

Annex A

Mandatory requirements

1. The following are mandatory requirements of this Code of Practice:
 - a. The governing body of each institution must take reasonable steps to ensure that there is a sound system of internal control within the institution.
 - b. Each institution must have an effective audit committee, which produces an annual report for the governing body and the designated officer.
 - c. *(Updated 16 September 2002.)* Members of the audit committee must not have executive authority or be members of a finance committee, unless the institution can satisfy the Council that there are good grounds and that the conditions in paragraph 48 of the Code have been met.
 - d. The audit committee of each institution, advised where appropriate by its internal audit service, must satisfy itself that satisfactory arrangements are in place to promote economy, efficiency and effectiveness.
 - e. Each institution must have an effective internal audit function, which reports at least annually to the governing body and the designated officer.
 - f. The work of the internal audit service must cover the whole of the internal control system of the institution.
 - g. The head of the internal audit service must have direct access to the institution's designated officer, the chairman of the audit committee and, if necessary, the chairman of the governing body. Internal, as well as external, auditors must also have unrestricted access to all records, assets, personnel and premises, and be authorised to obtain whatever information and explanations the head of the internal audit service or the external auditor considers necessary.
 - h. Fees paid to external auditors for other services must be disclosed separately in a note in the financial statements.
 - i. The Council's audit service, the HEFCEAS, must have access to all records, information and assets, and can require any officer to give any explanation which it considers necessary to fulfil its responsibilities. This includes access to any work of the internal auditor, or correspondence between internal and external auditors, and access to the work of the external auditor. For access to external audit work, the HEFCEAS will exchange letters where necessary with both parties to deal with confidentiality and the terms under which access is given.

j. The governing body must not accept any restriction of liability in respect of the external audit of the institution's financial statements.

k. The following information must be provided:

i. The governing body must send a copy of the audit committee's annual report to the HEFCE Chief Auditor, who would welcome a copy of the supporting annual report from the institution's internal audit service.

ii. The governing body must send to the HEFCE Chief Auditor, by 28 February in the following year, two copies of the external auditor's management letter and any management response.

iii. The designated officer must report any serious weaknesses, significant frauds or major accounting breakdowns without delay to the chairman of the audit committee, the chairman of the governing body, the head of internal audit and the HEFCE Accounting Officer. If the designated officer refuses to make an appropriate report, then the internal and external auditors must report to them directly.

iv. The governing body must inform the HEFCE Chief Auditor without delay of the removal or resignation of the external or internal auditors.

2. The Council will assess compliance with these requirements, having regard for the guidance on good practice and all of the audit arrangements that an institution has in place.

Annex B

Audit committee: model terms of reference

Introduction

The Council has certain mandatory requirements which must be included in the audit committee's terms of reference. However, the other elements of the model terms of reference will often have to be modified to suit local circumstances. The key question for audit committees is whether the arrangements within the institution meet the intentions behind these guidelines. These are that the audit committee is independent; that it has sufficient authority and resources to form an opinion and report on the internal control system, risk management and financial reporting arrangements of the institution; and that it can satisfy itself that the institution has adequate arrangements for ensuring economy, efficiency and effectiveness. The terms of reference should be formally approved by the governing body.

Model terms of reference

Constitution

1. The governing body has established a committee of the governing body known as the audit committee.

Membership

2. The committee and its chairman shall be appointed by the governing body, from among its own members, and must consist of members with no executive responsibility for the management of the institution. There shall be no fewer than three members; a quorum shall be two members. The chairman of the governing body will not normally be a member of the committee. The chairman of the committee will normally be a member of the governing body. Members should not have significant interests in the institution.

3. *(Updated 16 September 2002.)* At least one member should have a background in finance, accounting or auditing. The committee may, if it considers it necessary or desirable, co-opt members with particular expertise. No member of the committee may also be a member of the finance committee (or equivalent), unless specifically authorised by the Higher Education Funding Council for England (HEFCE) under the terms of paragraph 48 of the Code.

Attendance at meetings

4. The head of finance (or equivalent), the head of internal audit, and a representative of the external auditors shall normally attend meetings where business relevant to them is

to be discussed. However, at least once a year the committee should meet with the external and internal auditors without any officers present.

Frequency of meetings

5. Meetings shall normally be held at least twice each financial year. The external auditors or head of internal audit may request a meeting if they consider it necessary.

Authority

6. The committee is authorised by the governing body to investigate any activity within its terms of reference. It is authorised to seek any information it requires from any employee, and all employees are directed to co-operate with any request made by the committee.

7. The committee is authorised by the governing body to obtain outside legal or other independent professional advice and to secure the attendance of non-members with relevant experience and expertise if it considers this necessary, normally in consultation with the designated officer and/or chairman of the governing body. However, it may not incur direct expenditure in this respect in excess of £xx, without the prior approval of the governing body.

8. The audit committee may review the draft annual financial statements. Where reviewed, the committee should consider the external audit opinion, the statement of members' responsibilities, the corporate governance statement and any relevant issue raised in the external auditor's management letter. The committee should, where appropriate, confirm with the internal and external auditors that the effectiveness of the internal control system has been reviewed, and comment on this in its annual report to the governing body.

Duties

9. The duties of the committee shall be:

a. To advise the governing body on the appointment of the external auditors, the audit fee, the provision of any non-audit services by the external auditors and any questions of resignation or dismissal of the external auditors.

b. To discuss if necessary with the external auditors, before the audit begins, the nature and scope of the audit.

c. To discuss with the external auditors problems and reservations arising from the interim and final audits, including a review of the management letter incorporating management responses, and any other matters the external auditors may wish to discuss (in the absence of management where necessary).

d. To consider and advise the governing body on the appointment and terms of engagement of the internal audit service (and the head of internal audit, if applicable), the

audit fee, the provision of any non-audit services by the internal auditors and any questions of resignation or dismissal of the internal auditors.

e. To review the internal auditors' audit needs assessment and the audit plan; to consider major findings of internal audit investigations and management's response; and promote co-ordination between the internal and external auditors. The committee will ensure that the resources made available for internal audit are sufficient to meet the institution's needs (or make a recommendation to the governing body as appropriate).

f. To keep under review the effectiveness of internal control and risk management systems, and in particular to review the external auditors' management letter, the internal auditors' annual report, and management responses.

g. To monitor the implementation of agreed audit-based recommendations, from whatever source.

h. To ensure that all significant losses have been properly investigated and that the internal and external auditors, and where appropriate the HEFCE Accounting Officer, have been informed.

i. To oversee the institution's policy on fraud and irregularity, including being notified of any action taken under that policy.

j. To satisfy itself that satisfactory arrangements are in place to promote economy, efficiency and effectiveness.

k. To receive any relevant reports from the National Audit Office, the HEFCE and other organisations.

l. To monitor annually the performance and effectiveness of external and internal auditors, and to make recommendations to the governing body concerning their reappointment, where appropriate.

m. To consider elements of the annual financial statements in the presence of the external auditor, including the auditor's formal opinion, the statement of members' responsibilities and any corporate governance statement. This responsibility should be extended to include consideration of internal control and risk management statements. This is in line with the 2000 Accounts Direction, which includes a phased timetable leading to the adoption of internal control and risk management statements from 2002-03.

Reporting procedures

10. The minutes (or a report) of meetings of the committee will be circulated to all members of the governing body.

11. The committee will prepare an annual report for the institution's financial year. The report will be addressed to the governing body and designated officer, summarising the activity for the year. It will give the committee's opinion on the extent to which the governing body may rely on the internal control and risk management system and the arrangements for securing economy, efficiency and effectiveness. (This opinion should be based upon the information presented to the committee). The audit committee annual report should normally be submitted to the governing body before the members' responsibility statement in the annual financial statements is signed.

Clerking arrangements

12. The clerk to the audit committee will be the clerk to the governing body (or other appropriate independent individual).

Annex C

Procedures for external testing of external and internal audit

Introduction

1. External testing can be conducted in a number of ways. The most common method is a full tendering exercise. This should be considered for the provision of all external audit services, although it may depend on the institution's financial regulations. Guidance on how such an exercise could be conducted is set out below. However, institutions may find it appropriate to develop alternative models, for example comparison of current costs and coverage with that provided to a number of similar institutions. Whatever approach is adopted it should be fair, reasonable and well documented. The frequency of such testing is a matter for individual institutions, but it should normally take place at least every seven years. Institutions may contact the HEFCEAS for advice on all aspects of external testing.

2. However external testing is undertaken and whatever the result, no partner in a firm of auditors should be responsible for an institution's external audit for more than seven continuous years. After that period, the partner concerned should not resume responsibility for the external audit of the institution for five years.

3. External testing should be conducted in accordance with an institution's own purchasing procedures. European Community procurement requirements should be taken into account where the likely audit and related fees over the proposed contract period exceed the relevant threshold. External testing should take place as far in advance of the start date of the contract as possible, to provide continuity of service and so that the new auditors have enough time to prepare properly.

Tendering procedures

4. The audit committee should establish an evaluation committee which could consist of members of the governing body, management and representatives of the audit committee. This committee should agree on its selection criteria and the scope of the audit work required, and identify suitable providers. This should normally include the institution's present auditor. Information should be sought on each provider's track record and relevant experience. Factors such as the size, location and nature of the audit should be taken into account when the audit committee decides which providers to invite. The tender documentation could include or refer to the proposed terms of reference the institution will find acceptable. For external audit this will normally be based on the model letter of engagement shown at Annex F. For internal audit this will normally be based on the model terms of reference shown at Annex D. Providers should be asked to indicate what material changes to the model terms they would like the evaluation committee to consider.

5. The evaluation committee should then seek detailed proposals from at least three providers. The proposals should be evaluated using pre-determined assessment criteria.

The evaluation committee should draw up a short-list of at least three candidates and invite each of them to make an oral presentation. The institution may send a copy of their written proposals to the HEFCE Chief Auditor for comments at least two weeks before the interviews. Following the interviews, a recommendation on which provider to accept should be made to the governing body, or the audit committee where it has been given delegated authority in this respect.

6. The provider should be required to:
 - a. Operate in accordance with published audit standards.
 - b. Meet certain quality standards in completing its work.
 - c. Comply with terms of reference approved by the governing body.
 - d. Provide suitably qualified and experienced staff.
 - e. Endeavour to promote continuity of staffing.
 - f. Ensure that the staff employed will receive appropriate training.
 - g. Provide the HEFCEAS with access to relevant working papers and correspondence in accordance with this Audit Code of Practice.
 - h. Set out proposals for liaison with other auditors.
 - i. In respect of internal audit, set out the firm's position on the restriction of liability. Where a restriction is sought, the level should be stated, together with the firm's explanation of why liability should be restricted and why the level proposed is both reasonable and appropriate. When comparing different proposals, the institution's evaluation committee should take account of any differences in liability restriction. In particular, this evaluation should consider the risks and likely consequences of any loss suffered as a result of negligence, the level of professional indemnity held, and the wider interest of the institution's responsibility for public funds, as described in the Financial Memorandum with the HEFCE. See also paragraph 103 of this Code.
 - j. For non-statutory audit work conducted by the external auditor, the same principles in sub-paragraph i above should be applied by management and, where an agreement to restrict liability is reached, the governing body should be notified, through the audit committee.

7. The same firm should not normally be appointed as both internal and external auditors because this can lead to a loss of objectivity and independence. Appropriately qualified firms are not, however, disqualified from providing both external and internal audit services. Where adopted, the rationale for such arrangements should be clear, for

example when an institution or the contract value is so small that separation of the roles is impracticable. Where an accountancy firm provides both these services, institutions and their audit committees should ensure that:

- a. The separate roles of internal and external audit are clearly specified.
- b. A clear working relationship is established between the two sets of auditors.
- c. Provision of the services is the responsibility of different staff, particularly the partner and manager.
- d. Internal audit files remain the property of the institution.
- e. Internal audit files will be passed on if there is a change in auditors.

Qualifications of external providers

8. The provider should ideally be able to demonstrate a record in providing audit services which goes wider than HEFCE sector institutions. It should not be assumed that audit firms are qualified to provide internal audit services simply because they undertake external audit, or vice-versa. Auditors should normally be registered by an appropriate professional body.

Change of external provider

9. When any appointment is agreed by the governing body, institutions should inform the HEFCE Chief Auditor of their selection and provide a statement outlining the procedure adopted in making appointments.

Annex D

Internal audit service: model terms of reference

1. The internal audit service is responsible for providing an objective and independent appraisal of all the institution's activities, financial and otherwise. It should provide a service to the whole organisation, including the governing body and all levels of management. It is not an extension of, nor a substitute for, good management, although it can have a role in advising management. The internal audit service is responsible for giving assurance to the institution's governing body and designated officer on all control arrangements, including risk management and corporate governance. Internal audit also assists management by evaluating and reporting to them the effectiveness of the controls for which they are responsible. It remains the duty of management, not the internal auditor, to operate an adequate system of internal control and risk management. It is for management to determine whether or not to accept audit recommendations and to recognise and accept the risks of not taking action.

Scope

2. All the institution's activities, funded from whatever source, fall within the remit of the internal audit service. The internal audit service will consider the adequacy of controls necessary to secure propriety, economy, efficiency and effectiveness in all areas. It will seek to confirm that management have taken the necessary steps to achieve these objectives and manage the associated risks. The scope of internal audit work should cover all operational and management controls and should not be restricted to the audit of systems and controls necessary to form an opinion on the financial statements. This does not imply that all systems will be subject to review, but that all will be included in the audit risk assessment and hence considered for review following the assessment of risk. It follows that if internal audit is to give an opinion on the whole system then that will include academic operations. The role of internal audit in this area is to confirm that there are adequate systems for the management of teaching and learning and research. For example, internal audit could confirm that the examination system is operating effectively and meeting its objectives, but this does not mean that internal audit should form academic judgements. Similarly, internal audit might review a research grant to ensure that the requirements of the grant have been met, but it should not form a view on the merit of the research undertaken.

3. It is not within the remit of the internal audit service to question the appropriateness of policy decisions. However, internal audit is required to examine the arrangements by which such decisions are made, monitored and reviewed.

4. The internal audit service may also conduct any special reviews requested by the governing body, audit committee or designated officer, provided such reviews do not compromise its objectivity or independence, or achievement of the approved audit plan.

Responsibilities

5. The head of the internal audit service is required to give an annual opinion to the governing body and designated officer, through the audit committee, on the adequacy and effectiveness of the whole internal control and risk management system within the institution, and the extent to which the governing body can rely on it. He or she should also comment on other activities for which the governing body is responsible, and to which the internal audit service has access. The head of the internal audit service should give an opinion on whether the control arrangements, including those for economy, efficiency and effectiveness, are adequate and properly applied.

6. To provide the required assurance, the internal audit service will undertake a programme of work, based on a strategy authorised by the governing body on the advice of the audit committee. The programme will evaluate the arrangements in place:

- a. To establish and monitor the achievement of organisational objectives.
- b. To identify, assess and manage risks to those objectives.
- c. To advise on, formulate and evaluate policy within the responsibilities of the designated officer.
- d. To ensure compliance with policies, laws and regulations.
- e. To ascertain the integrity and reliability of financial and other information provided to management and stakeholders, including that used in decision making.
- f. To ascertain that systems of control are laid down and operate to promote the economic, efficient and effective use of resources and to safeguard assets.

Standards and approach

7. The internal audit service's work will be performed with due professional care, in accordance with appropriate professional auditing practice. It will have regard to the HM Treasury Standards and will comply with the HEFCE Audit Code of Practice.

8. In achieving its objectives the internal audit service should develop and implement an audit strategy that assesses the institution's risk management and control arrangements.

Independence

9. The internal audit service has no executive role, nor does it have any responsibility for the development, implementation or operation of systems. However, it may provide independent and objective advice on control, risk management and related matters,

subject to resource constraints. For day to day administrative purposes only, the head of internal audit should report to a senior officer within the institution, such as the institution's clerk or secretary. (The reporting arrangements should take account of the nature of audit work undertaken.) The head of internal audit shall have right of access to the designated officer.

10. Within the institution, responsibility for internal control and risk management rests with the governing body and management, who should ensure that appropriate and adequate arrangements exist without reliance on the institution's internal audit service. To preserve the objectivity and impartiality of the internal auditors' professional judgement, responsibility for implementing audit recommendations rests with management.

Access

11. The internal audit service has rights of access to all the institution's records, information and assets which it considers necessary to fulfil its responsibilities. Rights of access to other bodies funded by the institution should be set out in the conditions of funding. The head of internal audit has a right of direct access to the chairman of the governing body, the chairman of the audit committee and the designated officer. In turn, the internal audit service agrees to comply with any requests from the external auditors and the HEFCEAS for access to any information, files or working papers obtained or prepared during audit work that they need to discharge their responsibilities.

Reporting

12. The head of the internal audit service must submit an annual report to the governing body and designated officer through the audit committee, based on the institution's financial year. This should give an opinion on the whole framework of internal control, including risk management and governance at the institution, and on the arrangements for securing economy, efficiency and effectiveness. The auditor should also prepare, before the beginning of the year, a long-term strategy document supported by an assessment of resource needs, and an annual audit plan. These should be submitted to the governing body for approval following consultation with relevant managers and the designated officer, and after consideration by the audit committee.

13. The head of the internal audit service is accountable to the designated officer and the governing body through the audit committee for the performance of the service. He or she should also report audit findings to relevant managers (including the designated officer) and draw the attention of the audit committee to key issues and recommendations. This may be done by providing the committee with copies of all reports, or by reporting on an exception basis, or by providing a summary of key issues.

14. The internal audit service should usually produce its reports, in writing, within one month of completing each audit, giving an opinion on the system reviewed and making recommendations to improve systems where appropriate. Such reports should be copied

to the designated officer and may be copied to the audit committee. Managers will be required to respond to each audit report, usually within one month of issue, stating their proposed action with a timetable for implementing agreed recommendations. Material recommendations will usually be followed up some six to twelve months later. In addition the audit committee will monitor the implementation of audit recommendations.

15. The head of the internal audit service should report to the designated officer any serious weaknesses, significant fraud or major accounting breakdown discovered during the normal course of audit work. If the designated officer refuses to report the matter to the HEFCE Accounting Officer, the chairman of the audit committee and the chairman of the governing body, then the auditor must report to them directly.

Standards

16. The operation and conduct of the internal audit service should conform to the standards in HM Treasury Standards. Internal auditors should also have regard to advice provided by professional auditing and accountancy bodies, and any guidance produced by the HEFCE.

17. The head of internal audit should implement measures to monitor the effectiveness of the service and compliance with standards. In addition, the audit committee should consider and approve the performance measures used by internal audit, and should also consider asking the external auditor to provide an independent assessment of internal audit's effectiveness.

Liaison

18. The internal audit service will liaise with the external auditors and the HEFCE Audit Service to enhance the level of service it provides to the institution.

Annex E

Internal audit planning

1. The work of the internal audit service should be planned at each level of operation. The head of internal audit should prepare plans to carry out the responsibilities of the internal audit unit, for approval by the governing body on the advice of the audit committee.

Principles

2. Systematic planning helps an internal audit unit to achieve its objectives, and helps those with responsibility for reviewing the plans. Plans should be based on the terms of reference for the internal audit service approved by the governing body on the advice of the audit committee. The audit strategy should:

- a. Be developed to meet the needs of the institution using the institution's objectives and risk assessment as a primary resource.
- b. Include provision for the internal auditors to assess the adequacy of the institution's risk assessment.

Include a systematic and prioritised review of how effectively the organisation's risks are managed.

Consider the internal auditor's assessment of major risks even if particular risks are not included or prioritised in management's risk assessment.

Establish the resources and skills necessary to undertake the work necessary.

Describe the audit approach and techniques necessary to meet the audit objectives.

Set out the allocation of resources between audit and advisory work.

4. Plans should be aimed at implementing the audit strategy. For practical purposes, the plans will be expressed in periodic terms, usually an annual plan. The emphasis of audit plans will change from time to time. This may result from, for example, changes in the services provided or in institutional priorities. Plans should be sufficiently flexible and have adequate provision for contingencies to allow prompt response to unscheduled work.

Audit work plans

5. Work plans should be prepared in advance for every audit and should include objectives, resources, locations, timetables, methods, procedures, supervision, reporting and other relevant factors. Audit work within assignments should be tailored to address areas of greatest perceived risk.

Annex F

Model terms of engagement for external auditors

The HEFCEAS should be notified of any material difference between this model letter and the auditor's letter.

To the members of the governing body of

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Appointment and qualification

1. As appointed auditors of we agree to the following basis on which we shall perform our duties.
2. We understand that the governing body (*this will require modification where the governing body does not appoint the auditor*) will assess the auditors' work in each year and undertake a detailed review of the appointment at least every seven years. Remuneration will be fixed by the governing body on the advice of the audit committee.
3. We confirm that we are qualified as auditors in accordance with the meaning of the Companies Act 1985.

Responsibilities of the institution

4. We recognise that the governing body is responsible on behalf of the institution for:
 - a. Establishing and maintaining a system of controls, financial and otherwise, in order to carry on the operation of the institution in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure, as far as possible, the completeness and accuracy of the records.
 - b. Preparing financial statements that:
 - i. Comply with the institution's charter and statutes, all statutory requirements relating to the institution's financial affairs, the Financial Memorandum (dated) with the Higher Education Funding Council for England (HEFCE), any requirements of the Learning and Skills Council or the Teacher Training Agency (*if appropriate*), and other regulations relating to the constitution and activities of the institution and which are relevant to its financial affairs.
 - ii. Show a true and fair view of the state of the institution's affairs at 31 July, and of the cashflows and income and expenditure for the year then ended, taking into account where relevant and appropriate all required statutory and other disclosure requirements

and the Statement of Recommended Practice (SORP) on Accounting for Further and Higher Education Institutions.

- c. Preparing the Finance Record (or its successor) in accordance with instructions from the Higher Education Statistics Agency (HESA).

Standards of audit

5. We will undertake the audit of the institution's financial statements and such other matters as the governing body requires in accordance with auditing standards, having regard to relevant Auditing Guidelines and Auditing Standards issued by the Auditing Standards Board.

Reporting

6. We as auditors:

- a. Are responsible for making a report to the governing body on the financial statements which are to be laid before the governing body during our tenure of office.

- b. May be required to provide an audit report on the HESA Finance Record (or its successor) which should be consistent with our audit report on the institution's financial statements.

7. Our report will state whether in our opinion the financial statements show a true and fair view of the institution's affairs at 31 July, and of the cashflow and income and expenditure for the year then ended.

8. In arriving at our opinion we are required to consider the following matters and to report on any aspect where we are not satisfied, namely whether:

- a. Proper records are being kept by the institution.

- b. The financial statements agree with the accounting records.

- c. We have obtained all the information and explanations we think are necessary for the purpose of our audit.

- d. The financial statements comply with the Companies Act 1985 (where the institution is incorporated under the Companies Act) and, where appropriate, with the Statement of Recommended Practice on Accounting in Higher Education Institutions (SORP) or other legislative or regulatory requirements.

9. We will also report to the governing body whether, in all material respects, monies expended out of all non-recurrent grants and other funds from whatever source,

administered by the institution for specific purposes, have been properly applied to those purposes and, if appropriate, managed in compliance with any relevant legislation.

10. We have agreed with the institution the wording of an unqualified audit report at the time of our appointment. Any subsequent modifications or qualifications will then be based on our professional judgement, but comply with the Auditing Practices Board (APB) Auditing Standard: Audit Reports on Financial Statements (May 1993).

11. We undertake to report to the governing body (by way of a management letter which should be forwarded to the HEFCEAS by 28 February the following year), any significant matters arising from the audit which might lead to material errors or have impact on future audits. This could include areas where economies could be made or resources could be used more effectively, with advice for improvement. The management letter could include:

- a. Weaknesses in the structure of accounting systems and internal control.
- b. Deficiencies in the operation of accounting systems and internal control, including internal audit.
- c. Inappropriate accounting practices and regulations.
- d. Non-compliance with legislation, accounting standards, Funding Council requirements or other regulations.

Irregularities including fraud

12. The governing body is responsible for ensuring the establishment and maintenance of an adequate system of internal control. It is also responsible for ensuring compliance with statutory, taxation and other regulations, and for the prevention and detection of irregularities, including fraud. We are not required to search specifically for such matters and our audit should not therefore be relied on to disclose them. However, we shall plan and conduct our audit so that we have a reasonable expectation of detecting material mis-statements in the accounts resulting from irregularities, including fraud, or breach of regulations.

13. We will report in writing any serious weaknesses, fraud, irregularities or accounting breakdowns we come across in the normal course of our duties to the designated officer, and, where the designated officer refuses to make a report, to the governing body and to the HEFCE's Accounting Officer without delay.

Other work

14. We may be asked from time to time to provide additional services beyond the scope of the audit described above. This could involve investigation work and value for money reviews. Precise requirements will be agreed between the governing body and

ourselves in a separate engagement letter before any work is undertaken. Any systems development or consultancy work will be the responsibility of separate staff.

Access

15. We shall have rights of access at all times to the books, accounts and vouchers of the institution and to such information and explanations as we think necessary to perform our duties. We also expect to have access to internal audit files and working papers. We, in turn, agree to comply with any requests from the internal auditors and the HEFCE Audit Service for access to any information, files or working papers obtained or prepared during our audit that they need to discharge their responsibilities. The HEFCEAS will exchange letters where necessary with both parties which deal with confidentiality and the terms under which access is given.

16. We shall have the right of access to the chairman of the audit committee, the right to ask the chairman to convene a meeting of the audit committee if necessary, and the right to attend audit committee meetings where relevant business is to be discussed.

Annual meetings

17. We will be entitled to attend the meeting of the governing body to which the institution's annual reports and financial statements of account are presented. We will also be entitled to receive all notices of and other communications relating to that meeting which any member of the governing body is entitled to receive, and to be heard at any such meeting, on any part of the business which concerns us as auditors.

Termination of appointment

18. We understand that if there are serious shortcomings on our part the governing body may pass a resolution to remove us before the expiry of our term of office, notwithstanding any agreement between us and the institution.

Fees

19. *[A paragraph setting out the auditor's terms for charging and collecting fees should be included.]*

Other terms

20. *[Auditors may include certain additional paragraphs for internal purposes, for example on confidentiality, conflicts of interest, quality of service, complaints procedure and legal jurisdiction.]*

Agreement of terms

21. If the contents of this letter are not in accordance with your understanding of the arrangements made, we shall be pleased to receive your observations and to give you any further information you require. Otherwise we shall be grateful if you would confirm in writing your agreement to the terms of this letter by signing the enclosed copy and returning it to us. Once agreed, this letter will remain effective from one audit appointment to another until it is replaced.

Yours sincerely

[Signed by auditors]

On behalf of the governing body of, I confirm that the above terms are satisfactory.

Signed

Position

Date

Annex G

External audit report: suggested wording

The suggested form of the wording of the unqualified report (if appropriate) should be:

REPORT OF THE INDEPENDENT AUDITORS TO THE GOVERNING BODY OF

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We have audited the financial statements on pages to which have been prepared under the historical cost convention (as modified by the revaluation of certain fixed assets) and in accordance with the accounting policies set out on pages to

Respective responsibilities of the governing body and auditors

As described on page, the governing body is responsible for preparing the financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board and the Audit Code of Practice issued by the HEFCE. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the governing body in the preparation of the financial statements, and of whether the accounting policies are appropriate to the institution's [group's] circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material mis-statement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- i. The financial statements give a true and fair view of the state of affairs of the institution [and the group (*if appropriate*)] at 31 July 20xx, and of the surplus of income over expenditure, recognised gains and losses and cashflows of the institution [and the group (*include where the institution is incorporated under the Companies Act*)] for the year then ended and have been properly prepared in accordance with [the Companies Act

(include where the institution is incorporated under the Companies Act) and] the Statement of Recommended Practice on Accounting in Higher Education Institutions.

ii. Income from the Higher Education Funding Council for England, [the Learning and Skills Council and the Teacher Training Agency (*if appropriate*)] grants and income for specific purposes and from other restricted funds administered by the institution have been applied only for the purposes for which they were received.

iii. Income has been applied in accordance with the institution's statutes (or equivalent) and where appropriate in accordance with the Financial Memorandum with the Higher Education Funding Council for England.

Annex H

Audit committee annual report: model format

The Audit Code of Practice requires each institution's audit committee to prepare an annual report for submission to its own governing body (the internal audit annual report should be attached). The annual report should be prepared as early as possible in each year with the aim of it being available by the time the annual financial statements are signed. The report should be signed and dated by the chairman of the committee.

Paragraphs 59-60 of this Code give the core information suitable for the report. This model, used with discretion, suggests what a comprehensive report could contain (as appropriate).

Title	Full name of institution, Audit Committee Annual Report, year (<i>for example, 2001-02</i>). Addressed to governing body and designated officer.
Intro-duction	Period covered; this should specifically relate to the audit committee's work on the financial year when the work was carried out. However, any additional information should be given where appropriate, for example where the previous year's annual report could not include something due to timing, or something has occurred which requires special treatment.
Member-ship	Names; details of changes and dates thereof; terms of office; identify chairman; also separately give details of the clerk to the committee.
Meetings	Dates of meetings and who attended if useful or appropriate.
Terms of reference	If applicable, details of changes and their effect on the work of the committee.
Internal audit	<ul style="list-style-type: none"> • Name of provider; details of any changes made or due; fee basis; audit committee's assessment of performance for the year (including the use of performance measures and obtaining the views of the external auditor). • Review of appointment; when market testing is due for consideration. • Review of the internal audit annual report (which may be attached to the audit committee annual report); achievement of planned work; consideration of and comment on overall internal auditor's opinion on internal control system as necessary. • Review of audit needs assessment, strategic plan and annual plan as appropriate. Number of audit days last year/next year (compare); inclusion of value for money studies. Details of any restrictions placed on the work of the internal auditor. • Review of (planned) audit reports; title and brief details of coverage if applicable; audit committee's view of management responses to the findings and recommendations; details of any significant recommendations outstanding. • Review of unplanned or special reports; title and brief details of coverage if applicable; audit committee's view of management responses to the findings and recommendations; details of any significant recommendations outstanding. • Review of value for money studies; summary of important findings and recommendations.
External audit	<ul style="list-style-type: none"> • Name of provider; details of any changes made or due; fee basis; audit committee's assessment of performance for the year (for example, audit planning, timetable set and met); confirmation to governing body of recommendation of annual reappointment (or defer this to next meeting); when market testing is due for consideration. • Review of the external auditor's management letter (draft and final versions where appropriate); significant points arising; audit committee's view of management responses to the findings and recommendations.

Other work done	<p>Where undertaken, review of specific parts of the annual accounts (preferably between finance committee and the board/council) including members' responsibility and corporate governance statements, any relevant issue raised in the management letter and the external auditor's formal annual opinion.</p> <p>Review of the risk management strategy of the institution.</p> <p>Other work, including Funding Council reports, letters and other requirements (such as the HEFCE Audit Service report, student number audit if undertaken, value for money (VFM) studies; Audit Code of Practice review/changes); special reports or investigations arising not dealt with elsewhere (for example on fraud or irregularity); review of relevant NAO and other reports; other formal certificates or returns seen; review of Financial Regulations including amendments, communication or recommendations made; issues arising on trusts, joint ventures, subsidiary or associated companies; other VFM work such as a review of VFM strategy. Recommendations made not dealt with elsewhere.</p>
Other	<p>Issues not relevant to the reporting year, such as forthcoming events and issues relating to prior years.</p>
Opinion	<p>The audit committee's opinion on the extent to which reliance can be placed on the internal control and risk management systems at the institution and an opinion on the arrangements for securing economy, efficiency and effectiveness. (These opinions should be based upon the information presented to the committee.) The committee should consider whether those governing body's responsibilities, which are described in the members' responsibility statement in the annual accounts, have been satisfactorily discharged. Consider separate corporate governance statement where one is provided, including, from 2002-03 the statement on the effectiveness of the internal control and risk management systems and any audit report on that statement.</p>
Circulation	<p>Copy to the HEFCE Audit Service once approved by the governing body.</p>

See also Annex I

Annex I

Annual audit return from institutions

To be submitted with audit committee annual report.

This return is designed to act as a reminder to designated officers of the returns and information to be supplied under the Financial Memorandum and Audit Code of Practice and to seek other information that can inform the HEFCEAS risk assessment. In order to minimise the frequency of HEFCE audit work, this return is necessary to demonstrate continuing contact with institutions. HEFCE auditors will respond to each institution, on an annual basis, by providing the designated officer with an annual audit summary that demonstrates the HEFCEAS risk assessment of the institution. The assessment is based on any audit work undertaken in the year and on returns and information supplied by the institution.

Institution	
Period	
Return completed by (name of designated officer)	
Have you submitted the audit and other returns to the HEFCE as required under the Financial Memorandum and Audit Code of Practice including the financial statements, external audit management letter and internal audit annual report?	
Have there been any changes of senior postholder in the period, such as the designated officer or deputy, or finance director or other head of service? (If so, please provide details.)	
Has there been a change of external auditor in the period? (If so please provide details.)	
If your internal audit is provided under contract, has there been a change of provider, partner or manager in the period? (If so please provide details.)	
If your internal audit is provided in-house, has there been a change of head of internal audit in the period? (If so please provide details.)	
Was the internal audit plan for the period completed? (If not please give details.)	

Has there been a change of chair of the governing body?	
Have there been any changes to the membership of the audit committee?	
Has the audit committee been quorate throughout the year?	
Have you completed a review of institutional and/or governance effectiveness during this period? (See the Report of the National Committee of Inquiry into HE – the Dearing Report.) If so, please forward a copy of the report or action plan.	
Have you completed a review of effective financial management in this period (See HEFCE 98/29)? If so, could you advise us of the outcome or provide a copy of the report or action plan.	
Have there been any confirmed instances of fraud or impropriety that should have been notified as required under the Audit Code (Annex A)?	
Can you confirm that the requirements of the Financial Memorandum have been satisfied during the year, including that: <ul style="list-style-type: none"> • public funds have been applied for the purposes intended • there is a sound system of internal control • the institution remains solvent • the institution has complied with borrowing requirements • value for money has been pursued. 	

Signed.....

Dated.....

List of abbreviations

APB	Auditing Practices Board
APNs	Audit Practice Notes
CIPFA	Chartered Institute of Public Finance and Accountancy
CRSA	Control and risk self-assessment
CSA	Control self-assessment
DEL	Department for Employment and Learning in Northern Ireland
DfES	Department for Education and Skills
HE	Higher education
HEFCE	Higher Education Funding Council for England
HEFCEAS	HEFCE's Audit Service
HEI	Higher education institution
HESA	Higher Education Statistics Agency
ICAEW	Institute of Chartered Accountants in England and Wales
LSC	Learning and Skills Council
NAO	National Audit Office
SORP	Statement of Recommended Practice
The Code	HEFCE Audit Code of Practice
TTA	Teacher Training Agency
VFM	Value for money