

October 2005/41

Core funding/operations

Consultation

Responses should be made by

Friday 13 January 2006

This is a consultation on our plans for the method for allocating funds for teaching. Our goal is to create a method that provides institutions with stable and predictable funding through the introduction of variable fees. We aim to create a method that will improve the support and protection of our strategic priorities.

Review of the teaching funding method

Consultation on changes to the method

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To	Heads of HEFCE-funded higher education institutions Other relevant stakeholders
Of interest to those responsible for	Senior management, Finance, Governance
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Executive summary

Purpose

1. This is a consultation that seeks agreement to a number of proposed alterations to our main formula funding method for teaching.

Key points

2. We believe that we must review our funding methods in order to ensure that they remain robust. This document is the first formal consultation on the proposals we are making as result of this review process. We intend to conduct a further consultation in autumn 2006 on particular elements of the new method. We would welcome responses from all HEFCE-funded institutions and all relevant stakeholders. We intend to publish the outcomes of this consultation in March 2006.

3. The consultation document outlines a two-cycle approach to the review of the funding method. The first cycle, which we expect to last at least until the outcome of the Government's review of fee income in 2009, will address issues that require attention and put in place the foundations for changes that may be required in the future. The second cycle will address changes that might be needed post-2009.

4. The document sets our priorities for the funding method. In particular it considers:
 - the need for stability and predictability from HEFCE grant
 - our belief that we should support and protect strategic priorities through the funding method
 - the need for a simplified method.

5. There a number of proposals relating to the current funding method, in the following areas:
 - premiums (paragraphs 43 to 51)
 - cost information (paragraphs 56 to 62)
 - subject weightings (paragraphs 63 to 67)
 - fee assumptions (paragraphs 68 to 77)
 - volume measures (paragraphs 78 to 101)
 - data sources (paragraphs 102 to 107)
 - part-time provision (paragraphs 108 to 114)
 - widening participation (paragraphs 115 to 118).

6. Two events will be held as part of the consultation: in London on 9 December and Manchester on 13 December. Places are limited so early booking is advisable. Please contact Alison Felton for further information: e-mail a.felton@hefce.ac.uk, tel 0117 931 7078. We will also be running a dedicated seminar for further education colleges at the Association of Colleges' annual conference on 15-17 November.

Action required

7. Responses to this consultation should be made by **13 January 2006**, using the online form available on the web with this document at www.hefce.ac.uk under Publications.

8. We are aware that many of the issues considered in this document are complex. We will therefore be publishing a 'Frequently Asked Questions' guide in early November which will be built on as the consultation progresses. If you have any queries please contact Chris Taylor on c.taylor@hefce.ac.uk to enable us to make this FAQ guide as useful as possible.

Introduction

Background to HEFCE

9. HEFCE was set up by the Government in 1992 to administer public funds for higher education (HE) in England. We allocate most of the money directly to universities and higher education colleges; some also goes to further education colleges (FECs) to support their higher education programmes.

10. As a non-departmental public body, we have some autonomy from the Government. We work within a policy framework set by the Secretary of State for Education and Skills, but we are not part of the Department for Education and Skills (DfES). We provide independent and confidential advice to Government on the funding needs and development of universities and colleges, and contribute to forming policy.

11. In 2005-06, we distributed around £6 billion in public funds. This money supports four main areas of activity in higher education:

- teaching and learning
- widening participation of under-represented groups
- research
- strengthening links with business and the wider community.

12. Most of the money is distributed as a block grant, which institutions can decide how to allocate internally to meet their own priorities. Some activities, for example related to particular needs or policy aims, are funded through special initiatives, where there are restrictions on how the money is spent.

13. In all our activities we aim to be transparent. We consult the sector on the methods for allocating funds, and on any new initiatives, and publish detailed information on the processes. Further information on our work is available on the web at www.hefce.ac.uk.

HEFCE funding methods

14. As mentioned above, we provide funding to higher education institutions (HEIs) as a block grant. We calculate the grant through formula and non-formula funding methods, and apply different methods to calculate formula funding for teaching and for research. Around 60 per cent of our funding (£4,004 million in 2005-06) is allocated through the main formula funding method for teaching. The method is designed to allocate funding between institutions and we do not expect institutions to use the same method to distribute resources internally. In distributing the money, we aim to promote high quality cost-effective teaching, and in doing so to meet the diverse needs of students, employers and the nation.

15. When the Council was established in 1992, legislation created a unified higher education sector by abolishing the division between universities and polytechnics and colleges. Our first funding method for teaching provided stability for institutions, but in

some cases gave differing levels of funding for similar provision at different institutions for historical reasons.

16. In 1995, we conducted a fundamental review of that method. The method that emerged from the review was based on two main principles: that there should be similar resources for similar provision; and that growth in student numbers should be allocated selectively against pre-determined criteria. The new method was first used to allocate funding for teaching in 1998-99. It is still in operation, and is described in HEFCE 2005/34 'Funding higher education in England'. We would recommend that readers familiarise themselves with the structure of the current method before responding to this document.

17. In 1999-2000 we took on responsibility from the Learning and Skills Council (LSC) for directly funding all degree and diploma level provision in FECs. This led to an increase in the number of FECs directly funded by HEFCE. In 2002 we substantially increased funding to support widening participation, with around £260 million to support improving retention. We also made some changes to the method in 2003, which were introduced from 2004-05 (see HEFCE 2004/24). These resulted in some shifts in allocations, but did not involve revisiting the principles of the method.

Background to the review

18. We believe that it is good practice to review periodically the robustness of our methods for allocating funding. This is to ensure that those methods remain relevant as the HE sector, and the context in which it operates, evolve. Much has changed since the last fundamental review of the funding method in 1995, and we believe the time is now right for a further review to ensure the method remains fit for purpose.

19. In 2004 we commissioned SQW Ltd to evaluate the current method and to explore if it was likely to remain fit for purpose in the coming years. We also began discussions with the sector – through its representative bodies, our annual conference and a specialist 'sounding board' set up to inform the review – on how, if at all, the funding method would need to change.

The purpose and aims of the method

20. The funding method for teaching determines how we distribute around £4 billion of public money each year, and is the main funding source for many HEIs. The purpose of the funding method is therefore closely linked to the purpose of the Council as a whole.

21. This purpose is defined by our strategic plan. The plan sets out our broad vision for the development of HE over the next decade, and our strategy and proposed activities for moving towards it. It reflects extensive discussions with stakeholders, responses to a consultation document, and the Government's plans in the White Paper on the future of higher education. At the heart of this strategic plan are four core strategic aims:

- enhancing excellence in learning and teaching

- widening participation and fair access
- enhancing excellence in research
- enhancing the contribution of HE to the economy and society.

22. Underpinning these core aims are three cross-cutting supporting aims:

- building on institutions' strengths
- developing leadership, governance and management
- excellence in delivery: organisational development within HEFCE.

23. Our current strategic plan covers the years 2003-08 (HEFCE 2005/16). However, we are in the process of developing our 2006-11 strategic plan, with the aim of publishing it in April 2006. We will formally consult on this from November 2005 and have already undertaken a pre-consultation on the outline of the new plan.

24. We are accommodating our strategic policy developments for 2006-11 by evolving the new plan from the 2003-08 strategic plan, so that our mission statement and four core strategic aims remain unchanged. In addition, we will have a new cross-cutting aim – sustaining a high quality HE sector. This aim will focus on our role in sustaining a high quality HE sector that adapts to the developing needs of stakeholders, and which is recognised as globally competitive. It combines the existing cross-cutting supporting aims of 'building on institutions' strengths' and 'leadership, governance and management'.

25. Further details about our strategic plan are available from our web-site under About us.

26. Simple distinctions between types of activity are not always clear within institutions. We therefore believe that the funding method has a role to play in ensuring that all our strategic aims are met, but contributes most to the aims of enhancing excellence in learning and teaching, and of widening participation and fair access.

27. In our progress report on this review (HEFCE 2005/21), we published the aims of the funding method. These define the characteristics of HE that it is in the public interest for the funding method to help support and protect. They specify that the method should help to:

- Ensure an appropriate capacity of learning and teaching in HE at a sector-wide level.
- Ensure and promote a high standard of teaching quality and academic standards.
- Enable learning and teaching in HE to respond to the diverse needs and demands of students, business and wider society.

- d. Enable the higher education sector to provide innovative learning and teaching opportunities.
- e. Enable the sector to make higher education accessible to all those who could benefit from it.
- f. Enable the higher education sector to make the best use of public money to enhance the student learning experience.

28. We believe that the dynamism of higher education is a great strength and that intervention should be kept to a minimum. However, we also believe that it is in the public interest that we can and should take an overall view of higher education and its political and economic context. This is important so that we can identify where the aggregate individual interests of universities and colleges may fail to meet our strategic aims for HE, and so that we can support institutions to ensure that these aims are met.

An evolving context requires an evolving method

29. The main focus of our review of the funding method has therefore been on understanding the challenges that HE is facing both now and over the next 10-20 years and beyond; and considering the role that the funding method should play in delivering our aims over this period.

30. An important part of the economic context are the regulations governing the charging of tuition fees, and the impact that these have on the sector. One significant change has already taken place, with the introduction of capped variable fees for 2006-07. We must consider the impact that this and any subsequent changes to these regulations will have on our ability to ensure that the public interest is served through supporting the strategic aims of both the funding method and HEFCE as a whole.

31. Hypothetically, the more de-regulated and variable that fee income becomes, so we might expect the proportion of HEFCE funding received by many institutions to reduce, and with it their dependence on HEFCE. We might also expect the sector to become more diverse as a result of greater influence from market forces.

32. These changes may bring benefits to the sector in terms of increased income, but in a fully de-regulated fee system these changes could bring substantially greater risk to the delivery of our strategic aims. We believe that this would require HEFCE to take a more considered strategic role than currently, which would in turn require investment to be more focused on supporting and protecting those strategically important outcomes for HE that are in the public interest and that are potentially at risk.

33. However, the future of regulations governing fee income is unclear. The Government may review fee arrangements in 2009-10, and there may be major change as a result, but the outcome of this review is not in any way predictable.

34. We believe this uncertainty requires us to take a two-cycle approach to our review of the funding method. The first cycle, which we expect to last at least until the outcome of the Government's review, will address particular issues that require attention and put in place the foundations for changes that may be required in the future. The second cycle will address changes that might be needed post-2009.

35. Regardless of the outcome of the 2009 review we believe that the changes to fee regulations in 2006-07 will have some of the effects of a fully de-regulated fee system described above, and therefore require a response from HEFCE.

36. In the period to 2009 we do not envisage the new fee regime resulting in large scale, sector-wide change. For some institutions, however, in both the higher and further education sectors, there may well be significant implications. We believe therefore that we must take action now to put in place a funding method that supports and protects our strategic priorities better, and that provides a mechanism for further strategic targeting of funds if additional resources become available to the sector.

37. The evaluation of the current method by SQW Ltd¹, and early discussions with sector representative bodies, showed that, with some exceptions, the sector feels that the current method is broadly fit for purpose. It also found that HEIs wanted the method to deliver stability and predictability in funding for teaching, at least during the introduction of the new fee regime. We believe that a more targeted strategic approach to funding will be required in order to achieve this.

Consultation question 1

Do you agree that HEFCE should support and protect its strategic priorities through the funding method?

Shape of the new method

38. In HEFCE 2004/24 we highlighted the four key elements of our funding method that needed to be addressed:

- a. **Purpose** – what the funding is for.
- b. **Aims** – what the funding seeks to achieve in order to deliver the purpose.
- c. **Features and principles** – how the method will seek to achieve its aims.
- d. **Mechanisms** – exactly how we will allocate funds.

39. In that report we also established both the purpose and the aims of the new method. In this section we propose the principles and features that would define the shape of the new method and the detailed mechanisms to underpin it.

¹ 'Evaluation of the HEFCE teaching funding method', May 2005, www.hefce.ac.uk under Publications/R&D reports.

Features of the new method

40. The new funding method will display five features:
- a. Transparency. The funding method will be clear and public. The data on which allocations are based will be auditable and, wherever possible, public.
 - b. Predictability. The method and its parameters will be predictable, so that an institution knows how decisions it might take, and changes in its circumstances, will affect its funding.
 - c. Fairness. Differences in funding between institutions will be for justifiable reasons.
 - d. Efficiency. The funding method will impose as small a burden as possible on institutions, consistent with the principles outlined above.
 - e. Flexibility. The method will be flexible enough to respond in a strategic manner to external policy changes, and particularly to developments in HEFCE's own policies.

41. The first four of these features are identical to those of the current funding method. Nothing in the review to date has indicated that they are no longer appropriate. The 'flexibility' definition has been amended to reflect the need for the method to be more effective in supporting and protecting our strategic priorities.

Principles and shape of the new method

42. To provide stability and predictability we believe that the new funding method should in most respects continue with the same basic structure as our current method. This structure is a base price informed by the costs of teaching, multiplied by weightings to reflect the subjects taught and by the number of students (the volume). We believe that this supports the maintenance of capacity in the sector by taking account of the principal factors that both determine and differentiate funding. We therefore propose that the great majority of our funds should be allocated on the principle of a cost-informed tariff that reflects the volume and subjects taught. Specific issues relating to volume, subject and costing are discussed later in this document.

43. In order to deliver greater transparency, we propose to introduce a new feature to the funding method: targeted allocations that address the strategic aims of the method. In the current method we calculate premiums to recognise the additional costs for some types of students and institutions. These address strategic priorities and currently represent around 5 per cent of the funds we allocate through the method (not including the widening participation allocation). The premiums modify the basic calculation

described in paragraph 42, within a tolerance band². We currently apply premiums for the following:

- a. Students on long courses.
- b. Part-time students.
- c. Foundation degree students.
- d. London weighting.
- e. Institution-specific (specialist) factors.
- f. Old and historic buildings.
- g. Small institutions.

44. This approach has enabled us to fund differentially and to reflect different features of the HE sector. However, the evaluation of the current method and feedback from the sector suggest that the effectiveness, transparency, predictability and flexibility of the method could be improved through allocating this funding differently, and that stability can be supported in the face of potential market volatility.

45. The number of premiums and applying them to the basic calculation have led to an increasingly complex method, with changes sometimes resulting in unintended consequences. Furthermore, the dampening effect of the tolerance band has limited the efficacy of the premiums in providing financial benefit to institutions. An institution only receives additional funds if the increase in the activity that attracts a premium results in it moving outside its tolerance band. Otherwise its HEFCE grant for the current year is rolled forward to the following year.

46. We are therefore proposing to distribute the funding associated with premiums as targeted allocations of 'real' money, operating outside the tolerance band, not attached to the main formula but within the block grant. The widening participation allocation is an example of this approach currently in operation.

47. Each allocation would have a limited budget. However, this change means that all institutions – regardless of their current level of engagement with strategic priorities – would see a direct correlation between changes in levels of activity that contribute to an identified strategic priority and the release of funding. We believe that this is a more effective way of supporting and protecting our strategic priorities. It would also establish a mechanism that is better able to protect certain strategic priorities in the public interest if additional resources are made available to the sector and should the need arise. Table

² The tolerance band is the acceptable variation between the standard resource (a notional calculation of what the institution would get if its grant was calculated afresh each year), and the assumed resource (the teaching grant that we actually paid to the institution for the previous year, adjusted for various factors, including assumed income from fees). If the difference is no more than 5 per cent, either plus or minus, then the institution is within the tolerance band and its HEFCE grant will be carried forward from one year to the next. For more details see HEFCE 2005/34 'Funding higher education in England: how HEFCE allocates its funds'.

1 shows the proposed new shape of the funding method and the principles on which it is founded.

Table 1 Shape of the new method

Core teaching funding method – cost-informed block grant allocated against two principles:		Special funding
Principle A: tariff to reflect volume and subject	Principle B: targeted allocations that address strategic aims of the funding method	Principle: cost-informed and time-limited investment projects
<ul style="list-style-type: none"> • Base price including sector-wide fee assumption, phased in during introduction of variable fees • Multiplied by subject weighting and student load • Potentially based on data from HESA only • Subject to a tolerance band 	<ul style="list-style-type: none"> • Driven by formula • Outside the tolerance band • Uses various data sources as appropriate 	<ul style="list-style-type: none"> • Examples include Centres for Excellence in Teaching and Learning (CETLs) and support for strategically important and vulnerable subjects

48. To support predictability and maintain stability, and give maximum notice of change, we do not intend to introduce this new structure until 2007-08. In that year we would not introduce any fundamentally new focus for the targeted allocations, and would provide institutions with the cash equivalent of what they would have received under the current system of premiums. No institution would lose in cash terms in 2007-08 as result of the introduction of this new structure, and it is likely that no institution would lose in real terms.

49. From 2006-07 institutions can charge a maximum of £3,000 in fees for full-time home and EU undergraduates. While this cap remains, we will continue to distribute the overwhelming majority of our funds allocated through the teaching method through principle A. The funds available for allocations under principle B, including the widening participation allocation, are currently about 10 per cent of total teaching funding. The amount of funding distributed in this way from 2007-08 will be increased only if additional resources become available.

50. Replacing the premiums in 2007-08, with targeted allocations that operate outside the tolerance band, would set new figures for the 'standard resource' for each institution. This could alter their position within the tolerance band. We then expect to provide migration funding for those that fall outside the band as a result of the change. We do not expect the funding required to be substantial.

51. In 2006 we will consider the appropriateness of the current premiums and examine if there are new priorities that we wish to reflect from 2008-09. We intend to develop these priorities with the sector and its representative bodies, and to formally consult on them before any changes are made. The revised strategic priorities will determine funding under principle B from 2008-09 onwards.

Consultation question 2

Do you agree with the concept of replacing premiums with targeted allocations that are outside the tolerance band and that address strategic priorities?

Special funding

52. Special initiative funding remains unaffected by the proposals we have made in relation to the funding method. We remain committed to reducing the numbers of bidding competitions and moving towards more strategic allocations of funding. However, we believe that there is a continuing need for time-limited investment projects to pilot and support innovation, share risk and help drive change.

53. The proposed method provides a more practical means for mainstreaming and reducing special funding, and consequently a more dynamic and responsive funding method. This could occur by moving funds from special initiatives into the main funding method as a recurrent allocation, and eventually into the main tariff (see paragraph 42), as piloted innovation becomes proven and strategically important practice becomes increasingly embedded.

Higher education in further education colleges

54. Higher education delivered in FECs makes a vital and often unique contribution to widening participation, part-time education, and new and innovative provision. We currently have a broad-brush funding method with modifications designed to protect important and unique features of the HE sector. HE in FECs is one such feature.

55. We are aware that there are proposals in this document that may impact differently on FECs, and we address them in turn as they arise. We are confident that through using proxies, sampling, or alternative arrangements we can introduce measures to ensure that FECs are not disadvantaged. We will do this through ongoing consultation with the LSC, through working with the Association of Colleges (AOC) and talking to colleges directly to analyse the implications for them, and to find solutions where needed. We are also holding a dedicated seminar at the AOC's annual conference on 15-17 November to address issues relating to HE in FECs.

Details of the proposed changes

A cost-informed method

56. We propose to use more information on costs in assessing the funds we allocate for teaching, including but not restricted to the funding method, as we believe this will help to ensure the efficiency and sustainability of the sector over the coming years. To

this end we commissioned and worked closely with a team of consultants (JM Consulting and PA Consulting) to consider the viability of a more cost-based approach to the funding of teaching.³

57. The consultants' report states that more use of cost information could help achieve three objectives, developed and agreed in collaboration with HEFCE, which we now wish to pursue:

- a. Identifying the total costs of sustainable teaching, at a sector and an institutional level.
- b. Providing data to underpin the allocation of funding to institutions – either formulaically through the funding method, or through special initiatives or other one-off funding.
- c. Informing institutions and other stakeholders about the costs of teaching, to encourage more strategic thinking about their provision, and to encourage efficiency and innovation.

58. The report proposes using the Transparent Approach to Costing (TRAC) as the basis for a consistent national framework for collecting cost information to support HEFCE funding policies for teaching. The additional information required would be in six cost areas, to support the allocation of funds and institutional good management. These are:

- subject
- widening participation
- non-standard or high-cost delivery
- part-time provision
- institutions with a high cost base
- specific initiatives.

59. The new costing data would provide information that institutions increasingly need for their own purposes, such as deciding fee levels and allocating resources internally. It would require some extension to existing TRAC processes. In some areas, institutions are already costing teaching, and the only change might be to provide a more consistent framework of methods to support them. In other areas, we might require some additional costing processes. Wherever appropriate these could be done on a sample basis (by volunteer institutions) or by one-off studies, in order to minimise potential burdens on institutions.

60. The total burden involved would depend on the options we chose. The use of TRAC for teaching will mainly draw on existing processes, so we do not believe that burden or cost would be prohibitive. Moreover, 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.

³ 'Use of costs to inform the funding of teaching', JM Consulting and PA Consulting, October 2005. Available on the web at www.hefce.ac.uk under Publications/R&D reports.

61. We will work with the British Universities Finance Directors Group (BUFDG) and the AOC to assess and begin to take forward the detailed recommendations in the consultants' report over the 2005-06 period. Many of the changes can be introduced quite quickly, but costing data require several years of reporting before they can be considered robust enough to inform funding decisions. At all times we will involve the sector in developments and be aware of the need to minimise and manage the burden of any new measures introduced.

62. The use of cost data provides some challenges for HE in FECs, which do not use the TRAC methodology. We could ask FECs to adopt TRAC processes, but that would create a substantial burden for them. Also, the LSC is currently developing its own approach to costing further education provision, and this is likely to involve changes for FECs. So, we would need to consider how we can introduce cost-informed funding for FECs without adding to their administrative burden. An option might be to use the cost-informed data provided by HEIs, which will include the provision they franchise to FECs, as a proxy for the costs in directly-funded FECs. We will need to test how feasible this approach would be, and how we might implement it in practice.

Consultation question 3

Do you agree that we should develop a consistent national framework for the collection of cost information in accordance with TRAC principles?

Costing and subject weightings

63. The recent evaluation by SQW found that there was broad support in the sector for the current structure of price groups – cost weightings for four broad groups of subjects. Until more robust cost information is available we intend to maintain the price groups at their current weightings. Weightings are currently based on expenditure and student full-time equivalent (FTE) data by cost centre. For 2004-05 these weightings are as follows.

Price group	Description	Cost weight
A	The clinical stages of medicine and dentistry courses and veterinary science	4
B	Laboratory-based subjects (science, pre-clinical stages of medicine and dentistry, engineering and technology)	1.7
C	Subjects with a studio, laboratory or fieldwork element	1.3
D	All other subjects	1

64. The report by JM Consulting and PA Consulting suggests that a consistent national framework for the costing of teaching will provide information to revisit the appropriateness of the price group weightings. There will be issues to resolve around the specification and definition of subjects to be costed, and in reconciling the units of measurement used in the TRAC method and in returns made to the Higher Education

Statistics Agency (HESA). We do not expect these to be insurmountable. We intend to revisit these weightings within the national framework for the costing of teaching at the earliest opportunity.

Strategically important and vulnerable subjects

65. Subjects that are strategically important to the economy and society, but which may be vulnerable because of a mismatch between supply and demand, are an important feature of a diverse sector. However, HEIs are autonomous bodies, and receive a block grant that allows them to invest (and disinvest) in subject areas as fits with their strategic plans. The Roberts report into strategic subjects⁴ strongly supports these principles, which it maintains contribute to the dynamism of English HE.

66. The report recommends that a clear evidence base should be used, wherever possible, to support a market-led solution to the problem of strategic and vulnerable subjects: it argues that demand-side problems are not well addressed by supply-side solutions. We do not therefore intend to introduce different weightings for strategic and vulnerable subjects in the short term, but will consider their costs as part of the work to develop a national framework for the costing of teaching.

67. Nevertheless, we believe that we should take an overall view of higher education provision, to identify where the aggregate individual interests of universities and colleges do not necessarily match the national or regional interest. We are therefore engaging with a range of organisations, such as the Royal Academy of Engineering and the Royal Society of Chemistry, to support and increase demand for strategically important and vulnerable subjects. We are also working with UK Research Councils, subject bodies and users to develop proposals to address subject-specific problems.

Consultation question 4

Do you agree that we should not change subject weightings in the short term but should look to make more use of costs to inform them?

Assumptions about fee income to institutions

68. Most of our funding is being allocated through principle A (see Table 1). This is a tariff that reflects the volume of provision being undertaken by the sector in the four broad price groups discussed above. Institutions are free to spend this funding as they wish, within the restrictions of the block grant, as described in paragraph 14. They are also free to spend income generated from tuition fees as they wish. However, in order for our funding for principle A to be fairly distributed, we believe we must take account, at a sector-wide level, of both the costs of provision and the ability of the sector to meet these costs. We currently do this by making an assumption about the level of fees

⁴ 'Strategically important and vulnerable subjects: final report of the advisory group', HEFCE 2005/24, on the web at www.hefce.ac.uk under Publications.

charged to students. This does not affect the amount of public funding provided for teaching in higher education.

69. The amount of funding received by HEIs in fee income per full-time undergraduate student does not currently vary. Fee income therefore makes a fixed contribution to the cost of providing HE for those students. However, the cost of provision varies for different students. This happens as a result of many factors but primarily because of the cost of the subject they are studying. As we have already stated, we reflect the relativities between these costs through our four different price groups.

70. This fixed fee income then contributes to the costs of provision in a particular subject area, proportionate to the total costs. For example, if a low-cost course is weighted at 1 – say £2,000 – and the fee income for a student is £1,000, then potentially 50 per cent of this cost can be met by fee income. For a more expensive course we might assume a cost weighting of 4 – say £8,000 – then the fee income of £1,000 would only meet 12.5 per cent of the cost.

71. Our price groups take account of differences in cost, but they do not take account of these varying percentages of costs that could be met by fee income. We currently make a fee assumption in our calculations which enables us to adjust the grant per student by the level of the assumed fee. In our example above, for the low-cost grant we would be providing the remaining 50 per cent on top of the 50 per cent provided by fee income, and for the high cost grant the remaining 87.5 per cent.

72. If we were to make no fee assumption, we would fail to take account of the fact that lower cost subjects could have a greater proportion of their costs met by fee income than higher cost subjects. This would result in providing a disproportionate amount of public funding for lower cost subjects as opposed to higher cost subjects. This could create perverse incentives to recruit students in lower-cost areas, and would result in high-cost provision not being appropriately funded. This would neither be in the public interest nor maintain stability.

Consultation question 5

Do you agree that we should continue to make an assumption about the income from fees in calculating our grants for teaching?

The level of the fee assumption

73. We believe that the level of the fee assumption should be based on the best knowledge that we have. Although fee regulations will be relaxed from 2006 there is still an upper limit of £3,000 that can be charged. Analysis of agreements submitted to the Office for Fair Access (OFFA) suggests that most HEIs will charge the maximum fee.

74. We believe that £2,000 represents a conservative estimate of fee income to institutions, net of any bursaries they give to students. We therefore propose to phase in

a fee assumption of £2,000 for full-time undergraduates in real terms by 2008-09, when new fee arrangements will apply to most students in HE. A fee assumption of £1,750 would be made in 2007-08 as part of this phasing-in process.

75. We do not propose at this stage to change in real terms any other fee assumptions, such as for part-time or postgraduate students. This is because there has been no change to regulations governing the level of these fees. However, we would expect to keep all fee assumption levels under review.

76. The effect of not changing the assumptions for part-time and postgraduate students will be to alter the position in the tolerance band of institutions with high proportions of such students. Institutions with a higher than average proportion of part-time students in FTE terms will appear less well resourced compared to the standard. Migration funding would be provided if, as a result of such changes to the method, institutions fall below the tolerance band. We do not expect the adjustment to be substantial for the sector as a whole and would ensure that no institution will lose in cash terms in 2007-08 as a result of the introduction of this new structure.

77. We are aware that the average fee level in FECs may be lower than £3,000. We will be pursuing this issue in our conversations with the LSC, AOC and colleges, and expect to be able to introduce measures to ensure that our proposals do not unfairly discriminate against FECs.

Consultation question 6

Do you agree that we should make a fee assumption for full-time undergraduates, in real terms, of £1,750 in 2007-08 and £2,000 in 2008-09?

Volume measures

78. How we measure the volume of activity is an important factor in supporting our policies and priorities. It can give messages about the behaviours we want to encourage and also help to avoid unintended responses. We may choose to have different volume measures for different purposes, such as in the targeted allocations. The discussion which follows is concerned in detail with the volume measure that we use in allocating funds as a tariff to reflect volume and subject.

How activity is counted

79. The basic unit of measurement in the funding method is an FTE student. All students who meet certain threshold criteria are treated as full-time, with an FTE of 1. It is not generally possible to be counted as more than 1 FTE. Part-time activity is expressed in FTE terms by comparing it with the rate of study (length of time to achieve a qualification, or number of credit points studied in the year) of an equivalent full-time student.

80. We intend to maintain the FTE as the principal volume measure, and propose to use credit only as a means of funding in part the experiences of students who do not complete their studies.

81. In counting FTEs, we include students only if they complete their year of programme of study. In broad terms, we define a student as a non-completion if they do not either undergo the final assessment of, or pass, any module within their year of programme of study. Completion is measured against a student's study intentions for the year.

82. The recent evaluation of our funding method identified the treatment of non-completion as probably the most controversial aspect of the method. The main arguments against our current approach are as follows:

a. By not funding partial completion, we do not recognise a range of student achievements, and the associated efforts of institutions, as valid and fundable HE experiences.

b. The definition of completion assumes that students have fixed study intentions at the start of the year, and therefore constrains flexibility for institutions and students to agree changes to study patterns during the year.

c. Non-completions are not distributed evenly across the sector (as is effectively assumed through the current volume measure). Excluding them disadvantages those institutions that do most to widen participation, since students from under-represented groups are more likely to drop out. The treatment of non-completion is therefore at odds with HEFCE's strategic aim of widening participation.

d. We provide around £200 million through the widening participation allocation to compensate for the costs and risks that institutions incur by recruiting students that may be less likely to complete. This allocation for improving retention is based on prior educational attainment and age. However, the funding is seen as insufficient to offset the disadvantage that a significant element of student and institutional activity is not counted for funding purposes.

83. In short, our treatment of non-completions is thought unfair by a substantial number of institutions. The concept of an FTE has also come under pressure from institutions wishing us to measure their activity more finely and to deliver more flexibly.

84. Given these issues, it is appropriate to consider alternative ways to count students and the implications that these alternatives might have. We have identified two main alternatives to FTEs (each of which could in turn have a number of variations):

a. Funding on the basis of credit.

b. Funding to reflect institutional processes, such as numbers of guided learning hours.

85. We have rejected the second option as undesirable. Measuring guided learning hours would be very burdensome for institutions to report and does not sit comfortably with higher education, where much activity is self-led study outside the classroom or laboratory.

Credit-based funding

86. We commissioned a study to consider the feasibility and implications of funding on the basis of credit.⁵ As a result of this we do not believe that credit-based funding is an option for the immediate future.

87. The report highlighted that there are a number of practical difficulties to overcome before funding on the basis of credit would be possible. For many institutions it would involve an increased administrative burden, as it could only be achieved if they reported student activity at the module level.

88. There is also currently no national credit framework or consistent use of credit among institutions. In addition, to fund on the basis of credit may require allocations to be based on individualised student data collected at the end of each year – that is, HESA⁶ data for HEIs and LSC Individualised Learner Record (ILR) for FECs – instead of the current data collections we conduct each autumn (the HESES⁷ and HEIFES⁸ returns). Some of the implications of doing this are considered below.

89. These practical difficulties mean that moving to funding on the basis of credit is not viable in the short-term. We do, however, propose it as a direction in which we may wish to move in the future. In the meantime, there are steps that we can take that will support this possible move, and address the concerns that many institutions have over our treatment of non-completions.

90. In many respects we have the same issues around non-completion to consider with credit as with FTEs. In particular we would have a choice whether to fund:

- enrolments
- completed credit or
- awarded credit.

91. We would not wish to fund enrolments. It would provide funding for activity that is not undertaken, and may create too strong an incentive for institutions to recruit students who have little prospect of completing their studies. We also accept that any HE

⁵ 'Potential for using credits in the revised teaching funding method', August 2005, Higher Education Consultancy Group and CHEMS. Available on the web at www.hefce.ac.uk under Publications/R&D reports.

⁶ Higher Education Statistics Agency

⁷ Higher Education Students Early Statistics survey. The annual aggregate recruitment survey completed by HEIs, which informs our funding for teaching.

⁸ Higher Education in Further Education: Students survey. The annual aggregate recruitment survey completed by FECs, which informs our funding for teaching.

experience can be a beneficial experience, so there is a need to recognise partial completion, which cannot be done effectively by measuring enrolment.

92. Funding on the basis of credit completed or credit awarded are both feasible options for recognising smaller amounts of learning. Where they differ is in their treatment of completion. Funding on credit completed would maintain a definition of completion similar to that currently used for FTEs, whereas credit awarded would introduce the need for academic success.

Funding student achievement and progression

93. One of our strongest motivations for exploring credit-based funding is the need to support the provision of flexible learning opportunities. We believe that flexible learning will be of increasing importance for HE, both in terms of widening participation by groups that are hard to reach, and in terms of engagement with employers through new kinds of provision such as foundation degrees. It is likely, for example, that developments in this area, such as Lifelong Learning Networks, will require funding arrangements that enable and encourage students to transfer their learning achievements from one institution to another at different times.

94. We have already stated that in the future we may wish to direct more of our funding to protect and support particular HE outcomes in the public interest. We believe that support for student achievement and progression is central to the support of flexible learning, and is therefore an outcome that should be protected and supported by the volume measure.

95. We therefore think it may be worth considering funding on the basis of credit awarded in the longer term. The criterion of academic success means that it explicitly supports student achievement and progression. It would also enable us to recognise the achievements of students who were awarded credit in pursuit of a qualification, and so address concerns about lack of funding for partial completion. It would recognise that there are significant public interest benefits to an HE experience that falls short of gaining a qualification.

96. It could be argued that linking funding and academic success would compromise academic standards by encouraging institutions to pass students to ensure funding is received. We do not believe this to be the case. There is, for example, no evidence to suggest that our current definition of completion has encouraged institutions to ensure students complete for funding purposes rather than for educational reasons.

Consultation question 7

Do you agree with our proposal to consider moving in the longer term towards funding on the basis of credit awarded?

An interim measure

97. The phased approach to the review of the teaching funding method gives us an opportunity to address problems with the current method, and to develop and test new

ways of measuring activity, while still leaving our options open for the second cycle. We therefore propose to address the issue of not funding partial completion by developing the method to reflect credit awarded to students who are reported as non-completions.

98. This enables us to fund what non-completing students have successfully achieved. This could reflect the equivalent standard resource rate attributable pro rata to credit awarded, but might also take account of the contribution that the student's fee makes towards that resource level (on the basis that the institution may have retained the full fee, even if the student has not completed all the activity in the year). While HESES and HEIFES data are collected, the allocation would be derived by looking at credit awarded to non-completing students in previous years, as reported on the HESA or ILR returns, and normalised against the full-time equivalent credit. This would then be applied to the latest HESES and HEIFES non-completion rates.

99. This measure would be open only to institutions that provided individualised data that allowed us to identify credit points awarded. We will discuss with HESA and the LSC the implications for any changes to the data submitted by institutions.

100. The effect of this proposal will be to move institutions within or outside the tolerance band. Those that award an amount of credit to non-completing students that is above the sector average are likely to appear less well resourced (that is, they will move towards the -5 per cent boundary in the tolerance band if currently within or above it). This will require the provision of migration funding for institutions that appear less well resourced if they move below the tolerance band.

101. The earliest data that we could use for funding purposes would be from the 2007-08 record, which coincides with planned changes to the HESA student record. This gives institutions sufficient time to prepare for changes in data requirements. It also gives us a reasonable amount of time to develop systems and processes to ensure that credit data on the HESA record are fit for funding purposes. We could then make allocations on this new basis for 2009-10.

Consultation question 8

Do you agree with our proposal to reflect the credit awarded to students who are reported as non-completions, for institutions that report module information in their individualised student data returns?

Data sources

102. Two main data sources inform the funding method: the HESES and HEIFES surveys which collect in-year aggregate student numbers; and individualised HESA data (ILR data for FECs) which are reported at the year end. We currently use HESA/ILR data to provide more information about student characteristics to inform allocations, such as those for widening participation; and to reconcile with the aggregate data institutions previously reported to us in their HESES/HEIFES surveys.

103. We propose that we cease to use HESES and HEIFES data for funding purposes. That is not to say that some in-year reporting of aggregate student data would not be necessary. It would still be needed for government planning purposes, for example, to monitor progress towards the 50 per cent target for participation in HE. However, it could be collected in significantly reduced form as part of institutions' annual financial and planning returns, if these were submitted in the autumn.

104. There are three main reasons for this proposal:

- a. The removal of the complex HESES and HEIFES returns and their subsequent reconciliation against HESA and ILR data should reduce the administrative burden on institutions.
- b. We are already reviewing funding through the reconciliation of HESA data with HESES, and HEIFES with ILR data. The retrospective recalculation of grant in this way can be problematic for institutions, which can find that funding changes for at least a three-year period. Funding all institutions solely on their HESA and ILR data will avoid such retrospective changes to grant, and help to ensure all institutions are treated consistently in having allocations based solely on one data source.
- c. In the longer term, if we are to move to funding on the basis of credit awarded, then we will need to use data for completed years (to capture credit awarded), rather than forecast data (as contained in HESES and HEIFES).

105. There are, however, a number of technical questions that will need to be addressed before such a proposal can be implemented:

- a. The current reconciliation exercise uses a number of approximations to derive the reconstructed HESES return from HESA data, for example over the treatment of students whose completion status is pending. These approximations would need to be established as part of the funding rules or otherwise removed. Funding on the basis of credit awarded may help to resolve the difficulty of how to treat students whose completion status is not known at the time of the HESA submission, as funding would only be provided for credit awarded in the year.
- b. We would probably need to cease adjusting core grant within the year because of the time delay between the retrospective HESA returns and the prospective funding allocations. For funding for additional student numbers (ASNs), however, such an approach would be problematic, as we would be allocating additional funding for one year with no prospect of recovering it if the institution failed to recruit the additional students. This would be unacceptable from an accountability perspective, so we would still wish to adjust funding for each year in which ASNs were not delivered.

106. One of the likely concerns about using only HESA data for funding purposes is that it is more out-of-date. Therefore it may not reflect, for example, latest movements of student numbers between subject areas or levels. We do not consider this argument to be strong in most cases. All institutions would be treated equally – we would not be

using more up-to-date data for some, but not for others. We believe that significant movements of students between price groups would in general be rare and have only a modest impact on core grant (as opposed to ASN funding). In any event, the ending of in-year holdback of core grant (and its associated moderation) would be a significant benefit to many institutions. For directly-funded FECs and for some specialist HEIs, however, where HE numbers are relatively small, changes in student populations from year to year might have a more significant impact.

107. We do not underestimate, however, the significance of relying solely on HESA/ILR data for funding purposes, both in terms of changes in data provision and the accountability burden for institutions, and the technical issues that we would have to resolve to make the system work. However, if we are to fund on the basis of credit awarded, then we believe there is no alternative but to use only retrospective HESA and ILR data to drive allocations. The complexity involved means that this might take some years to implement fully.

Consultation question 9

Do you agree that we should move over time towards funding solely on the basis of HESA and ILR data collected at the end of the year, and cease to use HESSES and HEIFES data for funding purposes?

Support for part-time provision and widening participation

108. Widening participation and part-time provision were identified in the evaluation of the current method as two key areas which the sector felt were not adequately supported by the method. We believe that the measures we are proposing on funding non-completions and the re-distributive effect of making a fee assumption may go some way to addressing these concerns, but the future of support for these areas is worthy of further consideration here.

Part-time provision

109. It has been argued that recent measures to introduce variable fees in higher education, and new arrangements for student support, will raise some issues for part-time study. With few exceptions, HEIs will raise fees for full-time undergraduate programmes to the current maximum of £3,000 a year. The effect on full-time learners will be offset by the availability of grants, bursaries and deferred repayment.

110. Part-time learners do not have access to loans; they have access to less generous grants or bursaries; and must pay fees 'up front'. There is a means-tested course grant of £250, and income-related support for fees, with some institutions providing fee waivers where students are not eligible for tuition fee grants. In 2005-06 tuition fee grants will be between £590 a year for a half-time student to a maximum of £885 for 0.75 FTE or more. This is broadly pro rata to the existing maximum full-time fee of £1,175. Many part-time learners have fees paid by an employer or other agency.

111. There are a number of interrelated issues. Institutions are introducing higher fees for full-time programmes and will effectively receive those fees direct from the Government. Institutions which depend overwhelmingly on part-time provision have argued that the introduction of correspondingly higher fees for part-time students may deter those who do not have access to the same student support, and where there is no public provision to defer fee payment. In addition, it has been claimed that institutions may choose to prioritise their full-time provision, where income from relatively high fees is guaranteed, over part-time provision.

112. The HEFCE Board has considered these issues. It was conscious of the importance of part-time provision and listened carefully to those who thought that changes in student support arrangements put this at risk. It agreed that it would be premature to intervene in the new higher education market through a general subsidy for all part-time undergraduate provision, before that market had established itself and its effects had become clear. It also recognised that part-time learners are a heterogeneous group: many come from households that could afford higher fees, or have their fees paid by their employers.

113. The Board therefore resolved to maintain the part-time premium at its current level and to review the support given to part-time undergraduate provision and providers. It felt the review should take place when there was a clearer picture of how HEIs had been affected by the new fee regime for full-time undergraduate study. We expect to undertake the review during the first cycle of the teaching funding review, when details of recruitment to part-time courses are known.

114. The Board also gave broad support to ensuring that those most at risk of not being able to afford part-time study were protected by providing extra funds. Our widening participation strategic committee has advised that this should be undertaken through the existing funding stream for widening access for part-time students. We address this in the following section.

Consultation question 10

Do you agree that we should look to provide extra funds to support those most at risk of not being able to afford part-time study?

Support for widening participation

115. The widening participation allocation is in many ways a model of how we envisage the targeted allocations under principle B will work. The key issue here is the level of funds that we provide for widening participation. Alongside the evaluation of the current funding method, JM Consulting completed a report in 2004⁹ which highlighted that the costs of widening participation to institutions are greater than the current level of funds provided. Furthermore, as discussed in the previous section, we are committed to

⁹ 'The costs of widening participation in higher education', JM Consulting, available online at www.hefce.ac.uk under Publications/R&D reports.

providing extra funds for institutions to support those most at risk of not being able to afford part-time education. Over the coming year we therefore expect to explore ways of increasing the widening participation allocation to address this under-funding.

Supporting the most engaged

116. We have always maintained that the purpose of the widening participation allocation is to recognise the additional costs to HEIs of recruiting and supporting students from diverse backgrounds. JM Consulting's report found that those institutions most engaged in widening access would incur proportionally greater costs, not only through the increased volume of students and associated support costs, but by trying to engage with groups that were very hard to reach.

117. Widening participation remains a central strategic priority for HEFCE and for the funding method. As such we are considering whether these additional costs, incurred by institutions that have a significantly greater proportion of students from under-represented groups, should be recognised. This could be achieved by altering the allocation metrics to allow us to provide additional funds to such institutions. This may also encourage other institutions to invest further in widening participation.

118. We are aware that this change would raise some important questions both in policy terms and in implementation. We would want to ensure, for example, that we did not encourage institutions to recruit students who are unable to benefit from HE, simply to secure additional funding. We would also want to consider the balance of the sector as a whole and think through in detail the impact of encouraging institutions to grow in a prescribed manner. Equally we would want to ensure that those with a smaller proportion of students from under-represented groups did not lose out as a result. This means that the changes would only be possible if the overall level of funding for widening participation is increased. We would also need to explore carefully the point at which this additional funding could be 'triggered'.

119. All of these issues may be resolvable, and, if supported by the outcome of this consultation, will be considered over the coming year in our detailed thinking around how targeted strategic allocations will work in the new method.

Consultation question 11

Do you agree that we should investigate the possibility of recognising the additional costs incurred by institutions that have a significantly greater proportion than others of students from under-represented groups?

Additional information

120. Two consultation events will be held – in London on 9 December and Manchester on 13 December. Places are limited, so early booking is advisable. Please contact Alison Felton for further information: e-mail a.felton@hefce.ac.uk, tel 0117 931 7078. We will also be running a dedicated seminar for FECs at the AOC's annual conference on 15-17 November.

121. Responses to this consultation should be made by **13 January 2006**, using the online form available with this document at www.hefce.ac.uk under Publications. We are aware that many of the issues considered in this document are complex. We will therefore be publishing a 'Frequently Asked Questions' guide in early November, which will be built on as the consultation progresses. If you have any queries regarding this document please contact Chris Taylor on c.taylor@hefce.ac.uk to enable us to make this guide as useful as possible for all.

122. We will publish an analysis of responses to the consultation. Additionally, all responses may be disclosed on request, under the terms of the Freedom of Information Act. The Act gives a public right of access to any information held by a public authority, in this case HEFCE. This includes information provided in response to a consultation. We have a responsibility to decide whether any responses, including information about your identity, should be made public or treated as confidential. We can refuse to disclose information only in exceptional circumstances. This means responses to this consultation are unlikely to be treated as confidential except in very particular circumstances. Further information about the Act is available at www.informationcommissioner.gov.uk

123. Many of the propositions discussed have timing and transition implications which we have discussed throughout the document. We represent these together in Table 2 below.

124. In preparing this consultation we have focused on consulting on what we see as the major issues. There may well be other issues which we have not considered, or you may have comments that you wish to make that are not directly related to any of the questions so far. We would be happy to hear them.

Consultation question 12

Do you have any further comments?

Table 2 Timing and transition

Year	Targeted Allocations	Full-time undergraduate fee assumption (in real terms)	Consistent national framework for costing of teaching	Funding of credit awarded to non-completers
2005-06	No change to allocation	No change	Establish 'TRAC for teaching' implementation plan	No change
2006-07	No change to allocation Consultation on new metrics	No change	Establish consistent national framework for costing of teaching	Changes to HESA for 2007-08 made
2007-08	Allocation of existing premiums as targeted allocations	£1,750		Autumn 2008 HESA data returned
2008-09	Introduction of new allocations	£2,000		Included in calculation of allocations
2009-10	New allocations in operation	£2,000		

List of abbreviations

AOC	Association of Colleges
ASNs	Additional student numbers
BUFDG	British Universities Finance Directors Group
DfES	Department for Education and Skills
FAQ	Frequently asked questions
FEC	Further education college
FTE	Full-time equivalent
HE	Higher education
HEFCE	Higher Education Funding Council for England
HEI	Higher education institution
HEIFES	Higher Education in Further Education Students survey
HESA	Higher Education Statistics Agency
HESES	Higher Education Students Early Statistics survey
ILR	Individualised Learner Record
LSC	Learning and Skills Council
OFFA	Office for Fair Access
TRAC	Transparent Approach to Costing