Summary of conclusions and recommendations

Overview

1. We propose the creation of a consistent national framework for the collection of cost information to support HEFCE funding policies for Teaching, including the operation of the TFM. The most viable and least burdensome way to deliver this is through the existing framework of TRAC, which is already established in all UK HEIs. The additional information required would be in six cost areas needed to support the allocation of funding to institutions, and to inform institutional good management:

   - discipline (including non-completion)
   - widening participation
   - non-standard or high-cost delivery (course costing)
   - part-time provision
   - high cost base institutions
   - specific initiatives.

2. In each area, we identify a viable cost model which could deliver consistent national data to support the funding of Teaching, and which could also support institutions' needs for information for good management. In some areas several cost drivers are covered in the cost model, in others only one. But not all potential cost drivers are included: some are not significant; or not sufficiently independent of the others; others are too complex or burdensome to justify their use. For example, the level of study and year of programme are not sufficiently significant independent drivers of costs across the sector to justify collecting them on a national basis to inform the TFM (although of course individual institutions might choose to do so). This selection of cost drivers does not, however, mean that any costs would be excluded or ignored.

3. This new costing data would provide information that institutions increasingly need for their own purposes, such as fee-pricing and internal resource allocation. It would require some extension to TRAC processes. By covering Teaching, TRAC data and processes would become more useful to institutions, and more robust for research costing. There would be a burden, but with appropriate design this could be very much less significant than the burden institutions are currently incurring in respect of TRAC/fEC for Research. The benefits of better understanding of the costs of Teaching, and better allocation of resources and management of provision, would apply to all institutions and to over £4 billion of public expenditure.

The case for better cost information

4. The problem these proposals address is that the core business of higher education has not yet benefited from the type of improved financial management information that is now available for Research. The current TFM is informed by costs, but these are mostly imperfect, or are proxies for cost. The total costs of sustainable Teaching at institutional or sector level are not

known (and this inhibits HEFCE's ability to make the case for funding). The cost impact of policies such as WP, or foundation degrees, have been studied, but by one-off partial costing exercises, so HEFCE has not had the benefit of a comprehensive or holistic view of the full economic costs. Similarly, institutions find themselves making decisions about their portfolio and bidding for strategic initiatives without the sound knowledge of the full long-run cost implications.

5. The introduction of TRAC, since the present TFM was designed, provides an opportunity (if transactional costs and benefits justify this) to move towards a more directly cost-based approach for the TFM, and to use much better cost information to inform HEFCE and institutional policies. A parallel development is happening in respect of Research.

6. Improved information on costs could better inform HEFCE policy for Teaching and the funding of Teaching in three main areas, which we call cost objectives. These are illustrated in Figure (i) at the end of this chapter.

   a. Cost objective I: informing the total costs of sustainable Teaching, at sector and institutional level (to inform the needs for public funding).

   b. Cost objective II: providing data to inform the allocation of funding to institutions – either formulaically through the TFM, or through strategic initiatives or other one-off funding.

   c. Cost objective III: informing institutions and other stakeholders about costs of Teaching, to encourage more strategic thinking about their portfolio, and to encourage efficiency and innovation.

7. The total cost of sustainable Teaching is a central policy concern for HEFCE, and the additional burden of providing this information is very small – needing only fine-tuning of the existing TRAC annual reporting process. There is also a justification in respect of good management of £4 billion of public expenditure.

8. The main focus of our report is on objectives (II and III) – is it feasible to collect robust data on costs from institutions and to use this to inform the current TFM, and possible future TFMs? How could this be done? Is the burden of doing this justified by the benefits that would be gained? Would institutions find these same data useful for good management purposes?

9. In approaching these questions, we have assumed that, as a matter of principle, HEFCE should avoid asking for data which institutions do not need for their own management purposes, and that provision of information to support funding should therefore only use data that is also relevant to managing within institutions.

Policy context

10. In chapters 1 and 2, we summarise the policy background to this study, and the environment for greater use of costs in the TFM. We note that there is in

practice a spectrum of ways in which costs can inform funding (see Figure (ii) at the end of this chapter). We call the more direct cost to funding relationships cost-based funding, and the less direct, cost-informed funding. HEFCE will probably have to continue to operate with a mixture of these, although at all parts of the spectrum there is scope for making better use of costs to inform funding.

11. If the future funding of Teaching is viewed as a ‘three-box’ model, like those discussed in chapter 3 and illustrated in Figure (i), we could identify that:

    a. Discipline is the universal cost driver in the standard delivery box’ that covers the ’normal UK HE student experience’ incorporating a range of diverse experiences and environments (WP, relationships with Research, scholarship, differing size and style of institutions) and covers the significant part of all the costs of Teaching.

    b. The extra costs of ‘non-standard’ or ’exceptional levels of’ WP, non-standard delivery, part-time (PT), and high cost base are factors that, while relatively small in national terms, are important for policy, and where institutions need to know that their extra costs are recognised. These might be funded as ‘contract variations’ in the non-standard delivery box.

    c. Strategic initiatives would be in the non-recurrent one-off funding box.

12. The shape of any future TFM is not central to our remit, but will set the context within which improved cost information will be used. We conclude that the sector is likely to continue to evolve in the direction of a more market-based system, with HEFCE block grant funding representing a decreasing part of institutions’ total financing package. The role of HEFCE funding, and of the TFM, may change accordingly. It would be helpful if improved cost information could support the current type of multi-tariff TFM (where funding is driven by several cost drivers or cost weighting factors) and also a hypothetical, more streamlined and market-based kind of TFM that might be introduced in the medium term.

13. An important part of the policy context relates to the possible greater use of credits as a means to measure (and possibly fund) student achievement. A parallel study is looking at this.

14. At one level, the implications are modest since any decision by HEFCE to use credit as a volume measure in a future TFM need not imply that different costing methods would be required. The cost models we propose could operate (possibly with minor adjustments) equally effectively were a finer-grained measure of volume to be introduced. For example:

    a. Part-time and long course distinctions would be less meaningful, but the concept that the former requires a proportionately higher share of indirect costs (and the latter perhaps less) would remain equally valid.

    b. The definition and measurement of completion would change, and this would have significant implications for the non-completion cost model.

However, this model has yet to be developed and the appropriate definitions of completion would be built into its design.

c. As we do not propose a course costing model that covers all modules or programmes in institutions, the ability to cost more easily at this level (with a credit-based framework) would have little impact.

15. Overall, therefore, we do not see a switch to credit-based funding as problematic for the costing proposals we are making. However, that is not to say that a switch to credit-based funding would be cost-free. There could be additional cost implications for institutions, both in terms of the costs of reporting and measuring achievement at a more detailed level, and, more significantly, in terms of possible changes in student behaviour. If students took advantage of the freedom to switch in and out of programmes much more frequently, or wished to take more intensive accelerated courses, there would be clear resource implications for institutions.

Costing principles and cost drivers

16. In chapter 3, we define the costing approaches that are appropriate to serving the three purposes for improved cost information. We specify, at a high level, that cost methods should:

- follow TRAC principles
- be designed to fit as closely as possible with institutions' own needs and processes, rather than being one-off exercises
- provide an improvement over current information
- generally cover the whole sector (since all institutions need to understand their costs) – but in a few cases a sample may be appropriate.

17. In respect of more specific costing principles where some choices are open to HEFCE, we recommend that costs in the consistent national framework should:

a. be based on <u>absolute costs</u>, although relative costs and proxies will be useful in selected applications

b. be based on <u>full economic costs</u> not marginal or partial costs

c. be based on <u>historical costs (actual costs)</u> rather than theoretical or planned costs. Issues of efficiency should be addressed through related techniques including benchmarking and critical analysis. Planned costs will be needed for new initiatives

d. in the cases of new ventures or initiatives, be based on <u>whole-life costs</u>. TRAC full economic costs already include the cost of normal innovation and product development of existing activity

e. be designed to help institutional managers to understand their cost structure – such as distinguishing between fixed, variable, and semi-variable costs where appropriate

f. combine bottom-up and top-down costing approaches as appropriate.

18. We review a list of over 20 cost drivers which might be considered relevant to the TFM (or have been suggested to us). The criteria we use are that any cost drivers that HEFCE could consider using in a national framework for costing would have to be:

   a. relevant to policy features sought by HEFCE funding

   b. significant in terms of the level of costs they actually influence

   c. viable for use by HEFCE in terms of the balance of burden (or effort) they would require in relation to the benefits delivered.

19. We conclude that a reduced number of drivers should be directly incorporated into the new national framework. These all fall within the six cost models we have already noted and they are summarised in Figure (iii), found at the end of this chapter. A number of cost drivers are, therefore, not to be used directly, including specialist institutions; level of study; year of programme; complexity; (in)efficiency. The impact of these on costs is taken into account through other cost drivers or approaches, and we set out the reasoning for these decisions in chapter 3 and Appendix B.

Viable costing approaches

Total costs of Teaching and sustainability

20. In chapter 4, we show that information on the total costs of Teaching can be derived from existing TRAC processes with some minor changes in TRAC guidance to institutions around the separation of publicly funded and non-publicly funded Teaching. This can provide the total cost (and income) of HEFCE-funded Teaching for every HEI, and at sector level.

21. A potential issue is that some institutions with low research activity can invoke a dispensation which allows them to use simplified TRAC processes and this could affect data quality. We suggest that the terms of this should be revisited so that the threshold is made inclusive of Non-Publicly Funded Research and Other, but that the concept of a dispensation should remain.

22. Consistent sector-wide information on this cost objective will therefore be based on historical costs, as this is the only feasible approach. This is not ideal for HEFCE in terms of making a case for the total public funding required, or demonstrating and promoting efficiency and innovative approaches to delivery. However, these policy features can be supported by information derived from a periodic review of the appropriateness and variability of actual costs using techniques like benchmarking and critical analysis.

23. In terms of burden, this is a feasible and low-cost change to TRAC. Much of what is required is already being done by institutions, and the main change would be some restructuring of the costing models which would be done within institutions' finance departments. If spread over two-to-three years, this would be a very modest change. HEFCE will need to consider how it wishes to manage the benchmarking and critical analysis process, but benchmarking is already a requirement as part of TRAC/fEC and, overall, this change should not be burdensome. Benchmarking and critical analysis would also significantly benefit institutions' own understanding of their costs and is likely to be welcomed by many in the sector.

Information to support the TFM and good practice

24. In chapter 5, we propose six viable cost models (sometimes a single proposal, sometimes a series of options) that might inform the TFM and institutional good practice, and we suggest how each can be used by HEFCE to provide a better cost-based (or cost-informed) approach to its funding of Teaching. These proposals and options are necessarily detailed and technical in some places in order to test and demonstrate the feasibility of proposed methods. These cost models (in broadly descending order of the significance of the cost drivers they include) are:

- discipline (including non-completion)
- widening participation
- non-standard or high-cost delivery (course costing)
- part-time provision
- high cost base institutions
- specific initiatives.

25. **Discipline** is the strongest single driver of most Teaching costs in the current TFM, and it is logical that it should be the central common cost driver for all aspects of provision which are delivered across the whole sector, to a broadly comparable UK standard HE student experience. Unfortunately, it is not possible to write a specification of this experience, or therefore to cost this standard provision *ab initio* or bottom-up. However, there is a practical way to ring-fence this core discipline-driven education, which is to treat it as the residual (albeit largest) element after the other (smaller) cost elements have been eliminated (this is illustrated in Figure (iv) at the end of this chapter).

26. We define viable methods to calculate a discipline-related cost per student FTE for each cost centre, which could then be used by HEFCE to identify price bands. There are a number of costing issues to be resolved in achieving this, but none serious enough to make the methods impractical. New combined estates and indirect cost rates could be produced from this process (one for laboratory subjects, and one for non-laboratory) which would help institutions in other areas of the cost model (in particular, strategic initiatives).

27. The major issues are around the definition of disciplines, and the non-alignment of the units of measurement used by TRAC and the Higher Education Statistics Agency (HESA). The HESA approach is clearly the preferred method for identifying student numbers by cost centre, but institutions have TRAC costs at (institutionally-defined) department level, not

at HESA cost centre level. It would be a significant task for most institutions to reconfigure their costs robustly by HESA cost centre, with little benefit to institutions, and we do not think the burden of this would be justified. We therefore propose that most institutions would only provide robust cost data at price group level (not cost centre) on an annual basis. A smaller sample of volunteer or marker institutions could be used to provide more disaggregated data at cost centre level on a periodic basis to inform the allocation of cost centres to price groups.

28. The burden here would again be modest. A few institutions may not have robust academic time data at the level of all HEFCE price bands, and they would need to improve their time allocation to cost at this level. Some reconfiguring of cost models by the finance department may be required. The marker institutions would incur some additional work, but following experience with the TRAC pilot institutions, we expect that HEFCE would be able to find a few institutions who were interested in being more involved in this way, perhaps with some financial assistance.

29. **Non-completion** is an important element of the residual discipline costs which should, arguably, influence the TFM. However, there are difficulties here in terms of definitions and understanding of the cost drivers, as well as data quality, and it is too early to make a recommendation on the viability of this. For these reasons, we recommend that a study is done of the costs of non-completion, and, in the meantime, this is treated as a good management cost objective, not as one of the consistent national cost drivers to inform the TFM. There would, therefore, be no direct burden for institutions.

30. After discipline, **widening participation** is the largest and most significant driver of costs, and it is also a high policy priority. A detailed costing study of WP was completed very recently (2004) and this provides information on total costs to inform policy, and a framework of cost methods.

31. Given the high costs and importance of WP, we believe that HEFCE would be justified (a) in seeking to gain some further improvements in the cost data available for funding, and (b) in encouraging institutions to understand their costs better. We propose a menu of viable costing options, from which HEFCE and the sector could choose. These could provide increasing benefits, at the cost of increasing levels of effort. The more limited options would impose no new burdens.

32. The minimum option is probably to require institutions to assess their relative cost level for WP compared to the findings of the 2004 study. But we suggest that there would be clear benefits in doing more than this, including institutions identifying their own absolute levels of costs; some detailed national studies of aspects of WP; and studies of ‘should-be’ costs. These might require a few weeks’ work for a member of the finance department, and involve discussions with academics and senior managers. We believe that many institutions would be willing to put some effort into understanding these important costs better.

33. **Non-standard delivery** is an important part of the diversity and flexibility which HEFCE wishes to encourage. In practice, the costs of non-standard delivery that HEFCE would probably identify separately in the TFM are

relatively low (the volume is low), and an argument could be made that they could just be absorbed within the two large cost factors discussed above. However, it is important that institutions should not perceive a disincentive to diversity and flexibility, and so it is worth costing these factors, even if their absolute magnitude is modest. HEFCE already allocates premiums to certain aspects of this delivery (such as foundation degrees). We propose a course costing model that can be used to cost non-standard delivery.

34. This does not mean that institutions would be required to cost all courses. We are not proposing universal course or module costing. We are proposing that a consistent approach should be made available for the sector to use to cost any particular course or module, should they want to. HEFCE could use this cost model to identify non-standard methods of delivery which are driven by circumstances other than those inherent to a discipline, where the costs are materially and systematically different. The cost model could be used to address four of the identified cost drivers which relate to:

- non-standard forms of delivery (such as foundation degrees)
- high cost provision (such as courses at institutions with unusual pedagogic provision)
- strategically-important subjects with low student numbers
- long courses.

35. The costs of these can all inform the TFM, although in different ways. Course costing is also a key objective for internal management purposes in many institutions, and they will benefit from being provided with a consistent framework for doing this.

36. We recommend a cost model which would identify the cost per student of a particular existing course. This would be done by reference to a standard average course for the relevant discipline group, noting any significant variations. HEFCE would need to decide how far this method was to be incorporated into the consistent national costing framework – institutions could, for example, subsume the costs of this provision in their discipline costs; or use premiums as a proxy to identify the costs of this provision; or they could be required to carry out detailed costing using the course costing model.

37. The burden here could be very small, and could be limited to a small number of institutions. For example, HEFCE might choose not to make any mandatory requirements at all (TFM premiums could be based on existing cost data). Instead it could offer a standard approach to course costing for institutions to take up as they wished, but with the understanding that where there was a case to be made for elevated funding, institutions would have to use this method.

38. The approach we suggest for costing **part-time provision** is very similar. Part-time provision is very significant in volume terms, but the extra or additional costs of part-time students to institutions are relatively small across the sector as a whole. They have been studied recently, and a further Universities UK study is currently underway. Discussions about credit will have a bearing on how this operates in future.

39. The issue for this study is therefore about how best to identify the additional elements of cost which are incurred by all part-time students, and which are relatively more significant at lower FTE proportions (so higher for a 0.1FTE student than for a 0.8FTE). Here we propose options which HEFCE and the sector can consider. Much of the work can be done outside of institutions (that is, by HEFCE) and institutions can be provided with alternative standard models against which to compare their provision.

40. In respect of the **high cost base institutions**, we propose that existing TRAC principles are used when HEFCE chooses to review or update the existing premiums or weighting factors for elements such as London weighting and historic buildings. There is no new activity and no burden associated with this suggestion.

41. We propose a similar approach in respect of **specific (strategic) initiatives** this would involve no new activity and no additional burden for the sector, but it would of course mean that all future initiatives benefit from the same quality of cost information that informs the rest of HEFCE funding.

Conclusions

42. We have demonstrated that there is a viable set of consistent costing approaches that HEFCE could use to provide a better cost basis to support the TFM and associated policy. This would replace much of the similar activity that already exists in the sector, but is currently undertaken in an uncoordinated and inconsistent manner. It makes sense to base this new framework for costing on TRAC, and together these proposals could be seen as adding up to a third phase of TRAC (TRAC/Teaching). However, they would look quite different from the first two phases of TRAC in terms of the amount of effort or burden for institutions, which would be much lower.

43. We repeat that while some new work will be involved, these new TRAC/Teaching requirements would not be burdensome for institutions to implement. The detail of what will be involved could vary by type of institution, and will also depend on decisions HEFCE makes about which options it wishes to pursue, and how it implements our recommendations. In considering the justification for any extra burden, we would note that:

- many institutions are already doing some of the work we have suggested, but without central support or guidance

- the principle of subsidiarity we have invoked would mean that HEFCE would be asking institutions for information which they already need themselves for pricing and internal management

- the benefit of a demonstrably more equitable and cost-based allocation of £4 billion of public funding is significant, and it is difficult to sustain an argument that this is justified for research, but not for Teaching.

44. Our current work under TRAC leads us to believe that many institutions would welcome a focus on Teaching under TRAC, which will give a broader institutional context for the work they are already doing on TRAC/fEC. Nevertheless, there would need to be careful consultation and discussion on how to take this forward. We suggest that TRAC/Teaching would need to be implemented across the whole HE sector over a period of several years, and with careful attention to the support and guidance needed by institutions, and to project management arrangements. There will, therefore, be central costs.

45. TRAC is a UK-based system where responsibility for any changes to methods is now with the British Universities Finance Directors Group (BUFDG). Any changes proposed for England would need to be discussed with BUFDG and with the other Funding Councils. The changes could be introduced for England only, or UK-wide, if the other Funding Councils and BUFDG agree.

Figure (i): Cost objectives to inform the funding of Teaching
(Figure 2 in main report)

I. The total cost of publicly funded Teaching and Learning – each HEI, and whole sector

Teaching	Research	Other

HEFCE-fundable courses	other publicly funded	non-publicly funded

II. The allocation of resources to institutions

IIa. Formulaic or contract funding of teaching activity (TFM)

Consistent or standard provision

The standard high quality UK HE student experience

At all HEIs

Fundable recurrent variations

exceptional student diversity (e.g. WP, PT)

exceptional high-cost institutions (e.g. small, London, historic buildings)

exceptional provision (e.g. strategic subjects, WPL, national facilities)

At selected HEIs

IIb. Non-formulaic or bid funding of one-off or strategic variations

One-off/Strategic

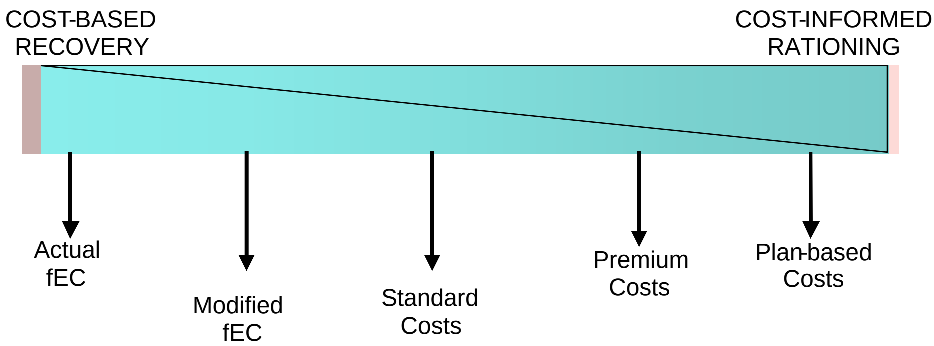
Innovation (bids for new centres/good practice)

Responsiveness (bids for new initiatives)
e.g. CETLs, Lifelong Learning Networks

III. To guide or inform good management and practice in institutions and achievement of other policy objectives not directly fundable

Internal resource allocation
Efficiency/value for money
Excellence
Sustainability/capacity
Diversity
Flexibility

Figure (ii): The spectrum of cost-related funding methods (Figure 1 in main report)



Method	Features
Actual fEC	Funding based on total actual costs incurred by each provider for eligible activities or outputs
Modified fEC	Funding for actual fEC of delivering eligible provision, weighted to reflect policy priorities or institutional plans
Standard Costs	Funding based on standardised assumed costs for categories of delivered provision
Premium Costs	Funding to recognise and encourage/reward additional costs incurred for special features of provision (delivered or planned)
Plan-based Costs	Allocation of available funds based on forward plans of institutions for eligible provision

Figure (iii): The required cost models (Table 2 in main report)

Consistent national costing framework (to support the TFM)	Supplementary costing models (for institutional use)
1. Disciplines 2. Widening participation 3. Course costing, covering: • non-standard modes of delivery as defined by HEFCE, • high cost exceptional provision as defined by HEFCE, • strategically important subjects • long courses 4. Part-time provision 5. High-cost base 6. Specific initiatives	• non-completion • specific courses or modules • other non-standard provision identified by institutions

Figure (iv): Establishing the cost of disciplines (Figure 4 in the main report)

Total institutional cost of HEFCE fundable Teaching by cost centre or price group

less

actual or standard costs arising from:

- widening participation
- part-time
- course related factors such as non-standard modes of delivery, or strategically important subjects
- high cost base
- specific initiatives

gives

Discipline costs expressed in terms of the absolute costs of each cost centre, or price group, net of other factors for which the costs are being established to inform the TFM

excluding

Total institutional cost of:
Research,
Other,
Non Public Funded Teaching,
non-HEFCE fundable Public Funded Teaching