

Annex C: Audit Code of Practice

Overview

1. In this Audit Code of Practice (the Code) the word ‘must’ denotes a mandatory requirement under the terms and conditions of funding, whereas ‘should’ denotes our view of good practice.
2. The Code sets out what we require higher education institutions (HEIs) to have in place to provide themselves and us with adequate assurance on good governance, internal controls, the management of risk and achieving value for money (VFM). How these requirements are met is for HEIs to decide themselves.

Governing bodies of HEIs

3. The responsibilities of governing bodies are set out at paragraph 22 of the terms and conditions of OfS funding and paragraph 21 of the terms and conditions of UKRI funding relating to funds administered through Research England. Governing bodies are responsible for the appointment and removal of external and internal auditors. Governing bodies are also responsible for appointing outsourced internal audit providers, on the advice of the Audit Committee, and for choosing to move between outsourced and insourced internal audit provision, also after taking advice from the Audit Committee. Staff appointments and terminations for insourced internal audit staff are a matter for management, with the Audit Committee advising on the appointment and termination of the Head of Internal Audit.

Audit committees in HEIs

4. Each HEI must have an audit committee which follows best practice in higher education corporate governance. The audit committee is responsible for assuring the governing body about the adequacy and effectiveness of:
 - risk management, control and governance
 - VFM
 - the management and quality assurance of data.
5. The Committee of University Chairs has published detailed guidance about audit committees (‘Handbook for members of audit committees in higher education institutions’, HEFCE 2008/06²¹). This reflects best governance practice, and the Office for Students (OfS) and Research England expect HEIs to take account of such guidance in meeting the required standards or explain why the guidance is not being applied and good practice is not being followed.
6. An audit committee can undertake whatever work²² it considers necessary to fulfil its role. This should include assuring itself about the effectiveness of its internal audit function and its external auditors. Audit committees will only be able to provide the necessary assurances if they are supported by suitably resourced internal audit and external audit functions, operating

²¹ Available at

http://webarchive.nationalarchives.gov.uk/20120118181328/http://www.hefce.ac.uk/pubs/hefce/2008/08_06/.

²² As described in HEFCE 2008/06.

to recognised professional standards. They should also consider evidence-based assurances from management.

7. Members of the audit committee must not have executive authority. Audit committees should include a minimum of three lay members of the governing body. Audit committee members should not be members of an HEI's finance committee or its equivalent. This is because it would create a potential conflict of interest when the audit committee is considering issues involving the finance committee. If an HEI's governing body determines that cross-representation involving one member is essential, this should be the subject of an explicit, recorded resolution, which sets out the rationale for such a decision – but it should not be an option for the chair of either committee or the chair of the governing body.
8. The committee must produce an annual report for the governing body and the accountable officer. The report must cover the financial year and include any significant issues up to the date of signing the report and its consideration of the financial statements for the year. The report must be presented to and reviewed by the governing body before the audited financial statements are signed.
9. The report must include the committee's opinion on the adequacy and effectiveness of the HEI's arrangements for:
 - risk management, control and governance
 - economy, efficiency and effectiveness (VFM)
 - management and quality assurance of data submitted to the Higher Education Statistics Agency, the Student Loans Company, HEFCE, the OfS, Research England and other bodies.
10. The final annual report to the governing body and the accountable officer must be shared with the OfS each year, and, on request, with Research England.

Internal audit arrangements in HEIs

11. Internal audit is a vital element in good corporate governance since it provides governing bodies, audit committees and accountable officers with independent assurance about the adequacy and effectiveness of risk management, control and governance, and VFM.
12. Consequently each HEI must have a suitably resourced internal audit function which must comply with the professional standards of the Chartered Institute of Internal Auditors. Internal audit terms of reference must make clear that its scope encompasses all the HEI's activities, the whole of its risk management, control and governance, and any aspect of VFM delivery.
13. The internal audit service must produce an annual report which must relate to the financial year and include any significant issues, up to the date of preparing the report, which affect the opinions. It must be addressed to the governing body and the accountable officer and must be considered by the audit committee.
14. The report must include the internal auditor's opinions on the adequacy and effectiveness of the HEI's arrangements for:
 - risk management, control and governance
 - economy, efficiency and effectiveness (VFM).
15. The final annual report to the governing body must be shared with the OfS each year, and, on request, with Research England.

16. The head of internal audit must have direct access to the HEI's accountable officer, the chair of the audit committee and, if necessary, the chair of the governing body.
17. Where internal audit is provided from an outside source, market testing should be undertaken at least every five years.

External audit arrangements in HEIs

18. External audit must provide an opinion to the governing body on whether funds (including public funds) have been applied for the intended purposes and on whether the financial statements provide a true and fair view of the financial results for the year. External audit must also form a view about whether an HEI is a going concern. External auditors of HEIs do not have a duty of care to the OfS and Research England.
19. HEIs may ask external auditors to provide additional services. The audit committee must agree all significant matters with a bearing on the auditor's objectivity and independence. Additional work must not impair the independence of the external audit opinion.
20. HEIs must disclose separately, by way of a note to the financial statements, the fees paid to their external auditors for other services.
21. External auditors must issue a report (or reports, if more than one, covering different stages of the annual audit) to those charged with governance, which records accounting issues and control deficiencies arising from the audit. The OfS and Research England would expect any issues around the use of charitable assets for non-charitable purposes to be highlighted in such reports. The HEI's management must provide written responses to any recommendations made or issues raised. The report(s), including management response, are one of the annual accountability returns which must be submitted to the OfS.
22. The report(s), with management responses, must be made available to the HEI's audit committee in time to inform the committee's annual report.

Audit report

23. The external auditors must report whether in all material respects:
 - a. The financial statements give a true and fair view of the state of the HEI's affairs, and of its income and expenditure, gains and losses, changes in reserves and cash flows for the year. They should take into account relevant statutory and other mandatory disclosure and accounting requirements, and OfS and Research England requirements.
 - b. The financial statements have been properly prepared in accordance with the financial reporting standards (FRS102) and the 'Statement of recommended practice: Accounting for further and higher education', and relevant legislation.
 - c. Funds from whatever source administered by the HEI for specific purposes have been properly applied to those purposes and managed in accordance with relevant legislation.
 - d. Funds provided by the OfS and Research England have been applied in accordance with these terms and conditions and any other terms and conditions attached to them.
 - e. The requirements of the OfS's accounts direction have been met.
24. Auditors should have regard to the specific requirements of the terms and conditions such as compliance with those relating to increases in financial commitments thresholds, or other

issues of non-compliance, in their management letters or reports, as set out in paragraph 23 above.

25. Market testing should be undertaken at least every seven years. One named individual partner in the firm is normally responsible for the HEI's audit; they should not hold this position for more than 10 consecutive years.

OfS and Research England access to auditors

26. The OfS and Research England may wish to communicate with an HEI's external or internal auditors, particularly in connection with an assurance review (until July 2018) or an accountability and governance review (from 1 August 2018 until 31 July 2019) and should have unrestricted access to do so. This will normally be arranged through the HEI's accountable officer or representative. The OfS and Research England will exchange letters where necessary with both parties to deal with confidentiality and the terms under which access is given.

Provision of audit services

27. Internal and external audit services must not be provided by the same firm or provider.

Auditors' access to information

28. Internal and external auditors must have unrestricted access to information – including all records, assets, personnel and premises – and be authorised to obtain whatever information and explanations the head of internal audit service or the external auditor considers necessary.

Restriction on auditors' liability

29. Where the internal audit service is provided through a contractual arrangement with an external provider, the provider may ask the HEI to agree to a restriction in the internal auditors' liability arising from any default by the auditors. Normally such liability should be without limit. However, HEIs may negotiate a restriction in liability so long as the decision is made on an informed basis and the liability remains at such a level as to provide reasonable recourse for the HEI. The governing body, through the audit committee, must be specifically notified of any request for a liability restriction.
30. HEIs must not agree to any restriction in external auditors' liability in respect of the external audit of their annual financial statements.
31. For other types of work performed by the external auditors, the provider may ask the HEI to agree to a restriction in the auditors' liability arising from any default by the auditors. However, as with internal audit services, HEIs may negotiate a restriction in liability if the decision is made on an informed basis and the liability remains at such a level as to provide reasonable recourse to the HEI. The governing body, through the audit committee, should be notified of any liability restriction agreed.

Appointment, removal or resignation of internal and external auditors

32. Governing bodies are responsible for the appointment and removal of external and internal auditors. Where auditors cease to hold office for any reason, they should provide the governing body with either a statement of any circumstances connected with their removal which they consider should be brought to the governing body's attention, or a statement that there are no

such circumstances. Any such statements must also be sent to the OfS by the accountable officer.