HOUSE OF LORDS

Industry and Regulators Committee

Corrected oral evidence: The Office for Students

Tuesday 2 May 2023

10.30 am

Watch the meeting

Members present: Baroness Taylor of Bolton (The Chair); Lord Agnew of Oulton; Baroness Bowles of Berkhamsted; Lord Burns; Lord Clement-Jones; Lord Cromwell; Lord Gilbert of Panteg; Baroness McGregor-Smith; Lord Reay.

Evidence Session No. 11 Heard in Public Questions 95 - 105

Witnesses

I: Nicola Owen, Deputy Chief Executive (Operations), Lancaster University, and Chair, Association of Heads of University Administration (AHUA); Erica Conway, Chief Financial Officer, University of Birmingham, and Chair, British Universities Finance Directors Group (BUFDG).

Examination of Witnesses

Nicola Owen and Erica Conway.

Q95 **The Chair:** Good morning. This is the Industry and Regulators Committee in the House of Lords. This is a public meeting. We have an inquiry into the Office for Students, and our witnesses today are Nicola Owen, who is chair of the Association of Heads of University Administration, and Erica Conway, who is chair of the British Universities Finance Directors Group. Thank you both for coming, and for the written evidence that you have sent in, which we have seen.

Can we start with a general question about how you have found engaging with the Office for Students? You deal with other regulators as well, but can you give us a general impression of the kind of relationship that exists between universities and the OfS?

Nicola Owen: Thank you for the invite to give evidence. It has changed a bit over time. Inevitably, at the beginning, there was a level of set-up and a very conscious level of separation. It was a different body and one that was very conscious not to be captured by the sector. Even at that stage, as we were working through things, there was some opportunity to highlight where things were not working or were not being operationalised in a particularly effective way.

Over time, we were able to make some changes, for example to reportable events, which were creating confusion, additional burden, and overreporting in some areas. When we were raising concerns about communication, we were able to make a bit of headway on simple things like a weekly round-up to vice-chancellors, so that they knew what was happening.

Had I not been in my sector role, I would have had very little opportunity to engage with the OfS. It is not clear where the lines of engagement would be, and things were largely sent from and to a general email box. As a head of operations and as a university secretary overseeing compliance with the conditions, it is pretty faceless as an organisation and a regulator, although some very recent contact suggests that that is starting to be taken on board.

It is not necessarily across the whole organisation. The relationships and engagement with the previous and the current director of fair access have been quite different in style. With the most recent changes in consultation, it has felt like a strikingly different way of engaging with the regulator. It is in relation to regulation and quality that it has been harder to try to navigate and to really get a sense of engagement that we might need.

The other element that I have been conscious of is that we have not really heard much about the voice from the governing body side, and my association supports governing bodies; most of our members are university secretaries of some kind. Again, it has been significant for the governing body, which has increasingly had responsibilities laid on it and new regulatory returns to comment on and review, to try to navigate and understand the role that the regulator is playing overall.

Regulation is not new to the sector at all. We deal with lots of formal regulators and agencies that operate in a regulatory or statutory framework. I would work regularly with the Information Commissioner’s Office, the Health and Safety Executive and the Competition and Markets Authority, for example. Other agencies such as the Office of the Independent Adjudicator or UKVI have teeth. We do not always like the outcomes that they might judge us on or work through, but it is quite different in tone and it feels like there is a difference in maturity between them, in the sense of the clarity and transparency of what framework you are needing to work with. It is also very much seen in the spirit of working with them and with the idea of enhancement and reaching the right outcome, which feels quite different from a lot of the engagement that we have with the OfS.

Erica Conway: I would echo most of the points that Nicola has made. Just to add a couple of things, it is important to remember that the OfS is still a developing regulator, and we have seen quite a lot of evidence over the last five years, particularly from the financial part of the sector, where it is trying to find its feet and work through what is required. The scale of data that it is drawing from the sector to try to help make its risk-based approach appropriate is one of the things that have been quite difficult to experience from the sector perspective. There are active dialogues with the finance teams in the OfS about how that might be improved. There are also examples of where it has tried to do things and not quite understood the impact on the sector.

The challenge that Nicola was referencing a little there is that it sometimes feels as if it goes down the route of deciding what the answer is, trying it and then changing it. There is more of an opportunity to discuss and engage, not necessarily through formal consultation but through the networks that it has and through sector groups like my own and Nicola’s, and to ask, “What’s the likely impact of this going to be?”, so that it is not then having to amend something that it has put out as policy.

Q96 **The Chair:** Do you think the OfS understands the autonomy of universities and that balance that has to be struck between making decisions that you think are right and appropriate, and being properly regulated? Do you think that its approach is proportionate in terms of the issues that it focuses on?

Nicola Owen: If I take the autonomy one first, in conversations that I have, there are certainly points where that autonomy is recognised. Increasingly, though, a number of the conditions, and certainly the way in which they have been operationalised, have become really quite prescriptive. Rather than stating the “what” of the condition and the expectation, and leaving it to institutions to decide how they can demonstrate that they meet that condition, it has come out with quite a number of prescriptive ways in which that is done.

Often, institutional autonomy is particularly focused on quality and standards. There have been some examples where the sector has felt that the lines are being blurred—for example, the way in which the level of prescription on the English language was introduced—I can come on to that at another point—or on the upcoming inspections and the way in which the evidence we are being required to keep is being held: the B4 condition that we referenced in our submission.

In terms of proportionality, in the engagements we have had with the OfS, we have, for several years now, been raising the level of regulatory burden and the level of expectation about things that are in place. In some of the dialogue that we have had with them, the perception has been raised that that is because institutions or their governing bodies are gold-plating things. I have also been told that maybe governing bodies are therefore not operating properly if they are being too risk averse and gold-plating things, so the proportionality, or the regulatory burden, is something that we are doing to ourselves.

There may be some truth in that, but what has not really been taken on board and understood is why that might be happening, pretty consistently, in some very mature institutions with very high-level, very experienced governors on board. That sense in which institutions understand what is being expected of them with regard to what they are being required to return, and have to make significant adaptations to the things that they would normally do in order to get over the line, has concerned us about the proportionality.

Erica Conway: Just to give another few examples, from the Office for Students' perspective, approximately 40% of the sector is home undergraduate students. In that population, there is quite a variety in the type of student, but they are trying to regulate that proportion of the sector's activity where 60% of it is subject to other regulation or other activities, so there is a challenge in the balance that they are trying to address.

From a general public perspective, the home undergraduate population tends to be the thing that we all know about. We have neighbours or friends who have kids at university, so that tends to be where it comes from. It is about recognising the burden of regulation and the depth of some of that regulation. All the financial reporting that we submit on an annual basis, which is factual and into the future, is at the same level of detail. Having to say what will happen to a very specific account balance in five years' time becomes quite difficult for us to do, so its usefulness to the regulator must be distorted by the way each of us is putting that information together. That is a particular area.

I also feel slightly concerned about proportionality, in that we are seeking to think about the worst that could happen if an institution was performing in an inappropriate and unacceptable way, and applying that through regulation and data to the rest of the sector. That, again, undermines the autonomy perspective. If we started from a position of most people trying to do the right things, that would significantly change the level of data, information and access that was required.

Q97 **Lord Reay:** Continuing on the theme of regulatory burden, what is the cost to institutions of complying with the OfS's regulatory framework? Do you think the OfS could be more communicative and clearer with providers on what is needed to comply with its requirements? To what extent might this mitigate regulatory costs?

Nicola Owen: I will start with the second part of your question. There are elements where better communication could help, and that is certainly one of the ways in which we worked with the OfS a number of years ago on reportable events. In trying to get a sense of how the OfS was going to respond to an event, the original guidance was effectively that institutions need to make their own judgment, but, in the end, the OfS will make the judgment. There was a lot of second-guessing as to how far we had to go and not knowing what the risks might be.

Some of the case studies or further guidance that the OfS has produced have been helpful, but there is a balance here. One way in which it has interpreted better communication is more prescription in regulation. The B4 condition that I referenced earlier is, at one level, quite a technical thing. It is in the wider quality and standards framework, and asks institutions to maintain and retain every item of assessed work for five years and, ideally, for that to be anonymised. That specific element was not consulted on. There was a different wording in the consultation. That level of prescription, which the OfS may have just assumed institutions did anyway, has the potential to make us make huge adaptations and build new systems, and it will certainly run into the tens if not hundreds of millions of pounds per year for the sector.

In terms of proportionality, it has been designed so that institutions cannot gameplay by sampling, and so the OfS can just ask for any institution's level of assessment over a number of years at any time. That does not seem proportionate to what it is trying to achieve. It is a careful balance between engagement in trying to help institutions to understand what the OfS is really looking for, and not overplaying that in the level of prescription that comes in.

Erica Conway: I would make a distinction between communication about what the Office for Students is trying to do in seeking help from the sector as to how that might best be achieved, as opposed to mandating how things will be delivered. It is the mandating that leads quite a lot of us into the challenge of thinking, "Okay. That's not how we were doing it. We now have to do something different".

As Nicola said, system change is a significant piece of work. There is some student reporting coming called HESA Data Futures. We have been waiting for three or four years for clarity in what exactly that needs to be, but that is a system change for all of us, because it requires us to collate student data in a slightly different way from the way we do it for ourselves. That is a burden of regulation. I am not aware of any institution that effectively has a department called "OfS governance response unit”, or something of that kind, to enable us to track exactly how much it is costing, and visibility becomes part of the challenge. We see the fees that we all have to pay and when we have had to take on extra people to do specific parts, so changes in systems is an example of that.

Where it is just an ongoing burden, that has been subsumed and is preventing people from doing something else. How that was achieved will be different across different institutions. That is part of the challenge of answering the specific question about the burden of regulation. I know some institutions have said that, for them, it is between four and 10 people. For most, it will inevitably be bits of other people’s jobs. It is the opportunity cost that we have lost as opposed to the specific cost of governance responding.

Lord Reay: Do providers receive information from the OfS as to why they are making these requests and introducing these regulations on issues such as B4? Do you get a sense of their telling you why this needs to be done and what objectives are being met?

Erica Conway: To an extent, but that tends to come once it is in place rather than in advance. This is the thing that we are trying to respond to when it comes to how you would do it. It is more at the point of saying, “Once we’ve mandated it, we’ll tell you what we’re trying to do”. Is that fair, Nicola?

Nicola Owen: I think so. There are points in consultation where some of that is still to be explained. There have been some consultations. The recent one on changes to the access agreement is probably a better example of practice where there has been an opportunity to engage as it is forming. That has not undermined in any way what the OfS is trying to do; it has just made it clearer to us the purpose of what it is trying to do and how that might be better achieved.

The example of B4 is a good one, in that I slightly worry that it was assumed institutions just did this anyway. I am yet to find an institution that did it like that. I have some understanding, because I have direct engagement with the OfS, of what it is trying to achieve from that, but if I were not in the role that I am in, and in an institution, it would not be particularly clear. It is then too late.

One thing that has worried me in that discussion is that it has been indicated to me that there is no way in which the OfS can un-expect things, having put something in place, if we are saying that it is not proportionate or realistic, and we are worrying about how we can achieve it in many cases. Assessment is not all about exams; all kinds of artworks and artifacts are produced as part of an assessment. But I am being told that there is no mechanism for undoing something, even if it needs changing, which does not quite seem to make sense. That is worrying, if that is the case.

Q98 **Lord Burns:** As you have mentioned, the OfS argues that it takes a risk-based approach to regulation. What evidence do you have that this is really happening?

Erica Conway: My day job is with the University of Birmingham. We have very limited engagement directly with the OfS and, therefore, have assumed that we are not at the high-risk end, which is where we would also seek to put ourselves.

The OfS recently released a couple of documentations about how it has been reviewing particular interventions and how it has undertaken those. They are relatively brief documents and, if one has the time to read them, they are quite helpful in indicating the type of work that is undertaken. In itself, that does seem proportionate, but, as I say, it does require you to have read it. You would not have known about it unless someone had drawn your attention to those particular pieces of information.

Lord Burns: We have had quite a lot of people saying that they are not really approaching it in that way and that, in practice, it does not feel like that. I am trying to get some idea of what the evidence is and what is happening on the ground.

Erica Conway: The difference that people are seeing on the ground is that level of the burden of regulation. There is no sense of stratification or saying, "If you're higher risk, there's more that we'll collect from you, more intervention that we'll take, and more governance and data responses that we will require". There is a level of data response that is pretty high for everybody, and the intervention is to say, "We'll come and see you and ask you about what you're doing". That is the burden that we are all pushing back on a little bit and asking, "Could you not look at stratifying where the areas of concern are and ask for more from them?" There is clarity, that the OfS is doing that, but the level that it is asking of everybody is pretty high already.

Nicola Owen: To the point that Erica made, silence is effectively the only clue that you are not a high-risk institution. As Erica said, the case studies that have been published are quite helpful in that regard. It is not only financial. There are other risks that it is looking for. We have been trying to encourage a bit more transparency about the outputs from recent quality investigations, and that may well be helpful.

Part of the issue is trying to second-guess how to respond to that sense of risk. Institutions ought to be confident enough to make their own assessment. That, to an extent, is a fair challenge from the OfS that has been played back to me in particular circumstances, but it would be helped a great deal by a better sense of engagement and better examples of what is happening, in ways that can help to inform that decision.

Q99 **Lord Burns:** On the same sort of lines, can you tell us something about how this regulatory baseline works?

Nicola Owen: The baseline is helpful at one level. If we go back to the establishment of the OfS, it was designed to encourage a level playing field", and all the new institutions that were encouraged to be set up through that regulatory framework would have to ensure that any student could expect to get a minimum or baseline level of quality standards and in the way in which an institution was governed and run.

However, as Erica says, that lack of stratification, in the sense of where that baseline is and whether other things will be placed on top of that, means that, as an institution, you are constantly adapting to this baseline. It does not particularly feel like a baseline. It feels like a significant and complex set of things that you are being asked to respond to or to apply.

I do not think that institutions have effectively just moved to the baseline; I think there is more confidence and higher expectations institutionally of what they do. But it means that you are diverting resources to adapting to meet that baseline, rather than just developing what you want to do in an area of study. Take the information that we got on the changes to the recent quality conditions. We now have to wade through a huge amount of data—certainly my institution has brought in additional resource—in order to understand, at a very granular level, whether we meet very specific outcomes or how far we are off them, et cetera. It is diverting, in some cases.

Lord Burns: So it has quite a big impact on you.

Nicola Owen: Yes.

Lord Burns: Do you think it is beneficial in terms of the outcomes? Does it lead to improvements and enhancements, or do you regard it largely as a bureaucratic load?

Erica Conway: The challenge goes back to my previous point. Where institutions were not performing very well in the areas of quality, it will have upped them, because there is a level of clarity. Those that were at a level above the baseline in the first place—including my own, I would like to think—are now responding by adjusting what we thought was the right thing to be doing, and we are not quite sure where that balance should end up. It is quite a painful process to work through for something that was reasonably high quality in the first place, so some of that depends on where you are in the sector.

Lord Burns: So this is a search for discovery of whether you are above the baseline.

Erica Conway: You would struggle to actively say, "I'm definitely above the baseline". We all start from the prospect of thinking that we are doing the right things and we are above the baseline, but we have to go through quite a lot of documentation from the OfS definition of the baseline. Whether that would be exactly where we would put it is a significant challenge.

Q100 **Lord Clement-Jones:** I need, first, to declare an interest as chair of the governing body of Queen Mary University of London.

You very helpfully answered some of the earlier questions I was going to ask, such as, “What is the nature of the OfS’s relationship with higher education providers, right from the get-go?” Do correct me if I am wrong, but you have also answered pretty comprehensively whether the OfS strikes the right balance between working collaboratively with universities and providing robust challenges.

There is a third question there. Do you feel that the OfS is close enough to the sector to understand the realities that it faces and the impacts of its own regulatory framework? You have alluded to the lack of communication and, if you like, the post hoc explanation after the regulation has been put in place, but are they close enough to the sector to understand what it is up to?

Nicola Owen: We have talked to them fairly recently about the balance they are striking between having members of staff who have experience of universities and who understand how things work and what issues there might be, and bringing in other staff from another area and new perspectives. There clearly needs to be a balance. There has been a lot of change in staffing in the Office for Students. I know it is trying to strike a balance in making sure that it has sufficient expertise and experience to bring that insight.

There are a number of things where it feels like the responses from the OfS do not necessarily fully understand the impact. I gave the governing body example. The tone was set pretty early on—I do not know whether you were there at the time, but you may remember this—when some institutions were one day late paying one of their designated body fees and every institution then received a letter. It required institutions to write a paper, go to their governing body and explain why that had happened and why it would not happen again.

When that was unpacked, a lot of that was to do with the way BACS had been set up and some of the data not being accurate. It will have taken effort to investigate that, to write, and for the council members to read and discuss. The reaction was very disproportionate. To a certain extent, it set the tone that it was looking to point out where compliance was not happening rather than to encourage it.

Erica Conway: I can give a second example that is similar. There are some very good people in the Office for Students and, from a one-to-one engagement perspective, it is hugely valuable. Particularly through my sector role, I get an awful lot of feedback and opportunity to feed in. It is what happens to that when it gets taken back in the OfS that, for me, becomes slightly more opaque.

Another example is access and participation plans in the sector, which are very important in showing that we are spending the money on the appropriate things and delivering the outcomes that are expected. I understand that there is a need to monitor that, but when it was first implemented there was a suggestion that it should become a note in financial statements. Again, that is a perfectly reasonable request.

It was then suggested, without conversation with audit firms or the sector, that that particular note should be subject to a specific level of materiality for audit, which was disproportionate and out of context of all the financial statements, and which none of the audit firms could deliver anyway, so that had to be rolled back. This was all happening at the point when people were producing their annual financial statements and taking them through governing bodies.

Again, the reaction of someone sitting on a governing body with limited interplay with the OfS would be, "I'm not quite sure I understand what was going on there". If we had had the conversation through the sector groups that existed before it was implemented, we might have been able to get to the same end position without the pain on the way.

Q101 **Lord Clement-Jones:** I recognise all those examples, believe me. You talked about staffing, Nicola, and the OfS is funded by fees from providers, adding to their costs. How does the OfS account for the value of money going into its own operations? Do you think it achieves value for money? Should we be adding more staff who really understand the higher education sector, for example?

Nicola Owen: It is hard to say whether it achieves value for money for the sector. There are certainly things that it does in the background that are not necessarily well known in institutions. That level of engagement and communication has not really been there. One example is its work with other stakeholders. Erica may have examples.

The way it has responded to its own operational value for money is that it produces an annual report. There is a strategy that sets out its plan for operational effectiveness, but that was set out in 2019-20. It included a target to reduce the fees by 10% by 2023. I do not think that is where any of us think that is headed, so are we confident that they have a plan?

To be fair, lots of things are being added into the OfS, and you have already received quite a lot of evidence on that. What we do not have a sense of is whether it is targeting its resources at the highest-risk areas or whether, again, the lack of stratification that we see is then replicated in the way that it organises things. Certainly, the sense in which it is being played back to us is that it needs to do more. From an institutional perspective, in a flat fee and inflationary environment on the undergraduate side, that is not playing very well.

Lord Clement-Jones: Erica, in your experience, are the fees rising substantially over time? Please do answer the value for money point as well.

Erica Conway: Since its inception, for a large institution, there have been small inflationary increases year on year. We had an indication that, for 2023-24, there could be a significant increase, but we have not seen that invoiced yet, so we are not entirely sure where that is going to land. Again, that is an example of where we have had some information saying, "This might be coming", and we are all waiting to see whether it will.

I think it was a 15%increase in one go, which would be substantial even against current levels of inflation, which is back to Nicola's point. What would we get for that? Is it a reflection of the additional requirements being placed on the OfS that require it to have additional staff? Will it have to do something different, or can it not make the efficiencies because of the scale of what it is being asked to do? That level of transparency is not there.

On the stratification that we have been talking about, there was a suggestion early on that a risk register that would be published by the OfS. All of us in the sector were quite concerned about that, not so much in wondering, "What if we are on it?" but, if such a register was published, it would almost make those institutions unsustainable. Who would go to an institution that was on a register?

I would support the current examples that it has published explaining why it does not make that information public. That is really important. We are not asking for specifics in order to know who is the highest risk in the sector so that we can all point at them. It is more about understanding the stratification, how it is working, what that means to us individually as institutions and what we have to do in response to that. That is the clarity that we are seeking.

Lord Clement-Jones: There is a level of opacity that makes it rather difficult to judge the value-for-money point, at the end of the day.

Erica Conway: I would also echo Nicola's point: value for money for whom? Ostensibly, if you look at the legislation, you could argue that the value for money is not for institutions but for the students who are serviced through the office. Therefore, asking us whether we get value for money is the wrong question.

Lord Gilbert of Panteg: Can we pick up on this issue of capacity? I am thinking about the criticisms that you have expressed about lack of proportionality, risk-based assessment and understanding of how the institutions work. What is your assessment of the capacity of the OfS to meet its current duties? Does it have the powers, resources and expertise that it needs? It will take on significant new duties when it takes on the designated quality body duties. Is it ready for that, or will it be a bit of a stretch for it to take on those additional duties, if you think that it does not have the capacity to fulfil its current duties?

Nicola Owen: The OfS certainly has sufficient powers, and those have extended beyond HERA. There has been further legislation that has expanded the scope of what it will do, and more is to come.

On resources, quite often it feels like the regulation is seeking to cure all ills in the sector. Conditions are being placed on the register for things that will not necessarily be solved by a set of processes and compliance checklists. I question the appropriateness of that. These are often complex social and cultural problems that will not necessarily be best solved by some of the things that are put in place.

As it is organised, we are hearing that that will put pressure on its resources. That is why the request for additional fees is likely to come through. With respect to the designated quality body, it evidently does not have the resource at the moment, in that it is out looking and recruiting for that expertise. It is not quite clear how it intends to play that role as a quality body. To gain any sense of confidence, and to respond to the diversity of providers in the sector, it will certainly have to increase in academic expertise and knowledge about what happens. That is clearly an area of significant concern at the moment.

Erica Conway: On that, and on the uncertainty as to whether it is a short-term or a longer-term arrangement, it will make recruiting the staff you want to deliver quite difficult, even on a short-term basis: "Am I coming for a role that's going to be here for a couple of years, or am I building a career path in the Office for Students?" That would attract a slightly different person, so that is a challenge.

In specific parts of the OfS, there are some challenges in how it responds to the regulation that it is being asked to enforce and the breadth of it. I am also concerned as to whether, in the regulator that is focused on student value for money, student quality and quality of institutions, putting all those things together makes it too much of an amorphous blob, and whether segregation is important. It is critical that we end up with a quality mark that is visible from the international stage as being accessible and appropriate, which is what the QAA previously gave us. If the OfS takes this role on more significantly, it will have to address those issues; otherwise, the marketability of our students in the global market becomes much more challenging.

Lord Gilbert of Panteg: Looking at the criticisms that you have expressed, which are largely about proportionality, understanding what the institutions are doing and what their practices are, its lack of capacity in its existing duties may be down to the fact that it just does not recruit enough people from the sector with experience of running universities and institutions. Otherwise, it seems to me that it would not have that problem and that it would demonstrate an understanding of how you operate.

Nicola Owen: There are certainly people who work there—and a few at senior levels, although fewer than before—who have had experience in the sector. It will always be difficult. Things are dynamic and do not remain the same, and there are potentially other ways of getting that understanding, but having that sense of balance, and sufficient expertise and understanding of what happens in the sector, is key. It has really helped the confidence of other agencies that we work with now or have worked with in the past.

Erica Conway: It goes back to the mechanism of engagement. Quite often, for many of us, the engagement is the response to a consultation, which is quite formal. We talked before about the confidence of not being on a list, or the concern because you do not get a visit, but that means that you do not have the opportunities to share what it looks like across the sector. There are multiple sector groups involved in that. The finance directors group engages with the finance lead in the OfS, but we do not engage more broadly with the team. That sense, from its own perspective, of what it is trying to do is uncertain. Is it just trying to look at specific data for specific organisations, or is it trying to look at everything and spot patterns that might give it an idea of where to go? I do not see that clarity for the people I come into contact with so they know what they need to respond to.

Q102 **Baroness McGregor-Smith:** It would be good to get your perspectives on the key financial risks for the sector in addition to what the OfS has already said. Do you think those risks are limited in any way to one particular group of providers, or are they more systemic?

Erica Conway: You have heard from others that the fixed fee for home undergraduates is a big challenge. Aligned with what we have been saying about the burden of regulation in delivering that, although the fee has stayed exactly the same, students' expectations have significantly increased, not just as a result of the pandemic but more broadly. Therefore, responding to that has become more difficult. We are trying to do more with less. To be fair, that is true across many sectors, but we have limited capacity to grow that.

All institutions have responded to that in different ways. Where you are very small and very specialist, your response to that is about significant cost control and probably a reduction in the offer. For broader institutions, it has been more about looking around the edges for the kinds of things we were doing that were the right thing to do either for student experience or for the communities in which we engage, and trying to cut those back.

In some institutions, such as my own, it is about looking for diversification of income and alternative sources. Ancillary things such as student accommodation, student services, international students and additional research from funders that are not the UK Government and so pay a little more all come into play, but the ability to do that varies. There has been quite a lot of discussion in the sector about the scale of reserves and cash holdings that sit in institutions. Although those numbers look large in many institutions, including my own, it is important to recognise that they represent relatively small amounts of expenditure. Something published last week on Wonkhe shows that most institutions are holding between three and four months' worth of cash. That is not a lot of money to be holding. Although the numbers are big, the scale of the operations is also big.

I would suggest that financial management is the consistent challenge across the sector. Beyond that, it is rather dependent on the type of institution that you are, your scale, and where you have been built from, as to what you can do.

Baroness McGregor-Smith: How did we get to a situation where most institutions are holding only three to four months of cash, in a sector that is clearly under pressure from not being able to lift fees, has seen really big inflationary moves since the pandemic, and was nearly shut for a while? Has that always been the case, or have diminishing cash returns just been happening gradually?

Erica Conway: The challenge to convert everything into cash has become much more difficult in the sector, as it has for all businesses, in the last three or four years. Interest rates for some parts of the sector have a significant impact. If you are looking for new funding now to help grow, that will be very difficult, because interest rates are so much higher now. That can be a significant draw. Fundamentally, it is about everybody doing the best they can in fairly challenging circumstances.

Baroness McGregor-Smith: Do you think that the sector and others that have had this challenge were comfortable in such a low interest rate environment and maybe did not think widely enough about what could happen if rates rose rapidly?

Erica Conway: I accept that that is probably a challenge. That is a UK-wide challenge as much as a sector challenge. We were complacent because they were low for a long time. You have to be as old as I am to remember high interest rates hitting you from a mortgage rate perspective. Most of our young people who have been graduating for the last 10 or 15 years have not seen high interest rates. That is prevalent as much from a societal perspective as from a sector perspective.

It comes back to something I suggested earlier. All good businesses and institutions will be doing forward planning usually of between three and 10 years, depending on their generation, what they are used to and what their governing bodies require of them. The level of data and the detail at which they do it will vary, and I am concerned that the level of detail that is required of some of us is different from what we would normally do for ourselves. We are spending time producing detail to support something from a regulation perspective that is different from what we would see as being the appropriate thing for us to do.

Baroness McGregor-Smith: Are you saying that it is more detailed?

Erica Conway: Yes, significantly more detailed.

Nicola Owen: You asked whether those risks are limited to particular groups of providers or whether they are more systemic. There is the risk that certain types of providers, in the way their recruitment or their activity is set up, will be more vulnerable to certain things, and others to different things. There are systemic risks, but there are also quite different risks in different parts of the sector. The pandemic highlighted the fragility and precarity of some of those income streams that institutions had increasingly come to depend on, in some cases, to balance the books and to subsidise and develop activity.

The OfS was designed in such a way that there would be winners and losers, and there would be greater competition. We are certainly in a period where, as Erica indicated, every institution is trying to diversify and think about ways of innovating and about different approaches to the business model, but that will lead to some instability. How we manage that in an overview of what is happening in the sector is much more difficult in the current environment.

Baroness McGregor-Smith: We have seen such extraordinary growth in the sector over a significant number of years. Do you think that is over? Do you think that it will be much more limited now?

Nicola Owen: We have all been preparing for and are aware of the fact that there will be a demographic shift, and we are heading into that. Looking across the broader sector, some institutions have grown hugely rapidly, which is throwing up new issues with student accommodation, for example. As Erica said, the financing of student accommodation has changed significantly.

There may be some constraints, but the business model almost leads you into a position where you need to keep growing to stand still. So you either look to address the inflationary environment through continuing efficiencies or you grow.

Baroness McGregor-Smith: Is the business model that has been created for universities over the last 10 or 20 years, say, the right model for the future, or should there be significant changes to it? At the moment, you have capped fees and you are always trying to increase numbers to offset the fact that efficiencies are getting tougher and tougher. Do you think the model needs to change?

Nicola Owen: The model does need to change. It is increasing the level of risk in the sector, and we will see more instability overall. Therefore, unless something changes, we will see more institutions getting into much more trouble.

Q103 **Lord Agnew of Oulton:** Maybe I will start with Erica, because I have been asking everyone this but getting rather waffly answers, to be honest with you. As a finance person, I have high hopes that you can give me a crisp answer. What I have been trying to get to in these sessions is a sense of the different business models that operate across the university system. Why is £9,000 a year for the undergrads inadequate when a sixth form college manages to do it for £6,000, give or take, for a far higher number of contact hours in a week, a longer academic year and larger groups of kids being educated?

Somebody watching this thing sent me a blog and quite a useful answer, but none of the people we have had through here over the last two months has given me any real reassurance that there is a set of models that operate. You will be in a good position to say, as a finance director of a big institution but also sitting in a reference group where you are talking to other finance directors. That is the first bit of it.

Linked to that, you said at the beginning of the session that we all obsess about the 40% who are undergrads and do not pay significant attention to the other 60%. I worry about the business model for postgrads, where there seems to be just the idea that you can haul in foreign students, charge them twice as much, focus on the largest country that sends them, China, and think that that is a long-term solution. Could you unpack that and give me your thoughts, please?

Erica Conway: The first was on your comparison of sixth-form colleges to universities. The most obvious thing that I would point to is the homogeneity of students who sit in sixth-form colleges as opposed to in universities. Most of the sixth-form college population will be 16 to 18 year-olds studying A-levels in set criteria. There are choices about exam bodies, but one sixth-form college will be teaching a set number of subjects to a set number of students in a particular way. They are teaching those students ostensibly to complete those exams with an endpoint position.

Universities are seen as providing so much more to their students. For 16 to 18 year-olds, there are parental care responsibilities that are starting to shift towards universities. Although a large proportion of the population are 18 to 21 year-olds, another proportion of the population are evening workers studying in their spare time. There are students from different parts of the UK and different backgrounds. There are different age groups.

The homogeneity is not there. The homogeneity in the subjects delivered is not there; if you study, say, geography at one institution, it will be different from geography at a different institution. You are not there to pass an exam but to gain a broader understanding of what it is to research, to understand data, and to conform to particular rules and skills development in relation to working for the future. I would argue that we make a slightly broader and different request of universities than we do of students, which is why the concept of universities as bigger versions of a school does not quite map.

Just in passing, because we have a sixth-form college in our specific group, I would not suggest that the sixth-form model is particularly well funded either across the UK. You could do it more cheaply, but sixth-form colleges struggle to do it for the money they have.

Lord Agnew of Oulton: How would that extend to colleges of technical education, which are operating on a much broader platform? I accept what you say about an A-level college. It has a very specific mission, so that is a very sound answer, but what about the tech colleges?

Erica Conway: Again, set criteria and curricula are being responded to there. There is breadth, but they are not trying to do everything in the way that universities are potentially asked to. There is a significant shift in what subjects students are studying at A-level. We are continuing in our sector to try to maintain the breadth as much as possible and to recognise students coming through different models. Although a student going on to study tech might study a variety of things, they are likely to have come through a very similar route to get into that position as opposed to coming from a university perspective.

Your concern about postgraduates picks up on the point that Nicola was making. The pressure on the universities to manage in a fixed-fee environment for the 40% has led us all to look for different options. Yes, the largest proportion of postgraduate students coming to the UK are from China. It is not for want of all of us trying to take students more broadly than that, but, in order to balance the books, with a declining fee and an increasing cost base we have to look to doing other things.

I would also argue that postgraduate students from overseas make a particular difference to the UK provision in their ability to mix with students from across the world. Many of them will filter into the workforce in the UK or in the academic environment, which feeds back into universities, so there is the self-populating, circuitous route to it that is quite important.

Lord Agnew of Oulton: If we are looking for business model improvements, what about a two-year course for a lot of courses that have only half a dozen contact hours a week? That would be far more efficient use of your infrastructure. You could extend the academic year. You would save the kids a third of their living and accommodation costs. Why does so little of that happen?

Erica Conway: That is partly due to student demand to be able to develop other skills. I am an arts graduate, so my contact hours were relatively low many decades ago when I went to university. The expectation was that, in the hours when I was not having contact, I was learning and developing my own skills outside that, which were then tested in that contact base. I would argue that you are developing a slightly different skills base if you are studying in an environment with fewer contact hours.

Lord Agnew of Oulton: I have one last question, and then I will let Nicola come in. You touched on interest rates in answer to an earlier question. I am worried that the university sector has been on a borrowing orgy over the last 10 years. Do you have a sense of how much of that is long-term fixed rate and how much is variable rate? To the point that you made, the whole country is having to readjust to the normalisation of interest rates. Anyone under the age of 35 has no real experience with it. Again, looking from your position and having a bird's eye view across the sector, can you give me a sense of how much of the debt is fixed and how much is variable?

Erica Conway: The vast proportion is fixed, so the issue is not an immediate one of the interest rates on those loans going up. It is about the rotation rate when they need refinancing. Most institutions are still looking out five to 10 years before they need to refinance. The concern is for anyone who has to refinance in the next couple of years.

Q104 **The Chair:** We are hearing anecdotal evidence that there are quite a number of universities in financial difficulties. We also heard from one vice-chancellor that, if he thought his university was in difficulty, he would be reluctant to go to the OfS for advice, help or information. Are we heading towards a crisis in university financing?

Erica Conway: There are definitely institutions that are struggling. As for the proportion of those across the sector, it is down to whether you would put your hand up and say to somebody that you were having difficulties. One of my roles is to have regular conversations with the banks as the sector representative. There are probably 10 or 15 institutions across the sector that would be on those banks' watchlists. What concerns them is not just the financial sustainability, but the ability to develop reasonable long-term plans that have thought-out alternative scenarios.

As a business lead, I have to say that that would be a concern to me as well if I was involved in a business that had not been through that process. The fact that the banks are raising it suggests that some institutions have that particular problem.

Nicola Owen: I would just amplify a couple of things that Erica said. It is a different system in its access to facilities and students' equipment needs. This is not Bunsen burner territory. Significant levels of investment go into student laboratories. We have the same fee for all subject areas, so there is a significant level of cross-subsidy. You touched on that in relation to the further model for postgraduate-taught and international students. That also plays into research activity, which is costed on an assumption of subsidy. There is also a structural issue in the way that cross-subsidy works. The former Financial Sustainability Strategy Group did good pieces of work on that and identified those kinds of subsidy issues, and they may be worth referring to.

This is not a static environment. A lot of us run significant estates. We have new things coming in, such as carbon net zero, which means a significant shift in the way we produce energy. You are constantly trying to adapt to and work through things in a diminishing resource, which is what is partly driving this juggling. Although I accept that there are some very big issues and risks relating to the level and number of sources of income that we can go to, and you can see how that has played out in the sector, the way in which the current business model operates is driving us in those directions.

Q105 **Lord Clement-Jones:** As the chair of a governing body, I have had some contact through the CUC with speeches from OfS dignitaries and so on, but I just wondered whether you thought the OfS had much of a relationship or an understanding of the role of governing bodies and the kinds of pressures that they are subject to.

Nicola Owen: Through my association, we try to articulate those issues to OfS, and I know the CUC does too. There has been a view somehow that governing bodies are not necessarily responding appropriately to OfS. They have become too risk averse or do not fully understand and take their accountabilities on board. There is a lot of work to do there.

We have certainly seen a significant increase in the number of things that have to be reported to governing bodies. Again, there is an opportunity cost to that in the way we draw on our members, particularly lay members. Sometimes I feel as though governing bodies have been given the responsibility, but it has not been tested whether, realistically, they can get under the bonnet sufficiently to understand and gain confidence on that. Even where you have very well-functioning relationships between a governing body and an executive management team, it is really difficult and time-consuming to get through that detail in order to make sure that, what are almost entirely volunteers in the sector, are signing their name against something that they have confidence in.

We are trying at points to test what they mean when they are asking governing bodies to do things. Some of the responses that have been played back to me suggest that governing bodies could decide to delegate responsibilities to subcommittees or to management. Again, it comes back to that dialogue and engagement.

Lord Clement-Jones: They would probably get criticised for that, I suspect.

Nicola Owen: There are things that could definitely be improved. Let us put it that way.

The Chair: Thank you very much for your evidence this morning. You have a very clear perspective of that relationship, so it was worth hearing from you both.