HE Update

Higher Education Governance:

Time to Change

April 2021

Introduction

Victorian oligarchs who helped establish the great civic universities of the 19th century might struggle to recognise today's higher education landscape. The Office for Students (OfS), HESA, the Quality Assurance Agency, Financial Reporting Standards, the Competition and Markets Authority, Access and Participation Plans and research funding and ethics would surely seem strange to them. Student recruitment and retention, not to mention the complexities of HR, estates, and climate change might be novel challenges too. Those oligarchs, though, would probably still recognise the governance structures and principles that continue to underpin much of the higher education sector. Is this dichotomy justifiable?

Despite enjoying the support of a cadre of high-calibre and motivated voluntary board members who offer a wealth of experience, the governance model that underpins the majority of English higher education providers feels outdated for four main reasons:

1. Newer higher education providers bring impressive commercial savoir-faire, focus and urgency to their decision making but perhaps have to learn more about, and adapt to, sector-specific requirements. Conversely, there may be some established higher education providers, although well-versed in sector-specific requirements, who are weighed down by established business routines and practices that may not be so relevant in a changing sector. The CUC Audit Committee Code, adopted by many universities, offers one example of this. The Code was developed and updated from this earlier regime and therefore may not adequately reflect the current regulatory environment. Whether because of limited management and governance bandwidth during a period of profound sector change, or because of reluctance to embark on significant governance change before the OfS has made its own expectations crystal clear, much of the sector has continued to invest resources in adhering to the Code. It is difficult to envisage commercially-driven organisations (who now have a foothold in the sector) taking such an approach. A more competitive market, with an accompanying need for swift and robust decision making, brings new and sometimes unfamiliar challenges for longstanding higher education providers, and these constraints are less common in more commercial organisations, whose governance frameworks may be leaner.
2. The OfS brings a very different style of regulation from its predecessor. Although billed as 'light touch', it arguably requires heightened vigilance from governing bodies to be confident that the conditions of registration are met. Two years into the new regime, the style, expectations, and modus operandi of the new regulator still seem opaque when compared to HEFCE. In part, OfS has had its infancy disrupted by the coronavirus pandemic, but in part this opacity also reflects the very different style adopted by the OfS. Its recent reaffirmation of principle-based regulation should help convince doubters and optimists that the halcyon days (when seen retrospectively) of HEFCE-style regulation will not be returning anytime soon: instead, the new regulator looks set to chart a

very different course. HEFCE tended to promote good governance through adherence to defined outputs and processes (for example, the annual suite of assurance returns). The OfS relies on a (sometimes nuanced and layered) suite of registration conditions. These don't (in our opinion) lend themselves to a 'tick box' assessment. Instead, the complexity of the conditions, and the severe consequence of a failure to adhere to them, require governing bodies to actively understand each registration condition and to carefully probe management assurances before they can reasonably conclude that the registration conditions continue to be met.

3. We previously argued that traditional governance standards, promulgated in the sector by the CUC, are in contrast to the Financial Reporting Council's Corporate Governance Code, which promotes a considered, reflective, and tailored approach instead of the 'performative governance' routines which sufficed during the HEFCE era. The March 2021 white paper 'Restoring trust in audit and corporate governance' from the Department of Business, Energy and Industrial Strategy lends added urgency to this argument. Media attention on the white paper has tended to focus on its far-reaching implications for external audit and the 'Big 4' accountancy firms. The white paper also proposes (1) a new regulator whose power and reach will go beyond that of the Financial Reporting Council and (2) to extend the definition of Public Interest Entities to include third sector organisations with an annual turnover of £100 million or more, and in so doing to bring most medium and large higher education providers directly within its remit. Heightened demands on, and unprecedented personal accountability for, board members in higher education providers follow inevitably from this.

4. Our annual comparison of sector risk registers with risk analyses from beyond the sector invariably indicates that higher education organisations are relatively introspective. Technological change and opportunity, and ethical, environmental, and social responsibilities in particular tend to be relatively underplayed in higher education, even though we suggest that they are no less applicable to this sector.

Higher education's faster paced commercial environment, more demanding sector regulation and an emergent, potentially more rigorous corporate governance regime indicate to us that the prevalent governance structure, with an unpaid non-executive tier that meets typically four or five times annually, may no longer suit current regulatory conditions. It is surely time to explore whether other governance models would serve higher education better.

Non-Executives: The Future

Non-executive directors, as in any business, play a valuable role in universities and are essential to deliver good governance. Non-executives bring a range of skills and an external perspective that complements the executive team. They can mitigate the risk of 'group think' within executive teams and can help moderate the dominance of chief executive officers.

A need for faster decision making in the new higher education market, coupled with increased personal risk and accountability for non-executives (arising from the changed stance by the OfS and the recent governance white paper), suggests that the 'typical' university model where boards and board committees meet four or five times a year is no longer tenable. Faster decision making is needed. The idea that board members can challenge and approve executive actions and proposals adequately in such a context heightens the risk that registration conditions may be breached and in future could pose an unacceptable personal risk for the non-executives themselves.

Increased workloads, coupled with increased personal risk and accountability (flowing from the government white paper – including the suggested Director Responsibility and Resilience statements), might also be expected to result in a reduced pool of individuals who are willing and able to fill non-executive roles.

There is also a case now for remunerated non-executives who engage with executives more intensively and more frequently – although there are constraints on this for charities and those institutions that have taken this forward typically limit remuneration for chairs of committees roles, or for the role of chair of the governing body.

Issues to consider

As well as monitoring the evolution of the government white paper, particularly the potential designation of their institutions as public interest entities and the concomitant implications for non-executives, we suggest that providers should reflect on the following:

- Consider benchmarking their governance and audit committee arrangements against the current FRC governance code. Whilst current FRC requirements will inevitably be superseded as the government white paper progresses, they are likely to be closer than the CUC code to the government's intended destination. More particularly, the FRC publications may be helpful in fostering a more appropriate mindset that will serve higher education providers well as governance requirements strengthen.
- Challenge existing governance and business practices to ensure that they align with current, and not previous, regulatory requirements. 1) An assurance map based upon the OfS registration conditions and on the statement of internal control is now an absolute necessity to ensure that regulatory risks are being managed. 2) Processes, customs, and habitual activities that do not support the assurance map need to be challenged.
- The traditional higher education sector tended to act collectively and from a regulatory compliance perspective there was safety in numbers. However:
    - Providers now frequently compete against each other, so understanding when to collaborate and when to compete is more difficult than ever before;
    - Increasing numbers of new providers with new mindsets, new perspectives and unencumbered with traditional 'baggage' are active in higher education. Low-cost airlines and fintech start-ups have disrupted other sectors. Higher

education providers need lean and agile mindsets, and decision making, business and compliance structures and processes that match those of new entrants. Other sectors illustrate the consequences that stem from a failure to respond; and

    - The relationship between the OfS and higher education providers is one to one so there is no longer safety in numbers. Individual providers need to ensure they comply with the regulatory framework: what does or does not happen in other providers will probably be seen as irrelevant in a one to one dialogue with the OfS. In this context, Universities UK, which had significant standing in the days of HEFCE, now seems to be held at more arm's length by the OfS and to be recognised as a lobby group rather than an authoritative source of coherent representation.

- Executives, non-executives, and governance officers need to assess and challenge their outlook and their thinking to ensure they focus on the areas that matter and are not cleaving to outdated customs and perspectives.
- Consider a pathway to new governance structures. The government white paper proposes that third sector organisations that are designated as public interest entities would be allowed an additional two years to adapt. Experience shows, though, that two years passes very quickly in the world of higher education governance, so early consideration would be advisable, and a head start in securing a potentially more limited pool of non-executive talent could be a source of competitive advantage.

Support from Uniac

Change comes from within, and individual higher education providers need to 'own' any analysis of their current situation and any proposed solutions, recognising their own operating conditions and status (whether as charities, or private organisations). Uniac are happy to discuss the content of this paper further with you.

We can also:

- support your development of an assurance framework;
- assess your compliance with all, or any, of the OfS registration conditions;
- help you migrate towards lean business and governance processes and to strip out or realign processes that have ceased to be relevant; and
- support governance reviews using the FRC standards as a benchmark.

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