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Higher Education Funding Council for Wales

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Cylchlythyr | Circular

Financial Management Code

Date:	16 June 2017
Reference:	W17/16HE
To:	Clerks to the governing bodies of regulated institutions in Wales for the attention of the governing bodies Heads of regulated institutions in Wales Other interested parties
Response by:	No response required
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This circular attaches the Financial Management Code for institutions regulated under the Higher Education (Wales) Act 2015.

If you require this document in an alternative accessible format, please email info@hefcw.ac.uk.

Noddir gan Lywodraeth Cymru
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Introduction

1. This circular attaches the Financial Management Code (the Code) which sets out provisions relating to the organisation and management of financial affairs for institutions regulated under the Higher Education (Wales) Act 2015.

2. The Code has been prepared following consultation as outlined in W17/15HE 'Outcomes of the consultation on the Financial Management Code'.

Further information

3. For further information, contact Matt Lody (tel 029 2085 9716; email matt.lody@hefcw.ac.uk).

Assessing the impact of our policies

4. We have carried out an equality impact assessment (EIA) screening to help safeguard against discrimination and promote equality. We also considered the impact of policies on the Welsh language, and Welsh language provision within the HE sector in Wales. Contact equality@hefcw.ac.uk for more information about EIAs.

Cyngor Cyllido Addysg
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Financial Management Code

v1.0

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Contents

Introduction

1. This Financial Management Code ("the Code") sets out the requirements concerning the organisation and management of financial affairs to which regulated institutions[1] must adhere. The Code has been prepared in response to the relevant provisions contained within the Higher Education (Wales) Act 2015 ("the 2015 Act").

2. HEFCW has been mindful of a number of guiding principles whilst preparing the Code. Primarily, these principles are:

    a. The need to maintain stakeholder confidence in the Higher Education sector;
    b. The protection of the public and student interest;
    c. Minimising regulatory burden and duplication;
    d. Recognising institutional autonomy;
    e. Reasonable and proportionate accountability;
    f. Where appropriate, being explicit about the need for the requirements laid out in this Code by linking the requirement to the organisation and management of the financial affairs of the institution;
    g. Adopting a consistency of approach with other UK funding councils where possible and appropriate (for example, in respect of financial requirements and the consideration of the student interest) in order that the regulatory environment supports the ability of Welsh institutions to operate competitively; and
    h. HEFCW's duties under the Equality Act 2010 and the Well-being of Future Generations Act (Wales) 2015.

    The definitions of terms used within this Code are set out within '**Annex D: Glossary**'

Application of this Code

3. This Code does not supersede the requirements of the institution's governing documents and the law relating to the institution's charitable status but is intended to complement and reinforce them. Nothing in this Code shall require the institution to act in a manner which would cause it to lose its charitable status, or which would be incompatible with its governing documents.

4. Where HEFCW uses the term 'must', it means it is a specific legal requirement or requirement under this Code. Institutions must comply with these requirements.

5. HEFCW uses 'should' for items it regards as minimum good practice, but for which there is no specific legislation or for which HEFCW is not setting a requirement under this Code; however, governing bodies must take such guidance into account. HEFCW will consider the extent to which an institution

[1] As defined in Part 2, S7(5)(b) of the Higher Education (Wales) Act 2015

has adopted the 'should' provisions (or alternative, equally robust arrangements) in the Institutional Risk Review - our annual assessment of risk.

6. A summary of 'must' and 'should' provisions is provided at **Annex C**.

7. Where an institution fails, or is likely to fail, to comply with a requirement imposed by this Code, HEFCW may instigate the processes within its Statement of Intervention.

8. This document takes effect from 01 August 2017.

Responsibilities of HEFCW

Preparation of this Code

9. This Code has been developed in response to the statutory requirement[2] on HEFCW to prepare a code relating to the organisation and management of the financial affairs of regulated institutions[3].

Review of the Code

10. HEFCW will keep this Code under review, and if appropriate, prepare and publish a revised Code following consultation with stakeholders. Revisions will be made subject to the procedure for approval of the Code by Welsh Ministers, as outlined in Section 28 of the 2015 Act.

Interpretation of statements within this document

11. Questions on the interpretation of any provision in this Code shall be resolved by HEFCW, in dialogue with the institution concerned.

12. HEFCW will publish any clarifications on interpretation where it is deemed to be of general application, and where the clarification itself does not lead to a fundamental change in the application and principle of the provision.

13. Where the clarification of any provision in the Code would require a fundamental change in the application and principle of the provision, HEFCW will review the Code as outlined in paragraph 10.

Monitoring and interventions

14. The HEFCW Chief Executive must satisfy himself or herself that the governing body of the institution has appropriate arrangements for the organisation and management of its financial affairs, and that the institution has neither failed, nor is likely to fail, to comply with any of the requirements of this Code.

[2] Within Part 4, S(27)(1) of the Higher Education (Wales) Act 2015
[3] As defined in Part 2, S7(5)(b) of the Higher Education (Wales) Act 2015

15. HEFCW will monitor compliance by each institution with the requirements set out within this Code.

Communicating concerns over financial affairs

16. In his/her role as Accounting Officer, the Chief Executive of HEFCW must inform the institution's governing body and/or its audit committee if (s)he has cause to believe that the institution has, or is likely to fail to comply with this Code.

Risk assessment of institutions

17. HEFCW is required to form a view as to whether the governing body of an institution has failed, or is likely to fail, to comply with a requirement imposed by this Code[4]. HEFCW runs a number of assurance processes to inform its view (see **Institutional engagement, support and safeguarding actions**), one of which is an annual, confidential risk assessment of each institution (the 'Institutional Risk Review').

18. HEFCW will provide the Institutional Risk Review to the institution's accountable officer (see paragraph 42) and governing body. HEFCW will not normally make its Institutional Risk Reviews public until at least three years have elapsed. This period, based on advice from the Information Commissioner, gives an institution that is designated as 'high risk', time to ameliorate its risk rating.

19. HEFCW will make its Institutional Risk Reviews available within this three-year period, on an exceptional and confidential basis, to other regulators and public funders (such as the Charity Commission and Welsh Government) with an interest in the institution to enable those bodies to make their own assessments of risk. In all cases where HEFCW is legally allowed to do so, institutions will be informed prior to sharing.

20. HEFCW will exceptionally make public an Institutional Risk Review at any stage if it has strong grounds for believing that it is in the collective student or public interest to do so. In so doing, HEFCW will take into account the impact that such a disclosure might have upon an institution. HEFCW will only share or publish its Institutional Risk Reviews after having notified the accountable officer (see paragraph 42) and governing body of the institution concerned.

21. HEFCW defines an institution as 'high risk' when in HEFCW's judgement, on the basis of the available evidence, the institution has failed, or is likely to fail to comply with the Financial Management Code over the short to medium term, and the impact of this leads to sustainability concerns over that period.

22. We define 'short to medium term' as 'the five-year period covered by the latest financial forecasts supplied to HEFCW by the institution.

[4] Part 4 S(31) and S(32) of the Higher Education (Wales) Act 2015

23. Further information on HEFCW's Institutional Risk Review process is provided in paragraphs 107 to 112.

Use of existing information

24. Wherever possible, HEFCW will seek to use existing information it already holds, where such information is up-to-date.

25. Where authorised to do so by the institution, HEFCW will take reasonable steps to secure up-to-date information from other bodies. Such steps will aim to reduce the burden on institutions that are required to supply information to HEFCW which duplicates information already submitted to other bodies.

Responsibility to act reasonably

26. In exercising its powers under this Code, HEFCW will act reasonably at all times.

27. HEFCW will respect commercial confidentiality within the constraints of the Freedom of Information Act 2000 and its own obligations to the Welsh Government under the Framework Document[5] and to any regulatory body.

Responsibilities of the institution to HEFCW and to students

Governing body responsibility for compliance with this document

28. The governing body of the institution must ensure that the institution takes all necessary steps to comply with this Code.

Proper stewardship of funds

29. The governing body of the institution must ensure that all reserves are used for the purposes intended.

30. The governing body should review any relevant guidance on accountability or propriety issued from time to time by HEFCW.

31. The governing body should also take into account the guidance of relevant stakeholder bodies in relation to the organisation and management of financial affairs.

Sound financial management

32. The governing body of the institution must ensure that it has appropriate arrangements for the organisation and management of its financial affairs, including an adequate and effective internal control environment.

[5] Available at www.hefcw.ac.uk/about_us/our_responsibilities/our_responsibilities.aspx

Plan on a sustainable basis

33. The governing body of the institution must plan and conduct its financial affairs on a sustainable basis.

34. 'Sustainable' is defined by reference to the common understanding of 'going concern', over the five-year period covered by the latest financial forecasts supplied to HEFCW by the institution.

35. In order to satisfy HEFCW that the institution has planned appropriately within this area, institutions which are subsidiaries must be able to demonstrate that either:

    a. they have a guarantee from their parent company – any such guarantee is subject to approval by HEFCW and HEFCW will only give its approval if it is satisfied that, taking the guarantee into account, the parent itself is sustainable over the short to medium term; or
    b. they plan and conduct their financial affairs on a sustainable basis and independently from their parent company.

36. Governing bodies must ensure that the institution has conducted a thorough risk assessment of adverse events that could give rise to sustainability concerns. The extent to which the risk assessment considers adverse events will be determined by reference to events which a reasonable, informed individual could foresee as giving rise to sustainability concerns. Governing bodies must inform HEFCW immediately if they consider that such an event is likely to occur.

37. HEFCW considers that there are a number of indicators that might show deficiencies in financial planning. The following areas might (in combination or alone, and depending upon the detail of the individual context) indicate an institution that is at risk of not being sustainable:

    a. Unplanned deficits;
    b. Net cash outflow from operating activities in two consecutive accounting years;
    c. Negative net cash (as defined within FRS 102 S(7), including cash and cash equivalents) for more than 30 days;
    d. Low levels of liquidity;
    e. High levels of gearing, particularly where the borrowing is repayable on demand or subject to interest rate changes;
    f. The breach or close breach of borrowing covenants, particularly where the requirement to immediately repay the outstanding debt as a result of the breach would lead to viability concerns;
    g. Forecasts indicating that the institution is not a going concern over the forecast period;
    h. Reliance upon unreasonable assumptions within the financial forecast, where the effect of modifying those assumptions to a more reasonable

basis results in the institution's forecasts no longer showing the institution to be a going concern; and/or

i. The institution suffers an 'adverse event' (see paragraph 36) where the consequences of the event risks the institution ceasing to be a going concern.

38. HEFCW does not provide an exhaustive list of indicators, and the institution should determine whether it has any other indicators which point to underlying sustainability concerns and deficiencies in financial planning. The governing body should consider the above areas to the extent that they are applicable to the institution.

39. Ultimately, such an assessment will depend upon the context and the specific details. HEFCW will make an assessment where it believes there are reasonable grounds for uncertainty over the process for ensuring sustainability, informed as necessary by dialogue with the institution.

40. In accordance with FSSG's[6] recommended good practice, institutions should prepare an ASSUR statement on an annual basis. This statement should be reviewed by the institution's governing body.

Effective risk management processes

41. The institution must ensure that it has an effective policy of risk management which is able to demonstrate that the organisation and management of the institution's financial affairs are appropriately controlled.

Accountable officer's role and responsibilities

42. The governing body must designate an individual (normally, but not necessarily, the head of the institution) as the 'accountable officer' to assist and enable the governing body to discharge its reporting responsibilities to HEFCW.

43. The governing body must notify HEFCW whenever it designates such an individual.

44. The accountable officer is personally responsible to the governing body for providing HEFCW with clear assurances that the terms of this Code are being met.

45. Unless requested otherwise by HEFCW, it is acceptable for the accountable officer to report to HEFCW in respect of the governing body's duties, provided that governing body consent has been given for the accountable officer to report on its behalf in respect of those duties.

[6] Financial Sustainability Strategy Group (www.hefce.ac.uk/funding/finsustain/fssg/)

46. On being notified by the governing body of a new accountable officer, HEFCW will write to the governing body to explain what the responsibilities of an accountable officer typically involve. Given that the accountable officer is responsible to the governing body, rather than HEFCW, it will be for the governing body to determine which responsibilities the accountable officer should conduct on its behalf.

47. The governing body should make arrangements for HEFCW to meet the accountable officer within a reasonable timeframe following their designation.

48. The governing body should require the accountable officer to advise it immediately if, at any time, it appears to the accountable officer that any action or policy under consideration by the governing body would constitute a failure to adhere to this Code.

Robust governance oversight of financial affairs

49. The governing body must ensure that there are robust governance arrangements in place that provide adequate and effective oversight of financial affairs.

50. The governing body of an institution has ultimate responsibility for overseeing the institution's activities, for determining its future direction, and fostering an environment in which the institution's mission is achieved. This responsibility cannot be delegated.

51. An institution's governing body and senior executive team are the primary stakeholders served by assurance and risk management processes. They are therefore the parties best positioned to provide oversight of these processes and to ensure that these operate effectively.

52. In order that the oversight outlined in paragraphs 49 and 51 is appropriately robust, institutions should adhere to recognised standards of good governance, such as the Higher Education Code of Governance issued by the Committee of University Chairs[7] ("Code of Governance") or, if a college in Wales primarily providing further education courses, the Code of Good Governance for Colleges in Wales issued by Colegau Cymru.

53. HEFCW considers that the elements contained within these codes represent good governance practices. However, HEFCW understands that some institutions may not have previously adhered to such codes and that the codes are voluntary, as well as recognising that institutions be able to apply alternative governance practices to achieve similar outcomes.

54. Institutions must include a statement within their annual report stating the degree to which they have adhered to one of the codes outlined above and identify which of the codes they have adhered to, or make a statement that they have not adhered to one of the identified codes. Where institutions have

[7] Accessible at www.universitychairs.ac.uk/publications/

not adhered to the applicable code stated above, an explanation must be given within the institution's annual report. The explanation must describe the alternative governance procedures adopted in lieu of those recommended by the codes. Non-compliance with an applicable code will be considered to be acceptable provided that the explanation within the annual report describes equally robust alternative arrangements that are in place or indicates that there are appropriate and reasonable grounds for non-adherence.

55. HEFCW will assess the institution's compliance with good governance practices as part of its annual Institutional Risk Review process. Inadequate and/or ineffective corporate governance arrangements may lead HEFCW to conclude that the institution is likely to fail to comply with a requirement imposed by this Code. This may in turn lead to HEFCW assessing an institution as being at 'high risk'.

56. Members of governing bodies must comply with the seven principles set out by the Committee on Standards in Public Life. The governing body must inform HEFCW's Chief Executive immediately should it become aware that a governing body member or accountable officer has violated one or more of these principles.

57. Governing bodies and accountable officers are accountable for their decisions and actions, the former being accountable to HEFCW and the latter to the governing body. Governing bodies must submit themselves to whatever scrutiny is appropriate to their office. They must also be as open as possible about all the decisions and actions that they take that may affect the institution's financial position.

58. HEFCW will write to the new chair of each governing body of an institution, on appointment, drawing attention to their responsibilities, and those of the governing body generally, under this Code and related guidance.

59. The governing body of the institution has a responsibility to protect the collective student interest and the public interest and must ensure that consideration of these elements takes place within its key decision making processes, insofar as is consistent with their obligations under charity law.

Composition of the governing body

60. The composition of the governing body is first and foremost the responsibility of the governing body itself, acting within the bounds of the institution's governing documents.

61. Governing bodies should have at least one member with relevant financial experience gained within a predominantly finance-based role. Whilst this is not a requirement, governing bodies must disclose within their annual report should they not meet this requirement, together with an explanation of the degree to which the governing body feels it has been able to obtain adequate financial assurance. HEFCW considers it to be good practice to co-opt

members to institutional finance committees to provide relevant additional expertise, should a demonstrable financial skills gap exist.

62. HEFCW will consider the composition of the governing body, as well as the governance structure in relation to financial affairs, within its annual Institutional Risk Review process.

Absence of, or removal of accountable officer

63. In extremis and after all due process has been exhausted, the HEFCW Chief Executive may conclude that the institution's accountable officer is unable or unwilling to meet his or her responsibilities to the governing body under this Code or is unduly influencing the relationship between HEFCW and the governing body. HEFCW may then require the institution's governing body to designate someone else to report to HEFCW on behalf of the governing body. In taking this action HEFCW will not seek to influence the employment relationship (if one exists) between the governing body and the accountable officer.

64. In the event of a prolonged absence from post (or absence that is reasonably expected to be prolonged) or a sudden departure of the accountable officer, the governing body must appoint an interim accountable officer. The governing body must ensure that HEFCW is made aware immediately of the identity of the interim accountable officer.

Responsibility for reporting significant events and failures

65. The institution's governing body must notify HEFCW of any failure, or likely failure to comply with this Code without delay. Should the accountable officer be implicated in wrongdoing in respect of that failure, this report must be made directly by the governing body.

66. In addition, the institution's governing body must also report any failure, or likely failure that has, or is likely to have, a material adverse impact on the financial position of the institution, as soon as this becomes apparent, to:

    a. The chair of the institution's audit committee;
    b. The entirety of the governing body;
    c. The institution's head of internal audit; and
    d. The external auditor.

67. The institution's governing body must inform HEFCW, without delay, about major changes in strategy and/or risk profile, plans for major restructuring and significant changes to interests in the institution (including merger with another institution or organisation), as these are likely to have financial implications for the institution.

68. The governing body must inform HEFCW without delay of the removal or resignation of the external or internal auditors before the end of the term of their appointment.

69. Where a failure at the institution has triggered a notification to be made to another regulator such as the Charity Commission, the governing body must also immediately inform HEFCW of the failure to the extent allowable by law.

Responsibility to provide HEFCW with accurate and timely information

70. The governing body must provide and make arrangements for HEFCW, or agents acting on its behalf, to receive such information, assistance and access to the institution's facilities as HEFCW or its agent reasonably requires for the purpose of exercising its functions in relation to compliance with the Code under the 2015 Act[8], regardless of how the information is held and accessed. HEFCW retains the right to enter the premises of an institution to do so, but will give reasonable notice to the governing body of such an action, except where the situation is urgent or if giving notice of the visit defeats the purpose of that visit.

71. If so requested, the supply of information to HEFCW must be made in a format prescribed by HEFCW, and through an assurance process that provides HEFCW with appropriate confidence in the accuracy of the information.

72. However, HEFCW will at all times act reasonably in its requests for information and will have regard to the costs of providing this information, and, where appropriate, to its confidentiality.

73. If an institution fails to provide information as required by HEFCW by the specified deadline, or that information is not of satisfactory quality, HEFCW reserves the right to any of the following:

    a. To carry out whatever reasonable investigations it deems necessary to collect the data;
    b. To use its own reasonable estimates of data which it requires to exercise its functions under the 2015 Act; or
    c. Direct an institution, through processes outlined within the Statement of Intervention[9] to take (or not to take) specified steps for the purpose of securing the provision of information, assistance or access.

Notification of changes to senior roles

74. Members of the Senior Executive team and those in senior governance roles carry significant responsibility for the organisation and management of the institution's financial affairs. For this reason, the governing body must notify HEFCW of the formal appointment of a new chair of the governing body, a new clerk to the governing body and the appointment of members of the Senior Executive team.

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[8] Under sections 31 – 34 of the Higher Education (Wales) Act 2015
[9] Powers given under Section 35(2) of the 2015 Act.

Legislative requirements

75. Institutions must comply with all legislative requirements applicable to them and their governing bodies.

Monitoring of complaints

76. Institutions must have a robust process in place for the handling of complaints made by students, staff and third parties insofar as they relate to financial matters. Governing bodies must request and receive a complaints report at least annually, which provides the governing body with assurance over the degree to which adequate and effective complaint handling processes are in place.

77. Institutions should remain appraised of the latest guidance from the Competition and Markets Authority and the Office of the Independent Adjudicator, or any successor bodies fulfilling those roles.

Prudent management of the estate

78. The institution's estate is likely to represent a materially significant part of the institution's asset base. Sound financial organisation and management processes include good management of the estate.

79. Institutions must manage their estate in a sustainable way, in line with an estates strategy and a maintenance plan, covering its long-term and routine maintenance requirements.

80. The institution should give due regard to the guidance issued from time to time by HEFCW on estate procedures.

81. HEFCW recommends that institutions prepare and regularly review space plans. The metrics for measuring the success of such plans should be pre-agreed by the governing body.

82. Governing bodies should receive an annual report outlining estates performance.

Negative cash forecasts

83. The institution must prepare cashflow forecasts on a regular basis. Institutions should prepare annual and monthly forecasts covering the upcoming 12 months.

84. The governing body must inform HEFCW immediately if, at any point in the upcoming 12 months, negative net cash (as defined within FRS 102 S(7), including cash and cash equivalents) is forecast for more than 30 consecutive days.

Financial commitments

85. The primary responsibility for assessing the affordability of, and risks around, financial commitments rests with an institution's governing bodies. HEFCW's role is to assess whether any financial commitments entered into by the institution present challenges to the institution's sustainability or indicate issues in the organisation and management of financial affairs.

86. Institutions must apply the following principles prior to entering into any financial commitments:

    a. The risks and affordability of any new on- and off-balance sheet financial commitments must be properly considered, including through the use of prudent, sensitised downside forecasts;
    b. Financial commitments must be consistent with the institution's strategic plan, financial strategy and treasury management policy;
    c. The source of any repayment of a financial commitment must be clearly identified and agreed by the governing body at the point of entering into that commitment;
    d. Planned financial commitments must represent value for money;
    e. The risk of triggering immediate default through failure to meet a condition of a financial commitment must be monitored and actively managed;
    f. The institution must ensure that it retains sufficient liquid cash or equivalents to service working capital requirements as well as a prudent level of liquid reserve to be called upon in the case of extraordinary events; and
    g. The institution's ability to maintain sustainability must not be impaired as a result of its financial commitments.

87. Institutions are able to make financial commitments up to a predefined threshold. This threshold is based on the ratio of an institution's operating cashflow (adjusted for several elements) to its drawn and undrawn borrowings. This ratio is set out separately. Please see our website for further details, and see '**Annex B: Increases to a financial commitments threshold**').

88. The governing body must formally request permission from HEFCW to increase its threshold before it agrees to any new financial commitments that would result in the institution breaching its threshold.

89. Annex B sets out how the financial commitments threshold is calculated, as well as the information HEFCW requires to assess requests to increase the threshold. When HEFCW designates an institution as 'high risk', the governing body must obtain written permission from HEFCW, in advance, for any increase in its financial commitments.

90. The threshold should not deter an institution from increasing its financial commitments where appropriate. The governing body must determine a level

of financial commitments that is both affordable and consistent with its financial strategy.

91. In relation to any request for permission submitted to HEFCW, HEFCW will ask the institution to confirm that:

    a. The governing body is assured that key information or opinions relating to the proposed commitment or financial circumstances have not been withheld from the governing body and the governing body has been supplied with all necessary information required to enable it to come to a reasonable, balanced conclusion;
    b. The proposal represents good value for money,
    c. The governing body confirms that paragraph 86 above has been complied with; and
    d. That, following receipt of this information, the governing body has approved the proposal as presented to HEFCW.

92. In responding to requests for permission, HEFCW aims to be helpful and pragmatic, taking into account the circumstances of each proposal.

Activity costs should form part of decision making

93. An institution should know the full cost of its activities and use this information to make decisions. If it does not seek to recover the full cost, this should be the result of a clear policy set by the governing body and included in the financial strategy, and must not risk putting the institution in financial difficulty.

Financial statement preparation

94. The institution must keep proper accounting records and must prepare financial statements in respect of each accounting period.

95. Institutions and their external auditors must comply with the prevailing Accounts Direction issued by HEFCW, which is published in an annual circular letter.

96. The governing body must provide HEFCW with a copy of its audited consolidated financial statements by the date specified in the annual Accounts Direction.

97. The governing body must also send the audited accounts of its subsidiaries to HEFCW by the date specified in the annual Accounts Direction.

HEFCW's assurance processes

Institutional engagement, support and safeguarding actions

98. The 2015 Act makes provision for HEFCW to issue directions, advice and/or assistance, or to conduct a review, if HEFCW is satisfied that the governing

body of an institution has failed, or is likely to fail, to comply with a requirement imposed by this Code. HEFCW therefore operates a number of assurance processes to inform this view; these are designed to provide HEFCW with the necessary assurance while minimising burden on the sector. The processes may include:

a. annual assurance returns;
b. HEFCW Assurance Reviews;
c. Other sources (as defined below);
d. Institutional Risk Reviews;
e. strategic planning documents; and
f. data audits and assurance.

99. As far as possible the assurance process between HEFCW and institutions is concentrated into an exchange of documents and dialogue during a specific period following the end of the financial year. HEFCW's aim is to minimise its demands on institutions, and as far as possible to rely on data and information that institutions have produced to meet their own needs and those of other regulators.

Annual assurance returns

100. HEFCW's assurance process involves reviewing a suite of assurance returns, including audited financial statements, financial forecasts and independent audit reports, which must be submitted to HEFCW by a specified date or dates. They provide HEFCW with a view of each institution's risk management, control and governance, sustainability and arrangements for managing and quality assuring data. By using such information and assurances, much of which is needed for internal management and assurance purposes by the institution, HEFCW is able to minimise its audit requirements and reduce burden.

101. The annual assurance returns are analysed by HEFCW as part of the annual Institutional Risk Review process, which results in a risk assessment of each institution. The risk assessment is reported to the institution's governing body and accountable officer. Sometimes HEFCW will ask for more information to clarify uncertainties.

HEFCW Assurance Review

102. The HEFCW Assurance Review is a short site visit to the institution to ensure that there are suitable accountability processes within each institution to assure the validity of its annual assurance returns. This helps HEFCW to validate the systems of self-regulation on which it relies.

103. HEFCW usually visits each institution once within a three-year period but reserves the right to arrange visits more frequently. HEFCW will give reasonable notice of its visit and seek to arrange a mutually convenient time.

Data assurance

104. Institutions must supply HEFCW with data to inform HEFCW's understanding of the institution. The responsibility for the quality and accuracy of those data rests with the institution. HEFCW relies on the institution's own data assurance processes where possible.

105. HEFCW monitors the reasonableness of data and undertakes verification, validation and reconciliation work between various datasets. HEFCW may undertake its own audits at institutions. Data audits assess the strength of institutional systems and controls as well as assessing the accuracy of the data submissions.

Other sources

106. HEFCW uses a number of mechanisms and sources to enable it to remain informed over risks to the institution, including:

a. **HEFCW's own institutional audit processes**, including data audits and cyclical assurance visits.
b. **The continuing dialogue that HEFCW has with each institution** about their changing priorities and strategies, and their reporting of material events.
c. **Information from other sources** including public bodies whose work might potentially impact on HEFCW's concerns in respect of the institution's sustainability or the organisation and management of its financial affairs.
d. **Information provided to HEFCW through public interest disclosures** but only when substantiated in dialogue between HEFCW and the institutions concerned, for example in relation to the application of fee limits.
e. **Other sources** of publicly available data.

Institutional Risk Reviews

107. HEFCW has a risk assessment system covering all institutions. This is an annual process that draws on the information that HEFCW routinely collects. Sometimes HEFCW will ask for more information to clarify its understanding. HEFCW classifies institutions according to three risk categories:

Low risk	The institution is unlikely to fail to comply with the Financial Management Code.
Moderate risk	The institution has, or may fail to comply with the Financial Management Code over the short to medium term, but the impact of this does not lead to sustainability concerns over that period.
High risk	The institution has, or is likely to fail to comply with the Financial Management Code over the short to medium term, and the impact of this leads to sustainability concerns over that period.

108. HEFCW's Statement of Intervention describes the range of ways in which it might respond to help institutions resolve difficulties and manage risks.

109. The work undertaken by HEFCW, augmented by information from other sources, enables HEFCW to make an annual risk assessment within the Institutional Risk Review process. For the majority of institutions this results in a letter from the HEFCW Chief Executive to the accountable officer, normally by the end of July, advising of HEFCW's Council's judgement of risk. The governing body must ensure that the accountable officer is instructed to supply risk assessment letters to the governing body in a timely manner. For some institutions a second risk assessment letter may be issued in the autumn following assessment of their financial forecast submissions in July.

110. The HEFCW risk assessment letter will be qualified by comments alerting the institution to concerns HEFCW has that must be addressed and which, in some cases, if not addressed, may lead to a worsening of the institution's risk status. The comments can cover a range of issues, including financial performance, future viability and issues of non-compliance with assurance requirements. Some of these matters are more serious than others. HEFCW will endeavour in such cases to explain the issues fully, and institutions should consider and deal with HEFCW's concerns.

111. In exceptional cases, HEFCW's judgment will be that an institution is 'high risk'. The process of making such a judgement is very thorough. In the event that such a judgement is made, it will be communicated to the institution concerned and HEFCW will act in accordance with the Statement of Intervention.

112. Beyond the exchange of assurance information each year, HEFCW welcomes the opportunity for regular and informal discussions with institutions about their plans and developments.

Audit Code of Practice

Governing bodies of institutions

113. Governing bodies are responsible for the appointment and removal of external and internal auditors.

114. Governing bodies are also responsible for appointing outsourced internal audit providers (on the advice of the institution's audit committee) and for choosing to move between outsourced and insourced internal audit provision, also after taking advice from the audit committee. Staff appointments and terminations for insourced internal audit staff are a matter for the institution's senior executive team, with the audit committee advising on the appointment and termination of the Head of Internal Audit.

115. The governing body must satisfy itself that where the institution has departed from the provisions in this Code that are prefaced with 'should' (i.e. our view of good practice) there are reasonable grounds for doing so and these reasons are not detrimental to the control environment within the institution. The governing body must provide assurance that they have taken such guidance into account if requested by HEFCW.

116. Where the clerk to the governing body has significant responsibilities at senior executive team level within the institution, the governing body must consider whether the independence of the clerk's position is at risk of being compromised. If so, the governing body must consider whether the role should be transferred to someone else or sufficient safeguards can be built into existing arrangements. This should be reviewed by the governing body at least every three years.

Audit committees in institutions

117. Each institution must have an audit committee which follows good practice in higher education corporate governance. The audit committee is responsible for assuring the governing body about the adequacy and effectiveness of:

    a. risk management, control and governance;
    b. economy, efficiency and effectiveness (VFM); and
    c. management and quality assurance of data submitted to HEFCW and other bodies such as the Higher Education Statistics Agency and the Student Loans Company

118. The Committee of University Chairs publishes detailed guidance about audit committees. This reflects good governance practice, and each governing body must take account of such guidance, as well as that of other relevant bodies, such as the Leadership Foundation, or explain within its annual report why the guidance is not being applied.

119. An audit committee can undertake whatever work it considers necessary to fulfil its role. This should include assuring itself about the effectiveness of the

internal audit function and the external auditors. Audit committees will only be able to provide the necessary assurances if they are supported by suitably resourced internal audit and external audit functions, operating to recognised professional standards. They should also consider evidence-based assurances from management.

120. Members of the audit committee must not have or exercise any executive management responsibilities. Audit committees should include a minimum of three lay members of the governing body. The chair of the governing body should not be a member of the audit committee.

121. Audit committees should usually have at least one member with relevant experience gained in a finance or audit role. Where an exception to this good practice is exercised, a disclosure must be made within the annual report stating the absence of finance or audit backgrounds, and outlining the relevant skills of the audit committee members.

122. Audit committee members should not be members of the institution’s finance committee or its equivalent. This is because it would create a potential conflict of interest when the audit committee is considering issues involving the finance committee. If an institution’s governing body determines that cross-representation involving one or more members is essential, this must be the subject of an explicit, recorded resolution, which sets out the rationale for such a decision. However, there must not be such cross-representation for the chair of either committee or the chair of the governing body.

123. Where internal audit undertakes advisory work, the audit committee must satisfy itself that the objectivity of future audit work over the same areas is not compromised.

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

125. The report should record the work of the audit committee and consider the following:

    a. The external auditors’ communications with those charged with governance and the external audit management letter;
    b. The internal auditor’s annual report;
    c. Audit reports and assurances received during the year in respect of the controls in place to manage the quality of data returns;
    d. Value for money work;
    e. Any relevant HEFCW correspondence, such as HEFCW’s risk assessment letter received as part of the Institutional Risk Review process.

126. The report must formally record the audit committee's opinion on the adequacy and effectiveness of the institution's arrangements for:

a. risk management, control and governance
b. economy, efficiency and effectiveness (VFM)
c. management and quality assurance of data used and submitted for regulatory purposes.

127. The finalised annual report to the governing body and the accountable officer must be shared with HEFCW each year.

Finance committees

128. Each institution should have a finance committee or equivalent, comprised of at least one individual with relevant finance experience. The finance committee should meet regularly to advise the governing body on the institution's financial matters.

129. Whilst convening a finance committee or equivalent is not a requirement of this Code, governing bodies must disclose within their annual report should they not have a finance committee, together with an explanation of the degree to which the governing body feels it has been able to obtain adequate financial assurance.

130. Where the institution has a finance committee, but that committee does not have at least one individual with relevant finance experience, a disclosure must be made within the annual report stating the absence of finance backgrounds, and outlining the relevant skills of the finance committee members.

Internal audit arrangements in institutions

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

132. Consequently each institution must have an internal audit function which complies with the Public Sector Internal Audit Standards[10] or successor standards. Internal audit terms of reference must make clear that its scope encompasses all the institution's activities, the whole of its risk management, control and governance, and any aspect of VFM delivery.

133. The internal audit function must be adequately resourced; that is, the internal audit function must be able to audit all key risk areas within a reasonable timeframe, with each individual audit being afforded sufficient time to allow adequate work to be undertaken.

[10] https://www.gov.uk/government/publications/public-sector-internal-audit-standards

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

135. The annual report must include the internal auditor's opinions on the adequacy and effectiveness of the institution's arrangements for:

a. risk management;
b. internal control; and
c. governance

136. The finalised annual report to the governing body must be shared with HEFCW each year.

137. The head of internal audit must have direct access to the institution's accountable officer, the head of the institution (if different to the accountable officer), the chair of the audit committee, the chair of the finance committee (where applicable) and, if necessary, the chair of the governing body.

138. Whether provided internally or externally, day to day line management and overall reporting arrangements for the internal audit service must be such as to preserve its objectivity by avoiding too great a concentration of responsibility and reporting within any one senior person at the institution. Particular attention must be paid to a reporting line where the head of internal audit reports to those charged with principal responsibility for risk management, financial management and/or governance processes. In such cases, the institution must design appropriate safeguards to protect the independence and objectivity of the head of internal audit.

139. The institution must formally document that the head of internal audit is unequivocally free to act in an independent manner in pursuit of their professional business and must not be fettered in their scope or reporting.

140. There should be periodic assessment of whether in-house or externally-sourced internal audit provision is the appropriate type of provision for the institution. This assessment should happen at least once every five years.

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

142. Safeguards must be put in place where internal audit review an area on which the same firm has previously provided advice in a consultancy capacity. These safeguards must ensure the objectivity and independence of the internal audit function.

143. Where an institution is assessed by HEFCW as being 'high risk', the action plan for addressing recommendations arising from internal audits covering core financial work, governance and risk management must be shared with HEFCW as soon as they are agreed, or an explanation forwarded in the event

of delay in agreeing the recommendations. The responsibility for sharing the management action plan rests with the governing body and not the internal auditor. However, internal auditors should remind the institution of their responsibilities should they become aware that information is not being shared. Under the terms of this Code, institutions must not penalise auditors who notify HEFCW of their suspicion of a deliberate delay in the reporting of this information to HEFCW, whether or not it be proven to be true.

144. The governing body must inform HEFCW without delay of the removal or resignation of the internal auditors and of the reasons.

External audit arrangements in institutions

145. External audit must provide an opinion to the governing body on whether funds (including public funds, where applicable) have been applied for the intended purposes and on whether the financial statements provide a true and fair view of the financial results for the year. External audit must also form a view about whether an institution is a going concern. External auditors of institutions do not owe a duty of care to HEFCW.

146. Institutions may commission external auditors to provide additional services. The institution's audit committee must provide its consent where such additional services may have a bearing on the auditors' objectivity and independence. Additional work must not impair the independence of the external audit opinion.

147. Institutions must disclose separately, by way of a note in the financial statements, the fees paid to their external auditors for other services and the nature of those services.

148. Market testing should normally be undertaken at least every five years. One named individual partner in the firm is normally responsible for the institution's audit; (s)he should not hold this position for more than five consecutive years. This may be extended to seven years where the criteria set out within the Auditing Standards Board Ethical Standard, Section 3 are met (excluding the requirement to be listed)[11].

External auditor selection procedures

149. Institutions must ensure that their external auditors are eligible for appointment as statutory auditors. Auditors must be registered with one of the appropriate professional bodies.

150. Selection criteria and procedures for the appointment of external auditors should be determined by the governing body in advance of receiving proposals and should be endorsed by the audit committee.

[11] The Auditing Practices Board Ethical Standard 3 (Revised) (https://frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/Revised-Ethical-Standard-June-2016.pdf)

External auditor's report

151. External auditors must issue to the governing body a report (or reports, if more than one, covering different stages of the annual audit), which records accounting issues and control deficiencies arising from the audit. Any issues around the use of charitable assets for non-charitable purposes must be highlighted in such reports. The institution's management must provide written responses to any recommendations made or issues raised. The report(s), including management response, is one of the annual assurance returns which must be submitted to HEFCW.

152. External auditors must comply with the reporting requirements of the prevailing annual Accounts Direction.

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

154. Auditors should, within their management letters or reports, have regard to the specific requirements of the Code such as compliance with those provisions relating to increases in financial commitments thresholds, or other issues of non-compliance as set out in paragraph 151 above.

HEFCW access to auditors

155. HEFCW may wish to communicate with an institution's external or internal auditors, particularly in connection with a HEFCW Assurance Review, and the governing body must ensure HEFCW has unrestricted access to do so. This will normally be arranged through the institution's accountable officer or representative. HEFCW will exchange letters where necessary with both parties to deal with confidentiality and the terms under which access is given.

Provision of audit services

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

Auditors' access to information

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

Limitation on auditors' liability

158. Where the internal audit service is provided through a contractual arrangement with an external provider, the provider may ask the institution to agree to a limitation of the provider's liability arising from its default. Normally such liability should be unlimited. However, institutions may negotiate a limitation of liability so long as the decision is made on an informed basis and

the liability remains at such a level as to provide reasonable recourse for the institution. The governing body, through the audit committee, must be specifically notified of any request for a liability limitation.

159. Institutions must not agree to any limitation of external auditors’ liability in respect of the external audit of their annual financial statements.

160. For other types of work performed by the external auditors, the provider may ask the institution to agree to a limitation of the provider’s liability arising from its default. However, as with internal audit services, institutions may negotiate a limitation of liability if the decision is made on an informed basis and the liability remains at such a level as to provide reasonable recourse for the institution. The governing body, through the audit committee, must be specifically notified of any request for a liability limitation.

Reporting serious failures

161. A serious failure to comply with the Code is usually determined by reference to the degree to which non-compliance has resulted in, or could reasonably be expected to result in:

    a. significant internal control deficiencies; and/or
    b. a significant risk to an institution’s sustainability, property, work, major stakeholders (e.g. students, staff, funders, regulators etc.) or reputation; and/or
    c. the extent to which non-compliance has been, or is suspected to have been, intentional or fraudulent.

162. Reportable fraud and financial irregularities encompassed by this definition includes those where one or more of the following apply:

    a. The sums of money are, or potentially are, in excess of £25,000;
    b. The particulars of the fraud or irregularity are novel, unusual or complex; or
    c. There is likely to be public interest because of the nature of the fraud or irregularity, or the people involved.

163. There may be cases of serious failure that fall outside this definition. In these cases, institutions can seek advice or clarification from HEFCW. In view of the public interest, institutions should normally notify the police of suspected or actual fraud. Where the police are not notified, the governing body should ensure that the institution’s audit committee is informed of the reason for not doing so.

164. Institutions must report serious failures to HEFCW at the time they are identified. Institutions must also sign the specific declaration in the annual assurance return that serious failures have been reported appropriately to HEFCW.

165. Serious failures, including those that are suspected but not confirmed, must be reported to the institution's internal auditors immediately, in order that they can assess the adequacy of the relevant controls and any impact on their opinion of risk management, control and governance processes.

166. In the event that internal investigations into suspected serious failures may be time-consuming, the institution should provide HEFCW with a provisional report.

167. The report relating to a serious failure must be sent to the HEFCW Chief Executive. Institutions should provide as much information as possible to help HEFCW understand the appropriateness of the response and what, if any, further action is planned. In particular the report must indicate:

a. whether the incident has happened or is suspected;
b. when it occurred and who was involved;
c. the impact of the incident on the institution and any stakeholders;
d. what inquiries have been made and actions taken, including any reports to other regulators or the police;
e. what controls were in place that applied to the incident, whether they were followed and, if not, why not; and
f. whether the governing body has determined that controls need to be introduced or revised – and if so, how and by when.

168. In extreme cases, a serious failure report may lead HEFCW to invite the Charity Commission to consider instituting an inquiry under section 46 of the Charities Act 2011.

169. HEFCW appreciates that information provided under paragraphs 161 to 167 may be of a sensitive nature, and it undertakes to treat it with care. As a public authority, HEFCW is subject to the Freedom of Information Act 2000. HEFCW will only disclose information to someone outside HEFCW where legally obliged to do so, as necessary to perform its duties under the Act, or after obtaining consent of the institution.

170. For the purposes of this code, a 'serious failure', where confirmed by HEFCW, constitutes a failure to comply with the terms of this Code; however, the courses of remediation available to HEFCW for serious failures are different to those for failure. More information is available within the Statement of Intervention.

Professional standards

171. Internal auditors must adhere at all times to the Public Sector Internal Audit standards or successor standards. External auditors must adhere at all times to the professional standards of a recognised accrediting accounting body.

172. Internal and external auditors must not take on any executive management responsibilities, or hold any interest - financial or non-financial, direct or indirect - in the institution (other than the normal employee or contractor

relationship, or the funding of any prize, scholarship or academic appointment).

173. It is generally not acceptable for a firm to provide an opinion as external auditor about the same firm's work as internal auditor, unless the audit partner has changed and the institution has requested and obtained sufficient assurances over the objectivity and independence of the external audit team.

Appointment, removal or resignation of internal and external auditors

174. Governing bodies are responsible for the appointment and removal of external and internal auditors. Where auditors cease to hold office for any reason, they should provide the governing body with either a statement of any circumstances connected with their resignation or removal which they consider should be brought to the governing body's attention, or a statement that there are no such circumstances.

175. Any such statements as outlined in paragraph 174 must also be sent to HEFCW by the governing body.

Signature of the Governing Body Chair

176. The chair of the governing body of (**name of institution**) must signify below that they have received the terms of this Code, as prepared under the 2015 Act.

Signed……………………………………………....................................

Dated ……………………………………

Annex A: Institutional engagement processes

Introduction

A1. This annex sets out how HEFCW will engage with and support institutions on matters relating to assurance and risk assessment. It also describes what will happen when, as a result of HEFCW's assessment, HEFCW finds that the institution has failed, or is likely to fail, to comply with a requirement imposed by this Code.

A2. The principles underlying HEFCW's engagement are that HEFCW will:

a. seek to work in partnership with institutions in the first instance;
b. respect the independence of institutions;
c. act reasonably and fairly;
d. engage transparently and consistently;
e. protect the collective interests of students, the public and the taxpayer;
f. maintain an open dialogue on matters of mutual interest;
g. seek to intervene only when necessary, but HEFCW will do so vigorously, using the full extent of its powers, when it judges that an institution's management and governing body are not effectively addressing risks in respect of the organisation and management of the institution's financial affairs;
h. be open with the institution in HEFCW's Institutional Risk Review and requirements and, if warranted, on student or public interest grounds, disclose its risk assessments publicly;
i. ensure its involvement is proportionate to the risks; and
j. end its enhanced involvement as early as possible.

How HEFCW engages

A3. In broad terms there are three levels at which HEFCW may engage with institutions:

a. normal contact;
b. focused; and/or
c. through the Statement of Intervention.

Each of these is dealt with below.

Normal contact

A4. As part of its routine engagement with institutions, HEFCW will seek to understand their mission, strategy and operational plans. This will help HEFCW to make appropriate responses to the needs of the institution and the higher education sector generally, and to gain assurance about matters that affect the delivery of HEFCW's own objectives. There will often be a formal visit by a representative of HEFCW to the institution each year, sometimes in addition to more frequent and less formal exchange of information and views. It is also part of HEFCW's normal contact to discuss an institution's assurance returns and give feedback, as part of the annual assurance returns exercise.

Focused dialogue

A5. There are occasions when it is to the advantage of both HEFCW and an institution to explore issues in more detail. For example, an institution may wish to secure HEFCW's support for particular plans, and HEFCW will want to understand how best to provide help to meet the institution's development needs and to ensure they fit with HEFCW's wider objectives for the higher education sector. Likewise, HEFCW may wish to discuss with an institution whether there are opportunities to improve its performance or work collaboratively with others. There will also be cases where an institution's risks are increasing because of strategic factors which impact upon its financial outlook, for instance, changes in student demand or increased competition, its performance or its internal control arrangements. At such times HEFCW will engage to try to ensure that the risks are appropriately addressed.

Statement of Intervention

A6. Where an institution fails, or is likely to fail, to comply with a requirement imposed by this Code, HEFCW may instigate the processes within the Statement of Intervention.

A7. The Statement of Intervention outlines the processes that HEFCW will undertake prior to formal intervention. HEFCW expects, in most cases, that an initial conversation with an institution, as outlined in the Statement of Intervention, will be able to resolve most minor cases of likely or actual non-compliance and this will be our preferred route of engagement in these cases. However, HEFCW retains the right to exercise its discretion and where necessary may initiate formal intervention processes. More detail on these processes is provided within the Statement of Intervention.

A8. As outlined within the Statement of Intervention, the process of engagement adopted by HEFCW will be determined by the degree of failure to comply with the Code.

A9. 'Serious failure' is defined in paragraph 161.

Annex B: Increases to a financial commitments threshold

Introduction

B1. Section 27(2)(a) of the 2015 Act states that the Code may make provision about circumstances in which an institution is to enter into a transaction of a class specified in the Code only with the consent of HEFCW.

B2. The governing body must request an increase in its financial commitments threshold from HEFCW, before it agrees to any new financial commitment:

a. Where the average ratio of an institution's operating cashflow (adjusted for several elements, as outlined below) to its drawn and undrawn borrowings exceeds the threshold set out by HEFCW (refer to website); or

b. Where the institution is assessed by HEFCW as being at high risk.

B3. All such requests should allow HEFCW a reasonable time (usually at least six working weeks) to examine the request and provide an opinion on it.

B4. The purpose of our review is to determine that the proposed financial commitments are affordable and have been provided appropriate scrutiny by the governing body. We do not (under this Code) have a role in other aspects of the financial commitments, such as setting conditions or restricting the use of funds.

B5. In the event that an institution chooses to proceed with borrowing where HEFCW's sanction has not been given, the risk assessment for that institution will be modified accordingly. It is possible, depending upon the circumstances, that HEFCW will determine that there are poor financial planning processes in place which ultimately may mean that the institution is not sustainable.

How the financial commitments threshold is calculated

B6. The metric template is based on the proforma financial statements issued by the Financial Reporting Group, part of the British Universities Finance Director's Group (http://www.bufdg.ac.uk/sorp/resources).

	Actual (prior year)	Actual (current year)	Forecast (years 1-4)
	£	£	£
Net cashflow from operating activities	20,834	34,836	xx
Add: Cash received from investment income	1,903	1,725	X
Endowment cash received	1,950	2,123	x
Deduct: Cash paid on interest on borrowings	(3,236)	(2,217)	(x)
Cash paid on interest element of finance leases	(278)	(240)	(x)
(a) Adjusted operating cashflow	**13,591**	**17,379**	**xx**

Year-end borrowings (drawn)	53,225	35,016	xx
Facilities (undrawn)	0	0	x
(b) Adjusted year-end borrowings	**53,225**	**35,016**	**xx**

Metric (b÷a)	**3.9**	**2.0**	**0.0**

B7. Where the adjusted operating cashflow (a) figure is negative it should be deemed to be £1.

Explanation of adjustments

B8. In the proforma accounts, investment and endowment income (notes five and six) have been excluded from the “Net cash inflow from operating activities”. They have been added back in the calculation because they are considered part of the cashflow available to repay borrowings.

B9. Interest payable on borrowings and finance leases (note 8) has been deducted in the calculation because they are considered a cost of operating activities.

B10. The figure for total year-end borrowings should agree with the total borrowings returned in the annual Financial Forecast submission.

What are financial commitments?

B11. Financial commitments should be defined as those that are on balance sheet, in accordance with FRS 102.

B12. Financial commitments include:

a. all financial commitments, whether self-financing or not, drawn or undrawn;

b. finance leases;

c. Private Finance Initiative arrangements which are accounted for as loans or finance leases in accordance with the requirements of Statement of Standard Accounting Practice 21 or Financial Reporting Standard 5; and

d. repayable grants.

B13. In calculating the threshold for financial commitments, pension fund liabilities and all provisions should be excluded.

B14. Where existing financial commitments exceed institutions' cashflow-based threshold at 1 September 2016, HEFCW will automatically agree to the higher financial commitment threshold, though any changes to financial commitments after this date will require an application to be made to HEFCW. As part of this transition, we may need to engage with some institutions about their ability to service their financial commitments.

B15. Where an institution exceeds its financial commitments threshold in the future because of a decline in its cashflow, it need not apply for a higher threshold, but the governing body must inform us of this fact. Whilst an application for a higher threshold will not be required, the decline in cashflow it is likely to lead to engagement with that institution about its ability to service its financial commitments. We will not consider such a scenario, taken in isolation, to represent a failure to meet the requirements of this Code, and HEFCW will take the context as a whole in to account.

Our response

B16. HEFCW takes a risk-based approach to each institution's application for an increase to its financial commitments threshold. This approach will determine whether the application is considered by the HEFCW Chief Executive or by the HEFCW Council. Institutions must therefore include their financial commitments plans as far as possible in their annual financial forecasts submissions, to enable HEFCW to review them at an early stage. Institutions are also advised to discuss their plans informally with HEFCW at an early stage. Where HEFCW approves an application for a higher financial commitments threshold, it will write to the institution setting out the revised threshold. As part of this process, HEFCW may set out additional requirements which will need to be adhered to.

Information required

B17. All applications for a higher financial commitments threshold must be signed by the chair of the governing body. By signing the application, the governing body confirms that it has reviewed the terms and conditions of the financial commitment, thereby providing assurance regarding value for money, and has reviewed affordability and compliance with banking covenants under different scenarios (meaning that the proposed financial commitments have been stress tested). In addition HEFCW asks for confirmation that the student interest has been considered in all applications.

B18. HEFCW sets out in ‘Table 1: Information required by HEFCW to consider a request to increase a financial commitments threshold’ the information it requires in order to be able to consider a request for an increase to an institution’s financial commitments threshold. This highlights the issues on which the institution’s own governing body should seek assurance before approving additional financial commitments. The main focus is on affordability and risk, not necessarily on the individual project.

Table 1: Information required by HEFCW to consider a request to increase a financial commitments threshold

Financial commitments
1. There should be a reasonable case for the new investment. Information required: a. A brief description of the new investment. b. An explanation of how it broadly fits with the institution's mission and strategic priorities. c. Confirmation that the institution has considered appropriate guidance on appraising investment decisions. d. A description of how the student interest will be taken into account.
2. The new financial commitments or refinancing arrangement (where these will result in an increase to the financial commitments threshold) should be consistent with the institution's financial strategy and represent good value for money. Information required: a. An explanation of why additional finance or refinancing is necessary and how this fits with the institution's financial strategy. b. The forms of finance considered and the selection process and criteria. c. The net present value for each financing option, and a brief explanation of why the chosen method was selected.
3. Details of the new financial commitments. Information required: a. Details of the chosen option, including name of lender, value of new financial commitment, repayment period, basis of repayment and financial covenants. b. Terms and conditions of the financing (such as a copy of the offer letter) and an evaluation of the risks and uncertainties.
4. The new investment and financial commitments must be affordable. Information required: An update of the latest financial forecasts, to include the impact of the new investment and financial commitments, and demonstration that they are affordable. This update must include any other material changes in the institution's financial prospects, including guarantees to third parties.

5. The institution's governing body must have made an informed decision about the new investment and financial commitments.

Information required:

a. Details of when the governing body approved the new investment and financial commitments, and a minute of the decision reached.

b. A summary of the information the governing body received in reaching its decision.

c. Confirmation that:

   i. No key information or opinions relating to the proposed commitment or financial circumstances have been withheld from the governing body and the governing body has been supplied with all necessary information required to allow reasonable individuals to come to a reasonable, balanced conclusion;
   ii. The governing body confirms that paragraph 86 of the Financial Management Code has been complied with;
   iii. That, following receipt of this information, the governing body has approved the borrowing as presented to HEFCW.

6. Details of the new threshold.

Information required:

a. Details of existing financial commitments (including the lender, terms, interest rate and financial covenants) and of the new financial commitments.

b. A calculation of the new threshold required.

Annex C: Summary of provisions

This annex provides a summary of ‘must’ and ‘should’ provisions contained within this Code. It is intended to provide a handy checklist for compliance with this Code and for the guidance that a governing body must take into account.

The provisions below are summarised versions of the provisions contained in the full text of the Code. Readers should always consult the full text of the Code where in doubt. In the event of inconsistencies and/or omissions between the summary provisions here, and the full text of the provisions in the Code, the full text of the provisions in the Code take precedence.

‘Must’ provisions

Provision	Paragraph reference	Compliant?
The governing body must ensure that the institution takes all necessary steps to comply with this Code.	28	
The governing body of the institution must ensure that all reserves are used for the purposes intended.	29	
The governing body of the institution must ensure that it has appropriate arrangements for the organisation and management of its financial affairs, including an adequate and effective internal control environment.	32	
The governing body of the institution must plan and conduct its financial affairs on a sustainable basis.	33	
Institutions which are subsidiaries must be able to demonstrate that they are financially viable (see text for details)	35	
Governing bodies must ensure that the institution has conducted a thorough risk assessment of adverse events that could give rise to sustainability concerns.	36	
Governing bodies must inform HEFCW immediately if they consider that an adverse event is likely to occur.	36	

The institution must ensure that it has an effective policy of risk management.	41	
The governing body must designate an individual as the ‘accountable officer’	42	
The governing body must notify HEFCW whenever it designates an accountable officer.	43	
The governing body must ensure that there are robust governance arrangements in place.	49	
Institutions must include a statement within their annual report stating the degree to which they have adhered to one of the stated governance codes.	54	
Members of governing bodies must comply with the seven principles set out by the Committee on Standards in Public Life.	56	
The governing body must inform HEFCW’s Chief Executive immediately should it become aware that a governing body member or accountable officer has violated one or more of these principles.	56	
Governing bodies must submit themselves to whatever scrutiny is appropriate to their office. They must also be as open as possible about all the decisions and actions that they take that may affect the institution’s financial position.	57	
The governing body must ensure that consideration of the collective student interest and the public interest takes place within its key decision making processes.	59	
Governing bodies must disclose within their annual report should they not have at least one member with relevant financial experience gained within a predominantly finance-based role, together with an explanation of the degree to which the governing body feels it has been able to obtain adequate financial assurance.	61	
The governing body must appoint an interim accountable officer in the event of a prolonged absence.	64	

(If an interim accountable officer appointed), the governing body must ensure that HEFCW is made aware immediately.	64	
The governing body must notify HEFCW of any failure, or likely failure to comply with this Code without delay.	65	
The governing body must report any failure, or likely failure that has, or is likely to have, a material adverse impact on the financial position of the institution to key individuals/stakeholders (see text for details)	66	
The governing body must inform HEFCW, without delay, about major changes in strategy and/or risk profile, plans for major restructuring and significant changes to interests.	67	
The governing body must inform HEFCW without delay of the removal or resignation of the external or internal auditors before the end of the term of their appointment.	68	
The governing body must also immediately inform HEFCW of a notification made to another regulator (subject to legality)	69	
The governing body must provide HEFCW or its agents with information, assistance and access to the institution’s facilities to exercise its functions under the Act.	70	
If requested, information must be supplied in a format prescribed by HEFCW, and through an assurance process that provides HEFCW with appropriate confidence.	71	
The governing body must notify HEFCW of the formal appointment of a new chair of the governing body, a new clerk to the governing body and the appointment of members of the Senior Executive team.	74	
Institutions must comply with all legislative requirements applicable to them and their governing bodies.	75	
Institutions must have a robust process in place for the handling of complaints made by students, staff and third parties.	76	

Governing bodies must request and receive a complaints report at least annually.	76	
Institutions must manage their estate in a sustainable way.	79	
The institution must prepare cashflow forecasts on a regular basis.	83	
The governing body must inform HEFCW immediately if, at any point in the upcoming 12 months, negative net cash (as defined within FRS 102 S(7), including cash and cash equivalents) is forecast for more than 30 consecutive days.	84	
Institutions must apply a set of principles prior to entering into any financial commitments (refer to main text).	86	
The governing body must obtain written permission from HEFCW to increase its threshold before it agrees to any new financial commitments that would result in the institution breaching its threshold.	88	
When HEFCW designates an institution as 'high risk', the governing body must obtain written permission from HEFCW, in advance, for any increase in its financial commitments.	89	
The governing body must determine a level of financial commitments that is both affordable and consistent with its financial strategy.	90	
If an institution chooses not to recover the full cost of its activities, the policy must not risk putting the institution in financial difficulty.	93	
The institution must keep proper accounting records and must prepare financial statements in respect of each accounting period.	94	
Institutions and their external auditors must comply with the prevailing Accounts Direction.	95	
The governing body must provide HEFCW with a copy of its audited consolidated financial statements by the date specified in the annual Accounts Direction.	96	

The governing body must send the audited accounts of its subsidiaries to HEFCW by the date in the Accounts Direction.	97	
Financial forecasts and independent audit reports must be submitted to HEFCW by a specified date or dates.	100	
Institutions must supply HEFCW with data to inform HEFCW's understanding of the institution.	104	
The governing body must ensure that the accountable officer is instructed to supply risk assessment letters to the governing body in a timely manner.	109	
The governing body must satisfy itself that where the institution has departed from the provisions in this Code that are prefaced with 'should' there are reasonable grounds for doing so and these reasons are not detrimental to the control environment within the institution.	115	
The governing body must provide assurance that they have taken 'should' provisions into account if requested by HEFCW.	115	
Where the clerk has significant responsibilities at senior executive level, the governing body must consider whether the independence of the clerk's position is at risk. If so, the governing body must consider whether transferring the role or examine the safeguards in place.	116	
Each institution must have an audit committee which follows good practice in higher education corporate governance.	117	
The governing body must take account of CUC and LFHE guidance, as well as that of other relevant bodies, or explain within its annual report why the guidance is not being applied.	118	
Members of the audit committee must not have or exercise any executive management responsibilities.	120	

Where an audit committee does not have at least one member with relevant experience gained in a finance or audit role, a disclosure must be made within the annual report.	121	
If there is cross-representation of members between a finance committee and audit committee, this must be accompanied by the subject of an explicit, recorded resolution, which sets out the rationale for such a decision.	122	
However, there must not be cross-representation on the finance committee and audit committee for the chair of either committee or the chair of the governing body.	122	
Where internal audit undertakes advisory work, the audit committee must satisfy itself that the objectivity of future audit work over the same areas is not compromised.	123	
The audit committee must produce an annual report for the governing body and the accountable officer, covering the financial year, including any significant issues up to the date of signing the report. The report must be reviewed by the governing body before the audited financial statements are signed.	124	
The audit committee annual report must record the committee's opinion on the adequacy and effectiveness of the institution's arrangements for: d. risk management, control and governance e. economy, efficiency and effectiveness (VFM) f. management and quality assurance of data used and submitted for regulatory purposes.	126	
The final audit committee annual report must be shared with HEFCW each year.	127	
Governing bodies must disclose within their annual report should they not have a finance committee, together with an explanation of	129	

the degree to adequate financial assurance has been obtained.		
Where the institution has a finance committee, but that committee does not have at least one individual with relevant finance experience, a disclosure must be made within the annual report stating the absence of finance backgrounds, and outlining the relevant skills of the finance committee members.	130	
Each institution must have an internal audit function which complies with the Public Sector Internal Audit Standards or successor standards.	132	
Internal audit terms of reference must make clear that its scope encompasses all the institution's activities, the whole of its risk management, control and governance, and any aspect of VFM delivery.	132	
The internal audit function must be adequately resourced.	133	
Internal audit must produce an annual report for each financial year including significant issues, up to the date of signing the report, which affect the opinions. It must be addressed to the governing body and the accountable officer and must be considered by the audit committee.	134	
The internal audit annual report must provide an opinion on the adequacy and effectiveness of the institution's arrangements for: a. risk management; b. internal control; and c. governance	135	
The finalised annual report to the governing body must be shared with HEFCW each year.	136	
The head of internal audit must have direct access to the institution's accountable officer, the head of the institution (if different to the accountable officer), the chair of the audit committee, the chair of the finance committee (where applicable) and, if necessary, the chair of the governing body.	137	

Day to day line management and overall reporting arrangements for the internal audit service must preserve its objectivity.	138	
The institution must formally document that the head of internal audit is unequivocally free to act in an independent manner in pursuit of their professional business and must not be fettered in their scope or reporting.	139	
Safeguards must be put in place where internal audit review an area on which the same firm has previously provided advice in a consultancy capacity.	142	
Internal audit recommendations from core financial work, governance and risk management must be shared promptly with HEFCW for institutions at high risk.	143	
The governing body must inform HEFCW without delay of the removal or resignation of the internal auditors and of the reasons.	144	
External audit must provide an opinion to the governing body on whether funds (including public funds) have been applied for the intended purposes and on whether the financial statements provide a true and fair view of the financial results for the year. External audit must also form a view about whether an institution is a going concern.	145	
The institution's audit committee must provide its consent where the provision of additional services may have a bearing on the auditors' objectivity and independence.	146	
Institutions must disclose separately, by way of a note in the financial statements, the fees paid to their external auditors for other services and the nature of those services.	147	
Institutions must ensure that their external auditors are eligible for appointment as statutory auditors. Auditors must be registered with one of the appropriate professional bodies.	149	

External auditors must issue report(s) which record accounting issues and control deficiencies found. The institution’s management must provide written responses to any recommendations made or issues raised.	151	
External auditors must comply with the reporting requirements of the prevailing annual Accounts Direction.	152	
The external audit report(s), with management responses, must be made available to the audit committee in time to inform the annual report.	153	
The governing body must ensure HEFCW has unrestricted access to communicate with the internal and external auditors.	155	
Internal and external audit services must not be provided by the same or a connected firm or provider.	156	
Internal and external auditors must have unrestricted access to information.	157	
The governing body, through the audit committee, must be specifically notified of the internal auditor’s request for a liability limitation.	158	
Institutions must not agree to any limitation of external auditors’ liability in respect of the external audit.	159	
The governing body, through the audit committee, must be specifically notified of an external auditor’s request for a liability limitation (on work that is not the external audit).	160	
Institutions must report serious failures to HEFCW at the time they are identified. Institutions must also sign the specific declaration in the annual assurance return that serious failures have been reported.	164	
Serious failures, including those that are suspected but not confirmed, must be reported to the institution’s internal auditors immediately.	165	

Reports of serious failures must be sent to the HEFCW Chief Executive. The report must include a number of items (see text for details).	167	
Internal auditors must adhere at all times to the Public Sector Internal Audit standards or successor standards. External auditors must adhere at all times to the professional standards of a recognised accrediting accounting body.	171	
Internal and external auditors must not take on any executive management responsibilities, or hold any interest - financial or non-financial, direct or indirect - in the institution (other than the normal employee or contractor relationship, or the funding of any prize, scholarship or academic appointment).	172	
Statements made by the auditors to the governing body regarding the cessation of their contract must also be sent to HEFCW by the governing body.	175	
The chair of the governing body must signify (by way of signing) that they have received the terms of this Code.	176	
Under certain circumstances, the governing body must request an increase its financial commitments threshold from HEFCW, before it agrees to any new financial commitment.	B2	
Where an institution exceeds its financial commitments threshold in the future because of a decline in its cashflow, it need not apply for a higher threshold, but the governing body must inform us of this fact.	B15	
Institutions must include their financial commitments plans as far as possible in their annual financial forecasts submissions.	B16	
All applications for a higher financial commitments threshold must be signed by the chair of the governing body.	B17	

‘Should’ provisions

Provision	Paragraph reference	Governing Body has taken into account?
The governing body should review any relevant guidance on accountability or propriety issued from time to time by HEFCW.	30	
The governing body should take into account the guidance of relevant stakeholder bodies in relation to the organisation and management of financial affairs.	31	
The institution should determine whether it has any indicators (other than those listed in this Code) which point to underlying sustainability concerns and deficiencies in financial planning.	38	
Institutions should prepare an ASSUR statement on an annual basis.	40	
The ASSUR statement should be reviewed by the institution’s governing body.	40	
The governing body should make arrangements for HEFCW to meet the accountable officer within a reasonable timeframe following their designation.	47	
The governing body should require the accountable officer to advise it immediately if, at any time, it appears to the accountable officer that any action or policy under consideration by the governing body would constitute a failure to adhere to this Code.	48	
Institutions should adhere to recognised standards of good governance.	52	
Governing bodies should have at least one member with relevant financial experience gained within a predominantly finance-based role.	61	
Institutions should remain appraised of the latest guidance from the Competition and Markets Authority and the Office of the Independent Adjudicator, or any successor bodies fulfilling those roles.	77	

The institution should give due regard to the guidance issued from time to time by HEFCW on estate procedures.	80	
The metrics for measuring the success of space plans should be pre-agreed by the governing body.	81	
Governing bodies should receive an annual report outlining estates performance.	82	
Institutions should prepare annual and monthly cashflow forecasts covering the upcoming 12 months.	83	
An institution should know the full cost of its activities and use this information to make decisions. If it does not seek to recover the full cost, this should be the result of a clear policy set by the governing body and included in the financial strategy.	93	
The governing body should consider the independence of the clerk's reporting line and effective management position at least every three years.	116	
The audit committee should assure itself about the effectiveness of the internal and external auditors. They should also consider evidence-based assurances from management.	119	
Audit committees should include a minimum of three lay members of the governing body.	120	
The chair of the governing body should not be a member of the audit committee.	120	
Audit committees should usually have at least one member with relevant experience gained in a finance or audit role.	121	
Audit committee members should not be members of the institution's finance committee or its equivalent.	122	
The audit committee annual report should record the work of the audit committee and consider a number of elements (refer to text).	125	
Each institution should have a finance committee or equivalent, comprised of at least one individual with relevant finance	128	

experience. The finance committee should meet regularly to advise the governing body on the institution's financial matters.		
There should be periodic assessment of whether in-house or externally-sourced internal audit provision is the appropriate type of provision for the institution. This assessment should happen at least once every five years.	140	
Where internal audit is provided from an external source, market testing should be undertaken at least every five years.	141	
Market testing of external audit should normally be undertaken at least every five years.	148	
Selection criteria and procedures for the appointment of external auditors should be determined by the governing body in advance of receiving proposals and should be endorsed by the audit committee.	150	
Auditors should, within their management letters or reports, have regard to the specific requirements of the Code such as compliance with those provisions relating to increases in financial commitments thresholds, or other issues of non-compliance (refer to text).	154	
Normally, liability in respect of an internal audit contract should be unlimited.	158	
Institutions should normally notify the police of suspected or actual fraud.	163	
In the event that internal investigations into suspected serious failures may be time-consuming, the institution should provide HEFCW with a provisional report.	166	
The report relating to a serious failure must be sent to the HEFCW Chief Executive. In reporting a serious failure to HEFCW, institutions should provide as much information as possible to help HEFCW understand the appropriateness of the response and what, if any, further action is planned.	167	

Where auditors cease to hold office for any reason, they should provide the governing body with either a statement of any circumstances connected with their resignation or removal which they consider should be brought to the governing body’s attention, or a statement that there are no such circumstances.	174	

Annex D: Glossary

In this Financial Management Code, the following definitions apply:

2015 Act	The Higher Education (Wales) Act 2015
Academic year	The 12 months from 1 August to 31 July.
Accountable officer	The officer accountable for the organisation and management of the institution’s financial affairs and for reporting to HEFCW on behalf of the institution’s governing body.
Accounting period	The period covered by the institution’s audited financial statements, usually the 12 months from 1 August to 31 July.
ASSUR	Annual Sustainability Assurance Report, developed by the FSSG.
BUFDG	British Universities Finance Directors Group
the Code	This Financial Management Code.
Code of Governance	The Higher Education Code of Governance, published by the Committee of University Chairs.
Framework document	The Framework Document between HEFCW and Welsh Government, which sets out the broad framework within which HEFCW operate.
FRS	Financial Reporting Standard.
FSSG	Financial Sustainability Strategy Group (http://www.hefce.ac.uk/whatwedo/lgm/finsustain/fssg/).
Governing body	i. For a training provider this means any persons responsible for the provider’s management. ii. For a provider designated by Welsh Government as an institution it means any persons responsible for the provider’s management. iii. For any other institution it means, for an institution conducted by a further education corporation or a higher education corporation, the corporation; in the case of a university, the executive governing body which has responsibility for the management and administration of its revenue and property and the conduct of its affairs; in the case of any other institution for which there is an instrument of

	government providing for the constitution of a governing body, the governing body so provided for; and in any other case, any board of governors of the institution or any persons responsible for the management of the institution, whether or not formally constituted as a governing body or board of governors. iv. For an external provider (as defined by the 2015 Act) that is not an institution it means any persons responsible for the provider's management.
governing document	In the case of a provider of higher education, conducted by a company, the company's memorandum and articles of association. In any other case, a document providing for the constitution and conduct of the provider of higher education.
HEFCW	Higher Education Funding Council for Wales.
the institution	a regulated institution, as defined in section 7(5)(b) of the Higher Education (Wales) Act 2015.
LFHE	Leadership Foundation for Higher Education.
SLC	Student Loans Company.
Senior Executive team	Defined in accordance with FRS 102's definition for 'key management personnel'; that is. "those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity". This is consistent with the approach that institutions will be required to take in identifying their Senior Executive team for use in financial statement disclosure under the FEHE Statement of Recommended Practice.
Short to medium term	The period covered by the latest financial forecasts supplied to HEFCW by the institution.
Sustainable	'Sustainable' is defined by reference to the common understanding of 'going concern', over the period covered by the latest financial forecasts supplied to HEFCW by the institution.
VFM	Value for money.

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