

15. The announcement of the new sustainability monitoring process was certainly perceived to cut across our efforts to lighten the burden on institutions. This is a requirement of the Treasury, working through the Research Base Funders' Forum, in return for significant increases in research funding for HEIs, and covers the whole UK. It is not an initiative from HEFCE. To minimise the impact on the sector we will integrate sustainability into the single conversation process, taking into account the comments we have received.

16. There was some debate as to which documents should be part of the process. The Transparent Approach to Costing (TRAC) return, currently submitted on 31 January following the year end, is one obvious omission. We mentioned the Higher Education Students Early Statistics return (HESES) but not the Research Activity Survey, both of which have a census date of 1 December and a return date one week later. We need to consider how to reconcile this with the proposed single conversation submission date (see paragraphs 18-24 below).

17. In supporting the new accountability arrangements, a number of institutions said they do not want us to reduce other forms of contact, such as visits by HEFCE regional teams, which 'add value'. We do not intend to decrease this kind of activity. As we said in the consultation document, we need to do further work on how regional team engagement can be linked with the single conversation process.

The common submission date

18. We asked institutions how soon they could implement the common submission date of 30 November for financial statements and forecasts (and all the other returns and assurances). Almost half (45 per cent) said they could do this now or by 2006; a further 37 per cent thought this would be achievable by 2007, and 4 per cent by 2008. Of the remainder, four gave a later date, the latest being 'not before 2010' (from one small specialist institution).

19. Some institutions doubted the benefit of bringing forward by one month (in practice only a few weeks) the deadline for submitting accounts. Seven were opposed in principle or felt that it would not be possible. Several suggested a common submission date of 31 December, meaning no change in the timetable for sending us accounts. While this would minimise disruption, it does not meet the general expectation from many stakeholders for more timely financial information. It could also be argued that since so many institutions would be able to comply relatively easily, there is no good reason for them all not to do so. We also believe that the value of information – both to us and institutions – diminishes over time.

20. In making this change we will consider how to address specific difficulties. It is our view that with adequate notice and support most of these institutions will be able to manage.

21. Given that so many respondents said they could implement the change for 2006, there is an opportunity to run a pilot study. This will allow us to refine the content of the dialogue, assess the impact on institutions, revise our internal processes and learn from the experience. Our aim is to roll out the single conversation process to the whole sector in 2007.

22. Although we did not specifically seek views at this stage, we indicated in the consultation document our wish to move to a submission date of 31 October in the longer term, after reviewing the costs and benefits. Thirty-five HEIs commented on

this, almost all unfavourably, saying it was impracticable or very difficult. Many pointed out the problem of reconciling this date with submitting the HESES return in early December, though the current review of the funding method for teaching (see HEFCE 2005/41) may result in greater reliance being placed on data collected in the summer by the Higher Education Statistics Agency (HESA).

23. Nonetheless, there are clearly some institutions that can – and wish – to meet this earlier date. This therefore makes it possible to run a second pilot study for the 31 October submission date, perhaps in 2007, to assess the implications for both us and institutions.

24. Whichever submission date is adopted, the new process will allow institutions to submit more up-to-date financial forecasts that take into account, for example, student recruitment in the current year. Some see this as an advantage; while others, perhaps with a pattern of later or mainly part-time recruitment, feel that such an expectation would be unrealistic. We will look at this in the pilot study.

HEFCE audits and the 'assurance dialogue'

25. The proposal here is to replace direct audits by HEFCE with a periodic shorter assurance dialogue, perhaps every three years, for institutions where assurances from their own audit and governance processes are reliable. This received backing from 95 per cent of institutions, though quite a few suggested an interval of every five years. We did not specify in detail how such a dialogue would operate, and we plan to work up proposals. Institutions have commented that such visits must demonstrably involve less work for them than the current audit process which, nonetheless, many have said is not particularly burdensome. We will aim to use the single conversation documentation rather than making additional demands on institutions.

Greater freedom for lower risk institutions

26. The main theme underlying all our proposals is that lower risk institutions should enjoy greater freedom from regulation: the effort in providing assurance to public funders for such institutions should be minimal and proportionate to risk. We invited the sector to suggest ways in which this could be delivered, and this has been one of the most fruitful aspects of the consultation exercise. Points raised are summarised at Annex A.

27. Broadly speaking, institutions have echoed our own thoughts and the principles endorsed by the Higher Education Regulation Review Group (HERRG), principally:

- a risk-based approach to regulation
- exception reporting
- greater reliance on institutions' own management and governance processes and outputs
- reducing the number of separate funding streams, and mainstreaming funding wherever possible.

28. Where separate funding remains, institutions felt that there should be an end to detailed or separate reporting or additional auditing. In other words, HEIs should only have to report by exception – letting us know when objectives are not being met or delivery is delayed – and we should rely on a single annual audit of the institution's financial statements. Particular comment was made about the distribution of HEFCE capital funding. We were praised for the work done so far to replace bidding with conditional allocations, for example, but were encouraged to do more. We are currently consulting the sector on proposals for distributing long-term capital funding that should address some of these issues (see HEFCE 2006/04).

29. 'Less information less frequently' was a common plea from institutions, and they gave a few specific examples. We can certainly look again at the content of the single conversation, and in particular whether it is possible to reduce the demands on smaller or specialist institutions.

30. The most radical suggestions involved eliminating all reports beyond the annual accounts, or the accounts and financial forecasts together, with perhaps the addition of the designated officer's annual assurance return. Such a minimal regime would need to be combined with a clear general

requirement for institutions to give an early indication of material adverse changes in their circumstances. Since we are planning to create a single accountability framework covering all public sector funders and stakeholders for higher education, this should be addressed in that context and through the steering group. It will be a challenge to secure agreement among the various parties even to the information currently envisaged in the single conversation.

31. There were several requests to give HEI's more freedom to borrow without prior consent from us. Currently our consent is required where the annualised servicing costs of borrowing are more than 4 per cent of the HEI's total income; and approval by the HEFCE Board is required when these costs exceed 7 per cent. Requests from institutions included: abandoning the 4 per cent threshold, but keeping the need for consent at 7 per cent; raising the borrowing thresholds; and replacing consent with advance notification. These and other ideas will be taken forward in the proposed review of the Financial Memorandum between us and institutions in 2006-07.

32. A few institutions felt that our existing proposals already go far enough, and that there is a risk of further de-regulation undermining public confidence. This may be more of an issue when we consider the needs of other funders and stakeholders. We have been reminded that other parties, such as banks, rely on our current oversight of the sector, and that less regulation by us might lead to more regulation by them, with consequent higher costs for some HEIs.

The 'support strategy'

33. Our support strategy for institutions at higher risk received clear endorsement. Virtually all institutions (93 per cent) explicitly agreed that it appropriately describes the ways in which we need to engage; only one disagreed.

34. One of the main issues raised here was the need to define terms and the method of making risk assessments. We need to assure institutions that an individual risk factor, such as cash-flow difficulties, would not necessarily result in an overall 'higher risk' categorisation. While welcoming clarification on the range of our possible interventions, some HEIs wanted assurance that our actions would be proportionate and sensitive, and that we would not be overly intrusive or demanding of institutions facing difficulties. Two replies emphasised that we should have an early dialogue with senior management before making a 'final' assessment. This is always our practice, but evidently we need to say this clearly. Others wondered if there should be an opportunity to appeal, given that our assessments could have consequences beyond the HEFCE-institution relationship. We would always hope to reach an agreed basis for our assessments, although this may not always be possible.

35. This leads on to a general concern about the disclosure of our risk assessments under the Freedom of Information Act, and the public impact of that. The Act is now a factor in our dealings with institutions, and we must continue to ensure that there is a sound basis for making assessments. The entire risk assessment process will be revised during 2006-07, to take into account the new accountability arrangements and the development of a single framework with other funders.

Data audit

36. We asked whether an institution's own auditors, rather than HEFCE, should provide assurance about student data returns. Half of all institutions rejected this proposal. The main reasons for this were:

- additional cost to the sector
- the risk of less consistency between institutions
- an institution's own auditors lacking the expertise and specialist knowledge of HEFCE staff
- possible unavailability of auditors at a busy time in the year.

37. Both HEIs and professional firms pointed to experience in the further education sector of relying on assurance of student data by internal auditors, which is not encouraging in terms of cost or burden on institutions. There was perhaps some uncertainty about the nature of our proposal, as it was not clear whether we intended each return to be audited, or

whether the system for preparing returns should be part of the cycle of internal audit activity. For many there was no obvious benefit to them or reduction in the burden. If we proceed, we need to give explicit guidance to both institutions and their auditors on how to conduct such audits.

38. Rather than dismiss the idea completely, we may offer cyclical audit by an institution's own auditors as an alternative to cyclical audit by us. Reliance on an institution's own processes and assurances is in keeping with the general spirit of the single conversation, as some have noted. The current review of the funding method for teaching might have an impact on what is done here, through possible greater reliance on the HESA return in the summer.

Working with other funders and stakeholders

39. The final consultation question asked whether all public sector investors and stakeholders should work together and use a common accountability framework and risk assessment model. This is the big potential gain for the sector that would deliver real reductions in the burden of accountability. Institutions recognised this, with near-unanimous support for the idea and no outright rejections of it.

40. Various respondents said that the common framework must not be too complex, and expressed a concern that convergence could actually increase the burden. We would not wish to proceed if that were so, as the whole objective is to reduce overlap, duplication and excessive demands for detail that could be better met by higher-level assurances. Both we and the sector need to have reasonable expectations. The problem of complying with EU funding rules was often mentioned, and this is a difficult issue for us to address. Many institutions wanted us to include non-public sector investors. In practice we are unlikely to be able to create a framework to suit everyone.

41. Developing the common framework will take considerable time and effort. A major part of the steering group's work will be to oversee the mapping of the accountability requirements of the various funders, to reach memoranda of understanding between them, and to negotiate processes that lead to simplification. At each key stage we will need to return to the sector to confirm that we are indeed proceeding in the right direction.

The steering group and next steps

42. As outlined in the consultation document, we are working with a steering group of sector representatives, public sector funders and other investors to develop and implement the new accountability framework (the current membership is at Annex B). The group met for the first time in January 2006 to consider responses to the consultation and the next steps. We expect it to remain in operation for up to two years, to address the following key issues:

- implementing the new accountability framework, including the single conversation
- co-ordinating accountability requirements with other funders and stakeholders
- creating a transparent institutional risk assessment process
- piloting the single conversation submission date of 30 November in 2006
- piloting the earlier submission date of 31 October (possibly in 2007)
- revising our Financial Memorandum with institutions
- revising our Accountability and Audit Code of Practice.

43. As proposals are developed in detail, we will seek views and confirmation from the sector and the other funders and stakeholders.

Annex A

Summary of consultation responses

Source of responses

Higher education institutions	98
Sector representative bodies	4
Audit firms	4
Professional bodies	1
Other stakeholders	1
Total	**108**

The analysis shown below is for HEIs only.

Q1: Do you foresee any major difficulties in adopting the 'single conversation' accountability process?

Yes or opposed in principle	15	15%
No	79	81%
Unclear, not specified or mixed view	4	4%

Q2: How soon will your institution be able to adopt the common submission date of 30 November for financial statements and forecasts?

2006 or 'immediately'	44	45%
2007	36	37%
2008	4	4%
Later	4	4%
Unable to answer	2	2%
Not possible to do, or opposed in principle	8	8%

Q3: Do you agree that where audit and governance assurances are reliable, direct audits by HEFCE should be replaced by a periodic 'assurance dialogue', which would form part of the single conversation?

Yes	93	95%
No	2	2%
No preference or mixed view	2	2%
No answer given	1	1%

Q4: In what ways do you think institutions presenting lower risks to public funding should enjoy greater freedom from regulation?

Comments included:

- no detailed reporting for specific initiatives
- no separate audits
- report by exception
- fewer special initiatives
- capital funding:
  - mainstream
  - early indications of future funding
  - ability to vire funds without approval
  - remove the 31 March deadline for expenditure
- a shorter single conversation
- no reporting beyond the annual accounts
  - plus financial forecasts
  - plus designated officer's annual assurance return
- greater freedom to borrow without consent
- a longer timeframe to submit accounts
- less frequent assurance visits
- abolish the HESA finance record
- abolish the TRAC return
- abolish the annual monitoring statement
- abolish reporting on sustainability, equality and diversity
- a lighter touch for smaller institutions
- accept reports in the HEI's own format
- less scrutiny of internal management and governance processes
- less inspection
- agree levels of autonomy with individual institutions
- no 'comply or explain' regime with good practice guidance.

Q5: Do you agree that the support strategy appropriately describes the ways in which HEFCE needs to engage more actively with institutions at higher risk?

Yes	91	93%
No	1	1%
Unclear, not specified or mixed view	5	5%
No answer given	1	1%

Q6: Should an institution's own auditors, rather than HEFCE, provide assurance about student data returns?

Yes	39	40%
No	49	50%
Unclear, not specified or mixed view	9	9%
No answer given	1	1%

Q7: Should all public sector investors and stakeholders in HE work together and use HEFCE's accountability framework and risk assessment model?

Yes	93	95%
No	0	0%
No preference or further discussion needed	4	4%
No answer given	1	1%

Annex B
Accountability framework: steering group membership

Organisation	Member
Association of Heads of University Administration	Fraser Woodburn, University Secretary, The Open University, and co-opted member of HEFCE’s Audit Committee
Committee of University Chairmen	To be determined
Engineering and Physical Sciences Research Council	Stuart Ward, Director (Resources)
HEFCE	Steve Egan, Acting Chief Executive (Chair)
HEFCE	Paul Greaves, Head of Assurance
HEFCE	David James, Finance and Risk Consultant
Higher Education Funding Council for Wales	Bethan Owen, Head of Risk Assessment
Higher Education Regulation Review Group	Steve Igoe, Director of Resources, Edge Hill College of Higher Education
Institution	Professor Michael Brown, Vice-Chancellor, Liverpool John Moores University
Institution	Dean Curtis, Director of Resources, Queen Mary University of London
Institution	Hari Punchihewa, Pro Vice-Chancellor (Resources) and Finance Director, University of Derby
Learning and Skills Council	Richard Healey, Director of Finance
National Audit Office	Erica Nicholls, Manager
NHS	Christina Pond, Director of Programmes, Skills for Health
NHS	Frances Harkins, Senior Policy Manager, Pre-Registration Education and Training
Office of Science and Technology	Roger Louth, Director of Resources and Policy
Quality Assurance Agency	Martin Johnson, Director of Resources Group
Regional Development Agency	Lis Smith, RDA National Skills Policy Manager, North West Development Agency
Standing Conference of Principals	Patricia Ambrose, Chief Executive
Scottish Funding Council	Brian Baverstock, Deputy Director, Financial Appraisal and Monitoring Services
Training and Development Agency	Ian Hopper, Head of Better Regulation
Treasury	Dr Ilona Blue, Science and Industry Team
Universities UK	Greg Wade, Policy Officer

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