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The higher the pedestal, the harder the fall

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There have been mixed reports over the last couple of years about the state of the HE sector. Whilst commentators differ when trying to quantify the risk, most agree that financial distress and failure are real risks.

All that doomsaying has at least given educational institutions of all sizes and models a timely wake-up call and an opportunity to try to get ahead of the problem. In response, we have seen proactive steps taken towards better fiscal management, measures to increase revenue and cost savings, critical analysis of forecasts, strategic options reviews and a willingness to at least consider tactical alliances and mergers. All of those steps are to be applauded, and the Office for Students’ (OfS) June 2021 report certainly suggests that the finances of universities and other higher education providers are broadly in good order. However, inevitably there will be some HE providers (particularly those who were in a weak financial position at the start of 2020) who will have been impacted by the difficulties and financial losses caused by Covid-19 and Brexit more than others, and it is these organisations who will be particularly nervous about the potential impact of the Government’s upcoming policy paper on funding and the possibility of a reduction in the cap on undergraduate fees being implemented as part of the comprehensive spending review in the autumn, particularly if, as seems likely, pressure on public finances make the Government reluctant to top up any shortfall by way of teaching grants.

An HE provider, like any corporate entity, can be run badly. Why should the taxpayer continue to support any entity that is fundamentally flawed when there are viable options to restructure, consolidate or transfer the provision of its services to more appropriate alternative providers? Put another way, what is the incentive to encourage providers to manage their finances prudently if all failing institutions are guaranteed a bailout?

The new restructuring regime in response to Covid-19

A ray of hope may be found in the new Higher Education Restructuring Regime to support HE providers in England who are at risk of market exit due to the challenges of Covid-19. On rollout, the Department for Education (DfE) was very clear to stress that this new regime does not represent a taxpayer-funded bail-out of individual organisations in the HE sector and it is not a guarantee that no organisation will fail.

This should not be mistaken as a soft or cushy option. Providers approaching the DfE for support will need a sound economic case for government intervention and, if approved, will be forced to make some difficult decisions. Providers will be expected to adapt so that they can, in time, start to make their own contribution to the nation’s future. That might involve governance changes, demonstrating a more enhanced regional focus, the delivery of quality higher technical education or apprenticeships and/or a realignment to subjects which deliver better graduate employment outcomes in areas of economic and societal importance. Providers will also be expected to evidence their efforts to tackle bureaucracy and crack down on administrative activities that do not demonstrably add value, including the funding of student unions, senior executive pay and other administrative costs.

Eligibility for support will be assessed on a case-by-case basis and intervention will be considered, in conjunction with an independent business review (IBR), if the following conditions are met:

1. There is a clear economic and value-for-money case for intervention – this should be a last-resort measure after all other finance options have been exhausted, including the government-backed business support schemes;

2. The problems are related to Covid-19 and there is a clear and sustainable model for future provision as a result of restructuring, meaning that the provider should not need further assistance; and

3. The failure of the provider would cause significant harm to the national or local economy or society.

The regime is not without its risks. Ultimately, having gone through this process, support may be refused or the recommendations of the IBR may suggest an alternative rescue mechanism which the provider may then be forced to accept.

What would happen without support?

The forced closure of an HE provider in circumstances where its debts were not underwritten would undeniably send shockwaves through the sector. It would have an impact on investment, borrowing, security, enforcement, stakeholder confidence and student enrolment; in short, all the factors that are relevant when considering the viability of a limited company. The introduction of the new regime is a clear message of the Government's intent that failing HE providers should share some of the responsibility for saving themselves and that we should be prepared for the consequences when some inevitably fail.

The Technical and Further Education Act ((TAFEA) 2017 introduced a special administration regime and clarified the insolvency options available to further education providers. Although TAFEA has rarely been used, at least those institutions and their stakeholders know where they stand. The same cannot be said for the HE sector.

There are currently 423 registered HE providers officially registered by the OfS. That includes a mix of different types of entity: those that were established by Royal Charter (34); those created by statute (65) or by Order of the Privy Council (18); and those other entities (including registered companies, unincorporated entities and/or registered charities) that cannot call themselves universities (306).

Understanding the underlying status of the HE provider is vital because, in the event of financial distress, there is no one-stop shop for determining the available insolvency options.

Exempt charities

Most HE providers are also exempt charities. An exempt charity has charitable status and its trustees are required to comply with the same general duties and responsibilities under charity law. Exempt charities are treated differently from charitable companies and the application of the Insolvency Act 1986 is significantly curtailed.

Instead, section 113 of the Charities Act 2011 provides for the presentation of a petition by the Attorney General for compulsory liquidation, most likely on the grounds that it is just and equitable to do so (section 122(1)(g) of the Insolvency Act 1986). There is often an overlap here with chartered providers, which may also share exempt charity status.

Chartered providers

The principles, powers and function of our oldest institutions and the way in which they are governed are enshrined in their Charters and Statutes. Insolvency was presumably so unthinkable when these charters were first bestowed by monarchy that, even today, the only options available at the provider's instigation are compulsory liquidation or receivership, neither of which share the OfS's objective of putting students' interests first.

Higher education corporations

Section 128 of the Higher Education and Research Act 2017 provides an additional option to give notice to the Secretary of State to request the dissolution of the corporation and the transfer of its property, rights and liabilities. Whilst this might appear drastic, it is perhaps preferable to the more draconian options outlined above, because it will at least offer opportunities to safeguard students' interests and to transfer existing provisions to an alternate provider.

Newcomers

More modern HE providers have been established as or converted to registered companies. Here we find ourselves on terra firma, as the normal suite of insolvency options under the Insolvency Act 1986 will apply. This enhanced toolkit means that these providers are better placed to adopt a process which meets the OfS's objectives of ensuring long-term viability and, in so doing, protect students' interests.

What should we do?

The absence of a standalone regime for HE providers creates an uncertain landscape in the event of failure. The new regime represents a safe refuge from which providers may either be rehabilitated or cast out into cold, unchartered territory. To avoid the latter, providers should give themselves the best chance of being able to benefit from that 'last chance saloon' by aligning themselves now to the thrust of Government policy enshrined in the objectives of the regime itself.

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