Higher education sector developments

July 2021

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Foreword

The higher education sector, like many others, has experienced a year unlike no other. It has had to and continues to adapt to a period of significant change as well as facing numerous challenges along the way. This is not solely due to the pandemic, but Brexit and the recent Skills for Jobs White Paper pose a long-lasting impact on the sector.

We have already started to see and will continue to see changes in the way higher education is delivered with elements of on-line learning likely to remain. The use of the campus will need to adapt, with a drive for more technical and practical learning, and a reduction in EU students now seems inevitable.

It is clear that these changes bring new challenges, however there are plenty of opportunities on the horizon for universities to take advantage of with increasing collaboration with further education colleges expected and the possibilities of blended learning and using digital resources to drive efficiencies and deliver new exciting experiences for students.

During such difficult times, universities have also had to deal with an increasing threat from cyber-attacks, rising pension costs, as well as having to contemplate ways of mitigating the potential disastrous impact of climate change. Transparency around the reporting of these risks is vital to maintain trust amongst key stakeholders and to demonstrate that measures are being taken to prevent any significant damage to the institution and the wider society.

There are also a few new regulatory notices and letters from the OfS to consider, a new Code of Practice for Higher Education Audit Committees, as well as the outcome of the BEIS consultation on the horizon.

This publication aims to give you an overview of the topics mentioned above, as well as some other current hot topics, including pension and tax updates which are relevant to the higher education sector.

We hope you find reading this document informative and we look forward to providing additional updates on the sector in the near future.

If there are any matters that you would like to discuss further, please do not hesitate to get in touch with your Grant Thornton contacts.

Sector risks

Covid-19 – the impact on the higher education sector

The past year and more has not been a time that anyone would have wished for, however, the sector has adapted well to the significant challenges and remains relatively robust financially. The hope is that we are on the path back to "normality", although "normality" might be slightly different to how we previously knew it to be.

It has become evident that the campus experience is what students have missed the most, but there are indications that some of the new digital ways of learning have been beneficial and could be here to stay. It may be that there is more scope for flexibility over the learning space and blended learning is where the future lies.

Several reports and articles have been written about post-Covid learning and the role of digital technology, and how it may have a key part to play in the future direction of learning and teaching. One of these is the detailed and insightful report "Learning and teaching reimagined: a new dawn for higher education?". This was produced by JISC, in collaboration with other sector bodies and specialists, focusing on the key challenges, opportunities and recommendations around a new blended way of learning.

Although there is positivity on the horizon, the virus and measures taken to contain it have undoubtedly impacted universities both operationally and financially, thus the future still remains uncertain. As a result of this, there are several accounting ramifications that universities will need to carefully consider when preparing their financial statements for 31 July 2021 year ends.

In July 2020 we produced a separate report on the impact of Covid-19 on the higher education sector, which focused on some of key challenges the sector was facing, along with the potential financial reporting and regulatory impact. Many of these are still relevant today along with the emergence of some new challenges to address.

Some of the key areas of financial reporting to consider, and included in more detail in our report are:

- **impairments of assets** where there are indicators, for example student accommodation that is not being utilised. It is important to note that the valuation method for buildings on campus will differ depending on the use of the building
- **onerous contract provisions** may be required where the onus of meeting unavoidable costs outweighs the economic benefits, for example catering contracts that have been committed to or property leases
- **accounting for research grants** will need to be reviewed, in particular where the research has had to be postponed or curtailed
- **accounting for Gift Aid payments by subsidiaries** will also need to be carefully reviewed to ensure sufficient distributable reserves are available, any tax implications of non-payment are considered, as well as whether Gift Aid payments should even be made given the uncertainty of the current climate
- **accounting for government support measures** will need to be assessed for each measure individually in line with the nature of support offered, and the terms and conditions attached to it, with the income and the related expense being recorded separately, rather than being netted off in the income statement
- **going concern assessments** will need to include stress testing based on various scenarios and the possibility of various outcomes with a particular focus on cash flows.

In addition to these points universities will need to carefully consider:

- whether they have any liabilities for refunds of tuition fees or accommodation
- are at risk of breaching any debt covenants or need to consider re-financing
- have any situations of non-compliance of governance or internal controls due to illness or lockdowns that may need disclosing.

Once the financial impact has been determined it is essential that the narrative in the front end of the annual report, and any accounting policies that have been affected reflect what is in the numbers. Transparency is key to demonstrating good governance and accountability.

Brexit

One key change in the external environment that has now been finalised is Brexit. Although each higher education institution is different, it is likely that most institutions will experience some impact from the UK's departure from the EU. Institutions will therefore need to reflect these challenges in their financial statements along with what mitigating actions they have put in place to reduce the significance of the impact.

Institutions will also need to consider the potential impact of Brexit in their forecasts. This will include undertaking contingency planning, stress testing, and ensuring that plans are sufficiently flexible to deal with whatever situations may arise as a result. These forecasts will then need to be taken into account when carrying out the going concern assessment and included in any related disclosures.

We have highlighted below some of the key challenges that we expect most boards to be thinking about:

EU students

As a result of the UK's departure from the European Union, EU/EEA and Swiss students coming to the UK for higher education will lose their "home fee status" that has until now allowed them to pay the same tuition fees as UK students. They will also lose access to British student loans and face the same limitations on their right to work after graduating as other international students, along with other restrictions.

According to an analysis prepared for the UK Department of Education by London Economics, the new rules may result in UK universities losing £62.5 million per year in tuition fees as a result of losing more than half (57%) of their first-year EU students.

Not all universities will face losses as a result of a reduction in EU students however, and the London Economics research predicts that it is the universities outside of the top tier that will feel the most impact, with estimates of losses per institution of £0.6 million a year on average.

In anticipation of Brexit, we are aware that some UK universities have been increasing their recruitment efforts in non-EU markets. In an early 2021 data release, the Universities and Colleges Admissions Service (UCAS) also reported a 40% drop in the number of EU applications to UK universities for the September 2021 intake, the number of non-EU applications, meanwhile, is up by 17%.

Research funding and collaboration

A settlement was reached as part of the trade deal ratified in January 2021 that the UK will still be able to participate in Horizon Europe, the EU research and innovation programme that will run from 2021 to 2027. The UK will participate as an associate, which will give UK scientists, researchers and businesses access to funding under the programme on equivalent terms as organisations in EU countries.

The only part of Horizon Europe in which the UK will not participate is the European Innovation Council (EIC) fund (the investment fund part of the EIC Accelerator Fund), to which the UK declined to sign up. This is a new funding stream in Horizon Europe which will award funding to SMEs in the form of equity. It should be noted that UK entities will still be eligible for grant based EIC funding streams

Increased costs in maintenance and building of estates

Those universities who spend a significant amount on maintaining their estates and are planning significant expansion in the future will see costs go up in this area. The construction sector is heavily reliant on imports from the EU in terms of materials, and the UK's exit from the single market will have huge ramifications. Inside housing reported that around 60% of all building materials come from Europe with 90% of all sawn wood and boards.

There is not only the issue of access and/or delays to maintenance and construction materials but also increased costs due to new tariffs. These challenges need to be considered as early as possible in any development plans to consider the impact they may have and source alternative suppliers where necessary. Any potential delays and additional costs will need to be factored into timetables and forecasts.

Erasmus Scheme

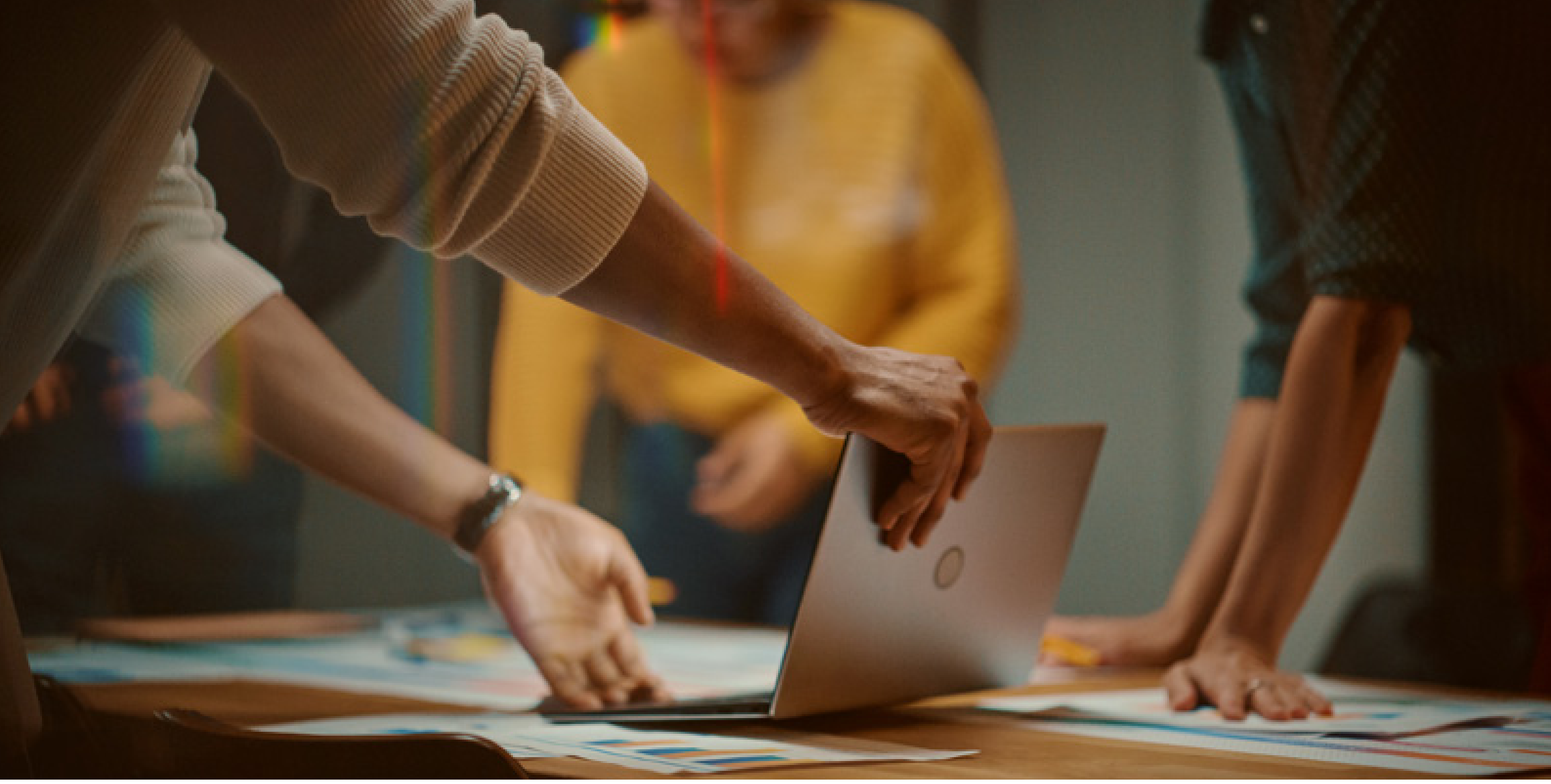
The End of Erasmus was also a major blow to universities, though the UK have agreed to be part of the Turing scheme. However this is not on the same level as Erasmus and does not have a reciprocal arrangement. It is yet to be seen whether this has any impact on the number students applying for language courses.

Resource

Grant Thornton is continually updating guidance and insights into Brexit, which is split into four priority areas:

- people and skills
- imports and exports
- tax and transactions
- cost and cashflow.

These cover off the potential impact and opportunities as well as practical steps organisations can take to prepare.



Cyber crime

One of the knock-on impacts of moving to an increasingly digital world is sadly a significant increase in cyber- crime, with several recent serious attacks on educational institutions.

In March 2021 there was a major cyber-attack at a Birmingham College which forced all campuses to close for a week and three universities were also reported to have suffered an attack in the same month. These are a stark warning that there is an ever-increasing threat, which should be at the top of institutions' risk register.

The National Cyber Security Centre (NCSC), published an alert at the end of March 2021 warning colleges and other education settings to take further precautions to protect themselves against ransomware following "an increased number" of attacks since late February 2021.

Some of the key recommendations included in both the alert and the detailed guidance were as follows:

- Make sure senior leaders understand the nature of the threat, the types of attack that can occur and the extent of damage it can cause.
- Have up-to date and tested offline backups of data as recent attacks have led to the loss of student coursework, school financial records, as well as data relating to COVID-19 testing.
- Do not encourage, endorse or condone the payment of ransom demands. It warned the "payment of ransoms has no guarantee of restoring access or services and will likely result in repeat incidents to educational settings".
- Implement a 'defence in depth' strategy in order to defend against malware and ransomware attacks. This includes effective vulnerability management, installing antivirus software, ensuring remote desk protocols are secure using multi factor authentication and implementing mechanisms to prevent phishing attacks.

Resource

Along with the NCSC guidance Grant Thornton's Head of Not for Profit, Paul Rao has recently published a deep dive into data and cyber security for the charity sector. Although this is focused primarily on the charity sector many of the recommendations are equally as applicable for the education sector and therefore, we recommended this as a useful read.

Governance and policy updates

Skills for Jobs White Paper

Published in January 2021, the Skills for Jobs White Paper ('White Paper') sets out how the Government will reform further education to bridge a skills gap which is now seen as holding the UK back economically in areas such engineering, health and social care.

The key principles aimed at delivering a focus on jobs and growth set out in the white paper include:

- putting employers at the heart of the system so that education and training leads to jobs that can improve productivity and fill skills gaps
- investing in higher-level technical qualifications that provide a valuable alternative to a university degree
- making sure people can access training and learning flexibly throughout their lives and are well-informed about what is on offer through great careers support
- reforming funding and accountability for providers to simplify how funds are allocated, give providers more autonomy, and ensure an effective accountability regime which delivers value for money
- supporting excellent teaching in further education.

Whilst there is increased focus on further education and as a result higher education providers may need to be conscious about the potential for a reduction in student numbers, this new impetus may also result in opportunities for the sector:

- delivery of higher-level technical qualifications need not only be by further education colleges, there will be scope for these to be delivered by higher education providers
- in recent years apprenticeships have been a key area of focus for Government, and this will continue with the White Paper stating the need to build on the success already achieved by reforms in this area. Degree apprenticeships are already offered by many higher education providers and this could represent a key growth area
- with an increased focus on technical, practical education universities will need to become more agile with their use of their campus and it is likely that the traditional lecture model may need to be adapted and facilities available on campus will become even more important to students when assessing education options
- many higher education providers already operate in collaboration with the further education sector, or in partnerships with employers in areas such as health and social care and engineering. The White Paper is likely to lead to the promotion of more "joined up" pathways in education. In the future this will could mean a move to even closer partnership and working arrangements, for example with further education colleges as direct subsidiaries of higher education providers or the formation of joint ventures
- the relationships with local schools and academies is likely to be increasingly important in attracting students.

To support providers with these changes in June 2021 the government launched the provider growth fund. The aim of this fund is to provide additional support for providers who are committed to building and creating additional capacity to deliver higher technical qualifications in the government's "target subjects" of digital, construction, health and science. Applications for this fund close on the 9 July 2021.

2021/22 Government Funding Letter

In January 2021, the Secretary of State for Education wrote to the Office for Students (OfS) setting out the higher education funding grant for the 2021/22 financial year and the Government's funding priorities. Key features of the letter were:

- total teaching and capital grant funding for 2021/22 at the same level as that provided in 2020/21
- a requirement for the OfS to prioritise high-cost subject funding to support "strategically important" subjects in the areas which support the NHS and wider healthcare policy, high-cost STEM subjects and/or specific labour markets. High-cost funding in areas which do not support these strategic priorities to be reduced by 50% in 2020/21
- the removal of London weightings from grant funding to support the "levelling up" agenda
- increased allocations to support student hardship and mental health
- protection of the element of funding allocated for student premiums to support disadvantaged students and those needing additional help
- an increase in small and specialist provider funding, particularly in the areas of performing and creative arts
- capital grant funding to be allocated based on a strategically targeting bidding process, rather than the previous allocations which were based on a formula setting an allocation for each provider.

The move to prioritisation of high-cost subject funding has attracted much attention, with some commentators interpreting the Government's January letter as an indication that overall funding for students on arts courses would be cut by 50%.

The OfS issued a statement on 6 May 2021 which clarified that the reduction in funding applied only to the subsidy provided to some institutions to assist with the delivery of subjects which are expensive to teach, and so classed as "high-cost". This funding had previously been at a level of around £243 per full time student per year; the change will see this reduced to £121.50 per full time student per year on "high-cost" courses which are not in the Governments "strategically important" subject areas. There is no proposed reduction to the level of tuition fee loans available to students on these "high-cost" courses or on arts courses more generally.

The OfS has consulted on its approach to implementing the Governments 2021/22 funding letter; the consultation period ran from 26 March 2021 to 6 May 2021 and the results of this consultation are expected to be published shortly.

The role of the audit committee in higher education

The past 12 months have seen increased pressure on financial sustainability, the emergence of new risks and new auditing standards as well as the prospect of additional scrutiny coming out of the BEIS consultation. The direction of travel in these developments places increased emphasis of the need for audit committees to oversee the effectiveness of their governance, risk management and financial reporting arrangements, to ensure the accuracy of financial information and to assess and challenge key assumptions and judgements made by management.

The Committee of University Chairs published a Code of Practice for Higher Education Audit Committees ('the Code of Practice') in May 2020 which further highlighted the role that audit committees can play in providing reassurance to the public, regulators and other stakeholders as to the effectiveness of audit arrangements within their institution.

We have seen high turnover of governors at many higher education institutions during this period and there is a need for institutions to support all governors, but particularly those serving on audit committees, to enable them to deliver their role effectively.

The Code of Practice highlights that sound governance includes arrangements for securing:

- effective risk management
- value for money
- legal and regulatory compliance
- reliable, accurate and timely management information
- management and quality assurance of data submitted to the Higher Education Statistics Agency, the Student Loans Company, the OfS and Funding Councils, Research England and other bodies
- appropriate disclosure and transparency
- a culture of uncompromising moral and ethical behaviour.

Responsibility for delivering these arrangements does not rest solely with the audit committee, but the committee can play a key role in ensuring that necessary arrangements are in place and can draw on the expertise of internal and external auditors in doing so.

Of the above areas, promoting an appropriate culture is perhaps the single most important, as this is the foundation on which other arrangements are built. The status and effectiveness of the audit committee can play a significant role in promoting the right culture – one in which people can admit mistakes, embrace continual improvement and welcome constructive challenge. The first step in promoting this kind of culture is to visibly and publicly adopt the Code of Practice.

Resource

Due to culture playing such an important part in success culture audits are becoming more and more common. The insight piece "Culture risk: hot topics on the agenda for 2021" from Grant Thornton looks into the current key areas of culture risk and why it is important to evaluate and monitor these. Grant Thornton's 2020 Corporate Governance Review looks into how companies are getting better at providing good accounts of their company culture however there is still a long way to go in companies assessing how they monitor and embed culture into the heart of their business.

All higher education institutions are different, be it in size, complexity and legal form. Therefore, the Code of Practice is set on an 'apply or explain' basis in which the governing body is given a set of elements but is not mandated to comply with all the provisions therein. Where institutions have chosen not to adopt certain elements of the Code of Practice, they must explain and justify the reasons why.

The Code of Practice lists the key elements of an effective audit committee as:

- the role of the audit committee is clearly understood
- audit committee membership is independent, experienced and effective
- audit committee meetings are properly organised and supported
- the audit committee has enough resources and access
- the audit committee communicates regularly and effectively with the governing body and appropriate stakeholders
- the audit committee undertakes periodic assessments of its effectiveness
- the audit committee exercises effective oversight of both internal and external audit.

Appendix 3 of the Code of Practice sets out potential questions which Audit Committee members can use to undertake a "self review" of the effectiveness of the Committee. We would encourage all higher education institutions to adopt the Code of Practice and undertake such a review in order to provide assurance that they continue to adopt best practice in governance arrangements.

Financial reporting and audit updates

Shaping the future of financial reporting

Future amendments to UK accounting standards: Periodic review 2022

UK accounting standards are subject to periodic reviews, at least every five years, to ensure they remain up-to-date and continue to require high-quality and cost effective financial reporting from entities within their scope.

The Financial Reporting Council (FRC) has started its next periodic review of FRS 102 (and other UK and Ireland accounting standards) and as part of this they launched a request for stakeholder views, earlier this year in March 2021.

The feedback and comments requested from stakeholders is on any aspect of the standard. This might include new issues or transactions that should be addressed, or comments or suggestions in relation to the current requirements under FRS 102.

In addition to topics raised by respondents, the review will consider major changes in IFRS yet to be reflected in FRS 102 – including IFRS 16 Leases. Clearly any changes to FRS 102 will impact the SORPs applied by public benefit entities.

Any changes to accounting standards that are proposed as a result of the periodic review will be subject to public consultation at a later date, not expected to be before 2022.

The effective date for any amendments is currently expected to be 1 January 2024. Stakeholders can provide comments on any aspect of the standards until 31 October 2021.

Further details can be found on the FRC website.

International Financial Reporting for Non-Profit Organistions ('IFR4NPO') Project

The IFR4NPO initiative ("The Project") was set up to develop international financial reporting guidance for non-profit organisations. The Project aims to address the unique characteristics of non-profit organisations and the types of transactions they undertake. The Project seeks to enable a more effective and accountable framework, with greater credibility, trust and lower costs of financial reporting.

In January 2021, the Project launched a Consultation Paper that seeks views on the approach to developing the guidance and the financial reporting and accounting issues that should be addressed in it.

The publication of this Consultation Paper gives non-profit organisations (NPOs) the opportunity, for the first time, to contribute to the development of international financial reporting for their sector.

The Consultation is split into two parts; part 1 focuses on defining which organisations are NPOs, and the needs of NPO stakeholders and users of their financial information, whilst part 2 considers NPO-specific financial reporting issues, setting out how key NPO-specific issues have been identified, and a criterion for prioritising the issues to be included in the final guidance. Response are requested by the end of July 2021 and September 2021 for the two parts respectively.

The Project's guidance may also inform the future development of FRS 102 and those SORPs applied by public benefit entities.

Further details can be found on the IFR4NPO website.

Restoring trust in audit and corporate governance

Like just about everything else at the moment, the audit profession is facing significant change. There have been recent updates to a number of key international auditing standards (ISAs) and the long awaited Government White Paper on audit ("The White Paper") has just been released.

The White Paper, seeks to bring into law many of the recommendations of the Brydon Review, as well as recommendations from the earlier reviews by John Kingman and the Competition and Markets Authority. The points included in the white paper are under consultation until 8th July 2021.

Some of the key points in the White Paper are as follows:

- introduction of a new regulator, the Audit, Reporting and Governance Authority (ARGA), which will have greater powers than the Financial Reporting Council (FRC)
- managed shared audits for larger companies
- operational separation of audit practice and non-audit functions for the larger firms
- new reporting obligations on auditors and company directors around the prevention of fraud
- option for the scope of audit to widen to include other matters, for example climate targets
- greater accountability for directors in a number of areas
- expansion of the definition of a Public Interest Entity ('PIE') beyond publicly listed companies to include the largest private companies
- the Government is also seeking views on whether the definition of a PIE could be widened to include third sector entities, such as charities, universities and housing associations, although with a different threshold. The threshold included for consultation in the White Paper is based on incoming resources greater than £100 million.

These recommendations are likely to have far reaching implications for audit firms and organisation alike.

We recommend that you discuss the potential impact with your auditors and advisers so that you can keep an eye on further developments and plan effectively.

Resource

Further details on the widening of the definition of a PIE and the potential impact can be found on Grant Thornton's website at the following link: "BEIS consultation: changing the public interest entity".

Revised International Standards on Auditing (ISAs UK)

The ISAs are reviewed on a regular basis and revised periodically as required. There have been a number of revisions recently for periods beginning on or after 15 December 2019, which are likely to impact the work undertaken by your auditors, both in terms of additional levels of scrutiny applied and the information and evidence auditors will require from universities to comply with the revisions to the standards. These new auditing standards also align with areas that the Financial Reporting Council (FRC) are focusing on in terms of audit quality.

We have summarised the key amendments below:

ISA (UK) 570 – Going concern
The revision of this ISA includes a specific requirement to:

- obtain sufficient appropriate audit evidence regarding whether a material uncertainty related to going concern exists
- provide a more robust challenge of management's assessment of going concern including the method chosen,
- information and assumptions used as well as the evidence provided to support the assessment
- "stand back" and consider all evidence obtained including contradictory evidence
- give a positive conclusion on whether management's use of the going concern basis of accounting is appropriate and include enhanced disclosures in the auditor's report regarding material uncertainties related to going concern.

ISA (UK) 540 – Auditing accounting estimates and related disclosures
The revision of this ISA includes a specific requirement to:

- separately assess inherent and control risks at the assertion level and to look at a spectrum of inherent risk
- place increasing importance on professional scepticism where accounting estimates are subject to a greater degree of estimation uncertainty or are affected to a greater degree by complexity, subjectivity, or other inherent risk factors
- enhance documentation around risk assessment of accounting estimates and how the planned procedures address the level of risk identified
- "stand back" and consider all evidence and the source of such evidence obtained including contradictory evidence
- enhance communications with those charged with governance and consider circumstances where additional written representations from management may be appropriate.

ISA (UK) 700 – Forming an opinion and reporting on financial statements
The revision of this ISA introduces a new requirement for the auditor's report to explain to what extent the audit was considered capable of detecting irregularities, including fraud.

Previously this requirement was only applicable to audits of Public Interest Entities (PIEs) but going forward applies to all entities.

The new requirement encompasses disclosure of the laws and regulations that the auditor identifies as being of significance as well as documenting how the audit was designed to identify non-compliance with such laws and regulations.

These requirements are likely to result in additional focus from universities in substantiating key judgements and assumptions, evidencing compliance with laws and regulations and formalising key considerations in detailed management papers for audit committees, boards and auditors. We therefore recommend that universities speak with their auditors during the planning stage about how to address these additional requirements.

Covid-19 related rent concessions

As a result of the global pandemic, various forms of rent concessions have been granted to lessees including payment holidays and deferral of lease payments. This may be significant for some universities and require further consideration as part of your year-end reporting. In October 2020, the FRC published amendments to FRS 102 which set out requirements for lessees and lessors to recognise the changes in operating lease payments arising from Covid-19 related rent concessions over the periods the change in lease payments is intended to compensate.

This accounting treatment is considered to reflect the economic substance of the intended benefit of the concessions and their temporary nature and provide more relevant information for users of the accounts.

The amendments only apply to rent concessions occurring as a direct consequence of the pandemic and only if all of the following conditions are met:

- the change in lease payments results in revised consideration for the lease that is less than the consideration for the lease immediately preceding the change; and
- there is no significant change to other terms and conditions of the lease.

Originally the amendments only affected payments due on or before 30 June 2021, however on the 9th June 2021 these amendments were extended so that they apply to rent concessions for which any reduction in lease payments affects payments originally due on or before 30 June 2022, provided the other conditions are met.

Extending the existing time condition by 12 months was considered necessary to ensure that concessions with similar characteristics that occur in similar circumstances are accounted for consistently and in a way that best reflects their substance.

The amendments are effective for accounting periods beginning on or after 1 January 2021, with early application permitted.

Universities that are lessees will need to distinguish temporary rent concessions separately from other changes in lease payments in their disclosures. Universities that are lessors are expected to provide disclosures on rent concessions granted. Paragraph 20.30(c) of FRS 102 requires lessors to provide a general description of their significant leasing arrangements, thus information about rent concessions granted is in scope of this requirement.

Companies (Miscellaneous Reporting) Regulations 2018

For many universities this will be the second year of including the requirements of the Companies (Miscellaneous Reporting) Regulations 2018 (the 'regulations') in their financial statements. As a reminder these regulations are applicable to all large UK companies, incorporated under the Companies Act 2006, with reporting periods beginning on or after 1 January 2019. Information Sheet 3, published by the Charity SORP making body, gives guidance on how the regulations apply to charitable companies.

Included in the regulations is a requirement to publish a "section 172 statement". Disclosure of this requirement has been mixed and therefore the FRC have published a useful guide on "how to make the Section 172 statement more useful", which in particular helps with guidance over the presentation of the statement.

Some of the key points included are:

- it should be a standalone statement, clearly identified in the annual report and referenced in the contents page
- use cross-referencing to enhance understanding of information contained in the statement
- don't let it just be a tick box exercise.

We would recommend that you read the FRC guidance in detail as transparency in disclosures can help build up trust in your organisation and support your university's core values.

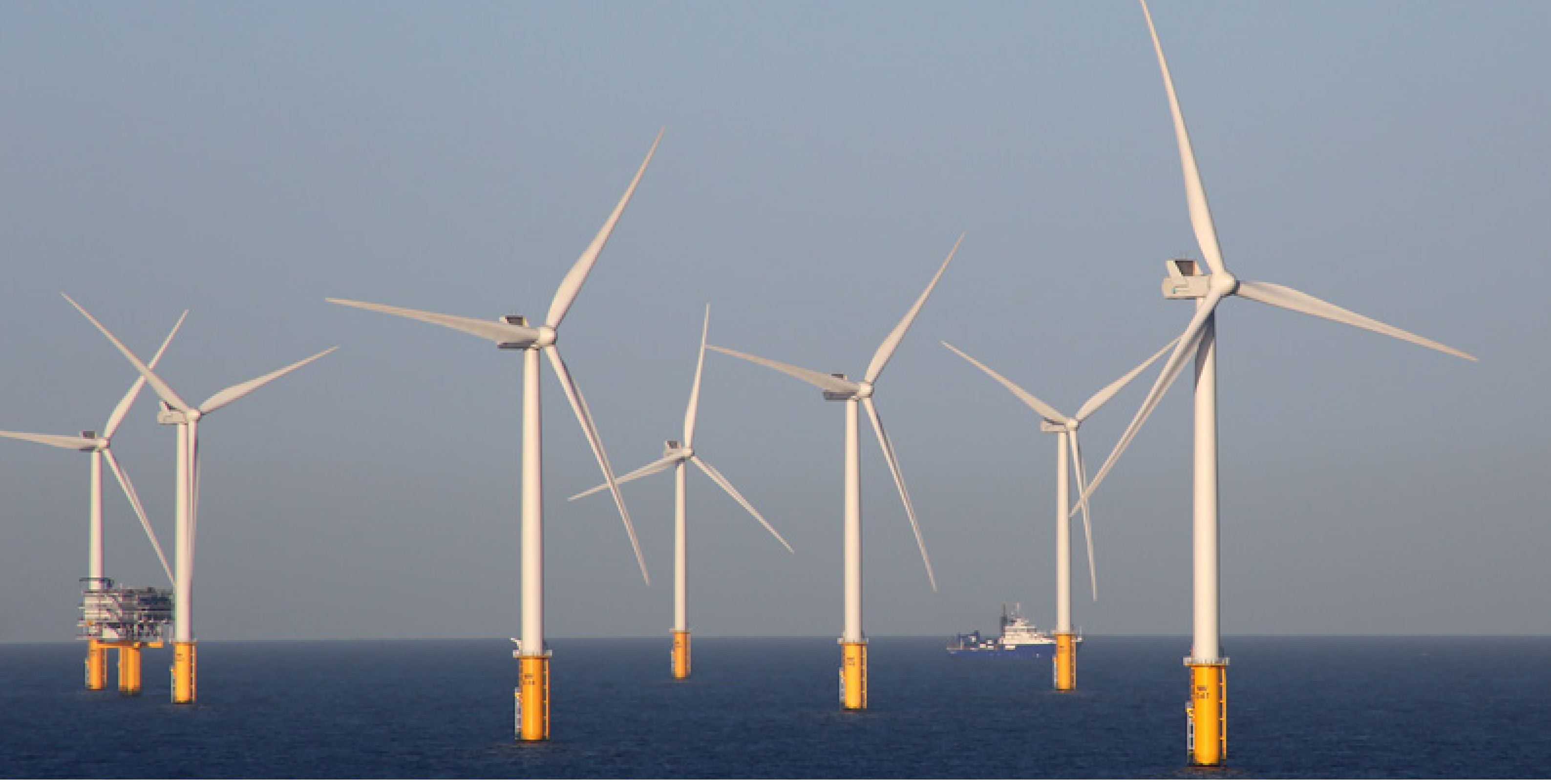
Streamlined Energy and Carbon Reporting (SECR)

In 2019 the SECR legislation was implemented to ensure large businesses are transparent about their energy use and deliver and report on efficiencies. It is effective for periods beginning on or after 1 April 2019 and therefore will be the second year of implementation for many universities.

In 2020, ICAEW's Financial Reporting Faculty hosted a webinar on the subject and identified the following as good practice:

- Make data collection as automated as possible so it is as reliable and consistent as possible
- Be transparent about any changes year on year and point out any trends
- Identify and explain any exceptional figures, using underlying figures where necessary
- Use multiple intensity measures if appropriate.

For further information on the requirements and applicability please visit the government guidance on this topic.



Climate change reporting

With regards to climate change reporting the requirements of the SECR regulations are just one small element. Climate change has the potential to have a significant impact on the university sector and therefore it is becoming increasingly important for universities to report on how they are considering the climate-related impact on their business model as well as addressing the related risks and opportunities.

Sustainable finance is becoming increasingly popular with a variety of options for institutions to choose from. Two of the main forms of this type of finance are; green loans, which are used solely for the purpose of financing green investments, and sustainability linked loans which can be used for any purpose but encourage the borrower to achieve predetermined ESG targets in return for pricing discounts. Sustainable deposits, bonds and investment strategies are also becoming increasingly popular and are now strongly encouraged by many stakeholders in the sector.

Universities will need to ensure that any disclosures in the accounts mirror any targets and strategies agreed and also consider how any climate risk identified or measures taken to mitigate this risk could impact the accounting policies and related notes in the financial statements, for example the impact on significant judgements and estimates.

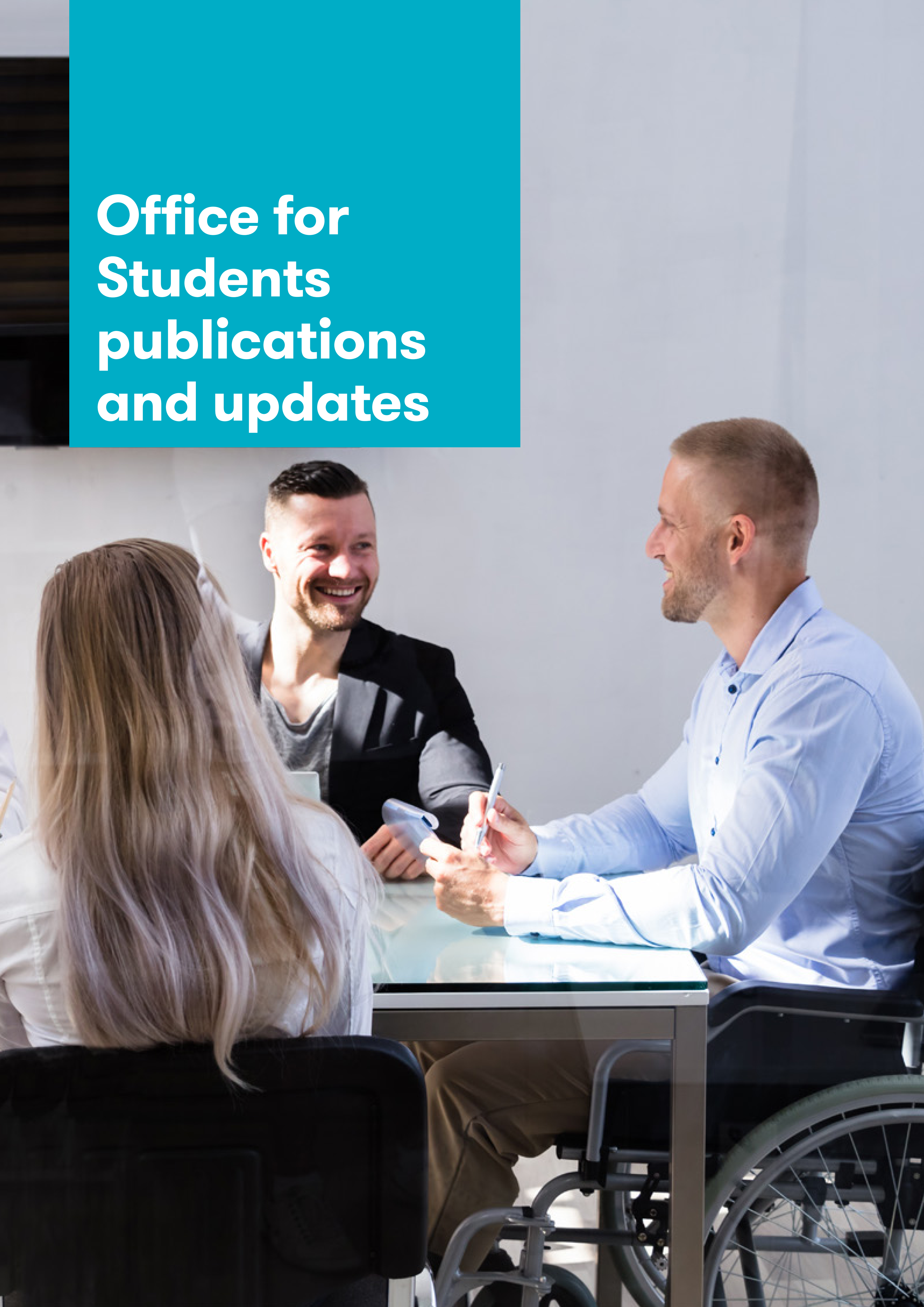
Throughout 2020, the Financial Reporting Council (FRC) undertook a thematic review of climate-related considerations by boards, companies, auditors, investors and other professional bodies, addressing the question 'how are companies developing their reporting on climate-related challenges?'.

The FRC review contains useful information and guidance with the following being the three main themes:

- **Further disclosure required on the risks identified and how organisations plan to deal with these** – minimum requirements are being met however the FRC and other stakeholders want more detail on the impact of climate change on the company, the associated risks and what plans are in place to mitigate these risks. Ideally looking at different scenarios and stress testing these
- **Further information required on any targets/strategic goals set** – organisations are starting to set strategic goals, for example achieving net zero carbon emissions by a set date, however these are often not backed up by disclosure on how they will be achieved, monitored or validated
- **Narrative reporting disclosures need to also be reflected in the numbers contained in the financial statements** – organisations are increasing their reporting in the front end but often this is not reflected in the numbers in the financial statements and related notes, which could lead to non-compliance with financial reporting standards.

We are likely to see increasing expectations from stakeholders for disclosure in this area, with further regulation to follow. Making disclosure in this area meaningful will be of benefit to both the university as well as the users of the accounts.

Office for Students publications and updates



The Office for Students (OfS) has published a number of regulatory advices, notices, reports and letters to providers over the last year. We have summarised a few of these below and some key messages, which we believe to be most relevant to financial performance and financial reporting for higher education providers. This is by no means an exhaustive list of all the publications that the OfS have issued in the year.

Regulatory notice 5: Condition Z3: Temporary provisions for sector stability and integrity

Regulatory notice 5 was published in July 2020 with the aim of protecting the stability and integrity of the English higher education sector during the unprecedented circumstances of the coronavirus pandemic. It has a proposed end date of 30th September 2021, however this could change.

The two main points to draw out from this regulatory notice are that the following are prohibited in all circumstances:

- Unconditional offers in circumstances where acceptance of that offer is subject to making a provider their first or only choice
- Making false or misleading statements about another HE provider with the object or effect of discouraging a student from registering with/accepting any offers made by them.

It is important to note that compliance with this regulatory notice is a condition of registration and therefore non-compliance could have serious consequences for a provider.

OfS review of compliance with Accounts Direction 2019

The BUFDG financial reporting workshops in April 2021 helpfully summarised the results of the OfS review of compliance with the 2019 Accounts Direction during the financial year to 31 July 2020. It was noted that overall compliance was good, however there were a pocket of issues as follows:

- **Submission of Audit Management letters** - the Accounts Direction states that external audit management letters should be provided to the OfS, however in some cases the incorrect documents were uploaded
- **Audit report wording** - external auditor funding assurance wording was not always complete
- **Corporate governance statement omissions** - inadequate disclosures were noted in the corporate governance statement, particularly in the areas of regularity and propriety
- **Statement of internal control omissions** - some internal control statements remained silent on whether there were any control weaknesses or not, whereas if no weaknesses were identified they should have included a positive statement confirming that there were "no significant internal control weaknesses"
- **Publication of financial statements** - the Accounts Direction states that providers must publish their audited financial statements on their website within two weeks of them being signed by the required individuals and, at the latest, five months after the end of the financial year to which they relate. In some cases, there were errors with the signatures and delays to publication
- **Remuneration disclosures** - errors and missing disclosures were noted around senior staff pay including remuneration from group companies, pay multiple and waivers

We recommend that you review the requirements of the Accounts Direction, in particular the areas noted above, to ensure that your financial statements are compliant with the requirements.

Higher education financial stability

The OfS published a report in December 2020 which provides a summary of the OfS's analysis of financial data returned by registered higher education providers in England (excluding further education colleges) to the OfS at the end of October 2020 as part of an 'interim financial data return'.

In aggregate the financial position is sound and there was stronger recruitment than predicted, however there is considerable variation depending on the provider and as we have seen there is still very significant uncertainty as the pandemic continues, so the situation could change quickly. Issues that could impact on income following the recent restrictions include:

- increase in students dropping out of courses
- increased demand for refunds for tuition fees and accommodation
- reduced income from accommodation and conference facilities.

Due to the current uncertainty around future restrictions and the long-term impact of the pandemic it is vital to ensure that forecasts have been stress tested against a number of different scenarios and that liquidity is a key focus.

Regulation during the current phase of the pandemic – January 2021

The OfS sent a letter to accountable officers in January 2021 updating them about regulation during the pandemic. They requested that providers undertake a review of compliance with consumer law in first half of spring term looking at the quality of education that was communicated and provided.

OfS expects providers to carry out the following:

- a review of compliance with consumer law looking at the university's communication with students regarding delivery of teaching and assessments and any changes students should expect
- look at whether the information provided was accurate in terms of delivery
- remind students of their entitlement to refunds/other forms of redress/other options where applicable.

Where a provider identifies that they haven't complied they should proactively consider offering refunds/other form of redress.

Regulatory notice 6: Condition C4: Student protection directions

Regulatory notice 6 was published in March 2021 with the aim of enabling the OfS to intervene more quickly and in a targeted way when it considers there to be a material risk that a registered provider may cease the provision of higher education.

A key indicator of material risk is where a provider has no evidence of sufficient funds to meet its day-to-day costs, and any other liabilities due, within the next 12 months, including where a provider's ability to meet its day-to-day costs or liabilities is likely to be reliant on specific factors where there is material uncertainty about whether these will be delivered in practice. These specific factors might include:

- securing additional borrowing or investment
- delivering significant business restructuring or other cost saving measures
- the decision or actions of a third party.

Where a material risk is identified the provider will be required to follow a "Student protection direction". The condition applies from 1 April 2021 to all providers registered with the OfS, except further education bodies.

Pension updates

The Pensions Act 2021

2021 is a year of significant change for pension schemes. The Pensions Bill 2019-21 finally received Royal Assent and become law as of 11 February 2021. Some of the many changes that impact Defined Benefit pension schemes include:

- measures to strengthen The Pension Regulator (TPR) powers – introducing new grounds for contribution notices (the 'employer insolvency test' and the 'employer resources' test)
- new criminal offences resulting in up to seven years' imprisonment and financial penalties
- changes to the notifiable events framework with financial penalties of up to £1 million
- new information gathering powers for TPR supported by new criminal and financial penalties.

Many of the changes are yet to be introduced and will require secondary legislation and/or guidance.

The measures are not expected to be retrospective but will bring new obligations for employers. As one example, the notifiable events regime will be updated and will require employers to provide advance notification to both TPR and the Scheme Trustees about certain corporate activity. It is likely that this notification will need to be accompanied by a statement on the impact of the event on the pension scheme, and how any detriment to covenant will be mitigated.

Guaranteed Minimum Pension (GMP) transfer ruling

In November 2020, the High Court ruled that trustees of defined benefit (DB) schemes that provided Guaranteed Minimum Pensions (GMPs) should revisit and, where necessary, top-up historic cash equivalent transfer values that were calculated on an un-equalised basis.

The ruling indicates that there is an obligation on trustees to top up transfer values paid since 17 May 1990 and that trustees of such schemes should be proactive in considering their obligations coming out from this judgment.

Universities will need to speak to their actuaries to calculate the impact of this ruling on their defined benefit schemes and where material, they should recognise a liability and a corresponding past service cost in their financial statements even if no claim has been made at the reporting date.

Universities Superannuation Scheme (USS) 2020 valuation

The USS is currently undergoing the 2020 valuation which is based on the scheme's position as at 31 March 2020.

It should have been completed within 15 months, i.e. by 30 June 2021, however because of the need to consult with employers and employees about the likely changes, the USS has confirmed that it was not possible to complete the valuation by this date and it is now expected to be finalised by April 2022.

On 3 March 2021, the USS published an update report that explained the funding challenges facing the scheme. The update suggested that even in the most favourable scenario considered, the overall contribution rate would need to rise to 42.1% of payroll. It currently stands at 30.7% and is already due to rise to 34.7% under the 2018 valuation.

Following this, Universities UK (UUK) put options forward that included changing future benefits. The USS Trustees board have reviewed these proposals and on the 18th June 2021 proposed a revised contribution of 31.2%.

At the time of our publication, the contribution rate is still under negotiation. Universities should look to stress tests the various scenarios in their financial planning and consider their risk management around the proposed changes.

VAT and tax updates

Domestic reverse charge for the construction sector

On 1 March 2021, the way VAT is accounted for in the construction sector fundamentally changed. A new domestic reverse charge ('DRC') was introduced by HMRC as a further measure to combat fraud and criminal activity in the sector. This change was to be implemented first on 1 October 2019, and then again on 1 October 2020 but was delayed both times.

The DRC removes the obligation for suppliers of standard and reduced rated construction services to other VAT registered construction businesses to account for any VAT due in respect of their supplies. Instead, the obligation to account for the supplier's output tax will transfer to the customer. If the customer is fully taxable (i.e they are able to reclaim all of the VAT incurred on the purchase of goods and services) they will be entitled to reclaim the VAT accounted for on the supplier's behalf on the same VAT return. As a result, there would be an equal output VAT liability and input VAT entitlement arising in the same VAT period and the supplier will have no opportunity to default on his payment obligations.

This mechanism means that VAT in the supply chain cannot go 'missing' if the supplier fails to pay over the VAT collected from the customer. This mechanism was introduced to combat the threat to the Exchequer arising from 'missing trader' or 'carousel fraud' and will now be extended to services within the construction sector.

There are a number of exceptions which include any services which are:

- ordinarily subject to VAT at the zero rate
- supplied to the final customer (i.e the customer is not making an onward supply of construction services)
- some, but not all, supplies between connected parties.

We recommend that providers familiarise themselves with the new rules to determine whether they make or receive any supplies that are subject to the DRC and therefore how they may be impacted by the changes.

VAT liability of electronic publications

UK VAT legislation allows the sale of certain printed matter, such as newspapers, books and periodicals to be supplied at the zero rate of VAT. From 1 May 2020, the legislation was amended so that the zero rating could also be applied to the sale of the majority of these items when they were supplied electronically. This is provided that the supply was not predominantly devoted to advertising or audio or visual content.

In the recent case of News Corp UK & Ireland, it sought to argue that supply of newspapers in an electronic format could be zero rated prior to the legislation change. Effectively allowing the zero rating to be backdated for the last four years. Whilst it was successful at the Upper Tribunal, the Court of Appeal reversed the decision to hold that electronic publications were standard rated (prior to the change in legislation).

Previously, we recommended that any affected businesses should protect their position by submitting a protective claim to suppliers for VAT that it may have been overcharged. However, it now appears that the position is settled unless New Corp is able to appeal further.

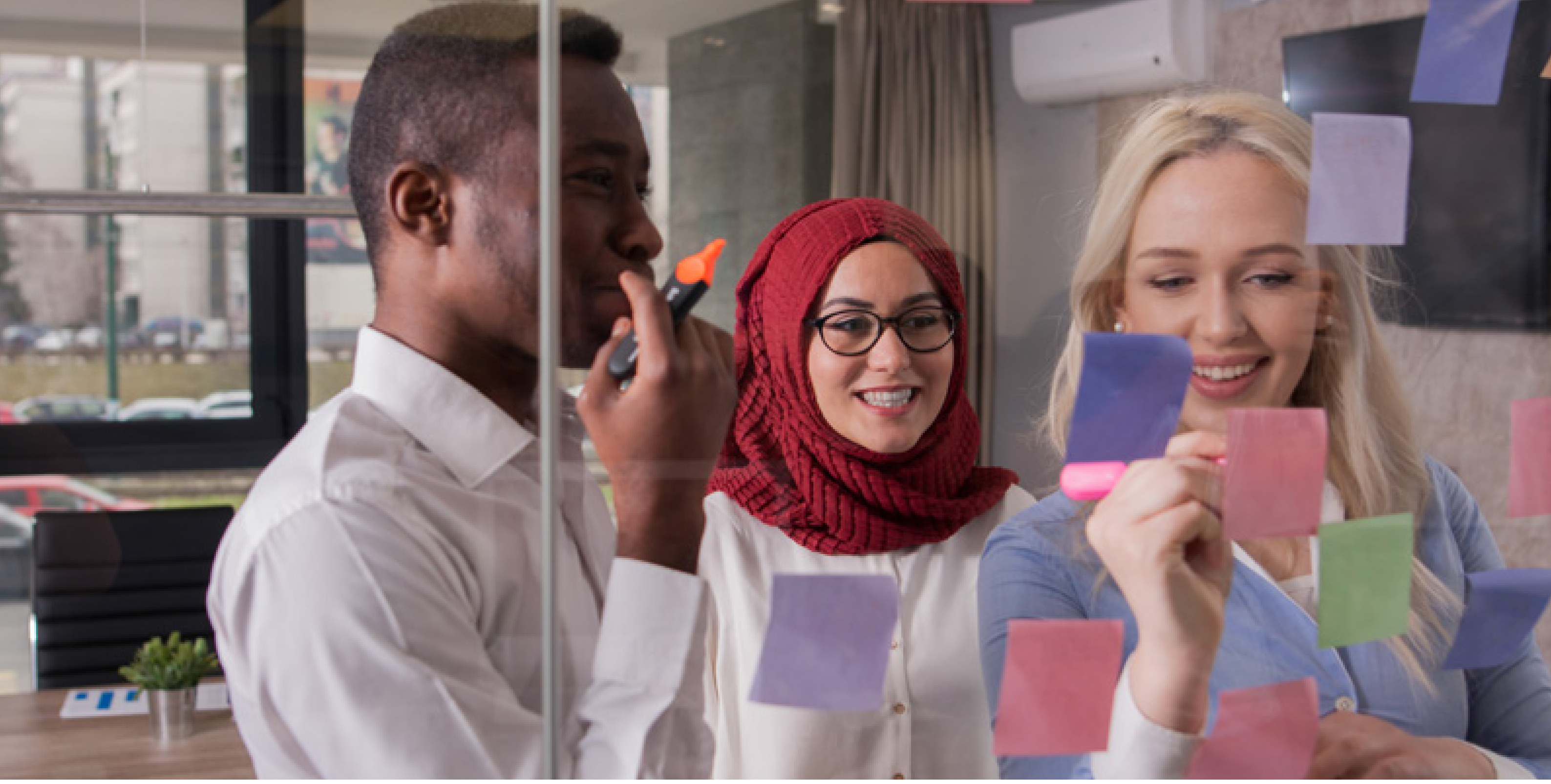
VAT grouping consultation

Where certain conditions are met, companies can choose to form a VAT group. Once part of a VAT group, the entities are regarded as a single taxable person for VAT purposes. Supplies between members of the same VAT group are normally disregarded. This can be beneficial for groups of associated corporate bodies that are required to restrict VAT recovery as it prevents VAT being charged on intra-group supplies.

For other groups, it can be beneficial to keep one or more entities outside of the VAT group. These entities would typically be fully taxable for VAT purposes.

HMRC were considering whether VAT grouping should be compulsory where there is common control between the entities and are consulting on the matter. Many sectors recommended that compulsory VAT grouping was not introduced. This is because of the negative impact it would have on the VAT recovery position. It can also make it more difficult for a business to be sold.

HMRC have now decided not to proceed with a change to the law, but to leave the current choice for taxpayers in relation to VAT grouping.



VAT treatment of grant funding for education

Historically, government funding received by further education colleges from either the Skills Funding Agency ('SFA') or the Education Funding Agency ('EFA') has been treated as non-business income.

However, in the recent case of Colchester Institute Corporation ('CIC'), the Upper Tribunal considered that this income should be a supply for VAT purposes. This was decided on a number of factors, including that the amount of funding provided was based on the number of students and the type of courses undertaken and so there was a direct link between the funding and the delivery of the courses.

Whilst the case was specifically in relation to a Lennartz repayment, the judgement may have wider implications within the education sector. This is particularly in relation to claiming the zero rating for the construction of a building (or part of a building) that will be used for a relevant charitable purpose. This relief requires there to be at least 95% use for non-business purposes. This non-business use previously came from the teaching of students that were fully funded from the SFA or EFA. However, where this income is regarded as being a business supply, it is unlikely that this relief would be able to be claimed.

This relief also has a 10-year clawback period and so there is a risk that where the zero rating was previously claimed, some of the VAT saved may be required to be repaid. However, please note that HMRC has not updated its guidance following this case. As such, the next step would be to wait for an update from HMRC as they may wish to appeal this case further.

UK VAT reverse charge

The "reverse charge" is the mechanism whereby the responsibility to account for VAT on a taxable supply which takes place in the UK is shifted from the supplier to the customer. As such, where a university purchases supplies of certain services from a supplier based outside the UK it should account for VAT on its VAT return via the reverse charge as if it had made the supply itself. The VAT which the university has self-accounted for on the reverse charge is then recoverable on the same VAT return, in accordance with the normal rules.

It has been the case for many years that the reverse charge applies to charitable entities provided they undertake some business activities for UK VAT purposes. The decision of the First Tier Tribunal in the recent Wellcome Trust case, however, tested the extent to which charitable entities are required to account for the reverse charge on purchases used for their non-business activities. In contrast to the current position, the First Tier Tribunal agreed that Wellcome Trust was not required to self-account for VAT via the reverse charge on supplies of investment management services received from managers based outside of the EU. This was because such services were wholly used for the purposes of managing Wellcome Trust's substantial investment portfolio- a "non-business" activity for VAT purposes.

HMRC has appealed the matter to the Upper Tribunal, which has since referred the matter to the European Court of Justice (CJEU). The advocate general ('AG') has now provided its opinion that the reverse charge should apply to all of Wellcome Trust purchases as it is a taxable person when taking all of its supplies into account. However, we are still waiting for the final decision of the CJEU and whether it follows the AG's opinion.

Universities therefore may wish to consider the implications and whether to make claims to protect their position until the outcome of the litigation is known.

Making Tax Digital for VAT

The Making Tax Digital ('MTD') requirements introduced on 1 April 2019 apply to all VAT registered taxpayers (with some minor exceptions), across all sectors, with income over the VAT registration threshold (currently £85,000).

There are three requirements under the MTD regulations which are as follows:

- Taxpayers are required to submit VAT returns using bridging software or an API enabled software
- There is a requirement to keep certain specified digital records
- Taxpayers are required to retain digital links for any digital records that feed into the VAT return

The first two requirements were mandatory from 1 April 2019 (or 1 October 2019 for those taxpayers that qualified for the deferral). However, for the third requirement HMRC introduced a soft-landing period before the full extent of digital links becomes compulsory. As such, this did not become a formal requirement until 1 April 2021.

HMRC's guidance in Notice 700/22 states that, once data has been entered into software used to keep digital records, any further transfer, modification etc. must be digitally linked to other pieces of software to create a digital journey. A digital link is one where the transfer of data can be made electronically between systems, i.e there is no manual intervention. This could be by the linking of cells in spreadsheets for example, but also includes CSV downloads, e-mails or via a digital drive.

We are encouraging all businesses to review their current VAT return process to ensure that is complies with all the requirements under MTD.

Making Tax Digital for corporation tax

The Government is looking to extend Making Tax Digital ('MTD') beyond VAT. This is not expected to be introduced for corporation tax until at least 2026, however HMRC have recently launched a consultation on the design of MTD for corporation tax, which closed on 5 March 2021. This specifically includes commentary on how this might affect charitable entities, including the following:

- Whether non-trading activities of charitable entities would be outside the scope of MTD
- How MTD will work in conjunction with charitable entities on periodic review
- Whether charitable entities need a tailored MTD service design

Gift aid and cancelled events/loan waivers

HMRC have confirmed that any 'waivers' of refunds, including waivers of loans from supporters to charities, can count as donations on which Gift Aid can be claimed. There will be conditions for this to apply and HMRC guidance is expected shortly.

Covid-19 and anticipated losses

HMRC has provided guidance on repayments of corporation tax due to its recognition of the exceptional circumstances that many industries are facing during the COVID-19 pandemic. Many businesses currently face losses accumulating in their current accounting period owing to the economic impacts of the pandemic.

In response, HMRC has now accepted that, in some circumstances, claims for repayments of corporation tax for prior periods may be made on anticipated losses before the current accounting period has concluded.

In order to claim relief, companies will be required to provide evidence to substantiate claims and support the quantum of losses expected to accumulate. It will be necessary to show that losses will comfortably cover any income of the current period and taxable profits of the prior period subject to the claim. This may require producing profit and loss forecasts, draft tax computations and assumptions behind any submitted figures.

This may not be relevant to trading subsidiaries who have made Gift Aid payments in the prior period, however losses can be utilised in the current period and it may be that no Gift Aid payment is necessary to reduce taxable profits. It is therefore worth speaking to your advisers early to establish whether this relief can be claimed.

Indian Equalisation Levy

The Indian government has recently introduced the Equalisation Levy ('EL') on consideration received by non-resident e-commerce operators for e-commerce supply or services.

The EL is levied on non-resident e-commerce operators at 2% on consideration for sales made to a person resident in India or to a person availing services/buying goods using an IP address located in India, if the threshold of 20 million Indian Rupees is breached.

An e-commerce operator is defined to be a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both.

The scope of "online provision of services" includes:

- acceptance of offer for sale
- placing/acceptance of purchase order
- payment of consideration, or
- supply of goods or provisions of services partly or wholly.

Given the wide definition of e-commerce operator for the purpose of the EL any non-resident providing online services through any digital or electronic platform is likely to get covered in the ambit of the EL. Should UK universities receive any such consideration we would recommend that further advice is sought from a specialist in this area.

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