Roundtable: financial resilience in HE

Higher Education Chairs of Audit Committee virtual roundtable

Introduction

Over the summer, Grant Thornton held a virtual discussion for Chairs of Audit Committee (or equivalent), focussing on the higher education (HE) sector and how the economic environment has affected the financial stability of higher education institutions (HEIs). The longer-term effects of frozen tuition fees, rising staff costs, and uncertainty in both domestic and international student numbers have increased the financial pressures on HEIs in recent years.

The discussion goes hand-in-hand with Grant Thornton's recent HE sector development report, which considers key risks facing the sector. The report considers issues including the impact of tuition fees and immigration policies issues across the UK and USA, as well as plans to diversify income streams. Speaking to HE leaders, the roundtable highlighted the current concerns and issues that HEIs are continuing to face.

Held under Chatham House Rule, the discussion raised a number of themes and questions which we outline in this report.

Going concern

Since the Covid-19 pandemic, going concern assessments have been an increasingly important part of an external audit process. The way that macroeconomic factors impact on different organisations can be hard to articulate into a forecast in an understandable way. Grant Thornton's going concern specialist, Julian Ayling-Rouse, spoke to the roundtable, highlighting the way that HEIs going concern assessments are increasingly challenging and complex.

Julian raised some hints and tips to ensure a robust assessment:

- An integrated model that combines the statement of comprehensive income, balance sheet and cash flow will enable management and trustees to fully understand financial effects across the organisation
- Make sure that the seasonality in cash flows is reflected
- Cash + available facilities + liquid assets = liquidity headroom
- Commentary on key assumptions – what has been assumed for student numbers, cost savings? Why?
- Severe-but-plausible scenario – what's the worst (but still possible) outcome?
- Reverse stress test – what will break your model (ideally in terms of student numbers for the following intake)?

One member of the roundtable queried how often audit committees should review sensitivity analyses. Often this happens once a year, usually around the time of external audit, but a quarterly or 6-monthly basis may be more appropriate, enabling committees to best understand any variations or changes within the year and avoid surprises at the year end. This approach would be particularly relevant for organisations with loan covenants or other external monitoring in place.

Given the difficulties that the sector is experiencing, a contributor to the roundtable flagged, **"[funders may take] a dim view of a modified audit opinion… it's not necessarily that somebody's got something wrong, but that there is a fundamental uncertainty or a material uncertainty as regards to the institution's ability to continue and therefore funders aren't going to look very kindly on that."** This generated discussion around relationships with funders: most funders for the sector are sophisticated and understand the pressures facing HE at present, so in the majority of cases, we could anticipate that funders would not be too shocked at modified audit reports in respect of going concern. Members of the roundtable also commented that they tend to have close relationships with key funders, so there is good awareness of issues individual organisations may be experiencing.

The discussion also looked at risk and the importance of identifying key risks, rather than including all possible risks, even those that are remote or low-level. Whilst audit and risk committees likely consider all possible risk areas on a risk register, for the purposes or a sensitivity analysis, main risks which relate to the operations of the HEI should be prioritised such as student numbers. A contributor to the roundtable made a fair comment that other expenses (for instance a cyber security incident) might significantly affect the going concern analysis but that these matters are much harder to predict. Where risks might have a large and lasting impact, but actually be implausible or unlikely, these are difficult to build into a 'severe-but-plausible' sensitivity analysis. Unfortunately, it will likely be the case that there are some unknown or unexpected risks that cannot be easily factored into such an assessment.

Financial resilience

Chris Petts, restructuring and advisory partner at Grant Thornton, joined the roundtable to discuss matters of operational restructuring and lending.

Operational restructuring: almost all HEIs are undergoing some form of cost reduction programme at present, due to rising cost base and a reduction in student numbers which means budgets are being squeezed from all angles. HEIs can have a high degree of unity and unionisation, and this can create barriers to change, particularly where we have seen high profile staff strike action across the sector. However, staff changes have meant that employees have been upskilled and become specialists in areas of crisis and cash management. Operational restructuring programmes have proven to be a challenge for many HEIs and delivered mixed results.

Lending: there is approximately £15bn of debt in the sector, and much of this is longer term (10-15 year terms). However, much of this is up for renewal in 2026 and lending terms in 2011-2016 were far more attractive than they are now, which means that some HEIs may be in for a shock when renegotiating terms. In addition, there's a real focus for HEIs at the moment around cash preservation, linked to the cost reduction programmes that are running, so expensive projects and non-essential CapEx has been delayed. We have seen a move towards HEIs seeking revolving credit facilities to provide liquidity headroom, but not actually use the facilities to fund capex projects as originally intended, with a real focus being on cash preservation.

The roundtable discussed their strategies at their respective HEIs and communication was the first area of interest flagged. One contributor commented that it was essential to, **"…[do] things in the right way and getting the comms right, that's common sense regardless of sector."** Another member whose HEI had avoided significant industrial action following rounds of cuts added that this was **"tribute to senior management who've spent a lot of time talking with workforce and unions… It's really detailed discussion and getting into the weeds of what you're doing and why."** The roundtable focussed on honesty of communications and how HEIs are uniquely placed in that they are not owned by shareholders who just need to squeeze the business of cash, but that savings are made to reinvest.

Reinvestment

The roundtable also reflected on what happens after those savings have been made. Most of the contributors had already explored cost saving programmes with their HEIs and were now stabilised in a position that does not necessarily generate much-needed cash for reinvestment back into the university. One member observed, **"next steps are fundamental… whether we look at different teaching models, [or] different ways of providing professional services support. I think that on the face of it, we've sort of cracked it, but actually I think all we've done is open ourselves up to the next layer of problems."**

Other members then commented on their own experiences, looking at ways to generate funds and reinvest. Options included franchising contracts, undertaken directly or through a Joint Venture (JV) arrangement, or supporting other HEIs by taking on students from failing or closing departments. There was some reticence in the group about franchising arrangements however, with one contributor offering that **"we are debating very strongly the brand risk around [franchising] and how you can manage that because that can manifest in so many different ways… reputation is really important."** Another contributor commented that there may be a risk with the financial sustainability of a franchise provider, meaning HEIs need to consider contingencies to support students who have been studying under a partner arrangement that may not survive. The roundtable agreed that brand and reputation is highly important to all HEIs and any external arrangements mut be entered into with appropriate analysis and due diligence of any third party.

Mergers may be an option further down the line, but one contributor reflected that this was not always a successful option, as seen in other sectors: **"very bad merger experience in the NHS, where a relatively competent District Hospital was required to take on a failing peer… the net result was a failing group."** At present, the roundtable members did not perceive mergers to be a viable option for their HEIs.

Tone from the top

The roundtable discussed the role of the Office for Students (OfS) and how their communications, whilst insightful, can be confusing for HEIs undergoing a transformation.

"…the OfS is saying, 'mergers and acquisitions or franchising is a risk because there have been historic issues with other areas in the sector.' I think it can cause quite a challenging set of circumstances because on the one hand, we obviously have to maintain financial sustainability, we have to improve, we have to make operational improvements. But if you go too far down the line, I think institutions worry that they will hit the point where the OfS suddenly starts taking notice of them…"

As the OfS continues to learn more about these alternative arrangements, the scrutiny increases, and it can seem that HEIs have fewer options for diversity of revenue. A member commented that innovation can be challenging to achieve. Those HEIs which are more forward-thinking and considering innovative methods to be cost-effective and maximise revenue may be limited in their achievements without seeing cultural change across the board.

Final thought

On reflection, the roundtable concurred that the risk environment is unique to the sector and **"Just generally, we're operating in a higher risk environment as an HE provider than maybe we were three or four years ago pre COVID."**

In summary, UK higher education institutions are facing mounting financial pressures due to frozen tuition fees, rising costs, and uncertain student numbers, prompting a need for robust going concern assessments and operational restructuring. Despite efforts to stabilize finances, challenges remain around reinvestment, lending renewals, and managing reputational risks in external partnerships, all within an increasingly scrutinized and high-risk environment.

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