Annex 2

Options for the corporate structure of the e-U

<u>Requirements</u>

1. In designing the corporate structure, there are a number of requirements to meet the objectives as developed in our report. These include:

   a. A structure that will create a sense of ownership of the e-U in UK HEIs, and that will secure their support and input. It must capitalise and build on the expertise and reputation for high quality learning that already exists, and use this to secure existing and new markets.

   b. A structure which provides the drive and flexibility to operate in this fast moving and rapidly developing market. The concept and need for the e-U have been driven by the recognition that new technology provides exciting new possibilities for delivering learning in new ways and to new markets. The potential of the e-learning market is galvanising existing competitors into action as well as attracting new names into the market daily. The e-U will be in competition with these highly commercial and focused operators. The UK brand will be an advantage, but it will need to be coupled with a dynamic, market orientated and fast moving organisation if it is going to succeed.

   c. A structure which is attractive to the private sector both as an investor and a partner. The e-U will need private sector investment and private sector commercial expertise to make it work. If it is to attract the right partners, they will want to be part of a commercially minded organisation and have access to a share of the profits. In return, and in addition to their investment, the e-U needs to have access to their marketing, contracting and other expertise.

   d. A means of harnessing a powerful combination of brands which will provide the e-U with credibility and access to key resources and services. Advice from specialist branding consultants suggests that the e-U will need to develop its own brand, but this process will be helped through tying in recognised quality brands to support the UK HE name.

   e. A structure which provides flexible arrangements to secure partnerships with a range of whichever companies or organisations can provide the best services to support the activities of the e-U.

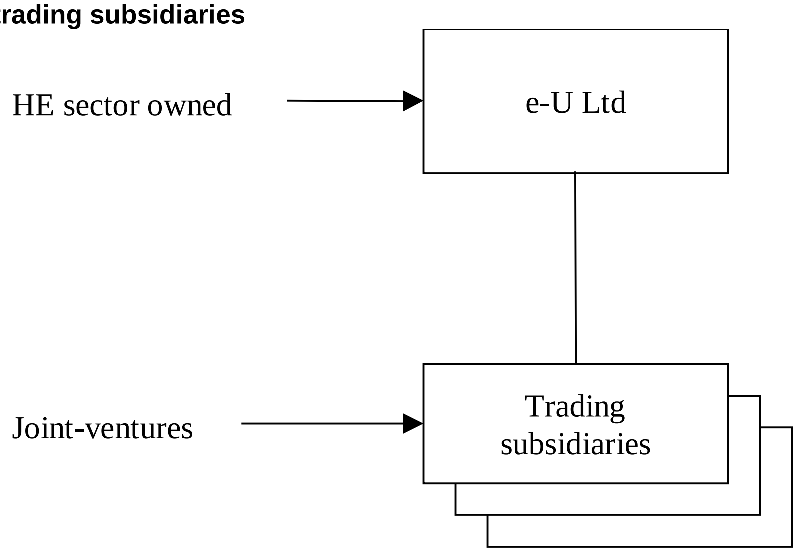
2. There are two givens which we assume will apply to any structure:

a. In appointing the chief executive and senior management team of the e-U, a key consideration will be to secure the drive, dynamism and experience necessary to develop the e-U. It is not the corporate structure alone that will provide the channel for securing private sector drive and expertise: this will also come from the management team. The team should have experience of the HE sector and the private sector and would have responsibility for devising the strategy and securing its delivery.

b. Whatever roles private sector organisations may play in the e-U corporate structure, contracts for delivering out-sourced e-U services would be awarded to the best provider, with no preferential rights for particular companies.

3. There are a number of possible structures, but our work has focused on four main options.

Option 1: e-U Ltd to be wholly owned by HE sector operating through a number of trading subsidiaries



Key features

4. The e-U Ltd would be wholly owned by the HE sector. It could be a company limited by guarantee with each HEI being a member. Alternatively, it could be a company with a share capital, with HEIs holding the shares. This might provide a more concrete expression of ownership by the HE sector, and a structure with greater flexibility for the future, for example in raising investment or even selling all or part of the company. Charitable status might be sought for one or more subsidiary companies through which the charitable activities of the e-U could be channelled.

5. The e-U Ltd would be set up as a self-standing organisation with a board of directors, management team and core staff. It would have responsibility for setting the strategic

direction of the e-U, for operating and overseeing the quality gateway, and for brokering the partnerships to deliver the e-U products.

6. Trading subsidiaries would be set up to deliver the e-U in specific geographical areas, specific subjects and for specific services. These would be joint ventures with the most appropriate partners, with such partners investing in equity in return for profit share. The e-U Ltd's share of these profits would be covenanted to it and used for further development. The trading subsidiaries could become substantial companies in their own right, offering a means for private sector partners to share in a clearly identified part of the e-U operation.

7. The main advantages of this structure include:

a. It may be attractive to the HEIs because it keeps ownership and control very clearly within the sector, thus ensuring that they are the guardians of quality and the use of the e-U name.

b. It would retain the independence of e-U Ltd and help in positioning it as an impartial and top quality provider. It would also allow it greater freedom to enter into partnerships with a variety of partners and providers at the trading level.

c. It would avoid the suspicion that private sector partners would be able to secure preferential positioning in tendering for particular services or parts of the e-U operation by virtue of their involvement at the top level.

d. Those HE sector bodies empowered to appoint the directors of the e-U company could choose to appoint individuals with private sector experience and expertise.

8. The drawbacks of this model include:

a. If it were set up as a company limited by guarantee, e-U Ltd would be less flexible for the future and, at this level, it would not be as attractive as an investment vehicle for external investors.

b. If ownership was restricted to the HE sector, investors would have to be involved at the subsidiary company level. Some potential partners and investors may be reluctant to be involved if overall strategy and direction were to be decided at the higher level from which they were excluded, and decided solely by representatives of the HE sector. This would cut off a major source of funding.

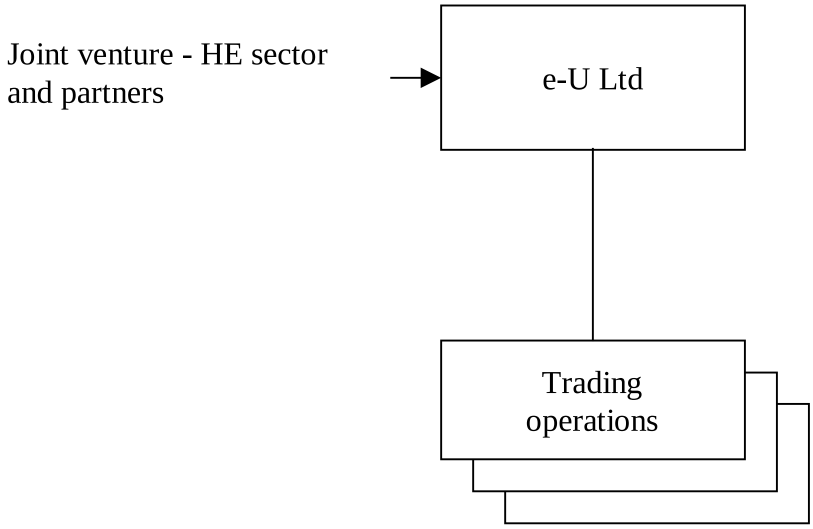
c. The e-U Ltd would not receive the potential benefit from the infusion at the top level of the drive and experience which private sector partners could bring in developing its strategy.

d. As a consequence of b and c, the opportunities for securing a significant private sector investment up front and at the top level would be foregone.

e.	Whilst performance-related remuneration packages could be devised, it could be difficult to attract e-business expertise into what would be a ‘not-for-profit’ organisation.

f.	Whilst the organisation would be developing relationships with the partner organisations at the operating level, it would be more difficult to build on these relationships and use their potential brand advantage from day one, compared with the opportunities available if the partners were involved at the higher level. The top level brand would be solely HE-derived, not HE-plus-others.

Option 2: e-U Ltd set up as a joint venture company with a small number of core partners.



Key features

9.	The e-U Ltd would be owned jointly by the HE sector and a small number of partners. The HE sector could hold an absolute or relative majority. Partners would contribute to up-front investment and share in the risk and rewards of the operation.

10.	The e-U would have its own brand and build on the brands of the UK HE sector plus the core (non-HE) partners.

11.	The e-U Ltd might operate either directly through operating divisions or through a network of other subsidiaries which might be joint ventures with other organisations (as in option 1).

12.	The advantages of this model include:

a.	As a company capable of making and distributing profits it would be attractive to external investors and relatively straightforward in terms of securing working arrangements with two or three key partners.

b. It offers possibilities of securing upfront investment in the overall concept.

c. It may have advantages in terms of setting up a brand and embedding two or three key brands alongside the UK HE sector. This may give a more powerful marketing message from the start of operations on which to build the e-U's own brand identity.

d. It would tie-in private sector commercial awareness and drive at the heart of the organisation and in determining its strategic development. It may also be more attractive to potential e-business staff to work for what might be seen to be a more private sector and commercially focused business.

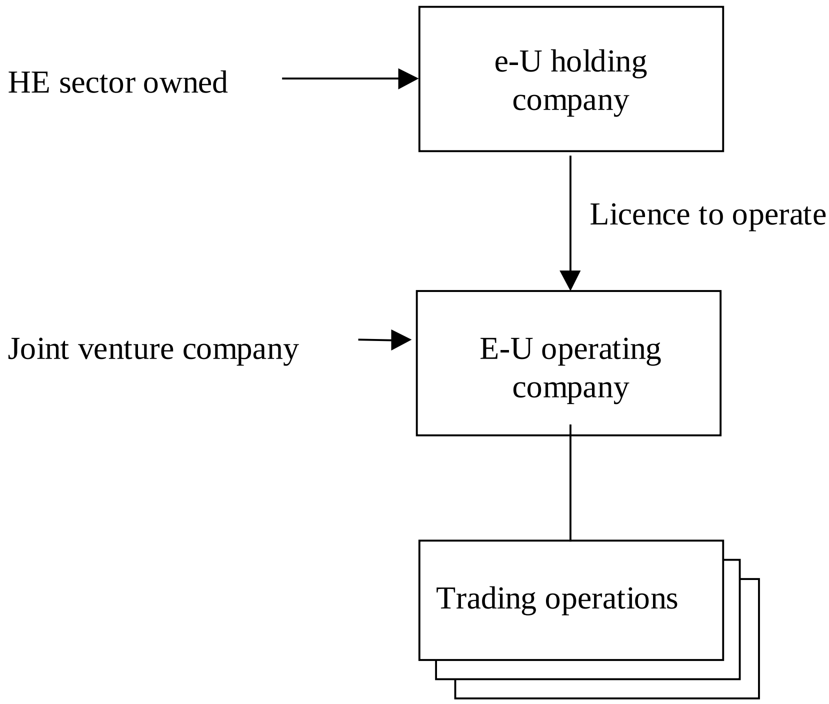
13. The drawbacks include:

a. It would be vital to find the right partners who were acceptable to the HE sector. There could be a risk of tying the e-U brand, and all that this entails in terms of UK HE quality, to organisations who could damage that reputation through their other activities.

b. There might be conflicts of interest which would have to be managed. The most obvious of these would be balancing the drive for commercial returns with quality of delivery. Of course this is not a new issue – HEIs themselves have to address this in their own operations. But it would be a major issue in this new area of learning delivery. It would be harder (although not impossible) within a single joint venture company to safeguard on a permanent basis the e-U's academic integrity and purpose.

c. A second potential conflict would be in ensuring that the e-U was able to secure relationships and contracts with the best suppliers in its different areas of business rather than being tied to using the partners' own organisations. This freedom would be important in supporting the reputation for high quality.

Option 3: HE sector owned holding company retaining the licence to the e-U brand, with the licence granted to a second company (e-U operating company) in which the holding company would hold equity along with a small number of partners



Key features

14. Under this option the HE sector would retain absolute ownership of the e-U brand through the e-U holding company and would license the ‘e-U operating company’ to manage and operate the e-U on its behalf. The operating company could be a joint venture with a small number of partners with equity investments.

15. The operating company would be responsible for all aspects of the operation and delivery of the e-U within the terms of the licence. As with option 2, it could operate either directly or via a number of subsidiaries which could, in turn, be joint ventures with other partners.

16. The holding company would be the vehicle for securing HE sector ownership and would have a board of directors. They in turn would appoint members to the board of the operating company alongside the partner organisations, but this would be the extent of the holding company’s involvement. The holding company could be a company limited by guarantee or it could be a company limited by shares. Either way it would have a passive, rather than an active, role in owning the brand and protecting its integrity. The profits of the operating company attributable to the HE sector would return to the holding company.

17. The advantages of this model include:

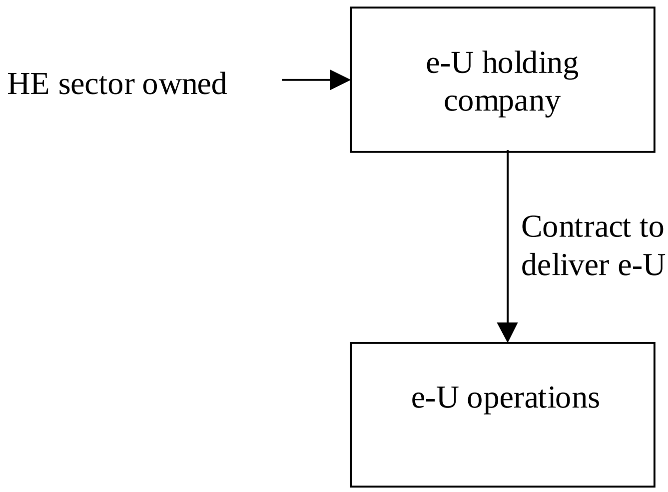
a. The HE sector owns and controls the brand through the licence. The holding company's role in the operations of the e-U would be through its right to appoint a number of directors to the operating company and through the terms agreed in issuing the licence.

b. The model has the advantages of option 2 in terms of attractiveness to other partners and in securing their investment and management expertise. It differs from option 1 in that matters relating to the top level strategy of delivery and operation would rest with the operating company.

18. The drawbacks of the model include those in option 2 concerned with securing the right partners and managing potential conflicts of interest.

19. The attractiveness of the operating company to private sector partners will depend to a large extent on the powers reserved to the holding company through the terms attached to the licence. Put simply, the greater the freedom given to the operating company, the more attractive it would be to external partners. On the other hand, the right partners would recognise the value to the success of the e-U enterprise of developing and maintaining a reputation for academic excellence, and that the holding company model could promote that reputation by demonstrating that the core academic purpose would be permanently safeguarded.

Option 4: HE sector owned holding company contracting with one or more partners to operate e-U on its behalf



Key features

20. The HE sector would own the e-U company and the name but contract out the management and delivery of the e-U to one or more organisations.

21. In many ways this would be similar to option 3 but the relationship would be by way of a contract rather than a joint venture.

22. The contracting company/ies may invest in order to secure the contract and in return for performance-related payments.

23. The advantages of this model include:

a. It would be attractive to the HE sector in retaining ownership within the sector (as options 1 and 3).

b. It would provide a means of securing private sector involvement and expertise in running the organisation (as options 2 and 3).

c. It could be a means of securing external investment in all levels of the organisation (as options 2 and 3).

d. An operating contract could be more attractive to some private sector organisations in offering greater specificity and certainty about the level of performance required.

24. The drawbacks include:

a. The contract would be very difficult to draw up in a fast moving and relatively unknown market. In the early years, there is bound to be a real issue of feeling the way and trying to provide the flexibility for the e-U to establish itself. Providing this flexibility whilst at the same time having good performance targets built in would be very difficult to achieve.

b. Whilst it would secure private sector involvement in the delivery of the e-U and it could be used to secure investment in return for the contract, it would not create the same degree of partnership and shared goals as would an equity sharing relationship within a jointly owned company. The efforts of the private sector operator would focus on delivering the contract rather than on the wider question of strategic building of the enterprise.

c. There are parts of the operation which could not be contracted to a private sector organisation – notably, the setting and safeguarding of academic quality and standards. So the concept of bundling the whole enterprise into a single contract would be difficult to secure, since there would have to be reserved activities remaining under the direct control and operation of HEIs.

Conclusions and recommendation

25. The preferred solution needs to provide the right balance between HE sector inclusion and private sector investment and involvement, as well as being able to put together a

powerful collection of brands from which to launch the e-U. It is also important that the e-U has the ability to set-up and launch as rapidly as possible, given the need to secure market presence and the lead time in developing new content and the technology platform.

26. Option 1 would have the attraction of setting up the e-U as an 'independent' organisation with strategy and direction controlled by the higher level company, and delivery through a series of joint ventures. The downsides of this model are that it would not allow private sector investment at the top level, and investment at the delivery level may not be as attractive. The other potential downside is that the top level organisation may not maximise the commercial and market focus and the drive which could be achieved through a closer relationship with private sector partners.

27. Option 2 would bring a much stronger commercial focus to the e-U. The downside is that it may not be 'inclusive' enough for the HE sector in the structure. HEIs would be a partner alongside a number of other players. On a more practical level, it would not provide a ready vehicle for the HE ownership. It would not be practical for each HEI to have a direct share in the joint venture company. Their ownership would have to be expressed collectively through the sector bodies.

28. Option 4 would provide the sector with clear ownership and would bring in commercial partners to deliver the operations though the contractual relationship. The weakness in this model would be the dependence on the contract for this delivery. The nature of the business would make the design of a contract very difficult indeed.

29. Option 3 would seem to achieve the right balance on the key issues:

a. It would secure HE ownership of the brand and the name. The holding company would also provide a corporate vehicle for the HE sector and it could be a company limited by guarantee or by shares.

b. Operations would be delivered through the operating company which would be the market face of the e-U and which would operate and deliver the e-U. The HE owned holding company could hold a majority of shares in the operating company and the right to appoint a number of directors. Equity stakes could be taken by key partners, again giving them the right to appoint a number of the directors.

c. The operating company could set up a series of subsidiaries with specific market, subject or service focuses through a further range of partnerships.

d. It would provide a means of getting the operation up and running rapidly using resources from the partner organisations.