



The Open
University

Financial Statements

for the year ended 31 July 2011



INSPIRING LEARNING

THE OPEN UNIVERSITY

REPORTS AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 JULY 2011

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THE OPEN UNIVERSITY**FINANCIAL HIGHLIGHTS**

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|---|----------------------------------|
| RESULTS, CASH FLOWS, ASSETS AND RESERVES | | |
| Funding body grants | 257.8 | 244.0 |
| Tuition fees and education contracts | 164.0 | 156.7 |
| Research grants and contracts | 15.6 | 17.0 |
| Other income | 29.2 | 29.1 |
| Endowment and investment income | 3.9 | 3.3 |
| TOTAL INCOME | 470.5 | 450.1 |
| TOTAL EXPENDITURE | 423.2 | 424.6 |
| SURPLUS FOR THE YEAR before taxation and exceptional items | 47.3 | 25.5 |
| Net cash flow from operating activities | 55.9 | 29.2 |
| Net returns on investments and servicing of finance | 4.7 | 3.3 |
| NET CASH FLOW BEFORE INVESTING ACTIVITIES AND TAX | 60.6 | 32.5 |
| Fixed assets | 172.8 | 182.4 |
| Endowment assets | 0.5 | 0.4 |
| Net current assets | 191.5 | 78.4 |
| TOTAL ASSETS LESS CURRENT LIABILITIES | 364.8 | 261.2 |
| TOTAL RESERVES | 215.2 | 166.1 |
| OTHER KEY STATISTICS | | |
| | Number | Number |
| Number of full-time equivalent students | 85,704 | 84,253 |
| Total number of students | 256,674 | 264,616 |
| Percentage of students satisfied with the quality of their course (taken from the respondents to the National Student Survey) | 93 | 93 |

THE OPEN UNIVERSITY

HIGHLIGHTS OF THE YEAR

The Open University has spent the last 42 years inspiring learning and creating higher educational opportunities with no barrier to entry. It has demonstrated excellence in research and teaching and confirmed its enormous reach through its use of open educational resources.

Key achievements in the year included:

- another excellent performance in the 2011 National Student Survey, ranked in terms of overall satisfaction
 - in the top four for the seventh year in succession in the UK
 - top in Scotland
 - top in Wales
 - top in Northern Ireland;
- the total individuals accessing the University's open educational resource website, OpenLearn, launched in October 2006, reached 17 million;
- the total downloads from The Open University iTunesU service, which is a powerful distribution system for putting all types of educational content into the hands of students, that was launched in June 2008, reached 37 million;
- following a successful bid to the Higher Education Funding Council for England, the University recruited an additional 1,500 full-time equivalent students to generate an additional one-off grant of £20.6 million, which was spent during the year in accordance with the terms of the grant;
- the total number of full-time equivalent students studying Open University credit bearing courses was 85,704, an increase of 2% from last year, following the 9% increase the previous year;
- 40% of full-time equivalent UK undergraduate students received either full or partial support for their fees, either through The Open University or from UK government sources;
- total income increased by 5% to £470.5 million, with a surplus of £47.3 million, or 10% of income before exceptional items, exceeding the target of 5% of income in the University's new financial strategy (previously 2%).

The result for this year, a surplus of 10% of total income, together with the drawing down of its £60 million loan facility, are important in placing the University in a stronger and more liquid position to weather the period of considerable economic uncertainty and the significant changes in the funding of higher education in the United Kingdom.

Constitution, Governance and Regulation

The Open University was incorporated by Royal Charter on 23 April 1969. It is registered at Companies House under number RC 000391 and its registered address is Walton Hall, Milton Keynes, MK7 6AA. Certain parts of the Charter, and the Statutes appended thereto, have been amended by the Privy Council, the last amendments being made in December 2005.

The Council of the University is, subject to the provisions of the Charter and Statutes, the executive governing body of the University and is responsible for the administration and management of the revenue and the property of the University. The University's corporate governance arrangements are described on pages 20 to 25 and the members of the University Council during the year ended 31 July 2011, who are the charity trustees, are listed on page 21.

The Higher Education Funding Council for England (HEFCE) is the principal regulator of those higher education institutions (HEIs) in England that are exempt charities, including The Open University, on behalf of the Charity Commission. As a charity registered in Scotland, the University is registered with the Office of the Scottish Charity Regulator under number SC038302.

The University is regulated principally by HEFCE under a Financial Memorandum, which defines the conditions under which the University receives public funds. The University complies with this Financial Memorandum and with the conditions of grant set out in funding agreements with the relevant grantor.

The University's principal advisors are listed on page 59.

Mission

The Open University has a distinctive place in UK higher education. It promotes educational opportunity and social justice by providing high-quality university education to all who wish to realise their ambitions and fulfil their potential, whatever their previous academic attainments. Through academic research, pedagogic innovation and collaborative partnership it seeks to be a world leader in the design, content and delivery of supported open and distance learning.

The Open University is:

- *open as to people* – making university study available to an increasingly large and diverse body of students and providing learning opportunities that meet individuals' lifelong needs;
- *open as to places* – providing learning opportunities in the home, workplace and community throughout the United Kingdom and selectively elsewhere, and serving an increasingly mobile population;
- *open as to methods* – using and developing the most effective media and technologies for learning, teaching and assessment, whilst attaching central importance to the personal academic support given to students, and working collaboratively with others to extend and enrich lifelong learning;
- *open as to ideas* – developing a vibrant academic community that reflects and supports the diversity of intellectual interests of all students and staff and that is dedicated to the advancement and sharing of knowledge through research and scholarship.

Distinctive Capabilities

The Open University has built up a set of distinctive capabilities as it has established itself as the dominant provider of supported open and distance learning in the United Kingdom and a leading player in the international arena. An examination of the University's business model has identified a set of operational strengths which can underpin its response to the challenges that lie ahead.

The Open University is a vibrant academic community that combines excellence in teaching, research and logistics to provide a unique brand of supported open and distance learning to a large and diverse body of students. It is able to deploy the following distinctive capabilities:

- a team approach to developing and producing materials;
- an expertise in supported open and distance learning, providing students with high quality learning materials, first class academic and personal support and excellent service and organisation;
- an ability to manage and support at scale a diverse range of students admitted through open entry;
- an ability to run a high-volume, distributed business and exploit opportunities of scale;
- an ability to undertake national partnerships with major public and private sector employers;
- use of leading edge technology.

The Open University has no formal entrance requirements for admission to its undergraduate degree and diploma programmes. As students are not studying at a conventional university campus but are reliant on the resources available, or delivered to them, at home, workplace or their community, The Open University faces unique challenges in retaining students in study and helping them to progress to further courses. It owes its success in this regard, as exemplified in its very high rankings for overall student satisfaction, to its Supported Open Learning methodology.

Strategic Objectives and Priorities

The University has agreed a broad strategic intent to adapt and strengthen the University to sustain its mission, which will be realised in three phases and the main effort will shift over time. These three phases are:

- to improve effectiveness, reduce cost and strengthen competitiveness;
- to identify and exploit new opportunities in existing markets; and,
- to identify and enter new markets to grow income.

The individual focus areas within these phases are supported by a common core of academic, administrative and operational units undertaking and supporting teaching, research and knowledge transfer, though service and product offerings may be created outside as well as within the University.

At the heart of this structure is a University-wide productivity programme designed to continuously improve operational efficiency – through changes to structures, to staff roles and to processes, and through the move toward e-business functions. This programme is an essential element of the University's preparations to deal with known reductions in public funding over the short- to medium-term. As part of this planning a range of possible funding scenarios continue to be modelled so that the University can be as well prepared as possible.

The Open University's strategic direction is described in more detail in its strategic plan, *OU Futures*, which is available on its website, and is reviewed annually.

Public Benefit

The charitable aims of The Open University are set out in its Royal Charter: "...the advancement and dissemination of learning and knowledge by teaching and research by a diversity of means such as broadcasting and technological devices appropriate to higher education, by correspondence tuition, residential courses and seminars and in other relevant ways, and to provide education of University and professional standards for its students and to promote the educational well-being of the community generally". This falls within the Charities Act 2006 charitable purpose of the advancement of education and the University's Council has taken into account the Charity Commission's guidance on the reporting of public benefit. The charitable aims are expanded in the mission statement on page 4.

The University operates throughout the United Kingdom and in over 100 countries globally. The main beneficiaries are its undergraduate and postgraduate students and the recipients of its research, much of which is freely available to the general public. The benefits can be summarised in two strands:

- The results of the vast majority of the research carried out by the University are published in the public domain and are available through Open Research Online – the University's Open Access repository of research publications and other research outputs, freely accessible by members of the public. In 2010/11 over 700 research outputs were published.
- The University registered 256,674 students in 2010/11, and ranks highly in student satisfaction. A significant amount of learning material is made freely available through the internet using websites such as 'iTunesU', 'YouTube', and the University's 'OpenLearn' resource.

The University is a fee charging charity. However, unlike other universities all students study part-time and the tuition fees are not subject to statutory regulation. The typical tuition fees for a student to complete an undergraduate degree at the University would be approximately £4,200 at 2010/11 fee rates, whereas the maximum regulated fees for students attending university full-time in England are £9,870. In addition, 29,813 full-time equivalent students studying with the University (40% of the total in the UK) benefitted from either full or partial financial support in 2010/11, as indicated in the following table:

Number and proportion of full-time equivalent UK undergraduate students at course start receiving financial support for tuition fees

| | Full financial support | | Partial financial support | | Students paying their own fees | | Sponsorship | | Total |
|------------------|---|------------|---------------------------|------------|--------------------------------|------------|--------------|------------|---------------|
| | Number | Proportion | Number | Proportion | Number | Proportion | Number | Proportion | |
| England | 20,534 | 33% | 3,425 | 5% | 34,300 | 55% | 4,413 | 7% | 62,672 |
| Scotland | 2,548 | 40% | 818 | 12% | 2,548 | 40% | 481 | 8% | 6,395 |
| Wales | 1,373 | 43% | 217 | 7% | 1,339 | 41% | 268 | 9% | 3,197 |
| Northern Ireland | 767 | 44% | 131 | 7% | 793 | 45% | 63 | 4% | 1,754 |
| Total UK | 25,222 | 34% | 4,591 | 6% | 38,980 | 53% | 5,225 | 7% | 74,018 |
| Full support - | Full cost of fees covered by financial support assessed on household income | | | | | | | | |
| Part support - | Part of fees covered by financial support assessed on household income (individual income for Individual Learning Accounts in Scotland) | | | | | | | | |
| Student paying - | Student pays the course fees with no direct financial support or sponsorship | | | | | | | | |

The University spent £3.3 million providing financial assistance to students in addition to the £10.9 million of funding bodies' access funds and bursaries disbursed to eligible students; these sources of assistance are included in the table above. In addition, unlike other universities, students study from home and often whilst in full-time employment, thereby diminishing their financial burden.

The University's wholly owned subsidiary, Open University Student Budget Accounts Limited, provides students with a deferred payment facility at a lower than market rate of interest. Around 22% of all students, or 34% of those paying their own fees, take advantage of this facility. Furthermore, it is known that some students paying their own fees subsequently have them reimbursed in whole or in part by their employers, but the precise number is not known.

Student Satisfaction

The Open University is committed to creating a curriculum that is fully attuned to student needs and aspirations, that reaches out to new groups of potential learners who seek career and personal advancement and that enables them to achieve success. It strives to provide the best possible learning experience for students, and so it is particularly pleasing that the first seven National Student Surveys ranked The Open University in the top four in respect of the overall satisfaction of its students. In 2011 The Open University was ranked second of those institutions having more than 200 responses, top in Scotland, top in Wales and top in Northern Ireland.

In the 2011 survey over 10,000 Open University students took part and 93% said they were satisfied overall. This year 335 institutions were surveyed, including further education colleges that offer higher education courses. The Open University has been at the forefront of the rankings since they were introduced in 2005: it is both gratifying that it maintains such a commanding position and a source of pride to achieve consistently outstanding results when operating at such a large scale.

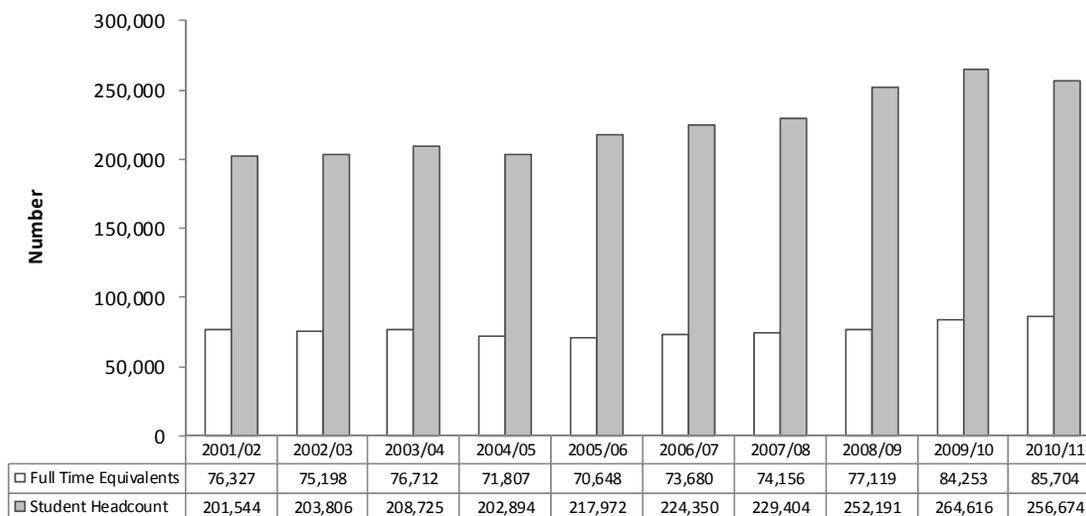
Institutional Audit

The 2009 Institutional Audit by the Quality Assurance Agency for Higher Education expressed confidence in the University’s management of the academic standards of its awards and of the learning opportunities available to students. The audit report identified a number of significant areas of good practice and made some useful recommendations for further improvements which the University has been pursuing.

Student Numbers

The key statistics on page 2 show that over the year student numbers fell by 7,942 or 3% to 256,674 and full-time equivalents grew by 1,451 or 2% to 85,704. Over the ten years since 2001, the increase in full-time equivalents was 9,377 or 12% and in individual students 55,130 or 27%. The faster growth in individual students over this decade reflects an increase in the proportion of students choosing to study shorter modules, although this trend has reversed slightly in the past year, coupled with a significant increase in the number of students validated by the University.

Full Time Equivalent (FTE) Students and Student Headcount



Financial Year

In terms of full-time equivalents, 35% of all part-time undergraduates in UK higher education institutions study with The Open University.

Research Outputs

The success of The Open University's research in the 2008 Research Assessment Exercise (RAE) was expressed through an increase of £3.4 million in the Higher Education Funding Council for England's (HEFCE) grant allocated on research criteria. However a consequence of the comprehensive spending review (CSR) was that HEFCE refocused the allocation of research funding to further enhance support to research excellence and in 2010/11 commenced the two year phasing of changes that would see withdrawal of funding from 3* rated research and the reallocation of that funding to 4* and 5* research across the sector. As a result of the refocusing the University's research grant decreased by £0.3 million from £10.8 million to £10.5 million.

Income from external research grants has decreased from £17.0 million to £15.6 million, a reflection of a tougher and uncertain external environment and the major changes now being implemented by research funders that are effecting both the current but also the future research portfolio of the University.

There has been a continued improvement in the number of directly registered research students of 7% and the proportion of new post graduate research students with some measure of external funding support to 43%. Significant improvements in post graduate research completion and award rates have also ensured that the University meets and, indeed, exceeds the HEFCE benchmarks.

Major changes in the external funding environment as various bodies adapt their policies and funding priorities to allow for mitigation of, and adaptation to, the challenges of the changing economic climate, continue to affect the University. These have included deferred announcement dates, in-project adjustments to the agreed funding for approved projects and the introduction of new criteria which define entry requirements for access to funding using evolving arguments of critical mass and quality thresholds. The University has also experienced some measure of reduced support from other procurers and supporters of research, for example business, industry and the third sector, and there is clear evidence of more significant cuts in private sector research and development budgets in the next financial year. There remains a cause for concern given the current depth and breadth of the University's research portfolio and the increasingly hostile external funding arena.

Risk and Risk Management

The Open University is committed to the management of risk in order to achieve its strategic and operational objectives. It has identified four principal risks that may affect its ability to deliver its strategic priorities. In order to mitigate these risks, the University has established a risk management process which ensures that risks are managed to an acceptable level. Each of the risks identified below has been assessed using this process and a programme of mitigating action identified to ensure that the likelihood and impact of any of them crystallising is minimised.

Significant decline in core UK market income may be caused by: failure to develop an appropriate strategic response to the new HE environment; withdrawn public funding not replaced with additional fee income; increased competition from other providers; failure to maintain innovation; and, narrowing focus of funding of research.

Failure to accurately forecast, report and achieve student number targets may be caused by: changes in student behaviour and demand; enquirers' experience does not meet expectations; complexity of funding methodologies and reporting requirements; failure to retain students and recruit from target groups; and, limits on access to student finance.

Failure to improve cost effectiveness may be caused by: failure to bring staff numbers and other costs in line with reduced public funding; lack of engagement of staff in reviewing operations and processes; failure to adopt new technologies; and, more demanding enquirers and students.

Staff not engaged with strategic objectives may be caused by: ineffective communication of strategic intent; lack of accountability; inability to identify skills needs and gaps; and, low staff turnover.

These risks, their potential impact and a description of the actions being taken to mitigate each of them are described in the University's strategic plan, *OU Futures*, which is available on its web site.

Treasury Management

The financing and liquidity of the Group and its exposure to financial risk are managed through the central treasury function of the Finance Division. The Group's formal financial strategy, discussed on page 11, sets minimum liquidity levels in order to ensure that sufficient financial flexibility is retained. Each year, as part of its normal planning processes, rolling five year financial forecasts are prepared: this process incorporates a review of capital expenditure and cash generation and so should enable any necessary future borrowing requirements to be negotiated well in advance of need.

The Group's foreign currency earnings form a very small proportion of total income and hence the overall exposure to exchange rate risk is small. Even when indirect foreign currency earnings, i.e. amounts invoiced in sterling to customers based outside the UK, are taken into account, the exposure to exchange rate risk remains small. It is therefore not appropriate to adopt particular strategies to reduce this risk, although this policy is kept under review.

The Group is potentially vulnerable to changing interest rates on its cash balances, which are held in the form of interest bearing deposits with financial institutions, in two money market liquidity funds and in UK fixed interest government bonds ("gilts") having a maturity within five years of the acquisition date. The cornerstone of the Group's treasury policy in very uncertain times remains the minimisation of risk: it limits and monitors the level of funds that may be placed in fixed rate deposits, money market funds or invested in UK gilts. Policies, incorporating clearly defined controls and reporting requirements, are in place to monitor credit and market risk, ensure sufficient liquidity, as well as to maintain the operating financial flexibility of the Group. Interest income is, however, a small proportion of total income and so, overall, the Group has low vulnerability to changing interest rates.

The University's Finance Committee keeps the Group's treasury policy under close review and has amended the policy as the instability in the financial markets has continued over the year and, indeed, increased over recent months. All deposits are currently placed for up to one year with a small number of the largest UK banks and building societies, in money market liquidity funds or invested in UK gilt-edged stocks of short maturities. Such has been the 'flight to quality' over the past two years, it is proving difficult to place deposits with the strongest financial institutions on acceptable terms. This accounts for the increased purchases of gilts and the introduction of money market liquidity funds, which has the advantage of further reducing credit risk although at the cost for the gilt holdings of a small increase in interest rate risk.

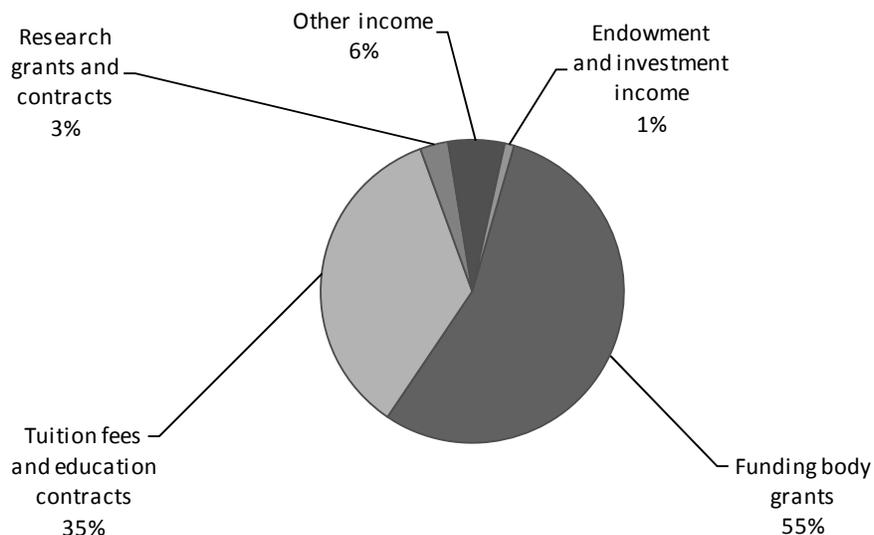
The counterparty profile of the University's deposits as at 31 July 2011 is set out in Note 16 and has not changed significantly since then.

The 2010 Operating and Financial Review reported on the position relating to amounts due from two UK subsidiaries of Icelandic banks. The total amount at risk relates to two two-year fixed term deposits, one of £5.0 million placed in October 2006 and the other of £1.5 million placed in March 2007, together with accrued interest of £0.4 million, less distributions received from the banks' administrators totalling £4.1 million. A provision of £1.4 million (31 July 2010, £1.7 million) has been made against these sums in these financial statements, representing our estimated recovery of 80% (31 July 2010, 80%) of the former deposit and 80% (31 July 2010, 65%) of the latter. The estimated recoveries are those published by the administrators based on their experience over the administration. As at 31 July 2011 60% of the former deposit and 58% of the latter had been returned to creditors by the administrators and further receipts are expected before the end of 2011.

The University drew down the £60 million loan facility from the Royal Bank of Scotland on 27 April 2011, as part of its strategy to ensure financial flexibility to meet the potential changes in the timing of how the University receives its teaching related income when the new funding arrangements for universities and students are implemented, which is discussed further on page 17. The potential impact of these changes and the likelihood of the UK higher education market taking several years to reach a new equilibrium, means that currently it would be unwise to invest with a time horizon exceeding one year or without the highest level of capital security available. Furthermore, the premium for taking more risk would not result in any significant contribution in the context of the University's total income.

Funding

UK universities derive their income from five categories of income, of which, because of the nature and scale of The Open University's teaching activities, two dominate, as illustrated by the following chart:



The Open University is unique amongst UK universities in operating across the whole of the UK and so is funded for its teaching activities by all the national higher education funding bodies. In respect of its research activities, it is funded by HEFCE and not by any of the other national funding bodies.

UK universities receive income from other sources in respect of their primary teaching and research activities: from tuition fees and education contracts for teaching and from project related research grants and contracts for research.

Grants from the national higher education funding bodies can be used to support the teaching of students anywhere in the world, although only EU students resident in the UK are eligible for inclusion in their funding formulae and resultant allocations. Whilst each funding body calculates the funding it allocates in different ways, the underlying principle, as it applies to The Open University, is the same: funding is provided at a set amount for each student who completes a specified unit of learning up to a total number of funded students for a given academic year. The value of the teaching grant per student is currently considerably higher than the fees charged to students. It follows that UK universities have little incentive to grow UK student numbers unless they can negotiate with the relevant funding body an increase in the student numbers that it is willing or able to fund, which in turn is dependent upon public expenditure limits and government policy. As universities will suffer claw back of teaching grant if the specified number of students fail to complete (subject to certain tolerances), they have every incentive to ensure that student completions do not fall below target.

Another feature of the UK funding regimes for teaching is that the national funding bodies agree the number of students for each university as a whole, except for some subject groupings that are dealt with separately.

Thus, whilst universities will set their own targets for recruitment of students by subject area and by level of study, their income from the national funding bodies is determined by the aggregate student numbers completing their specified studies in the year. Again, because the level of grant funding relating to UK students is significantly in excess of the fees charged to UK students, it follows that student numbers are managed at university level in order to maximise funding. The Open University is better placed than traditional universities in managing the operational implications of this feature of funding because it is not constrained by physical accommodation when recruiting students in particular disciplines.

Fees chargeable by UK universities to UK full-time students are regulated by government and are either waived or deferred on advantageous credit terms. Fees for UK part-time students are currently not regulated but neither are they eligible for waiver or deferral on advantageous terms; for this reason The Open University has put in place its own fee deferral arrangements at a subsidised rate of interest. Other UK universities are able to charge very high fees to overseas students choosing to study in the UK, whereas The Open University provides its teaching to overseas students in the countries in which they are resident, either directly or in partnership with a range of educational and commercial organisations, at fee levels that are acceptable in each market.

The Open University's other sources of funding are the same as other UK universities: research grants and contracts arising from competitive bids for funding from a range of public and private funders; other operating income from a wide variety of sources, including grants from European Union and charitable bodies; and, endowment and investment income.

The way in which universities in England and Wales are funded is to change significantly: these changes, which will be introduced in England from August 2012, are discussed in the section on future developments starting on page 17.

Financial Strategy

The University's financial strategy is designed to maintain financial flexibility at all times. The University's Finance Committee reviewed the financial strategy during the course of the year and the University's Council accepted the recommendation that it should be strengthened as part of the University's overall risk management process. This was due to the inherent variability in cash flows that will arise in the UK market environment when the funding regime changes from October 2012.

The University's financial strategy is expressed through three parameters:

- to maintain net current assets at a minimum of 90 days' expenditure (previously 30 days), with a medium-term target of 180 days expenditure;
- to at least balance normal recurring income with normal recurring expenditure, taking one year with another, over the medium-term and to aim for a surplus of 5% of income (previously 2%);
- to restrict the maximum level of borrowings to the value of £62 million (previously total fixed assets less deferred capital grants).

For the purposes of the parameter relating to net current assets, committed bank facilities are treated as being equivalent to net current assets.

These parameters are considered in the development and implementation of the Group's treasury policy, its normal planning, budgeting and medium-term forecasting cycle, and in the planning and execution of its capital building programme.

Long-Term Borrowing Facility

The University has a committed long-term borrowing facility with Royal Bank of Scotland of £60.0 million for a period of 25 years from October 2008. The loan was fully drawn down on 27 April 2011 and is secured on a part of the University's Walton Hall campus.

Royal Bank of Scotland also provided a loan of £3.0 million to one of the University's subsidiaries, which is being repaid over 20 years.

Creditor Payment Policy

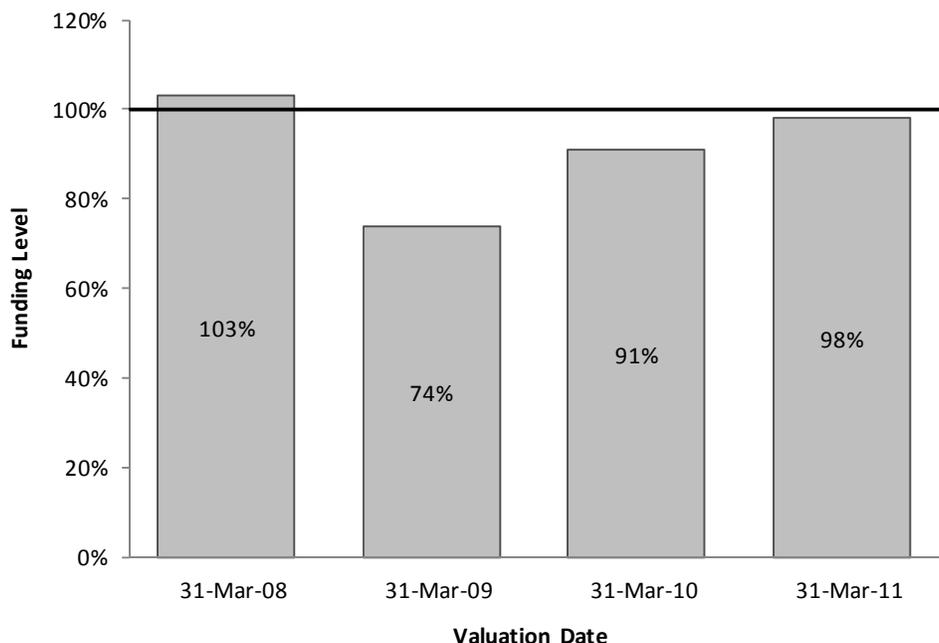
It is The Open University Group's policy to abide by terms of payment agreed with suppliers. Unless special terms apply, payment is made within 30 days of receipt of a valid invoice or after acceptance of the goods or services, whichever is the later.

Pensions

The University has only one defined benefit pension scheme available to its UK based staff, the national Universities Superannuation Scheme (USS). USS is completely independent of the University, which has no control over its policies or decisions.

The disclosures in Note 30 on pages 56 to 58 in respect of USS refer to the latest actuarial valuation, as at 31 March 2008. The funding level under the scheme-specific funding regime introduced by the Pensions Act was 103%. This was the first valuation to adopt this requirement. Since 31 March 2008 the funding level on this basis has fluctuated significantly as shown in the following graph.

Funding Level of USS: Scheme Specific Basis



On the basis set out in Financial Reporting Standard 17, *Retirement Benefits*, the funding level has declined from approximately 104% at 31 March 2008 to 86% at 31 March 2009 and then to 80% at 31 March 2010, before rising to 86% at 31 March 2011. The next full actuarial valuation, as at 31 March 2011, will not be published until early 2012.

At its meeting on the 9 June 2011 the trustee board considered an amending deed to the rules of USS containing the proposed changes in their final form as decided upon by the Joint Negotiating Committee at its meeting on 10 May 2011. The main changes are: for active members as at 1 October 2011, the normal pension age for future service will be 65 and in the future will be linked to state pension age; the member contribution rate will increase to 7.5%; and, there will be a cap on pension increases for service after the implementation date. In addition, there will be a new section of USS for new entrants who join after 1 October 2011 in which the employee contribution rate will be 6.5% and the benefits will be accumulated annually rather than based on the final salary. For both sections of the USS any future increases in required contributions will be shared by employers and employees at an agreed ratio, and a flexible retirement scheme will be introduced for contributing members aged 55 or over. The full list of changes can be found on the USS website: <http://www.uss.co.uk/>.

The USS trustee board confirmed the final form of the deed, which will be effective from 1 October 2011.

Diversity and Employment of Disabled Persons

The Open University is committed to diversifying and developing its staff base. Employee recruitment and grading processes, together with programmes for employee involvement, communication and training are all designed to promote equal opportunity to all irrespective of age, sex, race, religion, colour or sexual orientation.

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. If existing employees become disabled, every effort is made to continue their employment with the University and arrange appropriate training. It is the University's policy that the training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.

Employee Involvement and Training

The Open University places considerable value on the involvement of its employees and on good communication with them. Staff are informed through regular meetings, the extensive University intranet, open fora, staff newsletters, and other means. Staff are encouraged to participate in formal and informal consultation at University and Unit level, through membership of formal committees and informal working groups. The University provides technical and general training to all levels of staff and helps to build leadership capacity.

Accounting Policies

The Group financial statements have been prepared in accordance with the Statement of Principal Accounting Policies set out on pages 30 to 33, which are in accordance with applicable United Kingdom Accounting Standards. In accordance with Financial Reporting Standard 18, *Accounting Policies*, the University's Finance Committee has reviewed the Group's accounting policies and considers them to be the most appropriate to the Group's operations.

Although International Financial Reporting Standards (IFRS) apply to listed companies and public sector bodies in the UK, they do not currently apply to not-for-profit public benefit entities. It is anticipated that IFRS will be introduced for public benefit entities in 2014; at that point the University's accounting policies will be revised accordingly.

Scope of the Financial Statements

The financial statements comprise the consolidated results of the University and its trading subsidiary undertakings, together the 'Group'. The most significant of these subsidiaries are Open University Student Budget Accounts Limited (OUSBA) and Open University Worldwide Limited (OUW). The subsidiaries donate the bulk of their taxable profits to the University.

OUSBA provides credit facilities to students to enable them to pay fees due to the University. OUW undertakes activities that, for legal and commercial reasons, are most appropriately channelled through a limited liability company: these relate mainly to the commercial exploitation of the University's course materials and its rights therein throughout the world.

Results for the Year

The Group's results are summarised in the Financial Highlights on page 2.

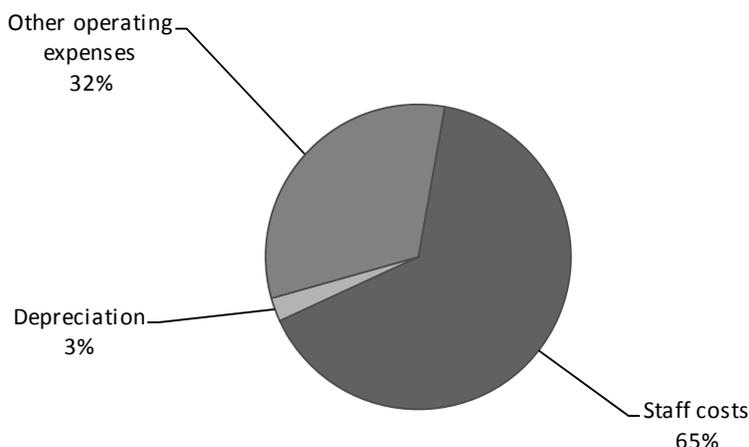
Total income increased by £20.4 million or 5% to £470.5 million.

Funding body grants increased by £13.8 million or 6% to £257.8 million. The recurrent grant from the Higher Education Funding Council for England (HEFCE) was £189.5 million and represented 86% of all recurrent grants from the various funding bodies. It decreased by £1.7 million or 1% from the total of £191.2 million in 2009/10. Recurrent grants from other funding bodies increased by £0.6 million from the total in 2009/10 to £30.9 million. Specific grants increased by £15.1 million to £31.9 million. This increase comprised a one-off grant from HEFCE of £20.6 million, partially offset by decreases in specific grants from all funding bodies totalling £5.5 million.

Fee income increased by £7.3 million or 5% to £164.0 million. The bulk of the increase was in respect of fees paid by students, or on their behalf by their employers, in the United Kingdom, which increased by £7.8 million to £141.6 million. The overall increase results from a combination of general fee inflation and the increase in full-time equivalent students referred to on page 7.

Income from research grants and contracts decreased by £1.4 million or 8% to £15.6 million, due to decreased value of work funded from Research Councils and other sources. Other income increased by £0.1 million to £29.2 million. Endowment and investment income increased by £0.6 million or 18% to £3.9 million as a result of increased balances invested.

Expenditure decreased by £1.4 million or less than 1% to £423.2 million and its distribution is set out in the following graph.



Total staff costs increased by £1.4 million or 1% to £276.6 million. £2.7 million of this increase resulted from nationally negotiated pay awards and progression of staff up incremental pay scales, offset by a £6.3 million saving from reductions in the number of full-time equivalent staff. A further £1.9 million of the increase is as a result of early retirement and severance payments. The balance of £3.1 million arose from an increase and change in mix in full-time and part-time staff.

Other (non-pay) operating expenses, excluding depreciation and interest, decreased by £1.5 million or 1% to £136.1 million.

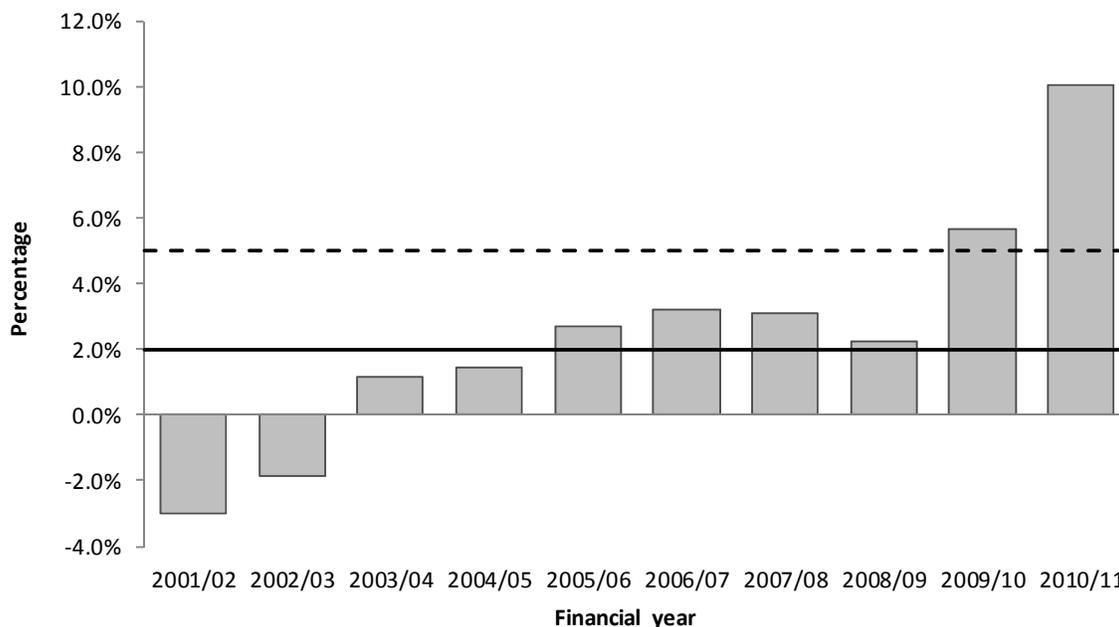
The net result was a surplus before tax and exceptional items for the year of £47.3 million compared to £25.5 million last year. In addition, exceptional items, comprising £0.7 million relating to a refund of VAT from Her Majesty's Revenue and Customs and £1.1 million relating to the sale of an office building, increased the surplus after the exceptional items to £49.1 million (year ended 31 July 2010, £26.1 million).

OPERATING AND FINANCIAL REVIEW (continued)

The 2010/11 surplus as a percentage of income was 10%. This highly creditable result was due to a combination of factors affecting both income and expenditure. The major improvement in income arose from the receipt of the University Modernisation Fund from HEFCE. In addition, cost increases were held at a much lower rate than the increase in income, due to a programme to reduce costs over an extended period to meet cuts in teaching grant as a result of the previous Government's decision to end funding for students in England studying for 'equivalent or lower qualifications' to those they already hold and the coalition Government's stated intention to reduce the public expenditure deficit.

The early commencement of expenditure reductions allows costs to be cut in a measured way so as to ensure that the quality of service to students is maintained, and has the beneficial effect of increasing the University's reserves at a time of such great uncertainty, and which will allow time to deal with any unexpected revenue reductions. The history of the University's financial performance over the past decade compared to the historic target of 2%, and the new target of 5%, set in its financial strategy is summarised in the following graph.

Surplus as a Percentage of Income



Cash Flow

The Financial Highlights on page 2 show that the Group generated a net cash inflow of £55.9 million from operating activities, an increase of £26.7 million compared to the previous year. Overall, the cash inflow before management of liquid resources shown on page 37 was £62.8 million, compared to £33.6 million last year.

Capital Projects

During the year additions to land and buildings totalled £3.7 million, and £2.7 million in new deferred capital grants were received.

The additions comprised completion of work on one new building to house science laboratories along with office accommodation, and the purchase of a small warehouse in Milton Keynes.

Balance Sheet

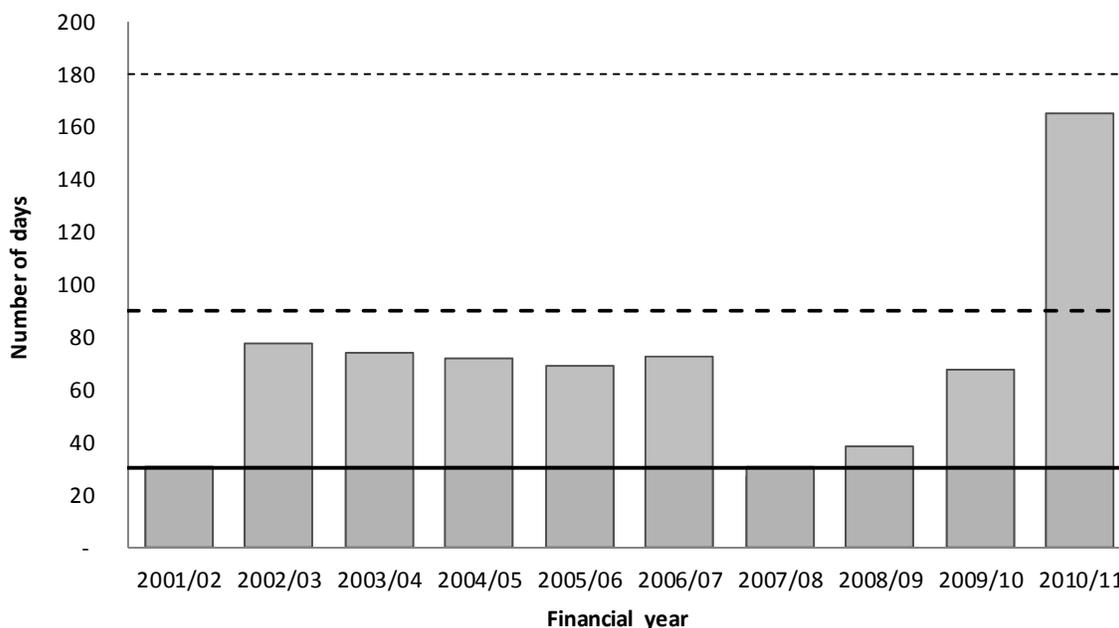
Tangible assets totalled £172.8 million at 31 July 2011, a decrease of £9.6 million since 31 July 2010 that reflects the end of a lengthy period of capital investment, with the result that depreciation is now exceeding the value of additions. The Estates Committee keeps the quality and operational capacity of the University’s buildings under review.

At 31 July 2011, net current assets were £191.5 million, an increase of £113.1 million or 144% from the previous year’s figure of £78.4 million. The 2011 figure represented 165 days of expenditure. This includes the draw down of a committed loan facility of £60.0 million on 27 April 2011, in itself equivalent to 52 days of expenditure.

On 16 October 2008 the University repaid the entire amount of £60.0 million borrowed under a previous facility, leaving in place the current underlying committed facility, in order to reduce its exposure to counterparty default in respect of its deposits. As a result of this decision, the amount repaid was reclassified from long-term liabilities to current liabilities as at 31 July 2008. This reduced reported net current assets at 31 July 2008 to 27 days’ worth of expenditure, as shown in the chart below, a little below the level of 30 days specified in the financial strategy. This had improved to 68 days by 31 July 2010. The committed facility of £60.0 million was subsequently drawn down on 27 April 2011 for the reasons given in the Treasury Management section on page 9. The aggregate of net current assets is 165 days’ worth of expenditure at 31 July 2011 (31 July 2010, 68 days).

The history of the University’s financial performance against its target to maintain net current assets at a minimum of 90 days’ expenditure (previously 30 days), with a medium-term target of 180 days expenditure, is summarised in the following graph.

Days Expenditure Represented By Net Current Assets



The University’s tuition fees are payable in advance of modules starting. This results in the University holding cash at the balance sheet date due to modules partially complete at 31 July and in respect of modules starting in the following financial year.

Future Developments

Funding of Teaching

HEFCE provided an additional allocation in 2010/11 of £20.6 million through its University Modernisation Fund. This was earmarked by HEFCE for a combination of funding of 1,500 additional students in 2010/11 along with investment to generate savings in future years that can be used to fund two further years of study for the additional students. As a result, HEFCE grants for 2011/12 will reduce in cash terms compared to 2010/11.

The funding environment for the teaching of higher education students in the UK is changing dramatically and the arrangements in each of the UK nations are diverging significantly. In England, the balance between grant funding paid to universities and colleges and fees charged to students is changing in 2012/13 from being biased largely towards the former to almost wholly the latter. As is the case now, many full-time students will be eligible for a loan from the Student Loans Company to meet the whole cost of their fees; for the first time access to fee loans is being extended to part-time students. In Wales, there will also be a shift from grant funding to funding almost wholly on the basis of student fees from either 2012 or 2013, although the students will be funded by a mixture of grants and repayable loans. In Scotland, higher education will remain free for full-time students; the cost of teaching part-time students will be met through a combination of fees, payable either by students or their employers to the extent that fees cannot be funded by grants to individuals, and, largely, the direct teaching grant funded for part-time students to universities. Finally, in Northern Ireland whilst the level of full-time student fees has been set at the current level plus inflation, there is currently no provision for loans for part-time students: primary legislation would be required for this and it is unlikely that loans would be available before 2013/14. In addition, HEFCE is discussing the transfer of funding for The Open University's students in Northern Ireland to the Department of Employment and Learning, which would complete the devolution process for The Open University.

These changes represent the biggest transformation in the funding of higher education in the history of The Open University, and arguably in the sector since the formation of the University Grants Committee in 1919.

In the first half of 2011 the University undertook a major project to develop a new UK market strategy. A general population segmentation was constructed to give a numerical understanding of attitudes, preferences and self-reported behaviours in order to group and understand segments of the higher education market. An analysis of the competitive environment was produced, enabling analysis of the competitive pressure in each segment. Research was undertaken using a trade-off approach to understand perceptions of pricing and value. A micro-segmentation of current Open University students was undertaken to give a deeper understanding of their motivation for study. The University's student database was analysed to validate and refine the market research, understand segment specific growth and inform completion and progression rate assumptions. Finally, an economic viability tool was developed to undertake financial modelling of different scenarios.

As a result of this work the Council has committed to the approach outlined below.

The Open University will focus its efforts to:

- Retain its positioning as the high quality pan-UK provider of part-time, flexible study for adults.
- Maintain its commitment to those from disadvantaged backgrounds: the aim is to ensure that these groups are as represented in the future Open University student population as they are today. This will be achieved, in part, through the roll out of a Widening Access and Success Programme that will provide low risk entry routes to HE.
- Continue to welcome all types of students. The University will focus attention on groups which it is particularly well-placed to serve. These are in the traditional heartlands for The Open University:
 - adults, both employed and unemployed, without an undergraduate degree looking for a qualification;
 - adults, generally older, looking to enhance their knowledge by studying modules;
 - employed graduates looking to study at postgraduate level.
- Retain an open access policy whilst supporting students on pathways which maximise their chances of success.

Future Developments (continued)

The Open University will succeed by:

- Orientating its marketing activities and messaging around the needs and preferences of these priority segments. As part of this it will be critical that the University:
 - clearly expresses to students the distinctive value of The Open University, the study options available and the price;
 - communicates effectively the funding options available to potential students to minimise the upfront cost for them and maximise affordability.

- Designing its offer around the needs and preferences of these priority segments. This will not require a radical overhaul of the University's curriculum content in the short term, but it will include:
 - providing much clearer and easier routes to qualifications for the majority of students (this will build on, but accelerate, the work already underway) and improving the support to students to stay with the University to complete qualifications;
 - ensuring Open University qualifications help students meet their career aims;
 - continuously improving the quality of the student experience and enhancing the University's reputation for quality for potential students.

In England The Open University will:

- Simplify pricing for the student by establishing a standard rate for all undergraduate courses and a pro rata price per credit.

- Price its undergraduate courses at £5,000 per annum per full-time equivalent for 2012/13.

- Put in place transitional arrangements for existing students in England.

Undergraduate pricing for the other UK nations and non-UK territories and postgraduate pricing for all areas will be determined in November 2011 and published by early 2012.

The changes to higher education funding have to be viewed through the prism of the global economic conditions. The recession that began in 2008 seemed to have ended in early 2011 but economic recovery world-wide has been faltering since June 2011, compounded by the very serious concerns surrounding government indebtedness in Europe and the United States of America and the resultant falls in the value of various asset classes since August 2011. In the UK, unemployment has not significantly increased, although the full impact of public spending cuts and losses to public sector jobs has yet to be felt. A study undertaken by London Economics found no correlation between economic conditions and demand for higher education; however, there is a risk that there may be a weakening of demand due to reduced ability and willingness of individuals to pay fees or employers being less inclined to sponsor students.

There is, though, potential for universities, and especially for The Open University, to provide an attractive solution for those who need to retrain for new careers or to protect current jobs. Part-time study whilst in work may be particularly attractive in the face of the increased tuition fees that all English universities will have to levy from 2012. Not only does The Open University offer the ability to study whilst in full time employment, but its announced fee of £5,000 per full time equivalent for 2012 compares favourably with other universities, many of which will be charging the maximum £9,000.

The Open University has considerable strengths to help it weather the changes in Government policy and the bleak economic climate and to help it take advantage of the opportunities that will be presented in this new environment. It is the leader in the UK part-time higher education market, with a growing market share, and is the only university that can operate at scale throughout the UK, thus having the capability of fulfilling a national role. With its open access policy, it promotes fair access for all who want to study higher education courses and so has a substantial and unique contribution to make to widening participation in the UK. The Open University has earned a world-wide reputation for the quality of its teaching. It is rated amongst the best in the UK for the excellence of its materials and for its approach to supported open learning, which uses methods and technologies that are appropriate to the students and their learning needs. This has been confirmed by the University's very high placings for its students' overall satisfaction in the National Student Survey for seven years.

Future Developments (continued)

International Activities

On the international front, the University has maintained its direct teaching activities in Europe and its partnership activities in Eastern Europe and the rest of the world. Through these activities some 45,000 students in more than 25 countries benefit from the University's materials and pedagogy. At the same time the University has boosted its involvement in teaching in Africa and Asia by working with a variety of public and private organisations. The University is seeking to put all its international activities on a more commercial footing, except where they can be funded from philanthropic donations, in view of the loss of UK public funding over the next few years.

Research

It is clear that UK public funding for research from both HEFCE, as core funding, and UK Research Councils, for individual projects, will come under some pressure as a result of the Comprehensive Spending Review and the Government's desire to concentrate research funding. These two sources, totalling some £19.0 million in 2010/11, form a relatively small but important part of the University's funding and steps will be taken to mitigate any future funding reductions once the various funding agencies' policies become clear.

People

The University's consistently excellent performance in the National Student Survey is down to the professionalism and commitment of its 11,000 employees. The Council thanks each one for their hard work over the past year in a challenging environment to position the University so strongly for the future.

The following members of Council retired from office in the last year: Mr S Barnett, Dr S Crompton, Mrs R Evans, Ms C McEwen and Mr A Peck. The Council wishes to express its gratitude for their contribution.

The Council also wishes to express its appreciation to the alumni and supporters of the University who made donations and bequests in the year. The total received in the year from these sources was £2.5 million, which is included in either new endowments or income.

Conclusion

At the time of writing much publicity is being given to the world-wide economic problems, the fragility of the financial sector and the austerity programmes of Western governments. On top of this the way in which universities in England and Wales are funded is to change significantly, making it difficult to predict how the student market will change and requiring expenditure on new systems and change programmes. However, the business model of The Open University looks increasingly relevant to those who have a thirst for knowledge or are in mid-career and need to change direction. If the UK is to prosper in a competitive globalised economy it has to raise its game as a knowledge economy, or face declining relative standards of living. The Open University, which provides excellent cost effective higher education, will be an important contributor to this transformation and enters this period of uncertainty in a strong financial position.

Approved by Council on 22 November 2011 and signed on its behalf by:

D M C E STEEN
Treasurer

M S HEDGES
Finance Director

M G BEAN
Vice-Chancellor

Corporate Governance and Accountability Arrangements

The Open University is a body incorporated by Royal Charter. Although the University does not have shareholders and is not a listed company, the University's Council is committed to achieving high standards of corporate governance in line with accepted best practice. Accordingly, the University's Council believes it is appropriate to report on compliance, as far as is practicable, with the appropriate provisions of the UK Corporate Governance Code (formerly the Combined Code) issued by the Financial Reporting Council in May 2010.

Throughout the year ended 31 July 2011, the University has been in compliance with all the Code provisions set out in the UK Corporate Governance Code insofar as they relate to universities.

In March 2009 the Committee of University Chairmen issued a Guide for Members of Higher Education Governing Bodies in the UK which incorporates a Governance Code of Practice. This code is voluntary and is intended to reflect good practice in a sector that comprises a large number of very diverse institutions. Institutions should state that they have had regard to the code, and where an institution's practices are not consistent with particular provisions of this code, an explanation should be published in the corporate governance statement of the annual audited financial statements.

In respect of the year ended 31 July 2011, the University's Council can report that there was no element of this Code with which the University's practice was not consistent.

The University Council

The membership of the Council is set out in the University Statutes. At the date of approval of these financial statements there are 23 members comprising: ex officio and co-opted external members; the Vice-Chancellor; the President of the Open University Students Association (OUSA) and a student and staff employees appointed after election. Since the University is a charity the Council members are the charity trustees. The roles of Chair and Vice-Chair of the Council are separated from the role of the University's Chief Executive, the Vice-Chancellor.

The University's Council has adopted a statement of primary responsibilities, which is published on the University's Freedom of Information and Governance websites. This statement sets out the Council's responsibilities in respect of the proper conduct of public business, strategic planning, monitoring effectiveness and performance, finance, audit, estate management, human resource management, equality and diversity, students' union, health and safety, and the appointment of the University Officers.

The Statement of Responsibilities of the University's Council on pages 26 and 27 describes its responsibilities in respect of maintaining accounting records, preparing financial statements and accountability arrangements. It also summarises the University's system of internal control and its system of risk identification and management.

The Council has the following committees: a Strategic Planning and Resources Committee (a joint committee with the Senate); a Finance Committee; a Membership Committee; a Remuneration Committee; a Staff Strategy Committee; an Estates Committee; a Development Committee; and, an Audit Committee. All of these committees are formally constituted with terms of reference. The Chair of each committee is an external Council member. The Council, on the recommendation of the Membership Committee, appoints all members of the Council who sit on these committees. The Council also appoints external members co-opted to Council committees. The corporate governance disclosures in respect of these committees follow those in respect of the Council itself.

THE OPEN UNIVERSITY

CORPORATE GOVERNANCE STATEMENT (continued)

The Council met four times during the year. The members of the University's Council during the year ended 31 July 2011, and their attendance at the meetings held during their membership in that year, together with members serving in the period after 31 July 2011 and up to the date on which the financial statements were approved, were:

Ex-officio members who are also officers of the University

| | |
|---------------------------------------|------------------------|
| Pro-Chancellor & Chair of the Council | Lord Haskins (4/4) |
| Treasurer | Mr D M C E Steen (4/4) |
| Vice-Chancellor (Employee) | Mr M G Bean (4/4) |

Ex officio members:

| | |
|---|--|
| President, Open University Students Association | Mrs R Evans (to 31 March 2011) (2/2) Mrs M Cantieri (from 1 April 2011) (2/2) |
|---|--|

Elected members:

| | |
|--------------------------------------|---|
| Members of Senate (Employees) | Dr S Ding (4/4) Professor J Fortune (4/4) Mr R O Humphreys (1/4) Dr C K Lloyd (3/4) Dr T O'Neil (4/4) |
| Associate Lecturers (Employees) | Dr I Falconer (4/4) Dr M Hopkins (3/4) |
| Open University Students Association | Ms L Murphy (3/4) |
| Non-academic Staff (Employees) | Dr S Crompton (to 1 April 2011) (1/2) Mrs S Dutton (from 3 June 2011) (1/1) |

External members co-opted by Council:

| | |
|---|-------------------------------------|
| Mr S Barnett Vice-Chair (to 31 July 2011) (3/4) | Mr P Mantle (2/4) |
| Mr E Briffa (4/4) | Ms R McCool (from 1 August 2011) |
| Mr H R Brown (4/4) | Ms C McEwen (to 31 July 2011) (3/4) |
| Dr A Freeling (4/4) | Mr A Peck (to 31 July 2011) (3/4) |
| Mrs C A Ighodaro (3/4) | Mrs R Spellman (3/4) |
| Mr BS Larkman (from 1 August 2011) | Professor W Stevely (4/4) |
| Mrs S Macpherson (4/4) | |

Members of the Vice-Chancellor's Executive in attendance at Council meetings:

| | |
|----------------------|---|
| University Secretary | Mr A F Woodburn |
| Finance Director | Mr M S Hedges |
| Director, Students | Mr W S Swann |
| Pro-Vice-Chancellors | Professor A Bassindale (from 17 January 2011 to 4 September 2011) |
| | Professor T Blackman (from 5 September 2011) |
| | Professor B R Heywood (to 21 January 2011) |
| | Professor D Kirkpatrick |
| | Professor A W Tait |

Strategic Planning and Resources Committee

In respect of its strategic and development responsibilities, the Council receives recommendations and advice from the Strategic Planning and Resources Committee, a joint committee of the Council and of the Senate, the body responsible for the University's academic affairs. It recommends to Council the distribution of resources within the University on the basis of its strategic direction and requirements.

The Strategic Planning and Resources Committee met four times during the year. The members during the year ended 31 July 2011, and their attendance at the meetings held during their membership, were:

External members of Council Lord Haskins - Chair (4/4)
Mr D M C E Steen (4/4)
Mr S Barnett (3/4)
Mr E Briffa (4/4)

Employees Mr M G Bean - Vice-Chancellor – Deputy Chair (4/4)
Dr S Bromley - Deans' representative (3/4)
Professor A De Roeck - Senate elected member (4/4)
Mr D Goldrie - Senate elected member (4/4)
Ms B Stephens - Senate elected member (3/4)

Members of the Vice-Chancellor's Executive in attendance at Strategic Planning and Resources Committee meetings:

Professor A Bassindale - Pro-Vice-Chancellor (from 17 January 2011)
Mr M S Hedges - Finance Director
Professor B R Heywood - Pro-Vice-Chancellor (to 21 January 2011)
Professor D Kirkpatrick - Pro-Vice-Chancellor
Dr A Madden - Director of Business Development (to 8 April 2011)
Mr D Matthewman - Chief Information Officer
Mr W S Swann - Director, Students
Professor A W Tait - Pro-Vice-Chancellor
Mr A F Woodburn - University Secretary

Membership Committee

The Membership Committee brings forward recommendations for the appointment or re-appointment of co-opted members of the Council, including recommendations on periods of office. It also makes recommendations to the Council for the appointment of Council members to committees of the Council and committees of the University to which Council members are appointed. Its recommendations to Council take into account the balance of skills, knowledge and experience of Council members and are based on assessment against objective criteria. It also considers issues of succession planning within the Council. It provides the Council with an annual review of attendance at meetings of the Council and its committees and monitors the attendance of members on a regular basis.

The Membership Committee has had four meetings during the year, three of which were held by correspondence. The members during the year ended 31 July 2011, and their attendance at the meetings held during their membership, were:

External members of Council Lord Haskins - Chair (4/4)
Mr S Barnett (3/4)
Ms C McEwen (4/4)

Employees Mr M G Bean - Vice-Chancellor (4/4)
Dr M Hopkins (3/4)
Mr R O Humphreys (3/4)

Finance Committee

The Finance Committee reviews and then recommends to Council the University's annual revenue and capital budgets and monitors performance in relation to the approved budgets. It reviews and then recommends to Council the financial regulations and financial policies that are applied by management. It reviews the annual financial statements, including significant matters of judgement arising that require review, and meets with the external auditors to discuss the outcome of their audit; it then recommends the financial statements to Council for approval.

The Finance Committee met six times during the year. The members during the year ended 31 July 2011 (of whom the Chair and two others have recent and relevant financial experience), and their attendance at the meetings held during their membership, were:

| | |
|------------------------------------|--|
| <i>External members of Council</i> | Mr D M C E Steen - Chair (6/6) Lord Haskins (6/6) Mr H R Brown (5/6) |
| <i>Other external members</i> | Mr B S Larkman (6/6) Mr F Neale (5/6) |
| <i>Employee</i> | Mr M G Bean - Vice-Chancellor (6/6) |
| <i>Officers in attendance</i> | Mr M S Hedges - Finance Director Mr A F Woodburn - University Secretary |

Estates Committee

The Estates Committee reviews and develops the University's estates strategy and related strategies for recommendation to Council. It reviews and recommends the rolling capital programme and monitors progress and expenditure thereon. It recommends expenditure proposals for individual capital development schemes and acquisitions to Finance Committee and Council.

The Estates Committee met twice during the year. The members during the year ended 31 July 2011, and their attendance at meetings during their membership, were:

| | |
|------------------------------------|--|
| <i>External members of Council</i> | Mr P Mantle - Chair (1/2) |
| <i>Other external members</i> | Mr R Booker (1/2) Mr R J Chenery (2/2) |
| <i>Employees</i> | Ms C Baume (to 10 March 2011) (0/1) Mr M S Hedges - Finance Director (1/2) Dr J Holloway (to 18 April 2011) (2/2) Ms A Howells (2/2) Ms M Kirby (from 11 March 2011) (1/1) Professor N Mason (from 5 May 2011) (0/0) Professor P J Potts (to 31 March 2011) (2/2) Professor D Rowland (from 18 May 2011) (0/0) Mrs N Whitsed (1/2) Mr A F Woodburn - University Secretary (1/2) |

Remuneration Committee

The Remuneration Committee determines the annual remuneration of and rewards to the most senior staff, including the Vice-Chancellor. The cost of living salary increases for all staff are determined by national pay negotiations for all universities.

External members of the Council receive no remuneration for their services although expenses incurred in attending meetings are met by the University. Members of the Council who are employees of the University receive no additional remuneration for their services to the Council although, once again, expenses incurred in attending meetings are met by the University. The aggregate expenses paid to or on behalf of members of Council in this capacity is disclosed in Note 7.

The Remuneration Committee met twice during the year. The members during the year ended 31 July 2011 and attendance at the meetings during their membership were:

External members of Council Lord Haskins - Chair (2/2)
Mr S Barnett (2/2)
Mr D M C E Steen (2/2)
Mr A Peck (2/2)

Development Committee

The Development Committee is responsible to the Council for strategies and policies relating to activities to raise donations in support of the University's strategic objective to broaden its funding.

The Development Committee met once during the year. The members during the year ended 31 July 2011, and their attendance at meetings during their membership, were:

External members of Council Dr A Freeling - Chair (1/1)
Lord Haskins (1/1)
Mr D M C E Steen (1/1)

Employee Mr M G Bean - Vice-Chancellor (1/1)

Officers in attendance Mr M S Hedges
Mr A F Woodburn
Ms E Prak

Staff Strategy Committee

The Staff Strategy Committee advises the Council, subject to the powers of the Senate in respect of academic staff, on the human resources implications of the strategies of the University. It contributes to the development of the University's policies and strategies relating to human resources and monitors their implementation. It also satisfies itself and provides assurance to the Council of the effectiveness of policies in respect of human resources matters.

The Staff Strategy Committee met twice during the year. The members during the year ended 31 July 2011, and their attendance at the meetings held during their membership, were:

External members of Council Mr A Peck - Chair (1/2)
Mrs R Spellman (1/2)

Other external members Ms A Corbyn (0/2)
Ms R McCool (2/2)

Employees Mr A Burrell (2/2)
Professor A Bassindale - Pro-Vice-Chancellor (from 8 April 2011) (2/2)
Professor B R Heywood - Pro-Vice-Chancellor (to 21 January 2011) (0/0)
Dr C K Lloyd (2/2)
Mr A F Woodburn - University Secretary (1/2)

Audit Committee

The Audit Committee comprises wholly external members, drawn from both within and outwith the Council, and so has no executive responsibility. During the year ended 31 July 2011 the Audit Committee met three times. Its members and their attendance at meetings held during their membership were:

| | |
|------------------------------------|--|
| <i>External members of Council</i> | Mrs C A Ighodaro - Chair (3/3) Ms C McEwen (3/3) Professor W Stevely (3/3) |
| <i>Other external members</i> | Mr C Hughes (from 7 June 2011) (1/1) Mr C Juman (2/3) Ms J Seeley (2/3) |

The Audit Committee relies substantially on the work of the internal and external auditors, on the information provided by management and on the response of management to the questions it raises.

The remit of the Audit Committee includes:

- reviewing the effectiveness of the Group's arrangements for risk management, control and governance;
- satisfying itself and assuring Council, with advice from the Chief Auditor, that satisfactory arrangements are in place to promote economy, efficiency and effectiveness;
- reviewing and approving the terms of reference of the Internal Audit function and monitoring its performance and effectiveness;
- advising the Council, as necessary, on the appointment and remuneration of the external auditors, and monitoring their performance and effectiveness;
- reviewing with the external auditors the scope and nature of the audit, including the report to Audit Committee written by the external auditors;
- assessing compliance with the regulatory framework relating to audit issues.

The external auditors have a standing arrangement to meet the Audit Committee members regularly without staff present. The auditors also attend meetings with staff to consider the items listed above and to review plans for the audit process.

The University's Internal Audit function is responsible for providing an objective and independent appraisal and assurance on all the University's activities, financial and otherwise. In particular, assurance on the arrangements for risk management, control, governance and value for money is delivered to the Council and the Vice-Chancellor, through the Audit Committee. All reviews undertaken by Internal Audit are considered with the management in the relevant operational unit. The reviews are also considered by the Vice-Chancellor, University Secretary and Finance Director and appropriate action confirmed to the Audit Committee. The Chief Auditor has unfettered access to the Audit Committee.

The Internal Audit work programme is drawn down from a risk-focused Audit Plan, which remains dynamic and is updated regularly to reflect changes in the University's risk profile. Internal Audit monitors the progress made by units in implementing agreed actions to ensure that they are addressed in a timely and effective manner, and reports regularly thereon to the Audit Committee.

The Audit Committee also keeps under review the independence and objectivity of the external auditors. In 2006 the decision was taken to segregate as far as possible the provision of audit related services from non-audit services in order to further enhance the independence of the external auditors. One piece of continuing work was commissioned in the year which will be started in 2011/12. In the prior year three small items of work were commissioned from PricewaterhouseCoopers, having obtained the specific approval of Audit Committee and having reached the view that this would not have an impact on their independence as external auditors. The fees for this work are disclosed in Note 7.

THE OPEN UNIVERSITY

RESPONSIBILITIES OF THE UNIVERSITY'S COUNCIL

In accordance with the University's Charter and Statutes, the Council is responsible for the administration and management of the University's affairs and is required to present audited financial statements for each financial year.

The Council is responsible for ensuring that proper accounting records are kept that disclose with reasonable accuracy at any time the financial position of the University and enable the financial statements to be prepared in accordance with the University's Charter and Statutes, the Statement of Recommended Practice on Accounting for Further and Higher Education Institutions and other relevant accounting standards. In addition, within the terms and conditions of the Financial Memorandum between the Higher Education Funding Council for England (HEFCE) and the University's Council and the HEFCE Accounts Direction, the Council, through its designated office holder, is required to prepare financial statements for each financial year that give a true and fair view of the University's state of affairs and the surplus or deficit and cash flows for that year.

In causing the financial statements to be prepared, the Council has ensured that:

- suitable accounting policies are selected and applied consistently;
- judgements and estimates are made that are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements;
- financial statements are prepared on the going concern basis unless it is inappropriate to presume that the University will continue in operation. The Council is satisfied that it has adequate resources to continue in operation for the foreseeable future: for this reason, the going concern basis continues to be adopted in the preparation of the financial statements.

The Council has taken reasonable steps to:

- ensure that funds from HEFCE, the Scottish Funding Council (SFC), the Higher Education Funding Council for Wales (HEFCW), the Department of Employment and Learning (Northern Ireland) (DELNI) and the Training and Development Agency for Schools (TDA) are used only for the purposes for which they have been given and in accordance with the Financial Memorandum with HEFCE and the Funding Agreements with SFC, HEFCW, DELNI and TDA and any other conditions which the Funding Councils or Agency may from time to time prescribe;
- ensure that there are appropriate financial and management controls in place to safeguard public funds and funds from other sources;
- ensure that there are effective systems of risk identification and management that cover all risks, produce a balanced portfolio of risk exposure, are based on a clearly articulated policy and approach, are monitored and reviewed regularly, are integrated into normal business processes and aligned to the University's strategic objectives and are managed by heads of units and senior managers;
- safeguard the assets of the University and prevent and detect fraud;
- secure the economical, efficient and effective management of the University's resources and expenditure.

THE OPEN UNIVERSITY

RESPONSIBILITIES OF THE UNIVERSITY'S COUNCIL (continued)

The key elements of the University's system of internal control, which is designed to discharge the responsibilities set out above, include the following:

- definitions of the responsibilities of, and the authority delegated to, heads of academic and administrative units;
- a medium and short-term planning process, supplemented by detailed annual income, expenditure, capital and cash flow budgets;
- regular reviews of academic performance and quarterly financial reviews involving variance reporting and updates of forecast outturns;
- defined and formalised requirements for approval and control of expenditure, with investment decisions involving capital or revenue expenditure being subject to formal detailed appraisal and review according to approval levels set by Council;
- Financial Regulations, including financial controls and procedures, approved by Finance Committee;
- a professional Internal Audit team whose annual programme is approved by Audit Committee.

The key elements of the University's system of risk identification and management, which is designed to discharge the responsibilities set out above, include the following:

- linking the identification and management of risk to the achievement of institutional objectives through the annual planning process;
- evaluating the likelihood and impact of risks becoming a reality as part of that same process and establishing mitigating controls;
- having review procedures that cover business, operational, compliance and financial risk;
- embedding risk assessment and internal control processes in the ongoing operations of all units;
- reporting regularly to Audit Committee, and then to Council, on internal control and risk;
- reporting annually to Council the principal results of risk identification, evaluation and management review.

Any system of internal control or risk management is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss.

In relation to the University's financial statements published on its website, the University's management is responsible to Council for the maintenance and integrity of The Open University website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

INDEPENDENT AUDITORS' REPORT to the Council of The Open University

We have audited the group and parent institution financial statements (the "financial statements") of The Open University for the year ended 31 July 2011 which comprise the Consolidated Income and Expenditure Account, the Consolidated and University Balance Sheets, the Consolidated Cash Flow Statement, the Consolidated Statement of Recognised Gains and Losses, the Statement of Principal Accounting Policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of Council members and auditors

As explained more fully in the Responsibilities of the University's Council set out on page 26 the Council is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Council as a body in accordance with Section 10 of the Charters and Statutes of the University and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and parent institution's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Council; and, the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the financial statements to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and University's affairs as at 31 July 2011 and of the group's income and expenditure, recognised gains and losses and cash flows for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and,
- have been prepared in accordance with the Statement of Recommended Practice – Accounting for Further and Higher Education.

Opinion on other matters prescribed in the HEFCE Audit Code of Practice issued under the Further and Higher Education Act 1992

In our opinion, in all material respects:

- funds from whatever source administered by the University for specific purposes have been properly applied to those purposes and, if relevant, managed in accordance with relevant legislation;
- income has been applied in accordance with the University's Statutes; and,
- funds provided by HEFCE have been applied in accordance with the Financial Memorandum and any other terms and conditions attached to them, with the Funding Agreement with the Scottish Funding Council, with the Funding Letter with the Higher Education Funding Council for Wales, with the Funding Agreement with the Department of Employment and Learning (Northern Ireland) and with the Funding Agreement with the Training and Development Agency for Schools.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matter, where the HEFCE Audit Code of Practice issued under the Further and Higher Education Act 1992 requires us to report to you if, in our opinion, the statement of internal control included as part of the Responsibilities of the University's Council is inconsistent with our knowledge of the parent institution and group.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Milton Keynes
22 November 2011

1 Basis of preparation

The financial statements have been prepared under the historical cost convention as modified by the revaluation of land and buildings, in accordance with the Statement of Recommended Practice, *Accounting for Further and Higher Education Institutions*, (SORP) published in July 2007 and in accordance with applicable United Kingdom Accounting Standards.

2 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the University and its subsidiary undertakings for the financial year ended 31 July 2011.

The consolidated financial statements do not include those of the Open University Students Association, as the University has no control or significant influence over policy decisions of the Association.

3 Recognition of income

- a. Fee income is credited to income over the period in which the students are studying. This is achieved by using a time apportionment basis over the period of the relevant module.

Fee income is stated gross; financial assistance to students, other fee waivers and provision for bad debts are included in other operating expenses.

Where students have registered, which is when the liability to pay the fees is created, for modules that begin in a future financial year, the income is included in creditors as student fee income in advance. Where these fees have not been paid wholly or partly in advance by the end of the financial year in which registration takes place or if payment will become due in a future financial year under an instalment credit agreement, the amount not received at the end of the financial year is included in debtors.

- b. Recurrent grants from Funding Bodies are credited to income in the period in which they are receivable.
- c. Non-recurrent grants received in respect of the acquisition or construction of buildings and equipment are treated as deferred capital grants and amortised in line with depreciation over the life of the assets. Non-recurrent grants received in respect of the acquisition of freehold land are treated as income in the period in which all conditions of the grants have been met.
- d. Income for specific purposes, such purposes being designated by the grant-making body or donor under a specific agreement or contract and which can only be applied for those specific purposes, is credited to income over the life of the agreement or contract when the conditions attaching to its receipt have been met, such as incurring the appropriate expenditure, including expenditure on indirect costs.
- e. Income from the sale of goods or services is credited to income when the goods or services are supplied to the external customers against the orders received or the terms of the contract have been satisfied.
- f. Interest receivable is credited to income on a daily basis.

4 Recognition of expenditure

- a. Expenditure is recognised in respect of goods and services received when supplied in accordance with contractual terms.
- b. Provision is made when a present obligation exists for a future liability in respect of a past event, it is probable that a transfer of economic benefits will be required to settle the obligation and where the amount of the obligation can be reliably estimated.
- c. Restructuring costs are recognised in respect of the direct expenditure of a reorganisation where plans are sufficiently detailed and well advanced, and where appropriate communication to those affected has been undertaken at the balance sheet date.
- d. Module development costs are charged to expenditure as they are incurred.
- e. The University has a maintenance plan designed to keep its estate in a constant state of good repair. The cost of maintenance is charged to expenditure in the period in which it is incurred.
- f. Loan interest and / or facility fees are charged to expenditure on a daily basis.

5 Foreign currencies

Transactions denominated in foreign currencies are recorded at the rate of exchange ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into sterling either at year end rates or, where there are related forward foreign exchange contracts, at contract rates. The resulting exchange differences are dealt with in the determination of income and expenditure for the financial year.

6 Pension schemes

In the United Kingdom the University participates in two schemes to provide retirement and death benefits for its employees, namely, the Universities Superannuation Scheme (USS), and, for a small number of staff, the Federated Superannuation System of Universities (FSSU). In the Republic of Ireland a small number of employees are members of the defined contribution Open University Retirement Solution Plan (OURSP). A small number of overseas based employees are members of defined contribution schemes.

a. Defined benefit scheme (USS)

The assets of the scheme are held in a separate trustee-administered fund. Because of the mutual nature of the scheme, the scheme's assets are not hypothecated to individual institutions and a scheme-wide contribution rate is set. The University is therefore exposed to actuarial risks associated with other institutions' employees and is unable to identify its share of the underlying assets and liabilities in full in USS on a consistent and reasonable basis and therefore, as required by FRS17, *Retirement Benefits*, the University accounts for the scheme as if it were a defined contribution scheme. As a result the amount charged to the income and expenditure account represents the contributions payable to the scheme in respect of the accounting period.

b. Defined contribution schemes (FSSU, OURSP and others)

The cost charged to the expenditure account is equal to the total of contributions payable in the year.

7 Leasing costs

Rental costs under operating leases are charged to expenditure in equal annual amounts over the period of the lease.

8 Stocks of finished goods

- a. Stocks of module materials are valued at the lower of cost and net realisable value. Provision is made for obsolete or surplus module materials.
- b. Stocks of materials for use at residential schools are written off when purchased.

9 Investments

- a. Investments in subsidiaries are shown at cost.
- b. Current asset investments comprise funds held on deposit. Interest is accrued on a daily basis.

10 Land and buildings

Land and buildings held at 31 July 1998 are shown in the balance sheet at the valuation on that date; land and buildings acquired after 31 July 1998 are shown at cost. The revaluation at 31 July 1998 was undertaken in accordance with the appraisal and valuation manual prepared by the Royal Institution of Chartered Surveyors. The Walton Hall campus was valued on the basis of depreciated replacement cost and all other buildings on the basis of existing use value. The valuation was conducted by Chesterton plc, International Property Consultants.

On adoption of FRS 15, *Tangible Fixed Assets*, the Group adopted the transitional provisions to retain the book value of land and buildings, many of which were last revalued in 1998, and has not adopted a policy of annual revaluations for the future. However, these values are subject to impairment reviews as set out in FRS 11, *Impairment of Fixed Assets and Goodwill*.

Freehold land is not depreciated as it is considered to have an indefinite useful life. Buildings are depreciated over their expected useful lives of 40 years. Where buildings have a major refurbishment to adapt them for another use or extend their original useful life, the refurbishment cost is depreciated over their revised expected useful lives, which is a maximum of 40 years from date of the adaptation. Minor refurbishments to buildings are depreciated over the remaining expected useful life of the building, with a maximum period of 10 years.

Where buildings are acquired with the aid of specific grants, they are capitalised and depreciated as above. The related grants are treated as deferred capital grants and released to income over the expected useful life of the buildings.

Where land is acquired with the aid of specific grants it is capitalised as above. The related grants are treated as income in the period in which all conditions of grant have been met.

11 Equipment

Equipment, including computers and software, costing less than £30,000 per individual item or group of related items is written off in the year of acquisition. All other equipment is capitalised.

Capitalised equipment is stated at cost and depreciated over its expected useful life as follows:

| | |
|---------------------|---------|
| Telephone equipment | 5 years |
| Motor vehicles | 4 years |
| Computing equipment | 3 years |
| Other equipment | 3 years |

Where equipment is acquired with the aid of specific grants, it is capitalised and depreciated as above. The related grants are treated as deferred capital grants and released to income over the expected useful life of the equipment, which is the period of the grant in respect of equipment acquired for specific research projects.

12 Heritage assets

Heritage assets costing or valued at over £30,000 are capitalised at cost or value on acquisition, where such a valuation is reasonably obtainable. Such assets are not depreciated. Other heritage assets are not capitalised. All costs incurred in relation to preservation and conservation of heritage assets are expensed as incurred.

The University library holds in its archives a small collection of personal and public papers and documents bequeathed to it by persons connected to the University, and a collection of historical documents related to the University. These items are not included in the financial statements since the University considers that it would not be practical to obtain a meaningful valuation.

13 Taxation status

The University is an exempt charity within the meaning of Schedule 2 of the Charities Act 1993 and as such is a charity within the meaning of Para 1 of Schedule 6 to the Finance Act 2010. Accordingly, the University is potentially exempt from taxation in respect of income or capital gains received within categories covered by sections 478-488 of the Corporation Tax Act 2010 (CTA 2010) (formerly enacted in Section 505 of the Income and Corporation Taxes Act 1988 (ICTA)) or Section 256 of the Taxation of Chargeable Gains Act 1992 to the extent that such income or gains are applied to exclusively charitable purposes. The University receives no similar exemption in respect of Value Added Tax and any tax incurred is either expensed or capitalised according to the nature of the underlying expenditure.

14 Accounting for donations

a. Unrestricted donations

Donations are recognised in the financial statements when the donation has been received or if, before receipt, there is sufficient evidence to provide necessary certainty that the donation will be received and the value of the incoming resource can be measured with sufficient reliability.

b. Endowment funds

Where donations are to be retained to the benefit of the University for purposes specified by the donors, they are accounted for as expendable endowments. Specifically the University has restricted expendable endowments whereby the donor has specified a particular objective other than the purchase or construction of tangible fixed assets, and the University can convert the donated sum into income.

CONSOLIDATED INCOME AND EXPENDITURE ACCOUNT for the Year Ended 31 July 2011

| | NOTES | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|-------|----------------------------------|----------------------------------|
| INCOME | | | |
| Funding body grants | 1 | 257.8 | 244.0 |
| Tuition fees and education contracts | 2 | 164.0 | 156.7 |
| Research grants and contracts | 3 | 15.6 | 17.0 |
| Other income | 4 | 29.2 | 29.1 |
| Endowment and investment income | 5 | 3.9 | 3.3 |
| Total income | | 470.5 | 450.1 |
| EXPENDITURE | | | |
| Staff costs | 6 | 276.6 | 275.2 |
| Other operating expenses | 7 | 136.1 | 137.6 |
| Depreciation | | 10.6 | 11.8 |
| Interest payable and other finance costs | 8 | (0.1) | 0.0 |
| Total expenditure | | 423.2 | 424.6 |
| Surplus after depreciation of assets at valuation and before tax and exceptional items | | 47.3 | 25.5 |
| Less: Taxation | 9 | 0.0 | 0.1 |
| Surplus after depreciation of assets at valuation and tax | | 47.3 | 25.4 |
| Exceptional items: continuing operations | 10 | 0.7 | 0.1 |
| disposal of fixed asset | 11 | 1.1 | 0.5 |
| Surplus after exceptional items | | 49.1 | 26.0 |
| Plus loss for the year transferred to accumulated income in endowment funds | 21 | 0.0 | 0.1 |
| Surplus for the year retained within general reserves | | 49.1 | 26.1 |
| NOTE OF HISTORICAL COST SURPLUS | | | |
| Surplus after depreciation of assets at valuation and tax | | 47.3 | 25.4 |
| Difference between an historical cost depreciation charge and the actual depreciation charge for the year | 22 | 0.9 | 1.4 |
| Historical cost surplus after tax | | 48.2 | 26.8 |

The income and expenditure account has been prepared on an historical basis as modified by the revaluation of land and buildings and is solely in respect of continuing activities.

The accounting policies on pages 30 to 33 and the notes on pages 38 to 58 form an integral part of these financial statements.

THE OPEN UNIVERSITY

CONSOLIDATED STATEMENT OF RECOGNISED GAINS AND LOSSES for the Year Ended 31 July 2011

| | NOTES | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|-------|----------------------------------|----------------------------------|
| Surplus on continuing operations after depreciation of assets at valuation, tax and exceptional items | | 49.1 | 26.0 |
| New expendable endowments | 14 | 0.1 | 0.0 |
| Total recognised gains relating to the year | | <u>49.2</u> | <u>26.0</u> |

The accounting policies on pages 30 to 33 and the notes on pages 38 to 58 form an integral part of these financial statements.

THE OPEN UNIVERSITY

BALANCE SHEETS as at 31 July 2011

| | NOTES | CONSOLIDATED | | UNIVERSITY | |
|--|-------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | | As At 31 July 2011 £m | As At 31 July 2010 £m | As At 31 July 2011 £m | As At 31 July 2010 £m |
| FIXED ASSETS | | | | | |
| Tangible assets | 12 | 172.8 | 182.4 | 170.3 | 179.8 |
| Investments | 13 | 0.0 | 0.0 | 1.0 | 1.0 |
| | | 172.8 | 182.4 | 171.3 | 180.8 |
| ENDOWMENT ASSETS | 14 | 0.5 | 0.4 | 0.5 | 0.4 |
| CURRENT ASSETS | | | | | |
| Stocks of finished goods | | 4.3 | 4.5 | 4.3 | 4.5 |
| Debtors - due within one year | 15 | 39.5 | 39.6 | 22.1 | 25.1 |
| - due after one year | | 0.2 | 0.2 | 63.1 | 63.1 |
| Gilts and term deposits | 16 | 194.5 | 131.7 | 194.5 | 131.7 |
| Cash at bank and in hand | | 76.1 | 17.7 | 71.4 | 13.2 |
| | | 314.6 | 193.7 | 355.4 | 237.6 |
| LESS CREDITORS: amounts falling due within one year | 17 | 123.1 | 115.3 | 164.8 | 160.3 |
| NET CURRENT ASSETS | | 191.5 | 78.4 | 190.6 | 77.3 |
| TOTAL ASSETS LESS CURRENT LIABILITIES | | 364.8 | 261.2 | 362.4 | 258.5 |
| LESS CREDITORS: amounts falling due after more than one year | 18 | 62.4 | 2.5 | 60.5 | 0.4 |
| LESS PROVISIONS for liabilities | 19 | 0.0 | 2.4 | 0.0 | 2.4 |
| TOTAL NET ASSETS | | 302.4 | 256.3 | 301.9 | 255.7 |
| DEFERRED CAPITAL GRANTS | 20 | 86.7 | 89.8 | 86.7 | 89.8 |
| ENDOWMENTS | | | | | |
| Expendable | 21 | 0.5 | 0.4 | 0.5 | 0.4 |
| RESERVES | 22 | | | | |
| Revaluation reserve | | 3.4 | 4.3 | 3.4 | 4.3 |
| General funds | | 211.8 | 161.8 | 211.3 | 161.2 |
| TOTAL RESERVES | | 215.2 | 166.1 | 214.7 | 165.5 |
| | | 302.4 | 256.3 | 301.9 | 255.7 |

The accounting policies on pages 30 to 33 and the notes on pages 38 to 58 form an integral part of these financial statements, which were approved by Council on 22 November 2011 and signed on its behalf by:

D M C E STEEN
Treasurer

M S HEDGES
Finance Director

M G BEAN
Vice-Chancellor

THE OPEN UNIVERSITY

CONSOLIDATED CASH FLOW STATEMENT for the Year Ended 31 July 2011

| | NOTES | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|-------|----------------------------------|----------------------------------|
| NET CASH INFLOW FROM OPERATING ACTIVITIES | 23 | 55.9 | 29.2 |
| RETURN ON INVESTMENTS AND SERVICING OF FINANCE | | | |
| Interest received | | 4.8 | 3.4 |
| Interest paid | | (0.1) | (0.1) |
| NET CASH INFLOW FROM RETURNS ON INVESTMENT AND SERVICING OF FINANCE | | 4.7 | 3.3 |
| TAX PAID | | 0.0 | (0.1) |
| CAPITAL EXPENDITURE | | | |
| Payments to acquire tangible assets | | (5.5) | (16.3) |
| Deferred capital grants received | | 2.7 | 16.9 |
| Proceeds of sale of fixed asset | | 5.0 | 0.6 |
| NET CASH INFLOW FROM CAPITAL EXPENDITURE | | 2.2 | 1.2 |
| CASH INFLOW BEFORE MANAGEMENT OF LIQUID RESOURCES | | 62.8 | 33.6 |
| MANAGEMENT OF LIQUID RESOURCES | | | |
| Cash transferred to term deposits or gilts | | (64.2) | (40.1) |
| FINANCING | | | |
| New bank loan drawn down in year | | 60.0 | 0.0 |
| Loan repayment in the year | | (0.2) | (0.1) |
| INCREASE/(DECREASE) IN CASH IN THE YEAR | 24,25 | 58.4 | (6.6) |

The accounting policies on pages 30 to 33 and the notes on pages 38 to 58 form an integral part of these financial statements.

1 FUNDING BODY GRANTS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|----------------------------------|----------------------------------|
| Recurrent grants | | |
| Higher Education Funding Council for England (HEFCE) | 189.5 | 191.2 |
| Scottish Funding Council (SFC) | 19.9 | 19.8 |
| Higher Education Funding Council for Wales (HEFCW) | 7.9 | 7.7 |
| Training and Development Agency for Schools (TDA) | 2.9 | 2.7 |
| Department of Employment and Learning (Northern Ireland) (DELNI) | 0.2 | 0.1 |
| | <u>220.4</u> | <u>221.5</u> |
| Specific grants | | |
| Higher Education Funding Council for England University Modernisation Fund | 20.6 | 0.0 |
| Other | 8.8 | 13.2 |
| Scottish Funding Council | 1.0 | 1.6 |
| Higher Education Funding Council for Wales | 1.5 | 2.0 |
| | <u>31.9</u> | <u>16.8</u> |
| Deferred capital grants released in year | | |
| Higher Education Funding Council for England - see Note 20 | | |
| Buildings | 4.9 | 4.9 |
| Equipment | 0.6 | 0.8 |
| | <u>5.5</u> | <u>5.7</u> |
| | <u>257.8</u> | <u>244.0</u> |

2 TUITION FEES AND EDUCATION CONTRACTS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|----------------------------------|----------------------------------|----------------------------------|
| Student fees | | |
| United Kingdom | 141.6 | 133.8 |
| Overseas | 21.2 | 21.9 |
| Research training support grants | 1.2 | 1.0 |
| | <u>164.0</u> | <u>156.7</u> |

3 RESEARCH GRANTS AND CONTRACTS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|----------------------------------|----------------------------------|
| Research Councils | 8.2 | 10.3 |
| Other sources, including industrial companies | 7.4 | 6.7 |
| | <u>15.6</u> | <u>17.0</u> |

4 OTHER INCOME

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--------------------------------------|----------------------------------|----------------------------------|
| Other grants and contracts | 16.7 | 17.8 |
| Royalties received | 0.3 | 0.2 |
| External computer services | 0.2 | 0.3 |
| Sub-tenants' rental and services | 0.1 | 0.5 |
| Validation fees | 2.3 | 2.1 |
| Released from deferred capital grant | 0.0 | 0.1 |
| Other income | 9.6 | 8.1 |
| | <u>29.2</u> | <u>29.1</u> |

5 ENDOWMENT AND INVESTMENT INCOME

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---------------------------|----------------------------------|----------------------------------|
| Interest on student loans | 0.6 | 0.6 |
| Other interest receivable | 3.3 | 2.7 |
| | <u>3.9</u> | <u>3.3</u> |

6 STAFF COSTS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|----------------------------------|----------------------------------|
| Staff costs | | |
| Salaries and other payments to employees | 229.6 | 228.6 |
| Social security costs | 15.9 | 16.1 |
| Pension costs - see Note 30 | 31.1 | 30.5 |
| | 276.6 | 275.2 |
| Staff costs by category | | |
| Full-time staff categories | 207.4 | 211.2 |
| Associate lecturers, residential school staff and examination marking fees | 58.1 | 55.4 |
| Other staff costs, including casual staff | 5.3 | 4.7 |
| Early retirement and voluntary severance | 5.8 | 3.9 |
| | 276.6 | 275.2 |

Remuneration of Higher Paid Employees

The emoluments of Mr M G Bean, the Vice-Chancellor from 1 October 2009, included in the above costs are £322,000 (year ended 31 July 2010, £293,000, together with £46,000 for the previous Vice-Chancellor). The University's pension contributions to the Universities Superannuation Scheme in respect of the Vice-Chancellor are paid at the same rates as for other academic staff and amounted to £52,000 (year ended 31 July 2010, £47,000, together with £6,000 for the previous Vice-Chancellor). The aggregate of these sums is £374,000 (year ended 31 July 2010, £340,000, together with £52,000 for the previous Vice-Chancellor).

Compensation for loss of office paid to UK based employees earning in excess of £100,000 and funded from general income was £35,000 (year ended 31 July 2010, £Nil).

The remuneration of other higher paid employees, excluding the University's pension contributions, was:

| | Staff Numbers 31 July 2011 | Staff Numbers 31 July 2010 |
|---------------------|----------------------------------|----------------------------------|
| £100,000 - £109,999 | 6 | 5 |
| £110,000 - £119,999 | 4 | 4 |
| £120,000 - £129,999 | 2 | 1 |
| £130,000 - £139,999 | 2 | 1 |
| £140,000 - £149,999 | 1 | 1 |
| £160,000 - £169,999 | 1 | 0 |
| £170,000 - £179,999 | 0 | 1 |
| | 0 | 1 |

Average staff numbers (including higher paid staff)

| | | |
|---|---------------|---------------|
| Full-time and part-time staff at Milton Keynes, Wellingborough, national and regional centres | 4,852 | 5,120 |
| Associate lecturers and residential school staff | 6,088 | 6,263 |
| | 10,940 | 11,383 |

7 OTHER OPERATING EXPENSES

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|----------------------------------|----------------------------------|
| Consumables and staff support | 48.1 | 46.8 |
| Teaching materials and residential schools | 17.4 | 18.3 |
| Student publications and recruitment | 16.1 | 16.6 |
| Financial assistance to students | 3.3 | 3.0 |
| Books and periodicals | 3.4 | 3.1 |
| Audio visual production | 6.7 | 7.6 |
| Heat, light, water and power | 2.8 | 3.9 |
| Repairs, general maintenance and equipment | 16.8 | 16.7 |
| Rents and rates | 7.7 | 7.6 |
| Students' association grant | 0.9 | 0.9 |
| Auditors' remuneration - Group audit fees | 0.1 | 0.1 |
| Other expenses | 12.8 | 13.0 |
| | 136.1 | 137.6 |

Included in the above are audit fees in respect of the University only of £0.10 million (year ended 31 July 2010, £0.10 million) and its subsidiaries of an aggregate of £0.02 million (year ended 31 July 2010, £0.02 million). Fees paid to the auditors for non-audit services totalled £Nil (year ended 31 July 2010, £0.02 million).

The total expenses paid to or on behalf of the members of Council in the year was £16,000 (year ended 31 July 2010, £17,000). This represents travel and subsistence expenses incurred in attending Council meetings in their official capacity and reflects the UK-wide distribution of the University's activities and distribution of its Council members. No payments or other benefits for being a member of Council were paid to, or waived by, Council members. Ten members of staff served on Council; the expenses paid to these staff specifically for serving on Council are included in the figure above. No other supplementary payment was made to these staff in their capacity as members of Council.

8 INTEREST PAYABLE AND OTHER FINANCE COSTS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|----------------------------------|----------------------------------|
| On bank loans, overdrafts and other loans: | | |
| Repayable wholly or partly in more than 5 years | 0.1 | 0.1 |
| Impairment on deposits | (0.2) | (0.1) |
| | <u>(0.1)</u> | <u>0.0</u> |

The University had in place two two-year fixed term deposits in UK subsidiaries of Icelandic banks that were put into administration in October 2008, one of £5.0 million placed in October 2006 and the other of £1.5 million placed in March 2007. The impairment provisions against the two deposits in administration have been reviewed in light of the latest guidelines from the administrators regarding the stream of repayments and final settlement. The level of provisions have been reduced, resulting in a write back of £0.2 million in the year. The principal amounts outstanding have been reduced by distributions received from the administrators totalling £4.1 million, and by the impairment, and are included in Note 16.

9 TAXATION

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---------------|----------------------------------|----------------------------------|
| Foreign taxes | <u>0.0</u> | <u>0.1</u> |

The foreign tax is withholding tax on royalty income received by Open University Worldwide Limited.

10 EXCEPTIONAL ITEM: continuing operations

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|----------------------------------|----------------------------------|
| VAT refund | 0.7 | 0.0 |
| Transfer of activity from The Open University Foundation | 0.0 | 0.1 |
| | <u>0.7</u> | <u>0.1</u> |

The exceptional item for the year ended 31 July 2011 represents a refund of VAT from Her Majesty's Revenue and Customs via one of the University's suppliers (see also Note 26).

The exceptional item for the year ended 31 July 2010 represents an agreed transfer of activities and underlying reserves from The Open University Foundation to The Open University by the Foundation's Trustees.

11 EXCEPTIONAL ITEM: disposal of fixed assets

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--------------------------------|----------------------------------|----------------------------------|
| Profit on disposal of building | 1.1 | 0.5 |

The exceptional item for the year ended 31 July 2011 represents the profit on disposal of an office building at Bedford Row in London.

The exceptional item for the year ended 31 July 2010 represents the disposal of a lease of an office building in Belfast.

12 TANGIBLE ASSETS

CONSOLIDATED

| | Land and Buildings £m | Buildings in the Course of Construction £m | Equipment £m | Total £m |
|--|-----------------------------|---|-----------------|---------------|
| Cost and valuation | | | | |
| At 1 August 2010 | 240.8 | 5.7 | 21.0 | 267.5 |
| Additions | 3.7 | 0.0 | 1.2 | 4.9 |
| Transfers | 5.7 | (5.7) | 0.0 | 0.0 |
| Disposals | (10.1) | 0.0 | (0.7) | (10.8) |
| At 31 July 2011 | 240.1 | 0.0 | 21.5 | 261.6 |
| Depreciation | | | | |
| At 1 August 2010 | 65.8 | 0.0 | 19.3 | 85.1 |
| Charge for year | 9.2 | 0.0 | 1.4 | 10.6 |
| Disposals | (6.2) | 0.0 | (0.7) | (6.9) |
| At 31 July 2011 | 68.8 | 0.0 | 20.0 | 88.8 |
| Net book amount | | | | |
| At 31 July 2011 | 171.3 | 0.0 | 1.5 | 172.8 |
| At 31 July 2010 | 175.0 | 5.7 | 1.7 | 182.4 |
| Financed by capital grants - see Note 20 | 86.1 | 0.0 | 0.6 | 86.7 |
| Financed from other sources | 85.2 | 0.0 | 0.9 | 86.1 |
| Net book amount | | | | |
| At 31 July 2011 | 171.3 | 0.0 | 1.5 | 172.8 |

As at 31 July 2011, there was £0.4 million of future capital expenditure for which either contracts had been placed or there was a firm intention to commence work (year ended 31 July 2010, £2.5 million).

If the land and buildings held at 31 July 1998 had not been revalued, the total value of land and buildings, including buildings in the course of construction, would have been included at the following amounts:

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|------------------------|----------------------------------|----------------------------------|
| Cost | 234.4 | 238.6 |
| Aggregate depreciation | 66.3 | 62.1 |
| Net book amount | 168.1 | 176.5 |

12 TANGIBLE ASSETS (continued)

UNIVERSITY

| | Land and Buildings £m | Buildings in the Course of Construction £m | Equipment £m | Total £m |
|--|-----------------------------|---|-----------------|---------------|
| Cost and valuation | | | | |
| At 1 August 2010 | 235.3 | 5.7 | 20.9 | 261.9 |
| Additions | 3.7 | 0.0 | 1.2 | 4.9 |
| Transfers | 5.7 | (5.7) | 0.0 | 0.0 |
| Disposals | (9.7) | 0.0 | (0.6) | (10.3) |
| At 31 July 2011 | 235.0 | 0.0 | 21.5 | 256.5 |
| Depreciation | | | | |
| At 1 August 2010 | 62.9 | 0.0 | 19.2 | 82.1 |
| Charge for year | 9.2 | 0.0 | 1.4 | 10.6 |
| Disposals | (5.9) | 0.0 | (0.6) | (6.5) |
| At 31 July 2011 | 66.2 | 0.0 | 20.0 | 86.2 |
| Net book amount | | | | |
| At 31 July 2011 | 168.8 | 0.0 | 1.5 | 170.3 |
| At 31 July 2010 | 172.4 | 5.7 | 1.7 | 179.8 |
| Financed by capital grants - see Note 20 | 86.1 | 0.0 | 0.6 | 86.7 |
| Financed from other sources | 82.7 | 0.0 | 0.9 | 83.6 |
| Net book amount | | | | |
| At 31 July 2011 | 168.8 | 0.0 | 1.5 | 170.3 |

The unamortised value of HEFCE capital grants amounted to £96.9 million (year ended 31 July 2010 £103.1 million). In the event that the related assets were either to be sold or ceased to be used for the provision of publically funded higher education, the University would either have to surrender the proceeds to HEFCE or use them in accordance with the Financial Memorandum with HEFCE.

13 INVESTMENTS

| | UNIVERSITY | |
|---|-----------------------------|-----------------------------|
| | As At 31 July 2011 £m | As At 31 July 2010 £m |
| Shares in wholly owned subsidiary companies: | | |
| Open University Student Budget Accounts Limited | 0.5 | 0.5 |
| Open University Worldwide Limited | 0.3 | 0.3 |
| | | |
| Long term loans: | | |
| Open University Worldwide Limited | 0.2 | 0.2 |
| | 1.0 | 1.0 |

Open University Student Budget Accounts Limited is registered in England and Wales and was established to provide students with a deferred payment facility. Around 22% of the students use this facility. The company operates under the Consumer Credit Act.

Open University Worldwide Limited is registered in England and Wales and is engaged in the commercial exploitation of the University's intellectual property assets through collaboration with partners overseas or direct sales of course materials. The company is also engaged in other trading activities and is partly financed by a long-term loan that carries interest at a fixed rate of 10% per annum.

The carrying value of the investments is supported by the subsidiaries' net assets.

Open University Business School Limited and Bookhire Limited are registered in England and Wales and are dormant.

Linked Charitable Entities

The University has links with three exempt charities that fall within paragraph (w) of Schedule 2 of the Charities Act 1993. All three are 100% owned subsidiaries of the University:

Bookhire Limited and OU Enterprises Limited are dormant companies.

OU Properties (Bristol) Limited does not have share capital or loans disclosed above, but its results, assets and liabilities are included in the consolidated financial statements. The Company is registered in England and Wales and owns a specific office building, which is leased to the University. Its charitable purpose is the advancement of education by the provision of assistance and benefit for the educational purposes of The Open University. It is financed through a specific bank facility.

OU PROPERTIES (BRISTOL) LIMITED

Reserves

| | £m |
|------------------|-------|
| At 1 August 2010 | 0.4 |
| Income | 0.3 |
| Expenditure | (0.2) |
| | 0.5 |

14 ENDOWMENT ASSETS

| | CONSOLIDATED AND UNIVERSITY | |
|--|----------------------------------|----------------------------------|
| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
| Balance at 1 August | 0.4 | 0.5 |
| Additions | 0.1 | 0.0 |
| Decrease in cash balances held for endowment funds | 0.0 | (0.1) |
| | <hr/> | <hr/> |
| Balance at 31 July | 0.5 | 0.4 |
| | <hr/> | <hr/> |
| Represented by: | | |
| Cash at bank held for endowment funds | 0.5 | 0.4 |
| | <hr/> | <hr/> |

The endowments were originally transferred from The Open University Foundation as at 30 May 2008.

15 DEBTORS

| | CONSOLIDATED | | UNIVERSITY | |
|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | As At 31 July 2011 £m | As At 31 July 2010 £m | As At 31 July 2011 £m | As At 31 July 2010 £m |
| Amounts falling due within one year | | | | |
| Students' loan accounts | 19.7 | 17.1 | 0.0 | 0.0 |
| Fee debtors | 0.5 | 0.9 | 0.5 | 0.9 |
| Amounts due from subsidiaries | 0.0 | 0.0 | 5.2 | 5.2 |
| Other debtors | 13.1 | 18.4 | 10.5 | 16.2 |
| | 33.3 | 36.4 | 16.2 | 22.3 |
| Prepayments and accrued income | 6.2 | 3.2 | 5.9 | 2.8 |
| | 39.5 | 39.6 | 22.1 | 25.1 |
| Amounts falling due after one year | 0.2 | 0.2 | 63.1 | 63.1 |

Students' loan accounts represent amounts due from students paying instalments under credit terms with The Open University's subsidiary company, Open University Student Budget Accounts Limited.

The University finances its two main operating subsidiaries, Open University Student Budget Accounts Limited and Open University Worldwide Limited, through long-term loans that are due for repayment or review in 2016. As at the 31 July 2011, the former subsidiary had an outstanding loan amount of £60.0 million at an interest rate equal to base rate (year ended 31 July 2010, £60.0 million). As at 31 July 2011, the latter subsidiary has an outstanding loan amount of £2.9 million at an interest rate equal to 1% over base rate (year ended 31 July 2010, £2.9 million). Under the loan agreement between the University and each subsidiary, the subsidiaries are required to lend back to the University at the same interest rate any surplus funds, as disclosed in Note 17.

There are no material debtors and prepayments denominated in currencies other than sterling.

16 GILTS AND TERM DEPOSITS

| | CONSOLIDATED | | UNIVERSITY | |
|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | As At 31 July 2011 £m | As At 31 July 2010 £m | As At 31 July 2011 £m | As At 31 July 2010 £m |
| UK gilt edged stock | 92.1 | 58.3 | 92.1 | 58.3 |
| Fixed term deposits maturing: In one year or less | 102.4 | 73.4 | 102.4 | 73.4 |
| | 194.5 | 131.7 | 194.5 | 131.7 |

The University holds tradable Treasury gilts with a redemption date of less than five years. At 31 July 2011 the weighted average redemption yield was 2.09% (year ended 31 July 2010, 2.43%) and the weighted average period to maturity was 1,015 days (year ended 31 July 2010, 880 days).

Fixed term deposits with more than 24 hours maturity at the balance sheet date are held with banks and building societies operating in the London market and licensed by the Financial Services Authority. The interest rates for these deposits are fixed for the duration of the deposit at time of placement. At 31 July 2011 the weighted average interest rate of these fixed rate deposits was 1.46% per annum (year ended 31 July 2010, 1.18% per annum) and the remaining weighted average period for which the interest rate is fixed on these deposits was 112 days (year ended 31 July 2010, 129 days). The fair value of these deposits and gilts was not materially different from the book value.

The total sum of £102.4 million includes £1.4 million in respect of expected future repayments from the administrators of the UK subsidiaries of Icelandic banks in accordance with Note 8.

The deposits shown in this note exclude accrued interest, which is included in prepayments and accrued income in Note 15.

17 CREDITORS: amounts falling due within one year

| | CONSOLIDATED | | UNIVERSITY | |
|---------------------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | As At 31 July 2011 £m | As At 31 July 2010 £m | As At 31 July 2011 £m | As At 31 July 2010 £m |
| Trade creditors | 11.2 | 12.2 | 11.1 | 12.1 |
| Student fee income in advance | 22.5 | 17.3 | 22.5 | 17.3 |
| Student fee income deferred | 45.7 | 44.6 | 45.4 | 44.5 |
| Grants and other contracts in advance | 14.6 | 11.1 | 13.9 | 10.6 |
| Other creditors and accruals | 29.1 | 30.1 | 32.5 | 32.7 |
| Amounts due to subsidiaries | 0.0 | 0.0 | 39.4 | 43.1 |
| | 123.1 | 115.3 | 164.8 | 160.3 |

A provision for fee debts of £4.2 million (year ended 31 July 2010, £3.2 million) in respect of student loans in the accounts of Open University Student Budget Accounts Limited is included in other creditors and accruals in the University's balance sheet, as the University bears the ultimate liability for the company's bad debts. Debtors in the consolidated balance sheet are shown net of the provision for bad debts.

Amounts due to subsidiaries includes surplus funds lent by the subsidiaries to the University under the terms of the loan agreements referred to in Note 15.

There are no material creditors denominated in currencies other than sterling.

18 CREDITORS: amounts falling due after more than one year

| | CONSOLIDATED | | UNIVERSITY | |
|----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| | As At 31 July 2011 £m | As At 31 July 2010 £m | As At 31 July 2011 £m | As At 31 July 2010 £m |
| Long-term loans | 61.9 | 2.1 | 60.0 | 0.0 |
| Salix revolving green fund | 0.5 | 0.4 | 0.5 | 0.4 |
| | 62.4 | 2.5 | 60.5 | 0.4 |

The Group has two long-term loan facilities.

A bank loan to the University of £60.0 million (year ended 31 July 2010, £Nil). This loan is secured on a part of the University's Walton Hall campus, denominated in sterling and repayable in October 2033. The interest margin over the London Inter-Bank Offered Rate is fixed over the life of the loan. At 31 July 2011 the interest rate on this loan was 0.8% per annum.

A bank loan to OU Properties (Bristol) Limited of £2.0 million, including £0.1 million due within one year and included in other creditors and accruals in Note 17 above, (year ended 31 July 2010, £2.2 million, including £0.1 million due within one year) is secured on a single office building, denominated in sterling and repayable in 80 quarterly instalments commencing on 1 October 2005 and ending on 1 July 2025. The rate of interest is fixed to the lender's base rate. At 31 July 2011 the interest rate on this loan was 0.7% per annum.

The Salix revolving green fund is a HEFCE backed fund to encourage investment in energy saving projects in the Higher Education sector. Funds will be repaid to Salix at the point when there are no more suitable eligible projects in which to invest.

19 PROVISIONS FOR LIABILITIES

| | CONSOLIDATED | | UNIVERSITY | |
|--------------------------------|---------------------|---------------------|---------------------|---------------------|
| | As At 2011 £m | As At 2010 £m | As At 2011 £m | As At 2010 £m |
| Early retirement scheme | | | | |
| Balance at 1 August | 2.4 | 0 | 2.4 | 0 |
| Utilised in year | (2.4) | 0 | (2.4) | 0 |
| Increase in provision | 0.0 | 2.4 | 0.0 | 2.4 |
| Balance at 31 July | 0.0 | 2.4 | 0.0 | 2.4 |

The early retirement scheme was launched in July 2010. The cost of the early retirement was estimated on the basis of applications, received and expected, that would have been agreed before the retirement date of 31 March 2011. The scheme was closed in the year.

20 DEFERRED CAPITAL GRANTS

| | CONSOLIDATED AND UNIVERSITY | | |
|---|-----------------------------|--------------|--------------|
| | Funding Bodies £m | Other £m | Total £m |
| At 1 August 2010 | | | |
| Buildings | 88.2 | 0.1 | 88.3 |
| Equipment | 0.9 | 0.6 | 1.5 |
| Total | 89.1 | 0.7 | 89.8 |
| Cash Receivable | | | |
| Buildings | 2.7 | 0.0 | 2.7 |
| Equipment | 0.0 | 0.0 | 0.0 |
| Total | 2.7 | 0.0 | 2.7 |
| Released to Income and Expenditure | | | |
| Buildings | (4.9) | 0.0 | (4.9) |
| Equipment | (0.6) | (0.3) | (0.9) |
| Total | (5.5) | (0.3) | (5.8) |
| At 31 July 2011 | | | |
| Buildings | 86.0 | 0.1 | 86.1 |
| Equipment | 0.3 | 0.3 | 0.6 |
| Total - see Note 12 | 86.3 | 0.4 | 86.7 |

21 ENDOWMENTS

| | CONSOLIDATED AND UNIVERSITY | | |
|---------------------------|--------------------------------|---------------------|---------------------|
| | Restricted Expendable £m | 2011 Total £m | 2010 Total £m |
| Balance at 1 August | | | |
| Capital | 0.5 | 0.5 | 0.5 |
| Accumulated expenditure | (0.1) | (0.1) | 0.0 |
| | <u>0.4</u> | <u>0.4</u> | <u>0.5</u> |
| Additions | 0.1 | 0.1 | 0.0 |
| Expenditure | 0.0 | 0.0 | (0.1) |
| | <u>0.5</u> | <u>0.5</u> | <u>0.4</u> |
| Balance at 31 July | 0.5 | 0.5 | 0.4 |
| Represented by: | | | |
| Capital | 0.5 | 0.5 | 0.5 |
| Accumulated expenditure | 0.0 | 0.0 | (0.1) |
| | <u>0.5</u> | <u>0.5</u> | <u>0.4</u> |

22 RESERVES

| | CONSOLIDATED UNIVERSITY | |
|--|-------------------------|--------------|
| | £m | £m |
| REVALUATION RESERVE | | |
| At 1 August 2010 | 4.3 | 4.3 |
| Transfer to general funds | | |
| Contributions to depreciation released in the year | (0.9) | (0.9) |
| | <u>3.4</u> | <u>3.4</u> |
| At 31 July 2011 | 3.4 | 3.4 |
| GENERAL FUNDS | | |
| At 1 August 2010 | 161.8 | 161.2 |
| Surplus for the year including exceptional items | 49.1 | 49.2 |
| Transfers from revaluation reserve | 0.9 | 0.9 |
| | <u>211.8</u> | <u>211.3</u> |
| At 31 July 2011 | 211.8 | 211.3 |

**23 RECONCILIATION OF SURPLUS BEFORE TAX
TO NET CASH INFLOW FROM OPERATING ACTIVITIES**

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|--|----------------------------------|----------------------------------|
| Surplus for the year before tax after exceptional item | 49.1 | 26.2 |
| Depreciation | 10.6 | 11.8 |
| Profit on disposal of fixed asset | (1.1) | (0.5) |
| Impairment of fixed assets | 0.1 | 0.3 |
| Deferred capital grant released to income | (5.8) | (6.0) |
| Endowment and investment income | (3.9) | (3.3) |
| Interest payable and other financial costs | (0.1) | 0.0 |
| Decrease / (increase) in stock | 0.2 | (0.6) |
| Decrease / (increase) in debtors | 0.8 | (2.0) |
| Increase in creditors | 8.4 | 0.9 |
| (Decrease) / increase in provisions | (2.4) | 2.4 |
| | 55.9 | 29.2 |

24 RECONCILIATION TO NET FUNDS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|---|----------------------------------|----------------------------------|
| Increase / (Decrease) in cash in the year | 58.4 | (6.6) |
| Movement in deposits | 62.8 | 39.6 |
| Movement in endowments | 0.1 | (0.1) |
| Movement in bank debt | (59.8) | 0.1 |
| Change in net funds | 61.5 | 33.0 |
| Net funds at 1 August | 147.7 | 114.7 |
| Net funds at 31 July | 209.2 | 147.7 |

25 ANALYSIS OF CHANGES IN NET FUNDS

| | At 1 August 2010 £m | Cash flows £m | Non cash movements £m | At 31 July 2011 £m |
|--------------------------|---------------------------|---------------------|-----------------------------|--------------------------|
| Cash at bank and in hand | 17.7 | 58.4 | 0.0 | 76.1 |
| Endowment assets | 0.4 | 0.1 | 0.0 | 0.5 |
| Fixed term deposits | 131.7 | 64.2 | (1.4) | 194.5 |
| Loans | (2.1) | (59.8) | 0.0 | (61.9) |
| Total | 147.7 | 62.9 | (1.4) | 209.2 |

26 CONTINGENCIES

Following the decision of the House of Lords in the Conde Nast/Fleming case and in common with many other organisations, a claim has been submitted on behalf of the University for the repayment of VAT incurred over the period 1973 to 1994, along with associated interest. In July 2011, Her Majesty's Revenue and Customs agreed the claim for the period 1973 to 1974. The amount of £0.7 million was received in October 2011 and has been treated as an exceptional item (see Note 10). The University considers that there are too many uncertainties for any reasonable estimate of the remaining amounts potentially recoverable to be calculated.

27 COMMITMENTS

LEASEHOLD PROPERTIES

During the year ended 31 July 2011 the Group paid £2.9 million (year ended 31 July 2010, £3.5 million) in respect of operating leases for long-leasehold properties.

The Group has obligations for annual payments under non-cancellable operating leases in respect of long-leasehold properties as follows:

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|-----------------------|----------------------------------|----------------------------------|
| Expiring: | | |
| within 1 year | 0.3 | 0.1 |
| between 2 and 5 years | 0.8 | 0.5 |
| over 5 years | 1.8 | 2.9 |
| Total | <u>2.9</u> | <u>3.5</u> |

A number of the property leases are subject to periodic rent reviews.

28 AMOUNTS DISBURSED AS AGENT

The Funding Council and TDA grants and bursaries set out below are available solely for students: the University acts only as paying agent. The grants and bursaries and related disbursements are therefore excluded from the Income and Expenditure Account; the balances carried forward are included in both current assets and in creditors falling due within one year and so there is no effect on net current assets. The separate HEFCE, SFC, HEFCW and TDA grants for the costs of administering the above items are included in the Income and Expenditure Account.

HEFCE ACCESS FOR LEARNING

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|-------------------------|----------------------------------|----------------------------------|
| Balance brought forward | 0.0 | 0.0 |
| Funding Body Grants | 6.6 | 7.2 |
| Disbursed to Students | (6.6) | (7.2) |
| Balance carried forward | <u>0.0</u> | <u>0.0</u> |

28 AMOUNTS DISBURSED AS AGENT (continued)

SFC ACCESS FUNDS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|-------------------------|----------------------------------|----------------------------------|
| Balance brought forward | (0.1) | (0.1) |
| Funding Body Grants | 3.1 | 2.5 |
| Disbursed to Students | (2.8) | (2.5) |
| | <hr/> | <hr/> |
| Balance carried forward | 0.2 | (0.1) |
| | <hr/> | <hr/> |

HEFCW ACCESS FUNDS

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|-------------------------|----------------------------------|----------------------------------|
| Balance brought forward | 0.1 | 0.1 |
| Funding Body Grants | 0.1 | 0.2 |
| Disbursed to Students | (0.1) | (0.2) |
| | <hr/> | <hr/> |
| Balance carried forward | 0.1 | 0.1 |
| | <hr/> | <hr/> |

TDA TRAINING BURSARIES

| | Year Ended 31 July 2011 £m | Year Ended 31 July 2010 £m |
|-------------------------|----------------------------------|----------------------------------|
| Balance brought forward | (0.1) | 0.3 |
| TDA Grants | 1.7 | 0.9 |
| Disbursed to Students | (1.4) | (1.3) |
| | <hr/> | <hr/> |
| Balance carried forward | 0.2 | (0.1) |
| | <hr/> | <hr/> |

29 RELATED PARTY TRANSACTIONS

Due to the nature of the University's operations and the composition of the Council (being drawn from both public and private sector organisations) it is inevitable that transactions will take place with organisations in which a member of Council may have an interest. All transactions in which a member of Council may have an interest are conducted at arm's length and in accordance with the University's financial regulations and normal procurement procedures.

The Standing Orders of the University's Council specify that one member shall be drawn from the Open University Student's Association (OUSA), a charity independent from the University that supports the University's students, in addition to the President of OUSA. The University provides funding to OUSA, which is shown in Note 7 on page 41.

No other material transactions have taken place.

30 PENSION SCHEMES

The University participates in the Universities Superannuation Scheme (USS), a defined benefit scheme which is contracted out of the State Second Pension (S2P). The assets of the scheme are held in a separate fund administered by the trustee, Universities Superannuation Scheme Limited. A small number of employees are also members of defined contribution schemes.

Defined Contribution Schemes

A small number of employees are members of the Federated Superannuation System for Universities (FSSU), which is administered by trustees and has assets independent of the University.

A small number of employees in the Republic of Ireland are members of The Open University Retirement Solution Plan. It is established under irrevocable trusts, of which the University is a co-trustee.

A small number of overseas based employees are members of defined contribution schemes in the countries in which they are employed.

The total pension cost for all these defined contribution schemes was £0.1 million (year ended 31 July 2010, £0.1 million).

Defined Benefit Scheme

Universities Superannuation Scheme

The University participates in the Universities Superannuation Scheme (USS), a defined benefit scheme which is externally funded and contracted out of the State Second Pension (S2P). The assets of the scheme are held in a separate fund administered by the trustee, Universities Superannuation Scheme Limited. The appointment of directors to the board of the trustee is determined by the Company's Articles of Association. Four of the directors are appointed by Universities UK; three are appointed by the University and College Union, of whom at least one must be a USS pensioner member; one is appointed by the Higher Education Funding Councils; and a minimum of two and a maximum of four are co-opted directors appointed by the management committee. Under the scheme trust deed and rules, the employer contribution rate is determined by the trustee, acting on actuarial advice.

The University is unable to identify its share of the underlying assets and liabilities of the scheme on a consistent and reasonable basis and therefore, as required by FRS 17, *Retirement Benefits*, accounts for the scheme as if it were a defined contribution scheme. As a result, the amount charged to the expenditure account represents the contributions payable to the scheme in respect of the accounting period.

The latest actuarial valuation of the scheme was at 31 March 2008. This was the first valuation for USS under the new scheme-specific funding regime introduced by the Pensions Act 2004, which requires schemes to adopt a statutory funding objective, which is to have sufficient and appropriate assets to cover their technical provisions.

The valuation was carried out using the projected unit method. The assumptions which have the most significant effect on the result of the valuation are those relating to the rate of return on investments (i.e. the valuation rate of interest), the rates of increase in salary and pensions and the assumed rates of mortality. In relation to the past service liabilities the financial assumptions were derived from market yields prevailing at the valuation date. It was assumed that the valuation rate of interest would be 6.4% per annum (which includes an additional assumed investment return over gilts of 2% per annum), salary increases would be 4.3% per annum (plus an additional allowance for increases in salaries due to age and promotion and a further amount of £1.35 billion of liabilities to reflect recent experience) and pensions would increase by 3.3% per annum. In relation to the future service liabilities it was assumed that the valuation rate of interest would be 6.1% per annum, including an

30 PENSION SCHEMES (continued)

additional investment return assumption of 1.7% per annum, salary increases would be 4.3% per annum (also plus an allowance for increases in salaries due to age and promotion) and pensions would increase by 3.3% per annum.

Standard mortality tables were used as follows:

| | |
|---------------------------|--|
| Pre-retirement mortality | PA92 MC YoB tables – rated down 1 year for males; no age rating for females. |
| Post-retirement mortality | PA92 MC YoB tables – rated down 1 year for males; no age rating for females. |

Use of these mortality tables reasonably reflects the actual USS experience but also provides an element of conservatism to allow for further small improvements in mortality rates. The assumed life expectations on retirement at age 65 are:

| | |
|-----------------------------------|-------------------|
| Males (females) currently aged 65 | 22.8 (24.8) years |
| Males (females) currently aged 45 | 24.0 (25.9) years |

At the valuation date, the value of the assets of the scheme was £28,842.6 million and the value of the scheme's technical provisions was £28,135.3 million indicating a surplus of £707.3 million. The assets therefore were sufficient to cover 103% of the benefits which had accrued to members after allowing for expected future increases in earnings.

The actuary also valued the scheme on a number of other bases as at the valuation date. On the scheme's historic gilts basis, using a valuation rate of interest in respect of past service liabilities of 4.4% per annum (the expected return on gilts) the funding level was approximately 71%. Under the Pension Protection Fund regulations introduced by the Pensions Act 2004 it was 107% funded; on a buy-out basis (i.e. assuming the Scheme had discontinued on the valuation date) the assets would have been approximately 79% of the amount necessary to secure all the USS benefits with an insurance company; and using the FRS17 formula as if USS was a single employer scheme, the actuary estimated that the funding level would have been approximately 104%.

Since 31 March 2008 global investment markets have continued to fluctuate and as at 31 March 2011 the market's assessment of inflation has increased slightly. The government has also announced a change to the inflation measure used in determining the official pension's index from the Retail Prices Index to the Consumer Prices Index. The actuary has taken this all into account in his funding level estimates at 31 March 2011 by reducing the assumption for pension increases from 3.3% to 2.9%. The actuary has estimated that the funding level under the scheme specific funding regime had fallen from 103% as at 31 March 2008 to 98% as at 31 March 2011 (a deficit of approximately £700 million). Over the past twelve months, the funding level has improved from 91%, as at 31 March 2010 to 98%. This estimate is based on the funding level at 31 March 2008, adjusted to reflect the fund's actual investment performance over the three years and changes in market conditions (market conditions affect both the valuation rate of interest and also the inflation assumption which in turn impacts on the salary and pension increase assumptions). The next formal valuation is as at 31 March 2011 and this will incorporate updated assumptions agreed by the trustee company. With effect from 1 October 2011, new joiners to the scheme will join the new revalued benefits section rather than existing final salary section. This change will have an impact, expected to be positive, on the future funding levels. On the FRS 17 basis, using an AA bond discount rate of 5.5% based on spot yields, the actuary estimated that the funding level at 31 March 2011 was 86%. An estimate of the funding level measured on a buy-out basis at that date was approximately 54%.

Surpluses or deficits which arise at future valuations may impact on the University's future contribution commitment. A deficit may require additional funding in the form of higher contribution requirements, where a surplus could, perhaps, be used to similarly reduce contribution requirements.

30 PENSION SCHEMES (continued)

The sensitivities regarding the principal assumptions used to measure the scheme liabilities on a technical provisions basis as at the date of the last triennial valuation are set out below:

| Assumption | Change in Assumption | Impact on scheme liabilities |
|----------------------------|---|-------------------------------------|
| Valuation rate of interest | Increase/decrease by 0.5% | Decrease/increase by £2.2 billion |
| Rate of pension increases | Increase/decrease by 0.5% | Increase/decrease by £1.5 billion |
| Rate of salary growth | Increase/decrease by 0.5% | Increase/decrease by £0.7 billion |
| Rate of mortality | More prudent assumption (Mortality used at last actuarial valuation, rated down by a further year for male members) | Increase by £1.6 billion |

USS is a “last man standing” scheme so that in the event of the insolvency of any of the participating employers in USS, the amount of any pension funding shortfall (which cannot otherwise be recovered) in respect of that employer will be spread across the remaining participant employers and reflected in the next actuarial valuation of the scheme.

The trustee believes that, over the long-term, equity investment and investment in selected alternative asset classes will provide superior returns to other investment classes. The management structure and targets set are designed to give the fund a bias towards equities through portfolios that are diversified both geographically and by sector. The trustee recognises that it would be possible to select investments producing income flows broadly similar to the estimated liability cash flows. However, in order to meet the long-term funding objective within a level of contributions that it considers the employers would be willing to make, the trustee has agreed to take on a degree of investment risk relative to the liabilities. This taking of investment risk seeks to target a greater return than the matching assets would provide whilst maintaining a prudent approach to meeting the fund’s liabilities. Before deciding to take investment risk relative to the liabilities, the trustee receives advice from its investment consultant and the scheme actuary, and considers the views of the employers. The strong positive cash flow of the scheme means that it is not necessary to realise investments to meet liabilities. The trustee believes that this, together with the ongoing flow of new entrants into the scheme and the strength of covenant of the employers enables it to take a long-term view of its investments. Short-term volatility of returns can be tolerated and need not feed through directly to the contribution rate. The actuary has confirmed that the scheme’s cash flow is likely to remain positive for the next ten years or more.

The next formal triennial actuarial valuation is due as at 31 March 2011. The contribution rate will be reviewed as part of each valuation.

The total pension cost for the University was £31.1 million (year ended 31 July 2010, £30.5 million). This includes £2.3 million outstanding contributions as at 31 July 2011 (year ended 31 July 2010, £2.5 million). Of the total pension cost, £2.8 million (year ended 31 July 2010, £2.8 million) related to costs in respect of early retirement.

Independent Auditors **PricewaterhouseCoopers LLP**
Chartered Accountants and Registered Auditors
Exchange House
Central Business Exchange
Midsummer Boulevard
Milton Keynes
MK9 2DF

Bankers **Royal Bank of Scotland Plc**
2nd Floor
152 Silbury Boulevard
Milton Keynes
Bucks
MK9 1LT

Investment Managers **BlackRock Investment Managers**
33 King William Street
London
EC4R 9AS

Insight Investment Management Ltd
33 Old Broad Street
London
EC2N 1HZ

Solicitors **Eversheds LLP**
Senator House
85 Queen Victoria Street
London
EC4V 4JL

Shoosmiths
1st Floor
Witan Gate House
500-600 Witan Gate West
Milton Keynes
MK9 1SH

Travers Smith
10 Snow Hill
London
EC1A 2AL

Stockbrokers **Barclays Wealth**
Tay House
300 Bath Street
Glasgow
G2 4LH

Taxation Advisors **KPMG LLP**
2 Cornwall Street
Birmingham
B3 2DL



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