

How HEFCE takes account of full economic costs in the funding we distribute for higher education

1. We expect the higher education institutions (HEIs) we fund to know and to seek to recover the full economic costs of their activities, in aggregate. The Financial, Memorandum between HEFCE and HEIs states¹:

Costing and pricing of activities

Institutions should know and understand the full economic costs of the activities² that they undertake, and this information should be taken into account within their management decision-making processes.

Institutions should seek to recover the full economic costs of all their activities, whether pricing is determined by reference to those full economic costs or by reference to prevailing market conditions. While there may be cases for individual projects or activities to be priced below their full economic costs, this should be done as a conscious decision, within the context of strategic objectives. Institutions are expected, taking one year with another, to recover, **in aggregate**, the full economic costs of all their activities across the full range of their activities.

The Council does not expect HEFCE funds to be used to subsidise non-public activities.

2. These requirements placed on HEIs apply to all activities, whether funded from public or private sources.

3. A number of public organisations have already stated their commitment to provide funding based on full economic costs, as determined by the Transparent Approach to Costing (TRAC) methodology. For example, government departments have been instructed by the Treasury that they should expect to pay at least 100 per cent of the full costs of the research they commission from HEIs³.

4. It is therefore right that we should set out how we will take account of full economic costs in the funding that we distribute for higher education.

¹ HEFCE 2003/54 paragraphs 68 to 70.

² 'Activities' in this context refers to the five categories of activities as defined for reporting under the Transparency Review (publicly funded teaching, non-publicly funded teaching, publicly funded research, non-publicly funded research, and other).

³ This can be found at www.ost.gov.uk/research/dualsupport.htm

Basis of the HEFCE approach

5. There is no single approach to taking account of full economic costs within our funding. So, for example, there are differences depending on whether the money is core funding for learning and teaching, widening participation and research; or non-core funding for particular activities; or where we are paying for a service. These differences are covered in more detail below. There is an assumption that activity will be maintained, but this is subject to sufficient funds being available.

Core funding

6. Core funding for learning and teaching, widening participation and research is provided to achieve the outcomes and objectives set out in the HEFCE strategic plan⁴. This funding is provided as a block grant and there is no direct link to the activities undertaken by HEIs to deliver the outputs, in terms of students or research, for which they are accountable.

7. As such, core funding contributes towards the total costs of the activities undertaken, but there will be other funding sources that also contribute to these costs. For example:

- tuition fees contribute to the full costs of learning and teaching
- Research Councils contribute 80 per cent of the full costs of research projects that they commission, with the remaining 20 per cent being met from the HEIs' other income streams, which could include HEFCE core research funding.

8. In our discussions with Government over the funding requirements of higher education, we will seek to secure levels of public funding for higher education that are sufficient to meet the full costs of activities for a specific volume, in aggregate, recognising that there may be other income streams for these activities.

Non-core funding

9. We do not intend to introduce changes to existing non-core funding programmes, but would do so for future rounds of existing programmes or for new programmes, where such changes are applicable.

10. There are two different approaches to these programmes, reflecting their different circumstances:

- Where the programme provides an allocation to all HEIs. This is similar to the approach for core funding, with allocations being determined by HEFCE. HEIs should identify the full costs of the activity and how any gap in funding would be met from within their total resources.

⁴ HEFCE 2003-08 strategic plan, HEFCE 2003/17 (updated April 2004 and April 2005).

- Where funding is not provided to all HEIs. In some cases we provide funding to achieve particular objectives, such as to develop best practice so that this can be disseminated widely across the sector. In these cases the HEI undertaking the work will benefit. HEIs should again identify the full economic costs of the activity. However, any funding proposals to us should take account of the benefits that will flow to the HEI if the funding proposal is successful.

11. In other cases, such as Strategic Development Fund projects, we are responding to proposals from HEIs. The criteria to assess such proposals will include that they support the objectives in our strategic plan, and that a sustainable business case can be demonstrated. Where proposals meet all the criteria and are accepted as fundable, and where the gains are for more than one HEI, or where there are wider benefits that could not be secured without funding, grants could be provided on a non-repayable basis. Where the gain or benefit is clearly solely to the HEI applying for funding, any grants would be on a repayable basis.

Provision of services to the higher education sector

12. In a few cases, we fund the provision of a service that benefits the whole higher education sector. The benefits that accrue to the provider are very small, or none, compared with those gained through the grant-funded programmes described in the previous section. The services are also likely to be additional to normal activity.

13. In these circumstances, we will meet the full costs of providing these services. We will introduce changes when contracts come up for renewal or when new services are sought.

July 2005