

***Some speculative thoughts on the insolvency of a traditional 'public' English university***

**(David Palfreyman, OxCHEPS, August 2016)**

- 1. Sooner or later, as with University College Cardiff (UCC) in the late-1980s, a 'public' English university will effectively become insolvent. This happened in the case of UCC because it failed to reduce its expenditure to match the decline in UGC grants following the 1981 cuts to Government's funding of HE and at the same time grossly over-estimated income from its recruitment of fee-paying International students, as well as badly miscalculating the cost of building projects: all in all, a perfect storm of managerial incompetence and governance failure.**
- 2. In the 2020s a university's financial crisis is likely to arise because it has a failed strategy for operating in the increasingly competitive HE marketplace. Probably it will have over-borrowed to over-expand its student numbers or its infrastructure (often both) and then finds the flow of fee-paying UK students and/or higher fees International students (including what will post-BREXIT be what were once EU students) is curtailed for a variety of possible demographic, market, or geopolitical reasons. Or perhaps its assessment of its REF – and soon its TEF – ranking proves to be over-optimistic, adversely affecting its actual against its projected earnings? Or maybe it will have failed to close-out adverse currency shifts and/or interest-rate rises in its debt arrangements? Or it could have under-estimated build costs for its glitzy new infrastructure, as well as over-estimating the sale proceeds from releasing its old premises?**
- 3. The Higher Education and Research Bill 2016 will, in theory (if enacted as drafted) protect the position of students in the winding-up of an insolvent university by the institution needing to satisfy the proposed Office for Students (OfS; created under**

**Part 1 of the Bill as the replacement for HEFCE) that it has in place effective financial arrangements for ensuring students do not experience undue detriment as the entity disappears (for instance, that they can complete their courses at the university itself or be transferred to another appropriate university or be adequately compensated financially if neither of these first two options prove viable): s13 of the Bill refers to ‘a student protection plan’. But the use of such a legislative requirement will, however, be only as good as the efficiency with which the OfS can police the credibility and quality of the hundred or so HEIs conjuring up these ‘living-will’ arrangements. In doing so, the OfS will need to understand: that the cost of sustaining teaching provision to see students to degree completion will be high; that the failing university which has already reduced entry grades to lure in students will not easily be able to arrange their transfer elsewhere; and that nobody knows from any case-law what is the equation for calculating the damages/compensation where the university ceases to trade and thereby breaches the university/student contract-to-educate (for example, will the contractual norm of reliance damages apply or the potentially more costly expectation measure of damages?).**

- 4. In Farrington & Palfreyman (2012, OUP) ‘The Law of Higher Education’ we addressed the insolvency of a university only in passing (para 16.16 re an institution structured as a registered charitable company under the Companies Act; and in an online ‘Law Update’ at the OxCHEPS website to para 16.16 we noted briefly that the position was uncertain for universities with the legal status of a charitable chartered corporation as are almost all the pre-1992 non-statutory universities (and as was UCC).**
- 5. These Notes seek to offer some speculative thoughts on what might happen if such a university hits financial problems in the potentially turbulent years to come. It asks what might be the impact of charity law, of the law of corporations, of insolvency law; also of any relationship between the university and**

**HEFCE or the PAC in terms of protecting any taxpayer-funding that has gone into or is going into the financially failed or failing entity.**

- 6. Under charity law the university would need to provide a serious incident report to its regulator (HEFCE acting on behalf of the Charity Commission; the CC itself in the case of Oxbridge colleges). One might reasonably hope and indeed assume that, if the university concerned is able to identify that it is in crisis and so make such a notification to HEFCE, then its Council members as charity trustees and in order to lessen the risk of incurring personal financial liability will have fulfilled their fiduciary duty by also calling in external expertise to assess the institution's financial position and viability (especially where, as in the UCC case, key officers such as the VC or the FD may well have already departed!). But, if the university is not engaging in realistic self-help or as supplementary to its efforts, HEFCE presumably can, under its powers as the lead regulator for universities as charities, send in a team to investigate the institution's governance, management, accounts, and strategic plan – doubtless, HEFCE has its emergency plan in place.**
- 7. Independent of HEFCE's role under charity law, it probably has authority anyway in the context of its funding contract with a university to trigger such an investigation – and the Bill even proposes broad 'powers of entry and search' (with a warrant) for the OfS in relation to 'relevant higher education premises' (s56 and Schedule 5)!**
- 8. In addition, as also with the UCC experience, the Accounting Officer to the PAC in the relevant HMG department (then the DES, but now conceivably both the department for education handling taxpayer-funding to HEFCE and for student loans, and also the department for business etc overseeing the transfer of taxpayer funds for research in universities?) will be able to trigger investigation of the state of a particular university's finances if there are reasonable grounds for believing public**

**money may be at risk – again, doubtless, the relevant Government department(s) have contingency plans.**

- 9. Depending on where such internally and externally triggered investigations of the university's financial sustainability get to, under the general law of corporations (see the 'Corporations' volume in 'Halsbury's Laws of England') and under Part V (ss220-229) of the Insolvency Act 1986 (and the related Insolvency Rules of SI1986/1925) the Court may wind-up a chartered corporation using the provisions for dealing with the actual or threatened insolvency of 'unregistered companies'. The process of liquidation can be the same as for companies registered under the Companies Act (s229(1), IA86).**
- 10. Assuming a university is liquidated and its creditors dealt with (presumably only after the cost of its student protection plan has been met?), what happens to the residual assets? Perhaps it can be said some assets, as once funded from UGC/UFC/HEFCE capital grants revert to the Government aka taxpayer? Then there seems to be a potential conflict between charity law and the law of corporations in that the former would require any remaining assets to be transferred under cy-près (see Halsbury's 'Charities' volume) to other charities with similar charitable objectives (other universities?), but the latter assumes all such property of a defunct chartered corporation becomes bona vacantia and hence finds its way to the Treasury (Halsbury's 'Corporations' volume, paras 504-506). In addition, within the liquidation process overseen by the Court any assets that are permanent endowment or held on specific trusts can't be accessed by the university's creditors – many universities will have funds held on specific trusts; not many will have permanent endowment outside of the Oxbridge colleges.**
- 11. Thus, where a university signals it is in financial crisis or where an external regulator/agency has reasonable cause to suspect it is, there appears to be several routes whereby an appropriate team of experts can be sent in by collective agreement of the institution and the various agencies to which**

**it is accountable (or even several such teams where there is no agreement on one team acting for all relevant parties) – where the university itself is not facing up to its deteriorating financial circumstances there also appears to be powers under various legal mechanisms whereby externally such investigation(s) can be triggered.**

- 12. A university in crisis will still need to run itself, since there is no power for an external agent to take control as if it were a failing academy school or NHS trust as public bodies since all universities are private corporations; but, if the Court is winding it up under the Insolvency Act, then presumably a liquidator takes control as when a registered company is wound up.**
- 13. In the UCC example there was, in fact, (eventually) close co-operation among its Council, the UGC, and the DES with the work of the investigatory teams (the writer being part of one) being pooled and the three parties kept apprised of what in the end was the Council's voluntary decision to merge with an adjacent (better managed) HEI – with an injection of UGC cash to deal with UGC's substantial accumulated deficit and a recovery plan involving a very sizeable number of redundancies (aided by generous USS terms for early-retirement), thereby avoiding technical insolvency and a formal winding-up process. On the UCC case see: Warner & Palfreyman (2003), 'Managing Crisis [in universities]'; and Shattock (1994), 'The UGC and the Management of British Universities'.**
- 14. The next incident in HE may, however, not involve a conveniently located and well-managed neighbouring HEI or a manageable level of debt – and certainly USS is no longer able to afford generous gestures!**
- 15. And, anyway, Government has already stated that it will not be in the business of rescuing universities that get themselves into a financial mess – especially where the provision for a student protection plan should mean the student-customers**

**will be provided for in the liquidation process as a first call upon the institution's assets.**

- 16. Whether the liquidator will find a ready market for the sale of a defunct university's premises and whether such a university has any sellable business goodwill as its degree-awarding powers, is another matter – especially were the premises to be in a remote location or in a depressed area (as opposed, say, to a site in London); a tarnished degree-awarding 'medallion' might still have value as a speedy route into HE for a new-entrant for-profit provider, but probably only if it can be refurbished via a judicious name change!**
- 17. Given the complexity of the above and the legal uncertainty, it is appropriate (if not already done) for the Universities Minister to ensure the various potential players (HEFCE/OfS, any relevant Accounting Officer) have updated their contingency plans for when unwise levels of debt catch up with Coketown University or the University of Barseshire...**
- 18. And the levels of debt being taken on by some universities is deeply worrying as shown in their annual accounts and in their strategic plans, leading one to wonder whether their lay-dominated Councils are always acting as a proper reality check on the ambitions of the well-paid corporate managers. As with the recent banking crisis, the cost of the mess at UCC was not met by its incompetent managers nor by its non-execs but by a combination of the hapless taxpayer and by innocent employees losing their jobs. At least the convenient merger meant that UCC students were not disadvantaged - and for next time with luck the student protection plan mechanism will be in working order if the OfS does its job. One suspects, however, that, even if the Government remains resolute in ensuring the taxpayer is not on the hook, as ever the main losers from sloppy governance and management will be the failed university's employees.**

