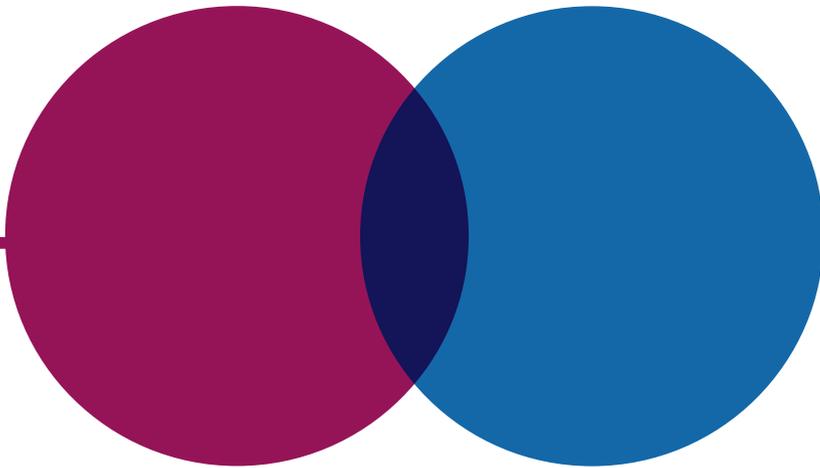




National Audit Office



Regulating the financial sustainability of higher education providers in England

Department for Education and
Office for Students

REPORT

**by the Comptroller
and Auditor General**

SESSION 2021-22

9 MARCH 2022

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Regulating the financial sustainability of higher education providers in England

**Department for Education and
Office for Students**

Report by the Comptroller and Auditor General

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to be printed on 7 March 2022

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Commons in accordance with Section 9 of the Act

**Gareth Davies
Comptroller and Auditor General
National Audit Office**

2 March 2022

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Key facts

2.3m

students attending higher education providers in England, excluding those in further education and sixth-form colleges

32%

of providers with an in-year deficit, excluding accounting adjustments for pension revaluations and provisions, in 2019/20

10

providers subject to enhanced monitoring by the Office for Students (the OfS), as at December 2021, because of heightened risk to their financial sustainability

- 254** higher education providers in England, excluding further education and sixth-form colleges, registered with the OfS in July 2021
- £36.1 billion** total income of higher education providers in 2019/20, of which 36% came from public sources
- 64** providers out of 247 (26%) forecast at the end of 2020/21 that their cash balance would fall below 30 days' net liquidity at some point in the next two years
- 33%** students viewing their course as providing good value for money in 2021, with 54% saying it was not good value for money
- £27.7 million** running costs of the OfS in 2020-21, mainly funded by registration fees paid by providers
- £2.8 billion** aggregate net in-year deficit for higher education providers in 2019/20 on a full economic cost basis, taking into account all the direct and indirect costs of sustaining their activities

Throughout this report, government financial years are written as, for example, '2020-21' and run from 1 April to 31 March; higher education sector academic and financial years are written as '2020/21' and run from 1 August to 31 July.

Summary

Introduction

1 Universities, and other higher education providers, are autonomous institutions with a high degree of financial as well as academic independence. They are free to conduct commercial activities in addition to teaching and research. For a provider to access government funding for research or teaching, however, or for its students to receive government tuition fee and maintenance loans, it must be registered by the Office for Students (the OfS), the sector regulator. The OfS is sponsored by the Department for Education (the Department).

2 In July 2021, there were 254 higher education providers in England registered with the OfS, excluding further education and sixth-form colleges, educating an estimated 2.3 million students. Of these, 1.8 million were from the UK, and 1.6 million were undergraduates. Some providers are also ‘anchor institutions’ with a significant influence within their local economies and communities. The total income of higher education providers in 2019/20 was £36.1 billion, 36% of which came from public sources.

3 The OfS has very broad objectives: to help students access higher education; ensure they have a high-quality experience of higher education; protect their interests while they study; make sure they can progress to employment or further study; and ensure they receive value for money. Should higher education providers become financially unsustainable or unviable, students would be adversely affected in all these areas. Financial pressure could increase the risk of providers failing, closing campuses or courses, reducing the quality of teaching, or limiting access.

4 This is our first report on the OfS, which began operating in 2018. Having spent its first year registering providers, it became fully operational as a regulator in August 2019. It was therefore still a relatively new body when the COVID-19 pandemic began in early 2020. Risks to the financial sustainability of higher education providers were already increasing, and the pandemic added major disruption and new risks to the sector – and consequent additional challenges to the OfS.

5 Our report focuses on the OfS’s responsibilities to protect students’ interests from the consequences of financial risk in higher education providers. We have not looked at the OfS’s other responsibilities for matters such as teaching quality. As the OfS is a young organisation we reviewed its performance with a view to identifying areas where it should focus as it continues to mature.

Key findings

Financial risk in the higher education sector

6 The proportion of providers with an in-year deficit, even after adjusting for the impact of pension deficits, increased from 5% in 2015/16 to 32% in 2019/20. Reported results for some providers over recent years have appeared volatile because they include large one-off accounting adjustments caused by revaluations in pension scheme liabilities – especially in respect of the Universities Superannuation Scheme, which has a large deficit. Excluding these adjustments to show a more consistent view of underlying trends, the proportion of providers with an in-year deficit has increased year on year. The number with an in-year deficit of 5% or more of income has also grown each year, from one out of 133 (1%) in 2015/16 to 37 out of 244 (15%) in 2019/20. Reporting a deficit in any one year is not necessarily evidence of underlying financial problems in an individual provider. However, of the 80 providers with an in-year deficit in 2019/20, 20 had been in deficit for at least three years. Although the population of providers has changed over time, in particular with the registration of many smaller providers, the recent trend of rising in-year deficits also applies to providers for which there are continuous data over the whole period from 2015/16. The OfS reported in July 2021 that 133 higher education providers in England, together with two in Northern Ireland, had an aggregate in-year deficit of £2.8 billion for 2019/20 on a full economic cost basis, taking into account all the indirect as well as direct costs of sustaining their activity – double the deficit of £1.4 billion reported in 2018/19 (paragraphs 1.12, 2.2, 2.4 and 2.8, and Figure 4).

7 Financial stress is not confined to one part of the sector. Higher education providers are a very diverse group, with different business models and financial performance reflecting wide variations in their numbers and type of students, size and sources of income and extent of research activity. The size of a provider, its entry requirements or whether it is a specialist institution, for example, are not predictors of financial strength. The 20 providers that have had an in-year deficit for at least three years range in size from 200 students to more than 30,000 (paragraphs 2.3 and 2.4).

8 The number of providers of all types that appear to be facing short-term risks to their financial sustainability and viability is small but not insignificant. The OfS uses liquidity (a measure of a provider's ability to continue to pay its bills) as an indicator of the risk of a provider failing. The OfS does not apply rigid targets, but it normally engages with providers if their liquidity falls below 30 days' expenditure. There is more variation within groups of otherwise similar providers than between these groups. During 2020/21, 33 out of 247 providers (13%) had forecast liquidity below 30 days – including at least one from each group (paragraph 2.4 and Figure 6).

9 Short-term financial risks are dominated by COVID-19, but medium- and long-term risks are systemic. The COVID-19 pandemic created immediate risks that providers would lose income from a potential fall in international student fees, and also from conferences, accommodation and research. At the same time, they had to invest in new ways of teaching. Providers still also face the systemic risks that existed before COVID-19. Valuations of pension schemes (particularly the Universities Superannuation Scheme) indicate that higher employer contributions will be needed. Publicly funded teaching and research make a loss across the sector once the full economic costs of those activities are taken into account. This makes the financial viability of some providers highly dependent on cross-subsidy, primarily from fees paid by international students. For most providers, the cost of research activity also exceeds the value of research grants. The OfS's own assessments have highlighted that many providers' medium- and long-term financial forecasts depend on assumed continued growth in overseas as well as domestic student numbers. The OfS has questioned whether it is realistic for all providers to be making similar assumptions in a competitive market (paragraphs 1.12, 2.6 to 2.11, 4.13 and 4.18, and Figure 8).

Effective regulation of financial sustainability

10 The OfS has adopted a deliberately data-led approach to regulation.

The OfS collects the same base set of detailed annual financial and performance data from all regulated providers. It also places a responsibility on providers to report events such as breach of conditions associated with loans or credit facilities (banking covenants), changes to teaching provision, or other events that might increase financial risk. The OfS relies on these data to identify providers for further scrutiny (paragraphs 3.8 to 3.10).

11 The OfS makes good use of the financial data it collects, analysing it in a systematic and structured way to identify providers for closer scrutiny. In this way, during 2021 it identified some 98 out of 245 providers (40%) for detailed review of their financial viability and sustainability. As part of its risk-based approach to regulation, the OfS applies a degree of judgement in setting the level of risk it is prepared to tolerate, reflecting its estimate that it does not have the resources to examine all providers in detail. The level of financial risk in providers the OfS accepts is, therefore, influenced by resource constraints as well as its perception of the potential impact on students. The OfS links the outcome of its financial analysis with other information it holds on providers. It seeks further information from providers where it has identified concerns about their financial sustainability. The OfS could usefully explore how it can use insights from its increased engagement with providers during the COVID-19 pandemic to supplement its existing knowledge of their business models. The OfS has undertaken some financial analysis and scenario modelling of key risks but does not yet have an integrated model to bring together and assess the impacts of ongoing, multiple and systemic risks to financial sustainability, carry out sensitivity analysis or test scenarios. It told us that it is planning to develop such a model – and that this work will in future help inform its assessment of risk in individual providers (paragraphs 3.6, 3.10 and 3.13 to 3.18).

12 As at December 2021, the OfS had made 10 providers subject to enhanced monitoring because of concerns about increased risk to their financial viability. It was also engaging with a further 13 providers to understand their level of risk. The OfS's interventions for financial viability and sustainability are based on its assessment of risk in individual providers. It has a range of regulatory responses available, including enhanced monitoring (that could include, for example, requiring additional information from the provider), imposing specific conditions, monetary penalties, and suspending or removing a provider's registration altogether (paragraphs 3.9, 3.14, 3.17 and 3.19).

13 The Department and the OfS have not yet been successful in achieving a good understanding among providers of why the OfS collects all the data it does, and how it uses it. The OfS collects the same data from all regulated bodies on the grounds that doing so allows it to apply consistent principles to identify risk, and therefore target interventions only where needed. It uses this information in support of its statutory functions to monitor and report on the financial sustainability of the sector as a whole, and to monitor (and, if necessary, intervene) in relation to financial viability and sustainability risks in individual providers. Some of the stakeholders and providers we spoke to, on the other hand, were critical of what they perceived as a 'one-size-fits-all' approach to data collection – and the corresponding regulatory burden – rather than a more tailored approach (paragraphs 3.9, and 3.11 to 3.13).

14 There is more the OfS could do to help the sector and other stakeholders understand its regulatory approach. Giving stakeholders clarity over the fundamental aim and means of regulation helps ensure a shared understanding of its purpose and intended outcomes. The OfS aims to be a principles-based regulator, which means it focuses on the outcomes it wants providers to achieve without prescribing how they should do so. The OfS relies heavily, although not exclusively, on financial metrics to identify risks to providers' financial sustainability and has designed a regulatory approach that does not involve routine discussion with individual providers. The sector bodies and providers that we spoke to told us that the OfS did not routinely speak with most providers, leading them to doubt whether the OfS had all the information needed to put financial data into context. The OfS told us it considered it had engaged with providers sufficiently to understand risks to their financial sustainability. Early in the COVID-19 pandemic, the OfS spoke to most providers to understand how they were responding to new pandemic-related risks. This engagement was well received in the sector and was an effective way to quickly understand emerging financial risks (paragraphs 3.4 to 3.6).

15 The Department responded to new financial challenges for providers during the COVID-19 pandemic by enhancing the role of the cross-government higher education financial sustainability oversight group. The Department has a coordinating role as the chair of the higher education financial sustainability oversight group – a cross-government group of officials from the Department, the Department for Business, Energy & Industrial Strategy (BEIS), UK Research and Innovation, and the OfS. During the pandemic, the group was strengthened by bringing in a representative from HM Treasury, given its interest in financial support measures that were being considered. The group does not have access to all the commercially sensitive provider-level data available to the OfS, and it provided a practical way to coordinate government intervention to support the sector during the pandemic (paragraph 3.24).

16 The OfS does not yet have a complete and transparent set of performance measures to demonstrate its own performance as a regulator. The OfS sets out on its website the measures against which it intends to assess how well it is performing its regulatory functions and whether it is delivering value for money. Out of 26 indicators, eight are still in development or have incomplete performance information, and a further 11 indicators do not yet have associated targets (paragraphs 1.10 and 3.25).

17 The OfS does not routinely ask providers and sector stakeholders for feedback on its own performance as a regulator. The Department, as primary sponsor of the OfS, holds quarterly performance reviews with the OfS's leaders. The Department maintains, and discusses with the OfS, a risk assessment of potential threats to the OfS's effective performance of its functions. Although the OfS consults widely on changes to the regulatory framework, it has no routine mechanism (for example, through a survey) to gain structured feedback from providers on its own performance (paragraphs 3.5 and 3.6).

Consequences for students and providers

18 The OfS lacks a strong measure with which to judge the value for money students get from their courses. The OfS routinely collects students' views on, for example, the quality of teaching and learning they are experiencing, and their perception of the value for money of their degree. It carries out an annual National Student Survey but, because it is open to final-year students only, it will not have captured the views of all students, particularly first-year undergraduates who are most likely to have been affected by the closure of university accommodation during the COVID-19 pandemic. In a separate survey in February/March 2021, 33% of undergraduates said they thought university offered good value for money and 54% thought it did not. The OfS does not attempt to define value for money, on the grounds that it may mean different things to different people or may change over time. The OfS argues that it seeks to track perceptions over time but, without a consistent definition, it lacks a strong measure with which to judge value for money (paragraphs 4.6 to 4.8).

19 The OfS found during the COVID-19 pandemic that it needed stronger powers of intervention to protect students' education when a provider is at material risk of market exit. The OfS requires all higher education providers to have in place a student protection plan that the OfS has approved as appropriate for the level of risk presented by the provider and for the risk to continuity of study for all its students. No student protection plan has ever had to be implemented at short notice. During the COVID-19 pandemic, however, the OfS identified that there were common weaknesses in student protection plans – including providers being over-optimistic about the risks they faced, lack of detail about what specific actions providers would take, and weak refund and compensation policies. The OfS implemented a new condition of registration, effective from 1 April 2021, giving it additional powers to direct providers it considers at material risk of market exit to implement specific measures to protect students (paragraphs 4.2 to 4.5).

20 Some providers would likely have faced financial difficulty had they been required to refund tuition fees. Student satisfaction fell sharply between 2020 and 2021, when pandemic lockdown measures were in place. The proportion of students viewing their course as good value for money also fell, from 38% in 2020 to 33% in 2021. The government's position was not to support tuition fee refunds. One of the smaller providers we spoke to told us that, had government applied more pressure to offer significant fee refunds, this would have caused it, and likely some similar providers, to fail (paragraphs 4.7, 4.8 and 4.20).

21 Higher education providers proved more resilient during the COVID-19 pandemic than government had feared. The Department's early modelling in May 2020 estimated that the adverse impact of COVID-19 on the sector could range between £3.9 billion and £22.3 billion, with a central estimate of a £13.9 billion loss in 2020/21. Providers were able, for example, to draw on their reserves or use commercial credit facilities to maintain cashflow, and some deferred capital spending plans. Importantly, income from overseas students' fees was maintained – there were 17% more non-EU students in 2020/21 than in 2019/20. Because of genuine concern at the beginning of the pandemic, however, that falling income could make providers unviable, the Department and BEIS both put in place measures to provide emergency support:

- **The Department accelerated payment of student fees to providers.** Providers were able to access £2.6 billion in the first term of the 2020/21 academic year that would normally have been paid later in the year.
- **The Department announced in July 2020 a restructuring regime to prevent chaotic market exit.** The scheme provided time-limited access to support and emergency funding and was intended as an intervention to be used in the last resort. The Department told us that it received 18 enquiries from providers, of which three had applied to the regime.
- **BEIS announced a 'research stabilisation package' intended to maintain UK research capacity.** Early modelling by BEIS, in May 2020, estimated that the extent of reliance on cross-subsidy for research income was £4.3 billion in 2018-19, and that some £3.0 billion could be at risk. The stabilisation package included £200 million in new government investment, and redistribution of £80 million of existing funding. BEIS also made available a package of loans and grants designed to make up for losses in international student numbers. Demand for that additional support was lower than forecast – BEIS provided funding to five applicants, totalling £21.4 million in loans and £298,000 grant funding (paragraphs 4.10 to 4.14 and 4.17).

22 A-level grade inflation distorted the higher education market and increased financial risk for some providers. The adoption of centre-assessed grades in place of examinations in summer 2020 caused significant grade inflation, making more students eligible for places at their first-choice provider and on high-tariff courses. As a result, some high-tariff universities were oversubscribed, and lower-tariff universities undersubscribed. Further grade inflation in summer 2021 compounded the situation. This has caused challenges for both oversubscribed and undersubscribed universities and increased financial risk for some providers in the medium as well as the short term. The Department anticipated that some high-cost courses would become oversubscribed and provided additional revenue and capital funding to support providers to increase capacity. The Department did not model or draw insights from the OfS to understand in advance the potential financial consequences on undersubscribed providers, despite the potential impacts being foreseeable (paragraphs 4.21 to 4.28).

Conclusion on value for money

23 The financial sustainability of higher education providers can have a profound impact on the quality and value for money of education for two million students every year. The current regulatory system, with the OfS at its heart, was established to protect the interests of students. So far, the OfS's regulatory approach has not witnessed any provider failures, but rising numbers of providers in deficit indicate increased financial pressure in the sector. At this early stage in its development as a regulator the OfS has had to adapt to the challenges of the COVID-19 pandemic, during which students' satisfaction with the value for money of their university education fell sharply. Its heavily data-driven approach to assessing financial risk does not yet have the full confidence of all providers.

24 To protect students' and taxpayers' interests adequately, the Department and the OfS should now reflect on the lessons that can be learned from good-practice principles of effective regulation. Implementing these will strengthen the OfS's understanding of the risks that pressures on the financial sustainability of providers pose for students. It will also build higher education providers' confidence in the OfS as a regulator, and better equip it to deal with sustained and increasing risks to providers' financial sustainability.

Recommendations

- 25** The Department should:
- a** **review, improve and agree with the OfS the key performance measures and other indicators it uses to hold the OfS to account**, to include measures of the impact of the regulatory regime, rather than measures outside the OfS's control;
 - b** **make clear what tolerance the government has for provider failure, and the circumstances under which it would or would not intervene**; and
 - c** together with the OfS, **assess how redistribution of student numbers between providers, as a result of higher A-level grades awarded in 2020 and 2021, has affected students' experiences and providers' finances**, and draw on this to understand the likely consequences following release of A-level grades awarded in 2022.
- 26** The OfS should:
- d** **communicate more effectively with the sector to build trust in its approach as a regulator**; improve providers' understanding of its attitude to risk and how it defines risk-based, proportionate, regulation; and be more ready to share sector insights to improve efficiency and competitiveness in the sector;
 - e** **set out how it will secure provider and stakeholder views of its work**;
 - f** **review, improve where necessary and then reauthorise student protection plans for all providers** to ensure they remain adequate and can respond to new risks; and
 - g** **prioritise finalising its key performance indicator on how it assesses the value for money students see in their education and set out how its work will reverse students' declining satisfaction rates.**

Part One

The higher education sector

1.1 This part of the report:

- gives an overview of the higher education sector;
- outlines the regulatory system government has put in place to oversee risks to students' and taxpayers' interests, should higher education providers become financially unviable; and
- explains how higher education providers are funded.

Higher education providers' status

1.2 Higher education providers are defined in the Higher Education and Research Act 2017, and the Education Reform Act 1988. They provide courses of a standard higher than A level, including certificates, diplomas, first degrees and postgraduate degrees. Slightly more than half (57%) have the power to award degrees. Institutions without degree-awarding powers of their own may run courses leading to degrees validated and awarded by providers with that power. Providers range from 'traditional' universities to more commercially focused private companies. They vary hugely in size and complexity – the smallest have fewer than 100 students. Others are part of larger commercial entities or have subsidiaries including international operations.

1.3 Higher education providers are autonomous institutions with a high degree of financial as well as academic independence and are free to conduct commercial activities in addition to teaching and research. If, however, a provider wishes to apply for government funding for research or teaching, or it wants its students to be able to apply for government tuition fee and maintenance loans and visas to study in the UK (if needed), it must be registered by the Office for Students (the OfS), the sector regulator.

1.4 To register, providers need to satisfy a number of conditions set by the OfS. These conditions cover: access and participation; academic quality and standards; student protection; financial sustainability; governance; information for students; and accountability for fees and funding. Some conditions need to be met at the time of registration and, together with additional ongoing conditions, must continue to be met. The OfS's oversight of financial sustainability is intended to protect students in the event that a provider becomes unviable or is unable to provide the course that students have paid for.

1.5 The size and shape of the regulated higher education sector has changed. In 2015/16, 133 providers were registered with the previous regulator, most of which were 'traditional' universities. In addition, private providers, which tended to be small and/or specialist in nature, could apply to the then Department for Business, Innovation & Skills to have their courses 'designated' so that their students could access student support. The OfS is now the regulator for all these providers. In July 2021, it was responsible for oversight of the financial sustainability and viability of 254 higher education providers in England educating an estimated 2.3 million students, including 1.8 million from the UK, and 1.6 million undergraduates.¹ There were also some 166 further education and sixth-form colleges registered with the OfS. Because the OfS relies on the work of the Education and Skills Funding Agency to regulate these bodies' financial sustainability, we have excluded them from the scope of this study.²

1 Student numbers are sourced from the Higher Education Statistics Authority's *Higher Education Student Statistics 2020/21*, which count what it describes as the number of 'instances' of each student being enrolled on a higher education course. This gives a good indication of the actual number of students because it counts part-time students as individual 'instances' rather than converting to full-time equivalent numbers. There may, however, be more than one instance per student in a provider's data, where, for example, a student terminates participation on one course then engages on another in the same academic year.

2 We have reported separately on the financial sustainability of further education and sixth-form colleges: Comptroller and Auditor General, *Financial sustainability of colleges in England*, Session 2019–2021, HC 728, National Audit Office, September 2020.

1.6 The total income of higher education providers in 2019/20 was £36.1 billion, 36% of which came from public sources. There is also, therefore, a risk to taxpayers' money should providers become financially unsustainable. For example, students at a failing provider may not complete their courses, making it less likely they will be able to pay back student loans; or there may be costs to the taxpayer arising from providers exiting the market. In addition, students may receive poor value for money as a result of actions to make savings or cut costs taken by providers that are under financial stress.

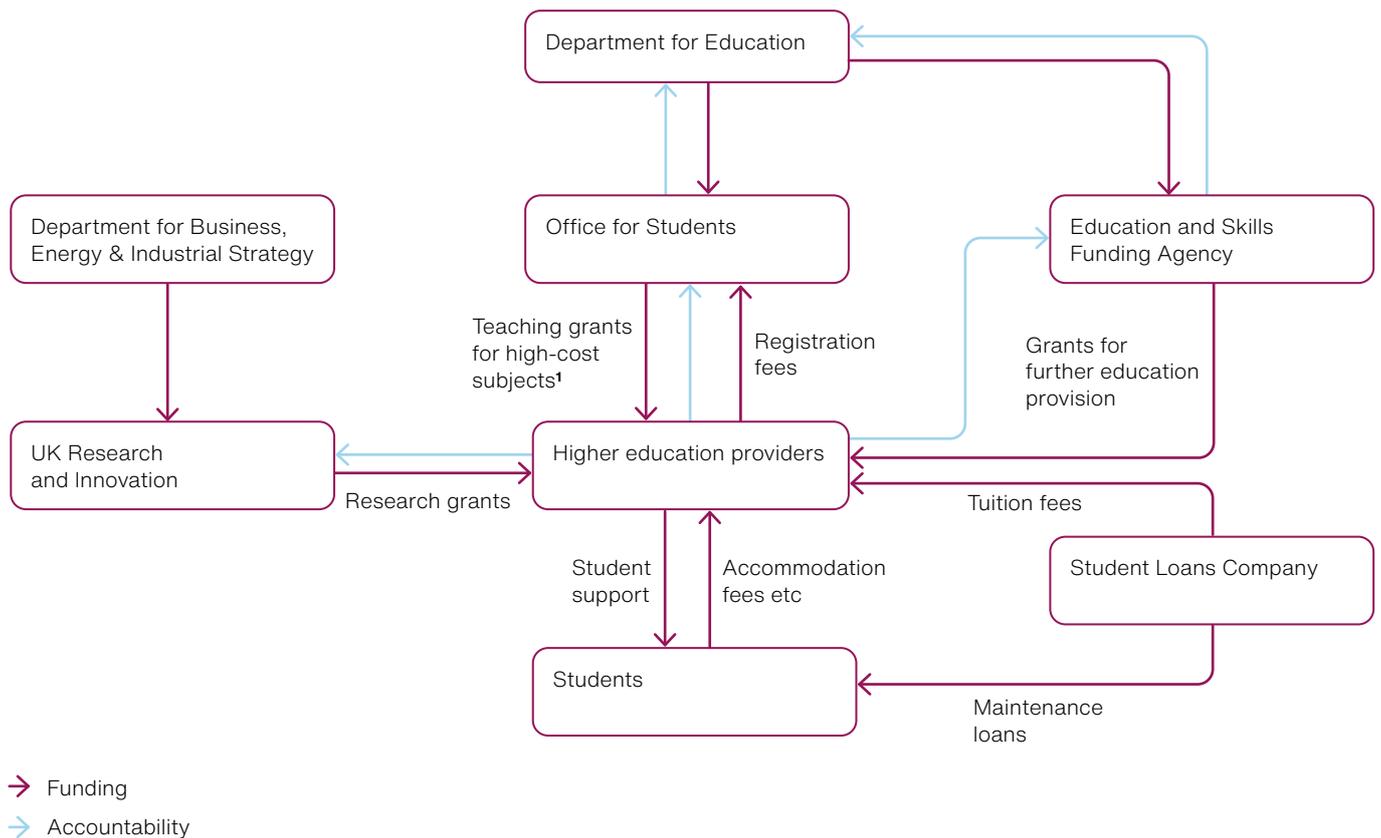
Oversight and regulation of higher education providers

1.7 The overall oversight framework within which higher education providers operate includes a number of public bodies (**Figure 1**). Those with responsibilities most relevant to financial sustainability issues are the Department for Education (the Department) and, to a lesser extent, the Department for Business, Energy & Industrial Strategy (BEIS), but primarily the OfS.

1.8 The Department is responsible for setting higher education policy and for the overall regulatory framework for the sector. It obtains assurance about the sector, including about providers' financial viability and sustainability, through the OfS's regulatory activities. BEIS is responsible for the public funding of higher education providers' research activities, which it administers through Research England and research councils, all part of UK Research and Innovation.

Figure 1
Overview of higher education funding and accountability

The overall oversight framework within which higher education providers operate includes a number of public bodies



Note

1 The Strategic Priorities Grant (formerly the Teaching Grant) is distributed by the Office for Students in accordance with guidance issued by the Secretary of State for Education. It is used to: support high-cost subjects considered strategically important for the economy and labour markets; support small and specialist providers; support disadvantaged and under-represented students; and fund support to mitigate student hardship and mental health issues.

The Office for Students

1.9 The OfS was established under the Higher Education and Research Act 2017, which sets out its functions, duties and powers. It began operating in 2018 and took on its full regulatory powers in August 2019. The OfS exists to ensure that English higher education is delivering positive outcomes for students – past, present and future. Its framework document, drawn up by the Department in consultation with the OfS, sets out its purpose as the independent regulator of higher education in England, with a commitment to efficient and effective regulation.³ Its four regulatory objectives are that all students, from all backgrounds, and with the ability and desire to undertake higher education:

- are supported to access, succeed in, and progress from, higher education;
- receive a high-quality academic experience, and their interests are protected while they study or in the event of provider, campus, or course closure;
- are able to progress into employment or further study and their qualifications hold their value over time; and
- receive value for money.

1.10 The OfS's running costs in 2020-21 were £27.7 million, of which £26.3 million (95%) was funded by registration fees paid by providers. Fee levels are split into bands based on providers' student numbers. In addition, the OfS distributes grant funding from the Department to providers – around £1.5 billion in 2020-21 – mostly in the form of recurrent teaching grants. The OfS has a fifth strategic objective, relating to its own performance, to be an efficient and effective regulator.

3 Department for Education, Office for Students, *Office for Students Framework Document*, October 2019.

Funding for higher education in England

1.11 Higher education providers are financed from a number of public and private sources (**Figure 2** overleaf):

- Tuition fees and education contracts, consisting largely of fees paid from student loans, and fee income from overseas students. These make up about half of providers' income (53.7% in 2019/20) across the sector.
- Teaching grants from funding bodies, largely the OfS.
- Research funding from a variety of sources including Research England, research councils, charities, government bodies, local and hospital authorities, and industry.
- Other income sources including accommodation, conferences, endowments and donations.

1.12 Many higher education teaching and research activities do not recover their full economic costs, and cross-subsidy is required for providers to make up for in-year deficits in these areas. Publicly funded teaching and research make a loss across the sector once the full economic costs of those activities are taken into account.⁴ Providers' financial viability depends on subsidising these activities from the surplus from non-publicly funded teaching – primarily fees from international students. In July 2021, the OfS reported an aggregate in-year deficit of £2.8 billion for higher education providers in England and Northern Ireland for 2019/20, compared with a deficit of £1.4 billion in 2018/19. In-year deficits for publicly funded teaching and research increased in 2019/20, but these activities were already loss-making before the pandemic (**Figure 3** on page 21).

1.13 The level of student fees, and the number of students going to university, has a material impact on the sustainability of individual providers and on the sector as a whole. Although student loans are repayable by recipients over a set term (currently 30 years), a proportion of these will not be repaid within this period. This proportion – the net present value of the debt not expected to be repaid – is effectively a public subsidy for higher education, paid for ultimately by the taxpayer. It is not a financial risk for higher education providers. The Department expects 53% of loans issued to full-time undergraduates in 2020-21 not to be paid back.

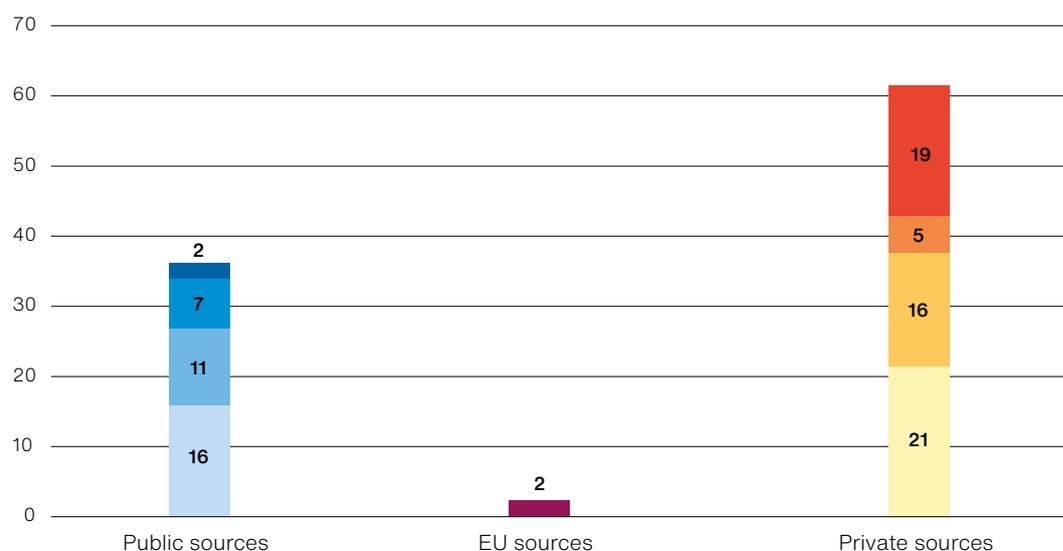
⁴ The Transparent Approach to Costing (TRAC) is the methodology developed with the higher education sector to help them cost their activities. It is an activity-based costing system adapted to academic culture in a way which also meets the needs of the main public funders of higher education. TRAC uses institutional expenditure information from published financial statements and 'cost adjustments' to provide the 'full economic cost' of activities. It therefore encompasses both the direct and indirect costs of activities and an adjustment to the historic expenditure to reflect the full, sustainable costs of the activities. Further information is available at www.trac.ac.uk/about/

Figure 2

Income sources by proportion for the higher education sector, 2019/20

Public sources accounted for 36% of the income of higher education providers

Proportion of total income of higher education providers (%)



	(£bn)	(%)
Public sources		
Other income – government, local authorities, health	0.8	2
Research grants – research councils, government, local and hospital authorities	2.6	7
Funding body grants – Office for Students, Research England	3.9	11
Tuition fees – UK and EU, loan subsidy and other public fees ¹	5.8	16
EU sources		
Research grants and other income – EU, EU-based charities, industry, commerce	0.9	2
Private sources		
Other income – residences, catering, other operating income, donations, endowments, investments	6.7	19
Research grants – charities, industry, other bodies	1.9	5
Tuition fees – non-EU overseas	5.9	16
Tuition fees – UK and EU, loan repaid and other private fees ²	7.7	21
Total	36.1	100

Notes

- 1 The £5.8 billion 'Tuition fees – UK and EU, loan subsidy and other public fees' comprises £4.9 billion fees for UK students, £0.3 billion fees for EU students and £0.5 billion for research training support grants and further education course fees.
- 2 The £7.7 billion 'Tuition fees – UK and EU, loan repaid and other private fees' comprises £6.3 billion fees for UK students, £0.8 billion fees for EU students and £0.6 billion for non-credit-bearing course fees.
- 3 Totals may not sum due to rounding.

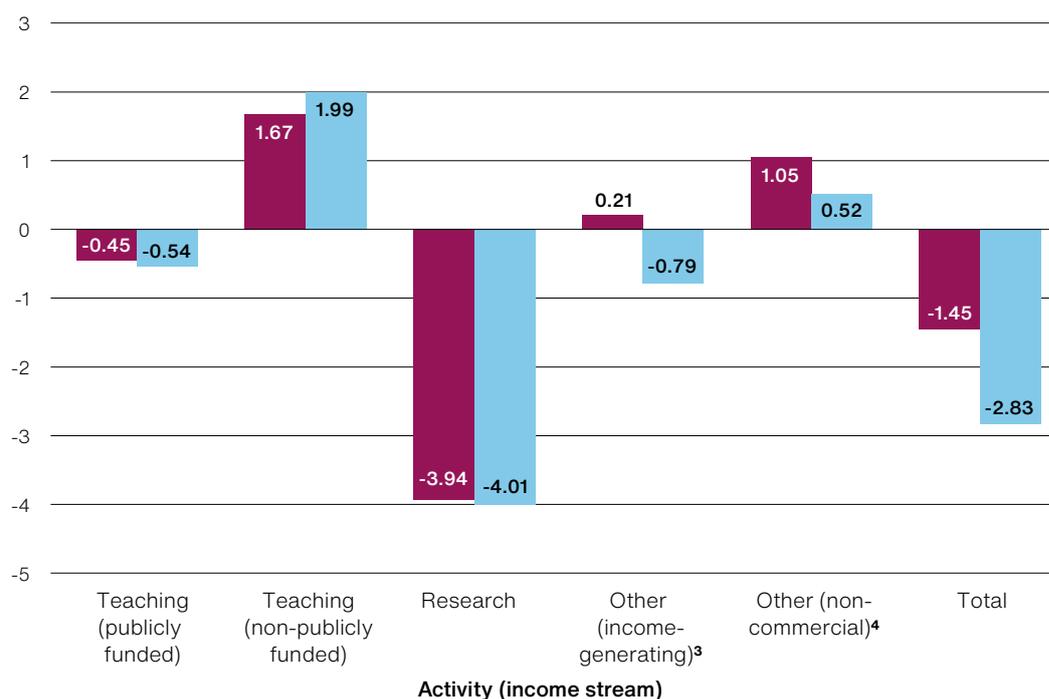
Source: National Audit Office analysis of Higher Education Statistics Agency financial data 2019/20 and Office for Students Annual Financial Return 2020

Figure 3

Income and full economic costs of higher education providers in England and Northern Ireland by activity, 2018/19 and 2019/20

In-year deficits from publicly funded teaching, research and overall activities increased in 2019/20

Profit/loss for each activity (£bn)



■ 2018/19

■ 2019/20

Notes

- 1 Not all higher education providers submit Transparent Approach to Costing (TRAC) data. This figure includes data from 133 providers in England, plus two in Northern Ireland.
- 2 There are different ways to categorise groups of providers with similar characteristics. Different categorisations are appropriate for different purposes. TRAC peer groups, used to collate data for the transparent approach to costing data set, are based on whether an institution has a medical school, its total income, the proportion of income received for research activities, and whether the institution is a specialist provider. These data are the most accessible way to show income and full economic costs by activity.
- 3 'Other (income-generating)' includes: commercial activities such as catering, conferences, commercially let facilities and residences; activities carried out through subsidiary companies such as publishing or commercial consultancy; knowledge transfer activity; and, for institutions with medical and dental schools, services provided to the NHS.
- 4 'Other (non-commercial)' includes activity such as investment and donations or endowments.

Source: Office for Students *Annual TRAC sector summary and analysis by TRAC peer group, 2018/19 and 2019/20*

Part Two

Indicators of financial sustainability

2.1 This part of the report:

- illustrates the extent to which financial risk in higher education providers has grown over the past five years; and
- explores the balance between short-, medium- and long-term risks.

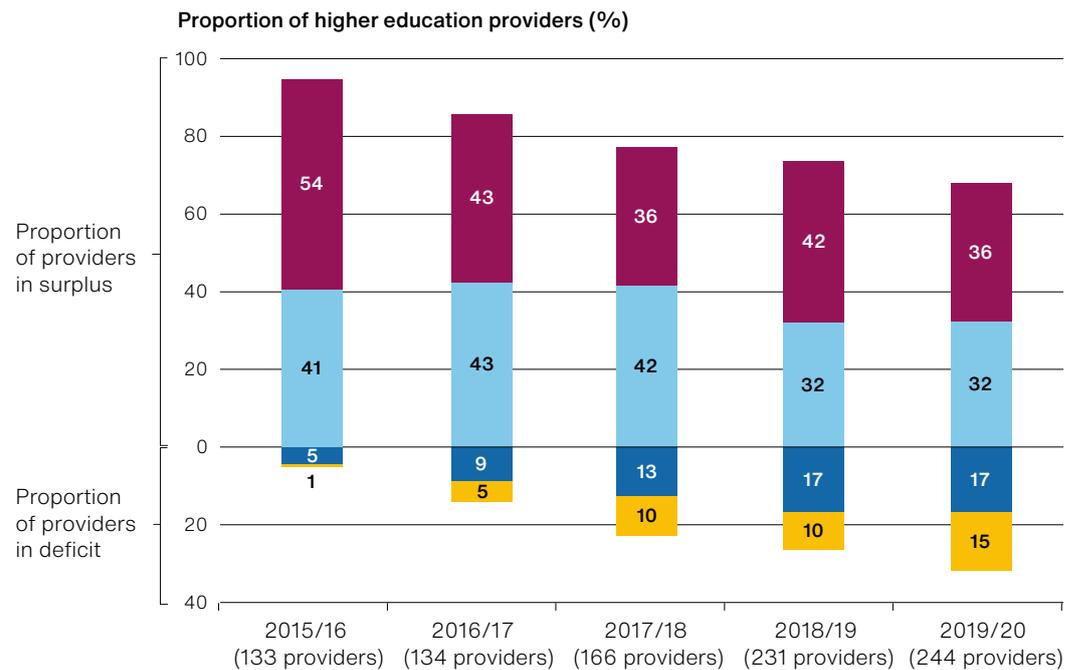
2.2 The number of higher education providers with an in-year deficit increased from seven (5%) in 2015/16 to 80 (32%) in 2019/20. The number with an in-year deficit of 5% of income or more has also grown each year, from one out of 133 (1%) in 2015/16 to 37 out of 244 (15%) in 2019/20 (**Figure 4**). This is an underlying trend which preceded the COVID-19 pandemic and is clear after excluding volatility caused by fluctuations in pension revaluations and changes to provisions. Although the population of providers has changed over time, in particular with the registration of many smaller providers, this trend also applies to the providers for which there are continuous data from 2015/16 to 2019/20. For this group, the proportion of providers with an in-year deficit rose from 5% to 36%, and those in deficit by 5% or more rose from zero to 12% in deficit by 2019/20. Reporting a deficit in any one year is not necessarily evidence of underlying financial problems in an individual provider, as it can be affected by one-off events or accounting adjustments. In 2019/20, however, of the 80 providers with an in-year deficit, 17 had been in deficit for the past two years and a further 20 for three years or more.

2.3 Higher education providers are a very diverse group, with different business models and financial performance reflecting wide variations in their numbers of students, size and sources of income, proportions of international and postgraduate students and extent of research activity. **Figure 5** on page 24 shows that some large institutions, as well as small providers, have an in-year deficit. There are 20 providers that have had an in-year deficit for at least three years, ranging in size from 200 students to more than 30,000.

Figure 4

Proportion of higher education providers with an in-year surplus or deficit (excluding pension provision adjustments), 2015/16 to 2019/20

The proportions of higher education providers with an in-year deficit, and those in deficit by 5% of income or more, have grown each year from 2015/16 to 2019/20



- Surplus equal to or greater than 5% of income
- Surplus equal to or greater than 0% and less than 5% of income
- Deficit greater than 0% and less than 5% of income
- Deficit equal to or greater than 5% of income

Notes

- 1 Data exclude volatility caused by accounting adjustments arising from pension revaluations and changes in provisions.
- 2 Surplus or deficit includes: gains or losses on investments and disposal of assets; shares of surpluses in joint ventures and associates; and taxation.
- 3 This figure excludes two providers for 2018/19 and three providers for 2019/20 reporting no income, for which it is not possible to calculate the surplus/deficit as a percentage of income.

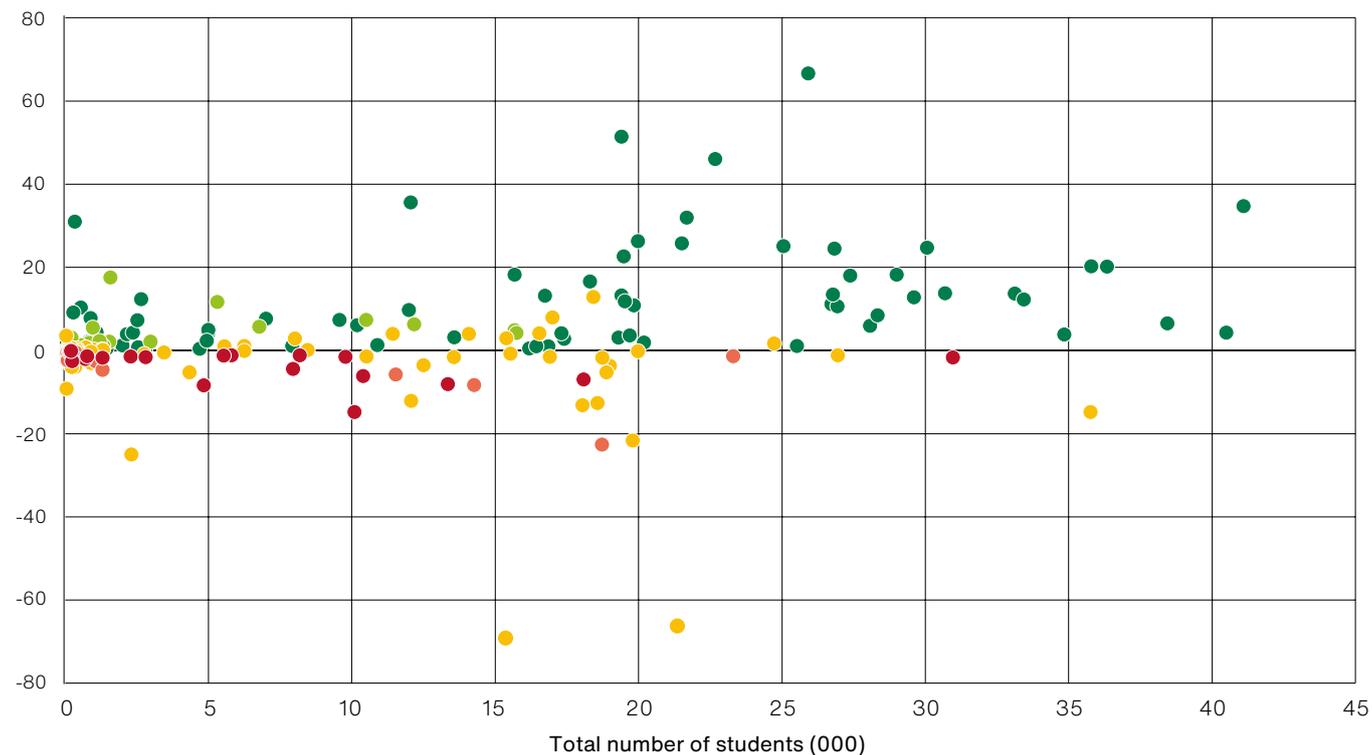
Source: National Audit Office analysis of Higher Education Statistics Agency financial data, 2015/16 to 2019/20

Figure 5

Number of students and in-year surplus or deficit (excluding pension provision adjustment) by higher education provider, 2019/20

There was a wide variation in the size and financial performance of higher education providers

In-year surplus/deficit in 2019/20 (£m)



- In surplus for the past three years or more
- In surplus for the past two years
- Mixed surplus/deficit over the past two years, or data only for one year
- In deficit for the past two years
- In deficit for the past three years or more

Notes

- 1 For ease of display, the Open University (96,560 students) is not shown.
- 2 Data exclude volatility caused by accounting adjustments arising from pension revaluations and changes in provisions.
- 3 Surplus or deficit includes: gains or losses on investments and disposal of assets; shares of surpluses in joint ventures and associates; and taxation.

Source: National Audit Office analysis of Higher Education Statistics Agency financial and student data 2019/20

2.4 A provider having an in-year deficit at any point does not necessarily mean that it is at immediate financial risk. It may, for example, have adequate credit facilities in place, or a temporary deficit. The Office for Students (the OfS) uses liquidity – a cash measure of a provider’s ability to continue to pay its bills – as another indicator of the level of financial risk faced by individual providers.⁵ The OfS does not apply targets, but it normally engages with providers if their liquidity falls below 30 days’ expenditure. On this measure, the risk of provider failure is low for the sector as a whole, but there is substantial variation within tariff groups and a small number of providers in each group that are potentially vulnerable.⁶ In 2020/21, 33 out of 247 providers (13%) had forecast that they would have liquidity below 30 days by the end of the year (**Figure 6** overleaf). There were 64 out of the 247 providers (26%) that forecast their lowest cash balance would be below 30 days’ net liquidity in at least one month during their next two accounting years.

2.5 Deficits and low liquidity may be managed by borrowing, which is another indicator of the level of financial risk that the OfS monitors.⁷ Although 75% of providers had borrowing in 2019/20, this had declined from 92% in 2015/16. The proportion of providers with borrowing exceeding 75% of annual income – a measure, like 30 days’ liquidity, that could indicate financial risk – has remained low during the study period and stood in November 2021 at 4.9% (12 providers), up from 3.8% (five providers) in 2015/16.

Short-, medium- and long-term financial risks

2.6 Financial sustainability depends upon the ability of providers to respond to challenges arising from long-term ongoing factors. These include the health of the UK and international economies, demographic changes, international competition for students and the need to maintain teaching quality, as well as emerging changes to the environment, such as EU Exit and COVID-19.

2.7 Since March 2020, the COVID-19 pandemic has resulted in:

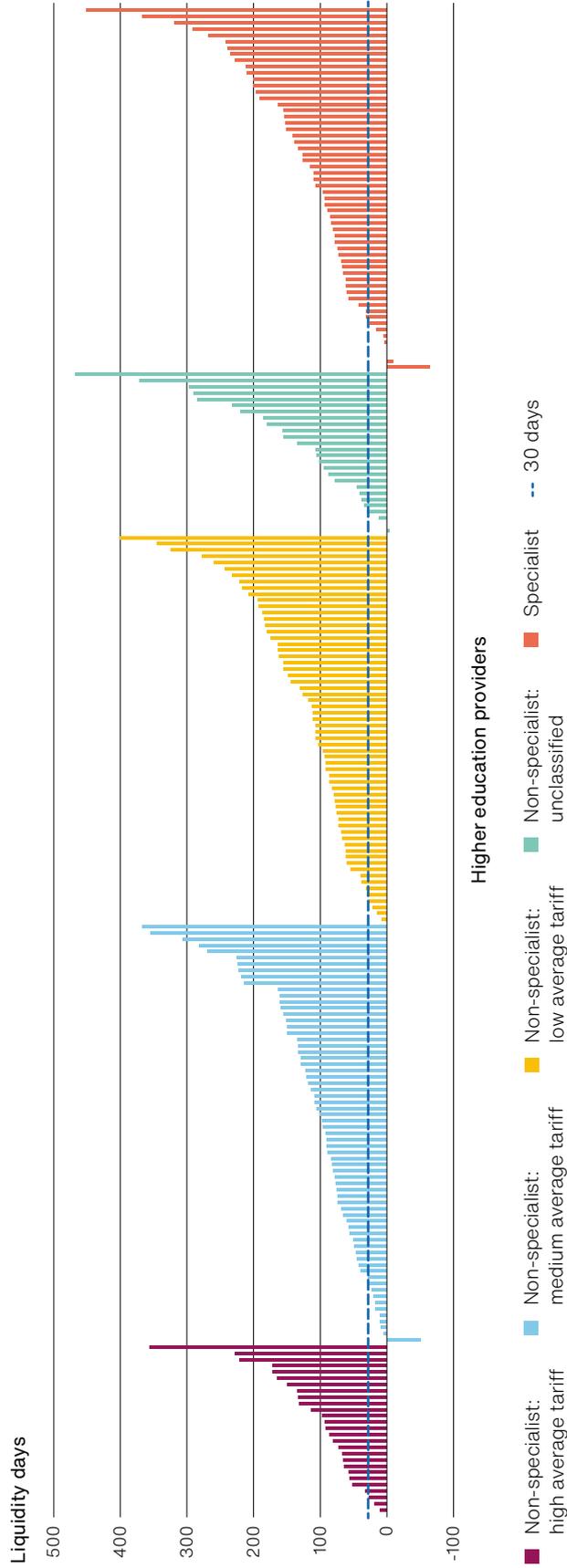
- increased risk of unplanned changes to income from tuition fees arising from deferrals or the impact of travel restrictions on international students;
- unexpected fluctuation in student numbers due to A-level grade inflation;
- disruptions to research funding; and
- reduced income from accommodation and conferences.

5 ‘Liquidity days’ means that, in the unlikely event that all income stopped and all expenditure carried on at the same rate, the provider would be able to rely on their cash reserves to operate for the given number of days.

6 Tariff groups are based on each provider’s entry requirements – the ‘tariff’ refers to the required number of Universities and Colleges Admissions Service (UCAS) points required.

7 In this context the indicator of financial risk related to borrowing is referred to as ‘gearing’ and is the sum of different elements of borrowing as a proportion of annual income.

Figure 6
Higher education providers' forecast liquidity days as at the end of 2020/21, by tariff group
There was substantial variation in liquidity within tariff groups, and a small number of providers in each group were potentially vulnerable



Notes

- 1 'Liquidity days' refers to the number of days from the financial year-end for which a provider is able to meet day-to-day expenses from cash and liquid assets, less overdrafts and debt repayments due within a year.
- 2 Each vertical line in the chart represents an individual provider.
- 3 'Tariff groups are based on each provider's entry requirements – the 'tariff' refers to the number of Universities and Colleges Admissions Service (UCAS) points required.
- 4 This figure shows the forecast position for the end of the 2020/21 financial year (which varies between providers, but is 31 July 2021 for longer-established higher education institutions), as at November 2021.
- 5 This figure includes data for 240 providers. It excludes five providers with liquidity days of more than 500, and two providers with liquidity days of fewer than -100, for ease of display.

Source: National Audit Office analysis of Office for Students (OfS) data on higher education providers' forecasts, and UCAS average tariff data provided by the OfS

2.8 There are also systemic long-term pressures specific to the sector, including increasing costs which are rising faster than income (**Figure 7** overleaf).

- From 2016/17 to 2019/20, income rose by 20.0%, largely due to an increase in student numbers generating greater tuition fee income, despite a freeze in domestic tuition fee levels.
- Over the same period, expenditure rose by 22.2%, and staff costs (54% of expenditure in 2019/20) also rose by 22.2%.⁸

2.9 Many providers' long-term financial forecasts assume continued growth in student numbers. **Figure 8** on page 29 shows that, across the sector as a whole, providers are expecting the number of EU students to continue to fall, but the numbers of domestic and international students to increase every year.

2.10 The viability of some providers depends heavily on income from international students to support the cost of other activities (**Figure 9** on pages 30 and 31). As noted above (paragraph 1.12), most higher education activity is loss-making, once the full economic costs of that activity are taken into account. The most profitable activity by far, generating a near £2 billion surplus across all providers, is teaching international students. The sector is particularly reliant on students from China and India. In 2019-20, more than 340,000 overseas students came from 204 countries worldwide (excluding the EU and UK): 35% of those came from China and 14% from India. We cannot conclude whether universities are right to make these assumptions about continued growth, in a competitive global market.

2.11 When registering providers in its first year of operation, the OfS found many had based their financial viability and sustainability on optimistic forecasts of growth in student numbers without convincing evidence of how this growth would be achieved. The OfS has continued to encourage caution in recruitment forecasts while recognising, in 2021, that providers might feel confident about recruitment over the next few years, for reasons including the expanded use of remote learning, an increase in the number of 18-year-olds and evidence from recent recruitment activity suggesting that strong demand remained from both domestic and international students.

2.12 In February 2022, following the 2019 Augar review, the government announced some higher education reforms and launched a consultation on others.⁹ Uncertainty remains for the sector while the outcome of the consultation is awaited. The consultation includes possible student number controls and the introduction of minimum eligibility requirements to access student finance, which could have implications for providers' assumptions about domestic student recruitment.

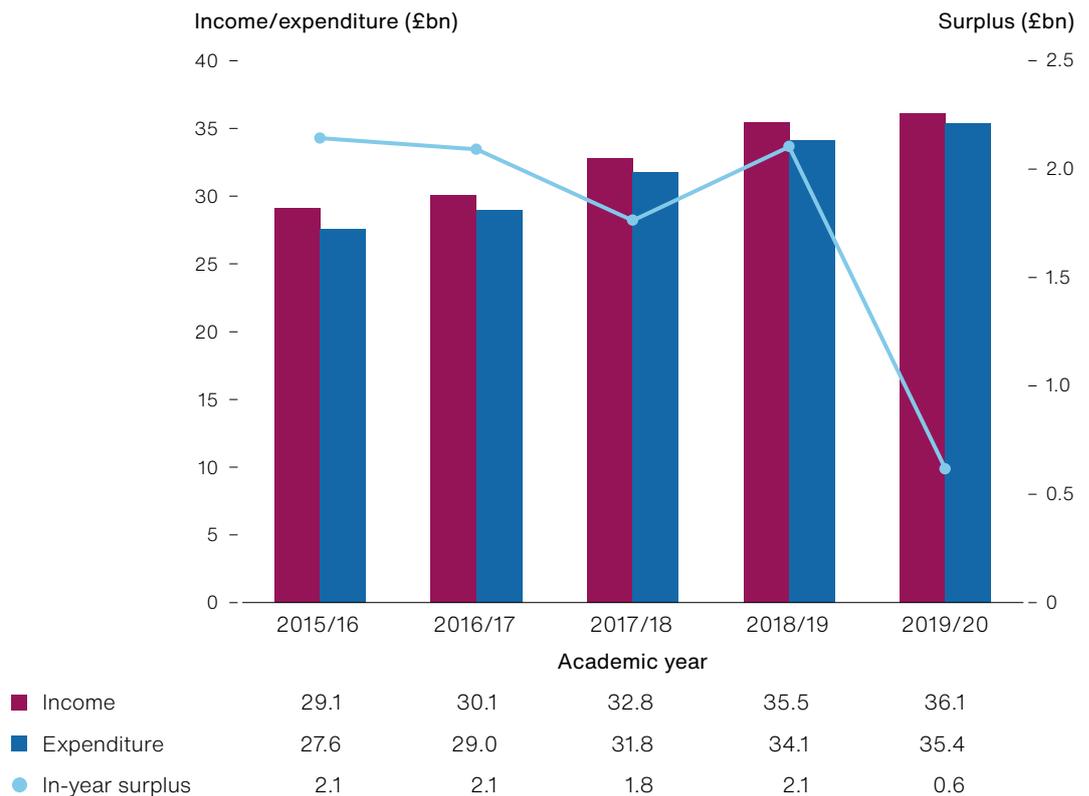
⁸ The population of providers has changed over the period. For providers which were in existence and registered for the whole period from 2016/17 to 2019/20, income rose by 14.5% and expenditure rose by 16.9%. The figure for staff costs excludes accounting adjustments made by providers to account for deficits in staff pension funds. The actuarial valuation of the Universities Superannuation Scheme in 2020 showed a shortfall between assets and liabilities of between £14.9 billion and £17.9 billion. In 2018, the valuation of the shortfall was £3.6 billion.

⁹ Department for Education, *Higher education policy statement and reform*, CP 617, February 2022.

Figure 7

Trends in income and expenditure (excluding pension provision adjustments) for the higher education sector, 2015/16 to 2019/20

At sector level, expenditure has risen at a faster rate than income and the overall in-year surplus is falling

**Notes**

- 1 Valuations of pension schemes (particularly the Universities Superannuation Scheme) indicate that higher employer contributions will be needed although, because valuations change, adjustments to take account of potential future liabilities can make underlying trends less clear. Data shown in this figure exclude volatility caused by accounting adjustments arising from pension revaluations and changes in provisions.
- 2 Surplus or deficit is in-year and includes: gains or losses on investments and disposal of assets; shares of surpluses in joint ventures and associates; and taxation.

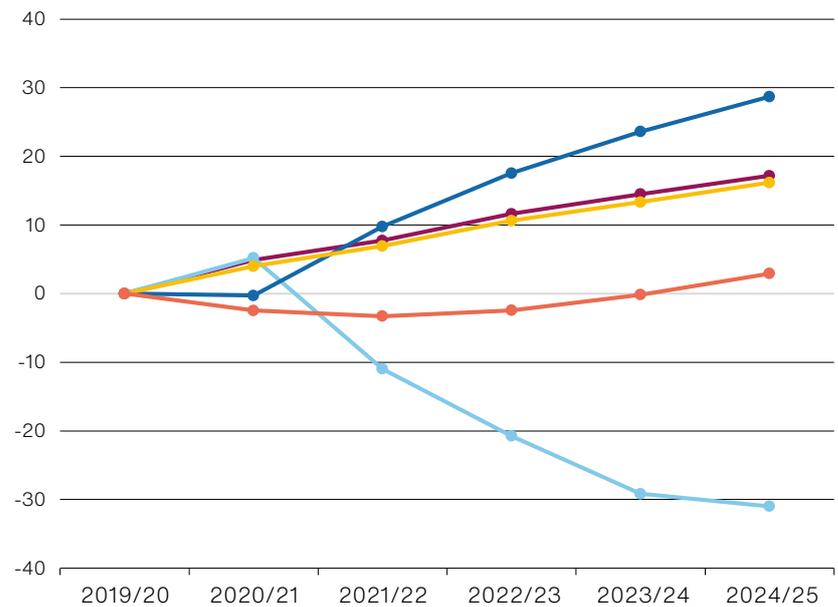
Source: National Audit Office analysis of Higher Education Statistics Agency financial data, 2015/16 to 2019/20

Figure 8

Forecast percentage change in student numbers (full-time equivalent) by domicile, 2019/20 to 2024/25

Providers are forecasting that the number of EU students studying in the UK will continue to fall each year, but that there will be continued increases in the numbers of domestic and non-EU international students

Forecast percentage change in full-time equivalent student numbers compared with 2019/20



	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
● UK students	0	5	8	12	14	17
● EU students	0	5	-11	-21	-29	-31
● Non-EU students	0	0	10	18	24	29
● Total students	0	4	7	11	13	16
● UK population aged 18-20 (projection)	0	-2	-3	-2	0	3

Notes

- 1 Changes to the forecast number of students for each year are shown relative to actual full-time-equivalent numbers in 2019/20 for each group of students, and to the projected UK population for 2019.
- 2 The projected UK population changes are derived from the projections of the population of 18- to 20-year-olds, at mid (calendar) year by age last birthday. In the majority of cases this will be the age at the start or continuation of courses in September or October of that year (so, for example, we have used the population projection for 2019 in relation to the 2019/20 academic year).

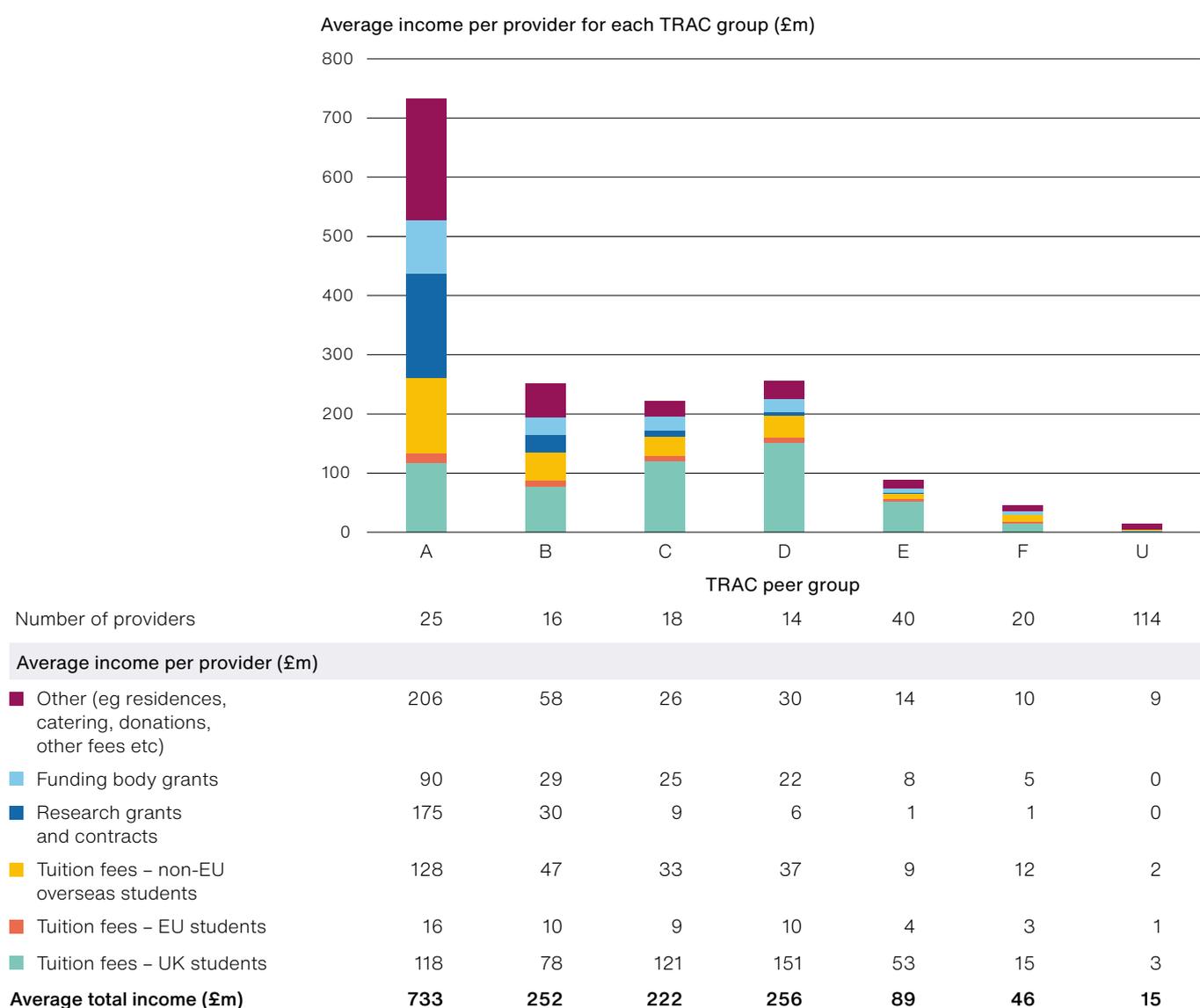
Source: National Audit Office analysis of Office for Students data on higher education providers' forecasts; Office for National Statistics population projections (2018 data files)

Figure 9

Average income of higher education providers and dependencies on different sources by peer group, 2019/20

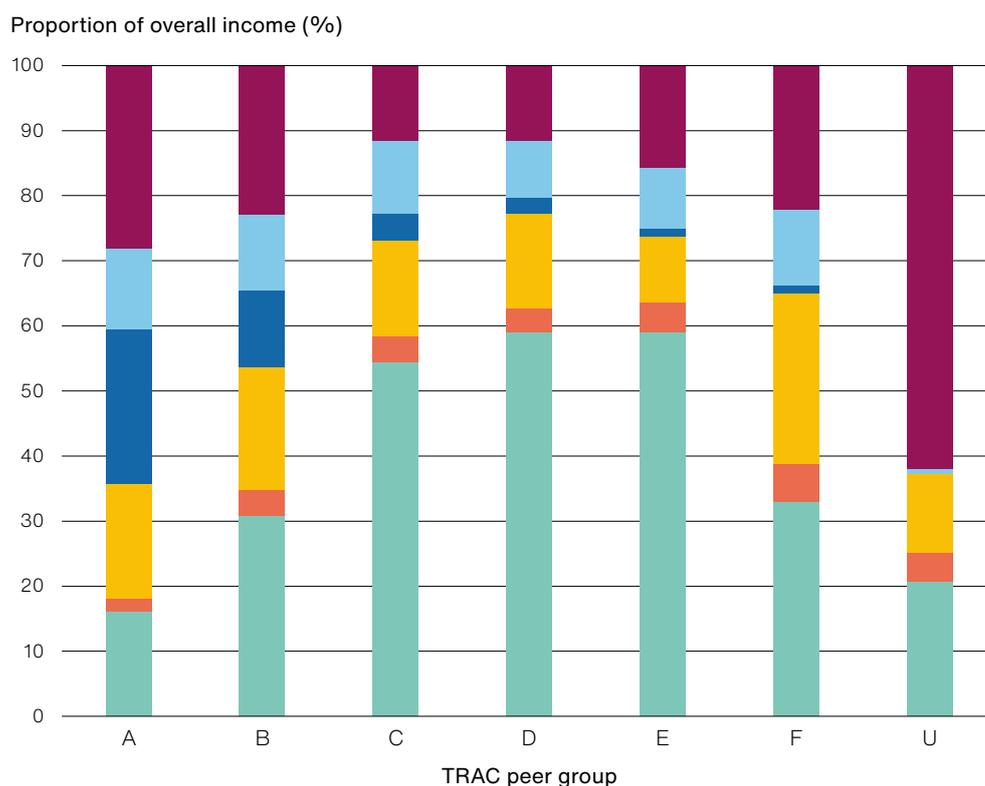
There is a wide variation in sizes and income dependencies of higher education providers

a) Total average income per provider, by income source and Transparent Approach to Costing (TRAC) group

**Notes**

- 1 There are different ways to categorise groups of providers with similar characteristics. Different categorisations are appropriate for different purposes. Transparent Approach to Costing (TRAC) peer groups, used to collate data for the TRAC data set, are based on whether an institution has a medical school, its total income, the proportion of income received for research activities, and whether the institution is a specialist provider. TRAC peer groups are useful to analyse the relative importance of different income sources, as in this figure.
- 2 Not all higher education providers submit TRAC data. This figure includes data from 247 providers.
- 3 The income category 'Other (eg residences, catering, donations, other fees etc)' includes tuition fees for activities other than higher education, for example further education course fees.
- 4 Totals may not sum due to rounding.

Source: National Audit Office analysis of Higher Education Statistics Agency financial data 2019/20, Office for Students Annual Financial Return 2020 and TRAC data

b) Average proportions of income from different sources, by TRAC group

	A	B	C	D	E	F	U
Number of providers	25	16	18	14	40	20	114
Average total income per provider (£m)	733	252	222	256	89	46	15

Proportion of overall income (%)

Other (eg residences, catering, donations, other fees etc)	28	23	12	12	16	22	62
Funding body grants	12	12	11	9	9	12	1
Research grants and contracts	24	12	4	3	1	1	0
Tuition fees – non-EU overseas students	18	19	15	15	10	26	12
Tuition fees – EU students	2	4	4	4	5	6	4
Tuition fees – UK students	16	31	54	59	59	33	21

Part Three

Effective regulation of financial sustainability

3.1 This part of the report:

- explains how the Office for Students (the OfS) assesses risks to higher education providers' financial sustainability; and, in that context
- draws on established good practice for regulators to help identify where the OfS has most scope to improve performance.

3.2 The National Audit Office has published a guide to the principles of effective regulation, based on our past audits of regulatory frameworks and engagement with departments, regulators and other stakeholders. The principles are those we would expect to see supporting effective regulation and high-performing regulators (**Figure 10**).¹⁰

3.3 The OfS's first year of operating with its full powers was disrupted by the COVID-19 pandemic. It has since begun to review aspects of its approach, including how it regulates for financial sustainability. Our work focused on the OfS's responsibilities to regulate providers' compliance with its financial viability and sustainability condition of registration ('condition D') that a provider must:

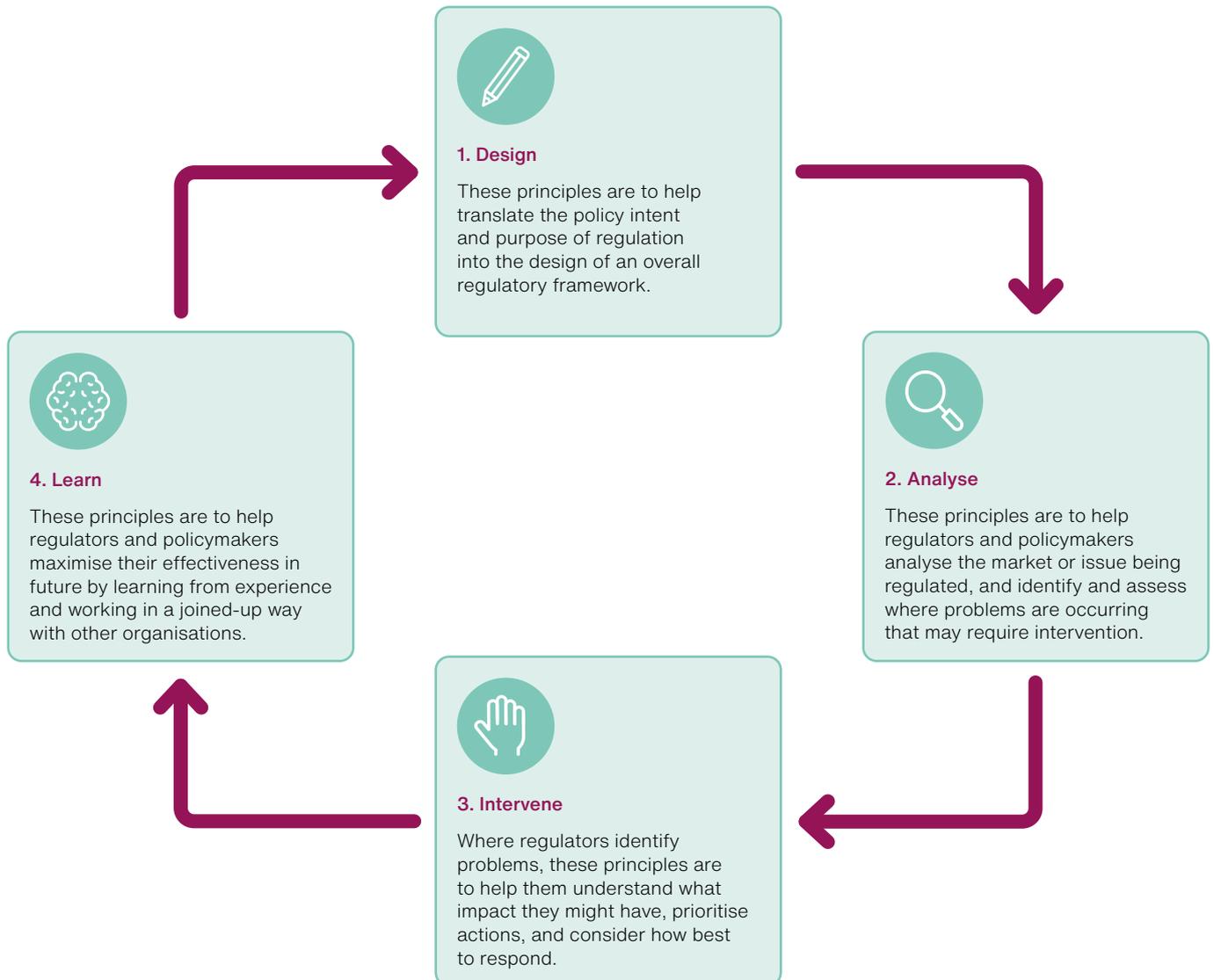
- be financially viable;
- be financially sustainable;
- have the necessary financial resources to provide and fully deliver the higher education courses as it has advertised and as it has contracted to deliver them; and
- have the necessary financial resources to continue to comply with all conditions of registration.

¹⁰ National Audit Office, *Principles of effective regulation*, May 2021.

Figure 10

The principles of effective regulation: a learning cycle

Our 2021 guide set out a learning cycle that described the key principles of effective regulation in four areas



Source: National Audit Office, *Principles of effective regulation*, May 2021

Design

3.4 Public clarity over the fundamental aim of regulation (and any regulators) helps ensure a shared understanding of its purpose and intended outcomes. The ‘design’ principles are intended to translate the policy intent and purpose of regulation into the design of an overall regulatory framework and to help regulators engage with stakeholders to understand needs and priorities. Giving due consideration to these design principles, when setting up or considering changes to a regulator or regulatory system, can avoid costly, untimely or disruptive remedial action later.

3.5 The Department for Education (the Department) deliberately designed the OfS to be different from its predecessor bodies, the Higher Education Funding Council for England (HEFCE) and the Office for Fair Access. The OfS would therefore have a different relationship with the sector – its primary role being that of a regulator rather than a funding body:

- To create and maintain its regulatory independence, and seeking to minimise regulatory burden, the OfS does not maintain close ongoing contact with individual providers it considers at low risk.
- The OfS aims to be a principles-based regulator, meaning it focuses on the outcomes it wants providers to achieve without prescribing how they should do so.
- The Department, as primary sponsor of the OfS, holds quarterly performance reviews with the OfS’s leaders. The Department maintains, and discusses with the OfS, a risk assessment of potential threats to the OfS’s effective performance of its functions.
- The OfS’s framework document establishes that it will be subject to a ‘tailored review’ to ensure, among other things, that it is delivering effectively against its aims and objectives. The Department expects this to be undertaken around 2023.

3.6 Where we found potential for improvement to system design, this related particularly to the quality of communication with providers, in explaining why the OfS takes the regulatory approach it does, and in listening to feedback:

- The OfS relies heavily, although not exclusively, on financial metrics to identify risks to providers' financial sustainability and to focus its resources on those most at risk. The sector bodies and providers that we spoke to, on the other hand, told us that, because the OfS had not routinely spoken to most providers, they were not confident that the OfS had all the information needed to contextualise the data it collects.
- Early in the COVID-19 pandemic, the OfS spoke to most providers to understand how they were responding to pandemic-related risks. This engagement was well received in the sector. The OfS also told us that this was the most effective way to understand quickly how providers were affected by the pandemic.
- The OfS consults widely on changes to the regulatory framework, but there is no routine way in which it captures structured stakeholder feedback (for example, using a survey) through which it can gather the views of regulated bodies on its own performance.

Analyse

3.7 The 'analyse' principles are intended to help regulators and policymakers: analyse the market or issue being regulated on an ongoing basis; identify and assess in a timely manner where problems may be occurring that require intervention; and understand what capacity is needed to respond appropriately.

3.8 The OfS deems a provider to be 'financially viable' when, in the OfS's judgement, there is no reason to suppose the provider is at material risk of insolvency within a period of three years from the date on which the judgement is made. It defines a 'financially sustainable' provider as one whose plans and protections show that it has sufficient financial resources to fulfil its advertised courses and conditions of registration for five years from the date on which the judgement is made and is likely to be able to operate in accordance with these plans and projections over this period.

3.9 The OfS requires providers to submit a detailed annual financial data return. It uses this information to monitor and report on the financial sustainability of the sector as a whole, and to monitor (and, if necessary, intervene) in relation to financial viability and sustainability risks in individual providers.¹¹ All providers, regardless of size or previous risk profile, are asked to submit the same base data (providers already subject to enhanced monitoring conditions may be asked to provide supplementary information). The standard data collection gives a consistent UK-wide data set, including the devolved administrations. The data set is published by the Higher Education Statistics Agency and provides transparency as well as enabling benchmarking by providers and other bodies. Some of the data collected also inform decision-making by other bodies, such as UK Research and Innovation. Information in the annual data return includes:

- audited financial statements for the preceding two years;
- financial forecasts for the current year and four subsequent years; and
- a commentary explaining any assumptions made in forecasting and explanations for any figures in the annual financial return that are, for example, out of line with previous trend data, including details of any scenario planning, sensitivity analysis or stress testing providers have carried out to mitigate risks arising from uncertainty in the data.

3.10 In addition to the annual return, the OfS requires providers to disclose ‘reportable events’, defined as “any event or matter that, in the reasonable judgement of the OfS, negatively affects or could negatively affect: the provider’s eligibility for registration with the OfS; the provider’s ability to comply with its conditions of registration; the provider’s eligibility for degree awarding powers (where applicable); or the provider’s eligibility for university title (where applicable)”. The OfS may also take into account additional information it has requested (for example, because it has already judged the provider as at increased risk), or information received from third parties, including students or whistleblowers.

3.11 Providers and stakeholders we spoke to saw the requirement for all providers to submit the same information as a one-size-fits-all, rather than a risk-based, approach. Some large, well-established providers considered they were at low risk of financial failure and should therefore be subject to a lighter-touch data requirement from the OfS; and some small providers saw the data requirements as placing a disproportionate regulatory burden on them.

¹¹ Section 68 of the Higher Education and Research Act 2017 places a statutory obligation on the OfS to monitor the financial sustainability of registered higher education providers, and to include in its annual report a summary of conclusions, drawn from its monitoring, regarding patterns, trends or other matters which it has identified.

3.12 Using the data available to it, the OfS goes through a number of stages to assess providers' financial sustainability:

- Annual financial return data are automatically validated using rules to test for realistic ranges and consistency with previous values, supported by accompanying information (such as the financial commentary).
- The OfS calculates a number of key financial risk indicators, including measures of cashflow, liquidity, in-year surplus/deficit, and borrowing. It uses these indicators, together with the financial commentary and other information submitted as part of the annual return, to identify and screen out providers that are at the lowest risk of financial failure.
- For providers not assessed as being at lowest risk, the OfS completes a more detailed financial viability and sustainability (FVS) assessment.
- The OfS's Compliance and Regulation Team is responsible for recommending, based on the financial information and any other knowledge held by the OfS on the provider, whether regulatory intervention may be required. The final decision over whether to intervene is taken according to the OfS's scheme of delegation.

3.13 Collectively, the review process represents an integrated assessment of provider risk using all the information held by the OfS. The assessment:

- uses a consistent set of data from providers;
- reviews data for evidence of risk against factors including liquidity, lowest forecast cash balances, cashflow, working capital and borrowing;
- requires a documented and approved decision paper for the outcome of the assessment process for each provider;
- links financial with non-financial data held by the OfS; and
- spreads assessment risk through having multiple sign-off points for judgements.

3.14 There are, however, areas where the process could be improved:

- The OfS does not have resources to scrutinise all providers' financial returns in detail and therefore has to prioritise providers it considers are highest risk – meaning that decisions about the level of risk the OfS accepts could be influenced by resource constraints.
- The OfS reviews financial commentaries, auditors' statements and other material supporting financial statements. Providers we spoke to doubted whether the OfS had all the information needed to put financial data into context. The OfS told us it considered it had engaged with providers sufficiently to understand risks to their financial sustainability.

3.15 The OfS has undertaken some financial analysis and scenario modelling of key risks, including the income challenges following the COVID-19 pandemic, escalating pension contributions and changes in recruitment. However, it does not yet have an integrated model to bring together and assess the impacts of ongoing, multiple and systemic risks to financial sustainability, carry out sensitivity analysis or test scenarios. It told us that it is planning to do so – and that this work will in future help inform its assessment of risk in individual providers.

Intervene

3.16 Where regulators identify problems that may require intervention, the 'intervene' principles are intended to help them: understand what impact they might have; prioritise actions; and consider how best to respond to achieve their intended outcomes with proportionate and timely responses.

3.17 The OfS has powers to respond to increased financial risk in providers by imposing requirements for enhanced monitoring (that could include, for example, requiring additional information from the provider), specific conditions and monetary penalties, or suspending or removing a provider's registration.

3.18 At the time of our review, the OfS was reviewing the annual financial data submitted by 247 out of 250 providers for the 2019/20 academic year (the 2020 annual financial return).¹² The OfS was still assessing information received from one of these providers, and one had deregistered. Of the remaining 245 providers, the numbers at each stage of assessment triage were:

- 144 providers were assessed as triaged out at the initial review stage, so did not have a more detailed FVS review;
- 98 providers had sufficient risks identified at triage stage to warrant a more detailed FVS review – the FVS review concluded that there were no material financial viability or sustainability issues needing follow-up although the Compliance and Regulation Team was advised to engage with 15 of the providers for further information; and
- three providers had issues identified in the FVS review serious enough for them to be passed to the Compliance and Regulation Team with a recommendation to consider whether a Condition D assessment (relating to a potential breach of the financial sustainability and viability condition of registration) was necessary and appropriate.

3.19 As at December 2021, 10 providers were subject to enhanced monitoring by the OfS as a result of regulatory concerns about their financial sustainability, and it was engaging with a further 13 providers to understand their level of risk. Some of these providers already had enhanced monitoring conditions in place, in which case the FVS assessment will not necessarily have flagged them up for further review.

3.20 There have, as yet, been no examples of provider collapse that would evidence failure in the OfS's interventions. It may also take several years for a provider to recover sufficient financial sustainability to come out of the OfS's enhanced monitoring regime. On the basis of our review of seven cases, to understand the process the OfS follows to assess risk in providers, we found:

- the OfS could demonstrate the reasons for its conclusions;
- the OfS applied consistent principles, combined with professional judgement, in deciding what interventions were appropriate; and
- all key decisions were reviewed by more senior staff.

¹² This round was not typical as it followed an interim assessment which occurred due to COVID-19, and the number of providers forwarded for consideration by the Compliance and Regulation Team was unusually low. At the time of writing, the OfS was waiting for three providers to sign off their financial returns.

3.21 The OfS adapted its approach during the COVID-19 pandemic to focus on short-term financial risks. It introduced an interim data collection in September and October 2020, seeking to understand the impact of the pandemic on providers' income, cashflow and liquidity, and changes to borrowing arrangements. It also reduced the number of reportable events, to reduce the regulatory burden on providers.

3.22 Providers we spoke to told us that, in their view, the regulatory system lacked transparency, in that they did not know what might or might not trigger regulatory intervention by the OfS. The OfS sets out in its regulatory framework how it intends to perform its functions. The framework defines financial viability and financial sustainability by reference to the conditions of registration. Because these conditions are principles-based, the OfS does not define triggers or thresholds that would prompt intervention. This means that, while the OfS could issue additional generic guidance, it takes its decisions on a case-by-case basis, taking into account a provider's specific circumstances.

Learn

3.23 It is important for regulators and policymakers to work collaboratively, measure progress and learn from experience to maximise effectiveness in future. The 'learn' principles are intended to help measure and report performance and outcomes against regulatory objectives, evaluate the real-world impact of interventions, and work in a joined-up way with other organisations in the regulatory landscape.

3.24 The OfS's accountabilities to Parliament and the Department are set out in the OfS framework document. The key mechanism by which it works with partner organisations in relation to financial sustainability is the higher education financial sustainability oversight group, led by the Department, and also including representatives from the Department for Business, Energy & Industrial Strategy (BEIS) and UK Research and Innovation. During the COVID-19 pandemic, the Department strengthened the group by bringing in a representative from HM Treasury, given its interest in financial support measures that were being considered. The OfS provides outputs from its sector-level analysis to the oversight group. It also shares information with the Department and BEIS but does not share some provider-level data such as forecasts and borrowing information, even with the Department, as they are viewed as commercially sensitive.

3.25 The OfS sets out on its website the range of performance indicators against which it intends to measure its own performance as a regulator. Where data are available, performance is shown with trend information and some commentary. The measures are set by the OfS Board, following discussion with the Department, and relate to the OfS's five strategic objectives. However, out of 26 indicators, eight are still in development or do not have complete performance information, and a further 11 indicators do not yet have associated targets, so it is not yet possible to get a fully rounded picture of the OfS's performance.

3.26 Sector stakeholders and providers we spoke to told us they did not feel they were getting value for money from the OfS. They said this was because the flow of information was one-way, and they received very little feedback or support.

Part Four

Consequences for students and providers

4.1 This part of the report:

- outlines how the Office for Students (the OfS) seeks to protect students from risks arising from pressure on higher education providers' finances;
- explains how government bodies and higher education providers, respectively, responded to the COVID-19 pandemic; and
- examines the consequences for students and providers of A-level grades awarded in 2020 and 2021.

How the OfS seeks to protect students from financial risk in higher education providers

The OfS's responsibilities

4.2 The OfS requires all higher education providers, as a condition of registration, to have in place and publish a student protection plan. This plan must be approved by the OfS as appropriate for the level of risk presented by the provider and for the risk to continuity of study for all its students. OfS guidance is that student protection plans should be proportionate, and that it will expect more detailed plans from providers with a higher risk of significant changes or closure than it does from providers at less risk. Typical remedies would be for the provider to ensure that existing students could complete their courses, or for them to transfer to another institution.

4.3 Since the OfS took on its full responsibilities in August 2019 there have been no instances of chaotic or unplanned market exit, for which rapid implementation of student protection plans would be needed to protect students' interests.¹³ The OfS reported in October 2019 that, in assessing applications for registration, it had found student protection plans very variable in quality. Because it believed it was not in students' interests to delay registration, the OfS had nonetheless approved a number of plans that were significantly below the standard it would expect. In those cases, it had asked providers to resubmit improved plans following publication of new guidance. One of the providers we spoke to echoed this, saying that there was wide variation in the length and coverage of plans, and that some had the feel of a 'tick-box' exercise. Another provider commented that it had found its student protection plan was not suitable to respond to pressures arising from the COVID-19 pandemic.

4.4 The OfS has identified weaknesses in student protection plans, including providers being over-optimistic about the risks they faced, lack of detail about what specific actions providers would take, and weak refund and compensation policies that did not explain that refunds and compensation would be available to students where the provider could no longer deliver a course as advertised. In the small number of cases where the OfS had required providers to undertake more detailed planning, it found that existing student protection plans had been the starting point for discussion, rather than a set of actions that could be taken.

4.5 In response to increased risk to all providers resulting from the COVID-19 pandemic, between July and September 2020 the OfS undertook a consultation on changes to allow it to intervene more quickly.¹⁴ Following the consultation, the OfS implemented a new condition of registration, effective from 1 April 2021. This gave it the power to issue student protection directions to providers it considers at material risk of market exit – requiring that provider to put in place or implement specific measures to protect students.

Students' views and experiences

4.6 The OfS routinely collects students' views on, for example, the quality of teaching and learning they are getting, and their perception of the value for money of their degree. It carries out an annual student survey, engages with the National Union of Students and listens to a panel of student representatives – the chair of which also sits on the OfS's own Board.

¹³ One higher education provider went into administration in 2019, shortly before the OfS assumed its full regulatory powers. It was not registered with the OfS and the Department for Education handled the provider's market exit.

¹⁴ The OfS consultation document and response are published on the OfS website, at www.officeforstudents.org.uk/publications/consultation-on-student-protection-directions/

4.7 The 2021 National Student Survey ran from 6 January to 30 April 2021 and was open to final-year undergraduate students in all publicly funded higher education providers across the UK.¹⁵ As such, it will not have captured the views of all students, particularly first-year undergraduates who are most likely to have been affected by the closure of university accommodation during the COVID-19 pandemic. The overall satisfaction rating for students in England has been stable in recent years at 82%–83% but in 2021 this fell to 75% (**Figure 11**).

4.8 The OfS commissions a separate survey each year, in which it asks students whether, considering the costs and benefits of university, they think it offers good value for money.¹⁶ For then-current undergraduates, the proportion answering ‘yes’ fell from 38% in 2020 to 33% in 2021, and the proportion answering ‘no’ rose from 48% to 54%. The OfS does not attempt to define value for money, saying that it means different things to different people and may shift over time, and that it seeks to track perceptions rather than impose its own definition on students.

Protecting students’ interests from increased financial risk faced by providers during the COVID-19 pandemic

4.9 The Department for Education (the Department), the Department for Business, Energy & Industrial Strategy (BEIS), and the OfS all responded to increased financial risks in higher education providers arising from the COVID-19 pandemic.

Intervention by the Department

4.10 The Department’s early modelling in May 2020, based on the limited information available at that time and when the consequences of COVID-19 were highly uncertain, estimated that the adverse impact of the pandemic on providers’ income could range between £3.9 billion and £22.3 billion, with a central estimate of a £13.9 billion loss in 2020/21. This was largely due to a projected loss of international students following the COVID-19 lockdown, combined with potential deferrals by domestic students and a drop in commercial income.

4.11 In May 2020 the Department announced that it would reprofile £2.6 billion of tuition fee income, so that the Student Loans Company would pay this to providers in the first term of the 2020/21 academic year rather than in the usual later tranches. The Department did this to support providers’ cashflow – reducing the risk of providers being unable to pay their bills, which could have led to disorderly market exit.

¹⁵ On 30 March 2021, following consultation, the OfS announced the results of the first stage of a review of the National Student Survey, undertaken to address concerns that the survey could be adversely impacting on quality and standards and creating significant unnecessary bureaucracy for universities and colleges. Phase 2 of the review is currently under way.

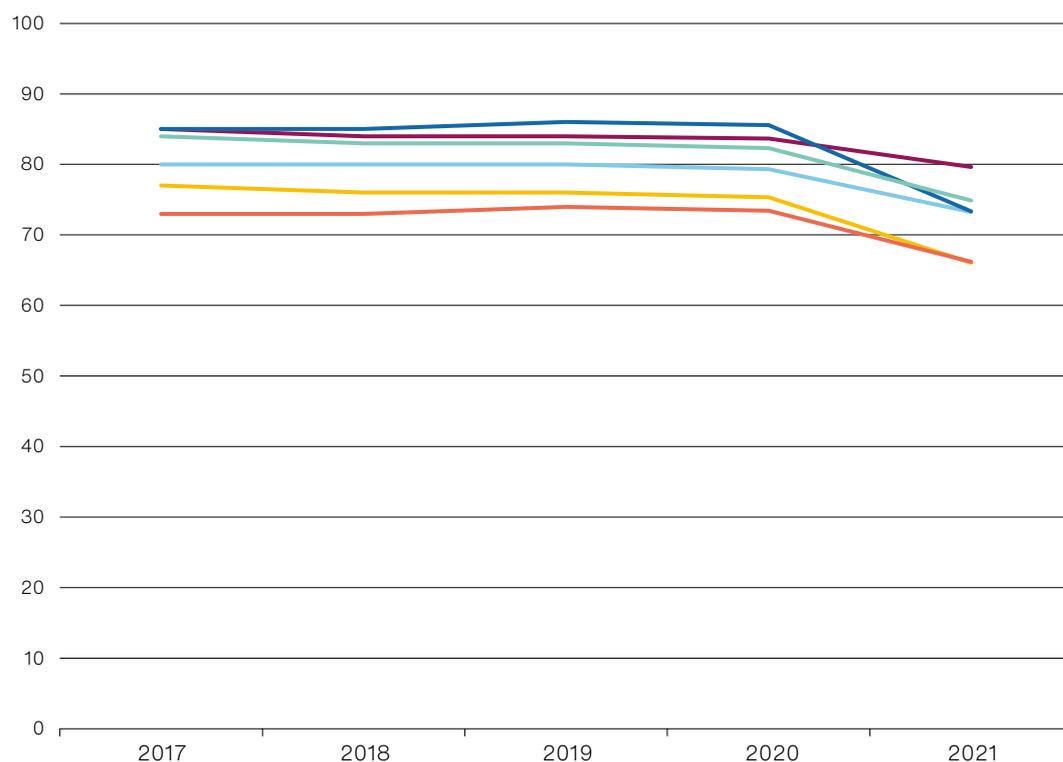
¹⁶ The survey population includes applicants, undergraduates, postgraduates and recent graduates. The 2020 survey was carried out between January and March; the 2021 survey was carried out between February and March. Details are published on the OfS website, at www.officeforstudents.org.uk/about/measures-of-our-success/value-for-money-performance-measures/students-who-believe-university-provides-good-value-for-money

Figure 11

Higher education student satisfaction, 2017 to 2021

Student satisfaction fell sharply between 2020 and 2021

Proportion of students who 'definitely' or 'mostly' agreed with each question (%)



Percentage point change from previous year	2016 to 2017	2017 to 2018	2018 to 2019	2019 to 2020	2020 to 2021
● The teaching on my course	-2	-1	0	0	-4
● Academic support	-2	0	0	-1	-6
● Learning resources	-1	0	+1	0	-12
● Learning community	n/a ³	-1	0	-1	-9
● Student voice	n/a ³	0	+1	-1	-7
● Overall satisfaction	-1	-1	0	-1	-7

Notes

- Teaching moved almost entirely online during the COVID-19 pandemic lockdown, with reductions in teaching hours, staff contact and access to resources affecting overall satisfaction. Individual experiences of online teaching will have varied by course and students' personal situations.
- The data in this figure reflect responses only in respect of higher education providers in England. Provider-level data are published at www.officeforstudents.org.uk/advice-and-guidance/student-information-and-data/national-student-survey-nss/nss-data-provider-level/.
- Questions relating to 'learning community' and 'student voice' were added to the survey in 2017, meaning there are no comparative data for 2016.

Source: National Audit Office analysis of National Student Survey data

4.12 On 16 July 2020, the Department announced that it was making available a 'higher education restructuring regime', providing time-limited access to emergency loans. The scheme was not intended to prevent all providers from exiting the market. The Department indicated that it would only intervene in the last resort where the failure of a provider would lead to significant harm. Advances would be conditional on providers demonstrating that they had realistic prospects of repayment. The Department removed the risk of higher education provider collapse due to financial failure, which it had escalated because of the potential impact of COVID-19, from its top-level risk register in March 2021. The Department took the view that the higher education restructuring regime provided adequate mitigation to reduce the risk to an acceptable level. The Department told us that it received 18 enquiries and that three providers had applied to the restructuring regime.

Intervention by BEIS

4.13 Higher education providers cannot cover the full cost of their activities from domestic students' tuition fees and publicly funded research grants. Many research-intensive universities are highly dependent on international student fee income to help support the cost of their research projects. Early modelling by BEIS, in May 2020, estimated that the extent of reliance on cross-subsidy for research income was £4.3 billion in 2018-19 and that some £3 billion could be at risk.

4.14 On 27 June 2020, BEIS announced a 'research stabilisation package' intended to maintain UK research capacity. This included £200 million in new government investment, and £80 million of existing funding to be redistributed by UK Research and Innovation (UKRI) to support research and development. BEIS also made available a package of loans and grants, designed to make up for losses in international student numbers ('Sustaining University Research Expertise' (SURE) funding). The package was designed to cover up to 80% of a provider's income losses for the academic year 2020/21, up to the value of non-publicly funded research activity in that university. By November 2020, BEIS had received 20 initial expressions of interest for SURE support. Because international student numbers were maintained at a much higher level than forecast, BEIS in fact provided funding to five applicants, totalling £21.4 million in loans and £298,000 grant funding.

4.15 BEIS is interested in the financial sustainability of providers to the extent that their financial position does not put at risk their ability to deliver top-quality research. BEIS relies on aggregated data from the OfS and analysis of the provider-level data by UKRI. UKRI and Research England, which commissions research projects from English providers, have agreements with the OfS to share provider-level data. UKRI and Research England maintain ongoing contact with directors of research at the universities they fund. BEIS told us that it views this intelligence as essential to understanding risks to providers' financial sustainability in good time. BEIS told us that it considers research-active institutions as less likely to fail, although they may scale back or cease research activities. As this could be damaging to local, regional or national research capability, BEIS views ongoing discussion of providers' plans as essential in case early intervention is needed.

Higher education providers' responses to the pandemic

4.16 Because of the OfS's overriding responsibility to protect students' interests, it was particularly important for it to understand the impact on students of providers' responses to the COVID-19 pandemic. New pressures on providers because of the pandemic, financial and non-financial, had potential to increase the risk faced by students that they would not be able to complete the courses they had been promised.

4.17 Despite fears of widespread financial harm, providers have so far proved financially resilient during the pandemic, using their reserves or commercial credit facilities, or deferring capital spending plans. Importantly, rather than falling in the way feared, the number of overseas students has continued to increase. Despite the COVID-19 pandemic, by the January 2021 Universities and Colleges Admissions Service (UCAS) deadline, there were 83,910 non-EU applicants to English providers, compared with 71,740 in January 2020 (a 17% increase).¹⁷

4.18 No providers exited the market. Some providers will have lost income directly as a result of lockdown restrictions, particularly from conferences and lettings, although the impact will have varied. Some of the providers we spoke to, for example, told us that closing buildings at the height of the pandemic had saved running costs, whereas others had kept buildings open. Providers also said that developing online learning quickly had been costly – even where they already had plans to develop blended learning, they had accelerated this dramatically.

¹⁷ These figures represent only a proportion of the total number of overseas students, not all of whom apply through UCAS.

Tuition fees

4.19 One of the reasons for the sharp decline, between 2020 and 2021, in students' satisfaction with their courses and in their perception of value for money was the shift to online learning required by lockdown restrictions, and restricted access to laboratories, libraries and other learning resources. There were calls for higher education providers to recognise this by refunding a proportion of tuition fees.

4.20 The government's position was not to support tuition fee refunds. The universities minister stated that "students ordinarily should not expect any fee refund if they are receiving adequate online learning and support". The government did not define what it regarded as 'adequate' in this context. Students were not consulted on this decision nor on how it affected the value for money of their experience, but students' responses to the National Student Survey show that their satisfaction with teaching and learning declined sharply between 2020 and 2021. The government's position reduced financial stress on providers – one of the smaller providers we spoke to told us that, had government applied more pressure to offer significant fee refunds, this would have led it, and likely some similar providers, to fail.

A-level grades awarded in 2020 and 2021

4.21 In March 2020 all schools and colleges in England were closed due to the COVID-19 pandemic and public examinations were cancelled. Ofqual, the examinations regulator, was asked to put in place an alternative system for assessing and allocating students' final grades. The method chosen was based on factors including centre-assessed grades (CAGs), pupil rankings and a computer model which took into account the past performance of individual schools. In August 2020, when students were informed of their final grades, 40% of students had been awarded grades lower than their CAGs. Following protests, the government decided that students should be awarded A-level grades based on CAGs. The move to CAGs caused significant grade inflation, making many more students than expected eligible for places at their first-choice provider and on high-tariff courses.

4.22 In May 2020, the Department announced a temporary cap on student numbers saying that this was "to ensure a fair, structured distribution of students across providers". Through the plans, English higher education providers would be able to recruit full-time undergraduate UK and EU students for 2020/21 up to a temporary set level, based on their forecasts for that academic year, plus an additional 5%. The government announced it would control those numbers through the student finance system. This action was a response to concerns that high-tariff providers would admit high numbers of domestic students to make up for an expected fall in the number of international students, at the expense of low-tariff providers and that such competition among providers would go against the interests of students and the sector. The Department reversed this decision three months later, in response to disruption in the 2020 A-level exam cycle, to "ensure students can progress to higher education".

4.23 In August 2020, at least one sector stakeholder highlighted risks of volatility in A-level grades destabilising the higher education market. Universities' plans had been made assuming that there would be limits to the number of students any individual university could take. Removing those limits, and with more students now qualified to enter their first-choice provider, meant that these plans needed to be reworked. For higher-tariff universities, this would mean revising assumptions about staff numbers, accommodation and teaching spaces, with the result that it would be challenging for institutions to protect the overall experience of each student. For universities with lower entry requirements normally expecting to recruit large numbers of students through clearing – those who had not achieved the grades for their first choice of university – there was a risk that it could make their financial position much less secure.

4.24 There was, in the event, no fall in international student numbers as had initially been feared. Combined with an increase in the number of domestic students with high A-level grades this meant that there were more students than forecast who qualified for places in high-tariff universities. A-level 'grade inflation' in 2020 generally benefited established (higher-tariff) universities more than lower-tariff providers. Further grade inflation in 2021 compounded the situation, with many medium- and low-tariff and specialist providers recruiting fewer students in 2021 than they had in 2019, despite a 10.8% overall rise in undergraduate entrant student numbers over the two years (**Figure 12** on pages 50 and 51).

4.25 The Department anticipated that A-level grade inflation caused by the adoption of CAGs could lead to high-cost courses being oversubscribed, and that some providers would need additional financial support as a consequence. In September 2020 it provided an additional £10 million to support teaching high-cost subjects, and up to £10 million capital funding to help oversubscribed providers expand capacity. The Department and the OfS told us that, while they did not model in advance whether the changes to A-level grades would, by themselves, lead to some providers becoming undersubscribed and what the financial consequences for those providers could be, they monitored data on student numbers at each provider as the admissions cycle concluded. The OfS used these data, covering international as well as domestic students, to inform its ongoing assessment of individual providers' financial sustainability.

4.26 In 2021, 44.3% of A-level entries in England were awarded A* or A – a 6.2 percentage point rise compared with 2020's results and a 19.1 percentage point rise compared with the pre-pandemic exam results of 2019. Providers told us that, combined with over-recruitment by high-tariff providers, this left some lower-tariff providers undersubscribed in 2020 and 2021. This has created both short- and medium-term financial risk, as shortfalls in planned numbers flow through into subsequent years.

Figure 12
 Change in the number of UK undergraduate student entrants to courses at English higher education providers between 2019 and 2021, by tariff group

Most high-tariff providers benefited from the increase in the overall number of student entrants, but many other providers recruited fewer students



Figure 12 *continued*

Change in the number of UK undergraduate student entrants to courses at English higher education providers between 2019 and 2021, by tariff group

Notes

- 1 This figure includes data for 141 out of the 162 providers for whom data exist for both 2019 and 2021. It excludes 21 providers with fewer than 100 entrants in 2019, in order to remove misleadingly large percentage changes due to changes in small numbers of students. The 10.8% overall increase in the number of entrants includes all 162 providers – the overall increase for the providers shown was 10.4%.
- 2 Each vertical line in the chart represents an individual provider.
- 3 The data on which the figure is based include a count of students already at each provider on 1 December plus a forecast of the number of students who will join in the remainder of the academic year.
- 4 Tariff groups are based on each provider's entry requirements – the 'tariff' refers to the number of Universities and Colleges Admissions Service (UCAS) points required.
- 5 Providers we spoke to described the differential impact of the 2020 and 2021 A-level grades. There may well be other reasons for individual providers' changes in student numbers.

Source: National Audit Office analysis of the Office for Students' (the OfS's) *Higher Education Students Early Statistics* 2019-20 and 2021-22 survey data, and UCAS average tariff data provided by the OfS

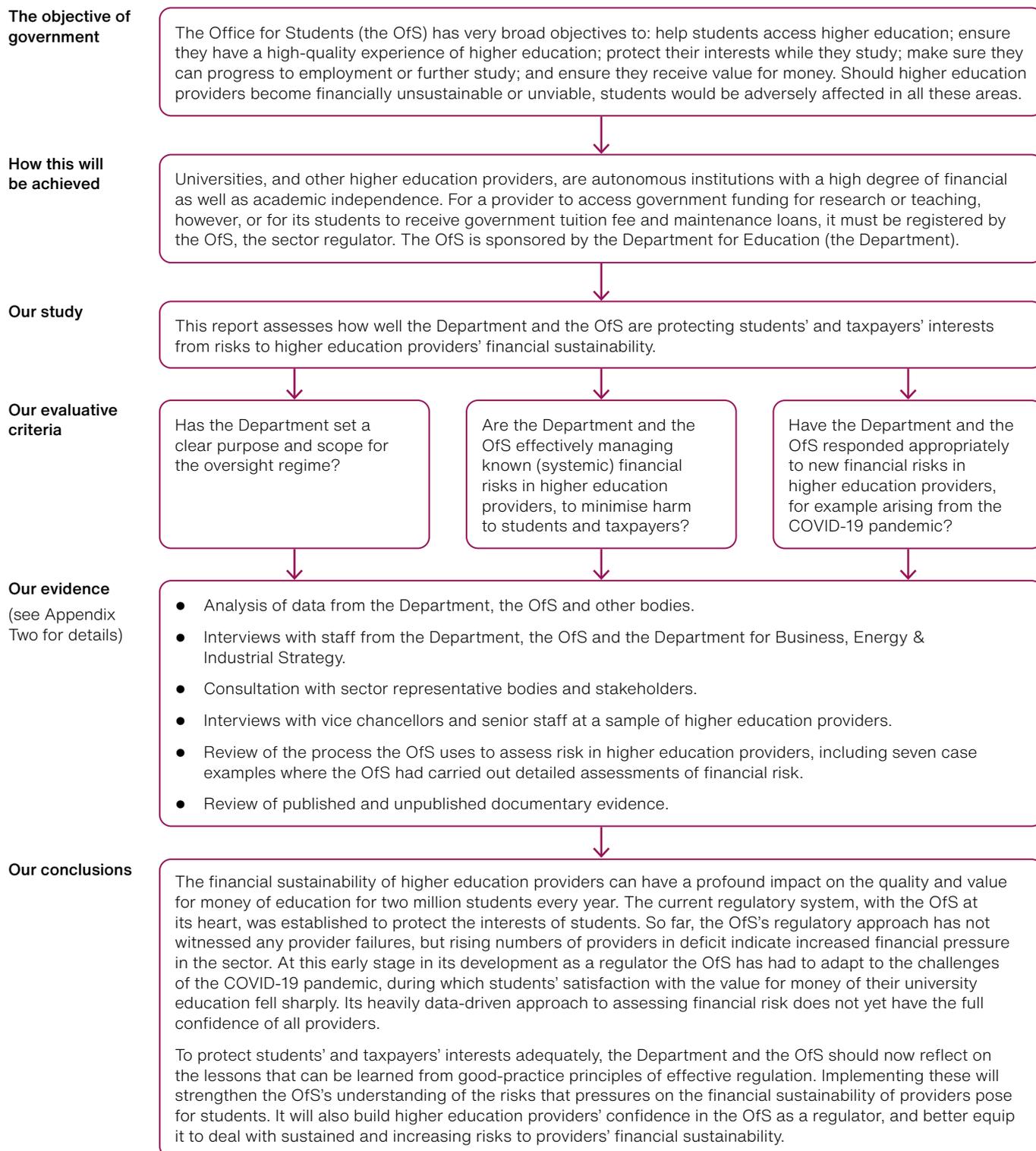
4.27 There have also been problems for some high-tariff providers who admitted more domestic students in 2021 than forecast (because more had achieved high grades). Domestic students are, overall, loss-making for providers (Figure 3). For the 2021/22 academic year, some oversubscribed universities offered financial incentives to students to defer entry, or struggled to find accommodation for their first-year students, raising questions about their ability to offer the student experience they promised.

4.28 There remains a risk of perpetuating distortion in the market in the medium term that could be damaging to the financial health of high-tariff and low-tariff providers. This is because over- or under-recruitment in one year affects income and expenditure over the whole length of a degree course. There may also be as-yet-unknown reputational impacts on under- and oversubscribed providers.

Appendix One

Our audit approach

- 1** This report focuses on the Office for Students' (the OfS's) responsibilities to protect students' interests from the consequences of financial risk in higher education providers.
- 2** The report:
 - gives an overview of the higher education sector, and of the regulatory system the government has put in place (Part One);
 - illustrates the financial risks in higher education providers (Part Two);
 - considers the current arrangements for regulating financial sustainability in higher education providers in light of regulatory good-practice guidance (Part Three); and
 - examines the consequences of increased financial risk for students and providers (Part Four).
- 3** We applied an analytical framework with evaluative criteria that considered what arrangements would be optimal for achieving value for money. By 'optimal' we mean the most desirable possible, while acknowledging expressed or implied restrictions or constraints.
- 4** Our audit approach is summarised in **Figure 13** and our evidence base is described in Appendix Two.

Figure 13**Our audit approach**

Appendix Two

Our evidence base

1 We reached our independent conclusions on whether the Office for Students (the OfS) is effectively regulating the financial sustainability of higher education providers, and whether it is being effectively sponsored by the Department for Education (the Department), after analysing evidence collected between July 2021 and February 2022. Our audit approach is outlined in Appendix One.

2 Our report covers higher education providers in England who are registered with the OfS. It excludes further education colleges and sixth-form colleges who are regulated by the Education and Skills Funding Agency, whose financial sustainability was the subject of a previous National Audit Office (NAO) report.¹⁸

3 In designing and carrying out our work, we took account of a previous NAO guide to the principles of effective regulation, based on our past audits of regulatory frameworks and engagement with departments, regulators and other stakeholders.¹⁹

4 We interviewed staff from the OfS, the Department, and the Department for Business, Energy & Industrial Strategy (BEIS).

- The people we interviewed at the OfS included officials responsible for the OfS's approach to regulation and analysing financial risk in higher education providers.
- The people we interviewed at the Department included officials responsible for the higher education financial sustainability oversight group, the COVID-19 restructuring regime and sponsorship of the OfS.
- Officials we interviewed at BEIS were members of the higher education financial sustainability oversight group and were responsible for the COVID-19 research stabilisation programme.

¹⁸ Comptroller and Auditor General, *Financial sustainability of colleges in England*, Session 2019–2021, HC 728, National Audit Office, September 2020.

¹⁹ National Audit Office, *Principles of effective regulation*, May 2021.

5 We reviewed published and unpublished documents from the Department and the OfS. We used this information to understand how the OfS exercises its regulatory authority with regard to financial sustainability, and how departments and other public bodies, including the OfS, coordinate to assure adequate oversight of financial risk. This included material relating to:

- the legislative and regulatory framework;
- outputs and analysis relating to the financial sustainability of higher education providers published by the OfS and other bodies, including the OfS's own reports on the financial sustainability of higher education providers, Transparent Approach to Costing (TRAC) reports, and reports published by stakeholders including Universities UK and the British Universities Finance Directors Group;
- relevant parts of the Department's top-level risk registers relating to risk of higher education provider failure; and
- the Department's sponsorship and oversight of the OfS.

6 We reviewed financial modelling undertaken by the OfS, relating to the potential financial impacts of:

- the COVID-19 pandemic;
- employers' pension costs; and
- potential changes to student tuition fees.

7 We analysed a range of data relevant to the financial sustainability of higher education providers:

- Financial information about providers:
 - Higher Education Statistics Agency data about the finances of providers from 2015/16 to 2019/20, used to analyse trends in actual values of income, expenditure, and in-year surplus/deficit.
 - Annual financial returns for 2018, 2019 and 2020 provided by the OfS, including two years of actuals data and five years of forecast data from providers. We used this to inform our review of the OfS's triage process, the degree of optimism or pessimism in provider forecasts, and for tuition fee analysis for 2019/20.
 - Data collected by the OfS about the income from, and full economic costs of, higher education providers' activities, as part of the OfS's TRAC data collections.

- Other information about providers:
 - Information from the Higher Education Statistics Agency about the number of students at higher education providers and sub-groups within this, for example by domicile (UK, EU, other non-UK), course level (undergraduate, postgraduate) and the proportion of students attending from areas of low participation.
 - Details, drawn from OfS data, about registered providers. These included alternative methods to group similar providers for comparative analysis, including TRAC peer groups and Universities and Colleges Admissions Service (UCAS) entry-tariff groups. We used this information to support our analysis of individual providers' financial position and student numbers.
 - Information from the OfS's Higher Education Students Early Statistics 2019-20 and 2021-22 survey data to analyse the impact of A-level grade inflation in 2020 and 2021 on the numbers of students entering different providers.
 - Office for National Statistics population projections (2018).

8 We interviewed stakeholder groups representative of the UK higher education sector:

- Association of Heads of University Administration;
- British Universities Finance Directors Group;
- Committee of University Chairs;
- GuildHE;
- Independent HE;
- National Union of Students; and
- Universities UK.

9 We interviewed senior staff (vice chancellors, finance directors and registrars) from 10 higher education providers. We selected eight providers to include a diversity of peer group types (as determined by proportion of income from research, medical schools, size and specialisation), student numbers, income, geographical location and income dependency. We spoke to a further two providers as a result of following up interviews with stakeholder bodies. The providers we spoke to were:

- Falmouth University;
- Leeds Conservatoire;
- Newcastle University;
- Nottingham Trent University;

- Staffordshire University;
- The London School of Economics and Political Science;
- University of Birmingham;
- University of Portsmouth;
- University of Sheffield; and
- Writtle University College.

10 We used case examples to review how the OfS assesses financial risk in providers.

- We interviewed OfS staff and reviewed supporting documents to evidence the process the OfS uses to assess financial viability and sustainability risk in higher education providers.
- We reviewed in more detail an illustrative sample of seven cases. These were cases where the OfS's initial triage had indicated there was sufficient financial risk to warrant a more detailed financial viability and sustainability assessment.
- We selected the sample cases to include a variety of providers for which the OfS's initial triage had indicated a range of risks (including some where there were few initial risk indicators and some where there were several risk indicators). Our selection included providers of different sizes, specialist providers and more conventional universities.
- Our review included three providers for which the detailed assessment recommended that the OfS's Compliance and Regulation Team consider whether the provider was in breach of, or was at risk of breaching, the financial viability and sustainability condition of registration (Condition D). In these three cases, the OfS continued or began enhanced monitoring. Of the remaining four cases we reviewed, the Compliance and Regulation Team concluded that three providers were not at increased risk, but that one was at increased risk and should be placed under enhanced monitoring.

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