



# **RCUK/UUK Review of the Impact of Full Economic Costing on the UK Higher Education Sector**

**A report prepared for Research Councils UK  
and Universities UK by a panel chaired by  
Professor Alan Alexander FRSE**

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# I. Executive Summary

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The Review aimed to a) assess the impact of the revised funding arrangements for research on the sustainability of research in Higher Education Institutions; b) advise on changes that would enhance the delivery of sustainability; and c) propose any changes needed in the operation of the full economic costing (fEC) system. The definition of sustainability used in TRAC methodology was accepted:

*“An institution is being managed on a sustainable basis if, taking one year with another, it is recovering its full economic costs across its activities as a whole, and is investing in its infrastructure (physical, human, and intellectual) at a rate adequate to maintain its future productive capacity appropriate to the needs of its strategic plan and students, sponsors and other customer requirements.”*

## **Background to the introduction of full Economic Costing (fEC) in the HE Sector**

Faster growth in project-related funding (including significant growth in income from the Research Councils and charities) than in the block grant of core research funds has historically put considerable stress on the sustainability of institutions' research activity and infrastructure. The absence of robust cost data had led many institutions to underestimate the costs of research and other projects, so that historically much research has been undertaken below cost.

From before the Dearing Report in 1997 [1] Government and HEIs have been concerned about sustainability, and a succession of reports and consultations [2-10], including the 2004 Science and Innovation Investment Framework [5], highlighted the problem. As a result, the Government agreed that the Research Councils should pay 80% fEC for projects they funded as from April 2006. The impact of this major change was to be reviewed after three years, and this report constitutes that review.

The Review looks widely at impacts across different aspects of sustainability in HEIs including the implications of fEC for interactions with Government, charity, business and European research funders.

The Review's overarching conclusion is that almost all measures of HEI sustainability have significantly improved during the current decade, with a major part of this increase being due to the introduction of fEC payments by Research Councils and other funders. The Review therefore recommends that fEC payments should continue on the current model, with a number of technical improvements and with clearer demonstration of sustainability monitoring and governance on the part of HEIs (Recommendations 1 & 2).

## **Physical and Financial Sustainability**

The financial situation for UK universities has improved markedly over the current decade. The imbalance between project-research and core funding has been stabilised. Over the past six years (02/03 to 07/08) project-research funding has increased by 4.7% (8.0% for Research Councils) annually in real terms, and the Quality Related (QR) element of Funding Councils block research grant by 5.5%.

Not only has the ratio of 'project' to 'baseline' research stabilised, but the contribution to the full costs of project-research funding has significantly increased. This is particularly true for Research Council grants, but it is also the case for funding from Government, business, and to a lesser extent charities and the EU. fEC is still in its early days, and it has proved difficult to quantify the exact contribution that it has made to achieving a more sustainable research base in HEIs, but the message is a positive one.

While research funding has markedly increased, and most of the metrics used to measure financial and physical sustainability have recorded improvements, it is of concern that the Transparency Review for 2007/08 concluded that research makes an annual TRAC-adjusted deficit in excess of £2 billion. Operating surpluses have declined since 2005-06 for the major research active universities, and there is a risk that the current recession and the consequential movement in exchanges rates, together with increases in HEI salary and utilities costs, may jeopardise the gains in physical and human sustainability which have been achieved. Sustainability reporting should therefore be given greater prominence both internally in universities and across the HEI sector.

Transparency Review data has been collected for the past two years showing income and TRAC-adjusted costs by type of funding organisation. This data is extremely valuable, but the data could usefully be analysed looking at the impact of research intensity or HEI size on the recovery of fEC. It is recommended that Transparency Review data is published on a UK basis, averaged by TRAC Peer Review Groups (Recommendation 3).

There is no specific mention of HEI sustainability in the Science and Innovation Investment Framework Annual Reports for 2006, 2007 or 2008 or in the 2008 Innovation Report. Sustainability metrics could be given greater prominence in future reports (Recommendation 4).

The governance of sustainability within HEIs will continue to be important. There are many examples of good practice, but a strengthened and more consistent embedding of sustainability into governance processes is needed (Recommendation 5).

There is scope for HEIs to use their internal Trigger Metrics and Key Performance Indicators as supporting evidence within their annual Capital Investment Framework submissions to the Funding Councils (Recommendation 5).

The Review recognises that universities have put significant effort into producing Sustainability Frameworks and proposes that guidance should be given by the Funding Councils on the intended future use of these, and how they can be more effectively embedded within strategic planning and management processes (Recommendation 6).

The Review received comments from individuals and Learned Societies suggesting that more of the fEC uplift should be passed directly to the investigators who win the grants and contracts. The Review was clear, however, that estates and indirect rates are calculated on an institutional basis, and it is for HEIs to manage sustainability across all departments, while clearly explaining to academic staff the bases on which fEC is calculated and grant income is distributed.

In the conduct of the Review the issue has arisen of how the fEC and sustainability processes can drive efficiency within the system. UK HEIs already achieve outstanding output and impacts on relatively lower investment than competitors. However, it is proposed that the sector, together with the Research and Funding Councils, explore how further efficiency drivers can be incorporated into the process of operating and monitoring fEC, and how assurance can be provided that the fEC uplift is contributing to sustainability rather than increasing volume (Recommendation 7).

There are many issues surrounding the use of fEC for maintenance of facilities and equipment, the overlap of direct and estates costs with equipment access charges and resources from capital investment funds, and direct funding of equipment use. Clarification of these issues should be provided by the TRAC Development Group and RCUK (Recommendation 8).

### **Human Sustainability**

Roberts' funding, QR funding, employment law and the Researcher Concordat (and in England the Funding Council Support for Rewarding and Developing Staff initiative) have all made significant contributions in recent years to the sustainability of human resources committed to research. Universities indicated that fEC is also contributing to this, particularly in providing greater flexibility to departments to provide support for development activities and bridging funding to retain staff between externally supported research contracts.

The Review notes the Concordat on Career Development of Researchers, and as part of its implementation it recommends that the possibility of developing metrics to better understand and monitor the sustainability of human resources be explored. This will be particularly important as the Roberts' agenda evolves (Recommendation 9). To inform this, it will also be helpful to improve the consistency with which the HESA staff identifier is used to record staff movements.

## Research Council and National Academy implementation of fEC

fEC has on the whole been introduced successfully by Research Councils and National Academies. The Review was particularly interested in the impact of fEC on proposals, and notes that post-fEC changes in the Directly Incurred costs and staff-hours requested were largely as expected.

The number of proposals to the Research Councils slightly increased following the introduction of fEC, and decreased significantly in 2008. There is no evidence that the decline in success rates, evident since before 2003, has been influenced by fEC.

The Review notes concerns that changes to TRAC rules may be over-complicating the system and reducing its transparency. A detailed list of comments and recommendations on the need to harmonise the interpretation of fEC rules by different Research Councils is being acted upon by RCUK (Recommendation 10), and comments are included in the report from the TRAC Development Group on TRAC issues raised by HEIs.

## Government Departments

Most HEIs indicated that they recovered significantly less than 100% FEC from Government Departments and that major differences exist between and within departments. The Review has found that research funded by Government departments is increasingly placed using competitive contracts, and Transparency Review data for 2007/08 indicates that percentage FEC recovery may be in the region of 75%.

Central and local Government funding of research shown in HEI financial returns has increased by 3.5% annually in real terms since 2002/03. The Review recognises that Government departments operate in an environment which makes it difficult for them to record the FEC percentage paid. A recommendation is therefore made to HEIs to monitor FEC-recovery on each research contract and grant, and to use aggregate figures for different funder types as internal performance indicators (Recommendation 11).

Where HEIs are contracted as sole providers of research to Government departments, such research should continue to be supported at 100% FEC (Recommendation 12).

## Charities

Twenty-three percent of project-research income is received from Charities, and the Review recognises the vital role that this funding plays for many university departments. Transparency Review data for 2007/08 indicates that across the UK HE sector around 60% FEC is being recovered directly from UK-based Charities.

The sustainability of this funding has been enhanced by the introduction of the Charities Research Support Fund in England and its equivalents in the devolved administrations. The principle behind this support is well established, but there is scope for greater transparency and coordination between Funding Councils and charities in the manner with which the uplift is calculated. There also needs to be clearer understanding of the level of 'top-up' funding needed to bring percentage FEC recovery on charity research grants close to that paid by Research Councils (Recommendation 13).

Charities have different policies regarding the degree to which they contribute towards some Directly Allocated components of fEC (for example investigator salaries). It is recommended that the Association of Medical Research Charities should maintain a website to summarise this information, including links to the grant rules pages of their members, and that individual charities should provide clearer information on the components of Directly Allocated costs which they are likely to support (Recommendation 14).

## Business and industry

HEIs are increasingly using fEC costing data to inform the pricing of business and industry projects. Cost is not always the primary factor, however, and many institutions make informed judgements based on non-financial aspects, as well as the need to maintain sustainability. It is crucial that this continues and that the professionalism of staff involved in pricing and negotiating is enhanced to ensure that they are well equipped with appropriate commercial skills (Recommendation 15).

Transparency Review data for 2007/08 indicates that around 75% of fEC<sup>2</sup> is being recovered on contracts with industry. The Review recognises that there is a general concern among business and industry partners about the increasing costs of research in the UK. The CBI Inter-Company Academic Relations Group (ICARG) asserts that the UK is the 'most expensive country in world for Research Assistants'. These increases are being attributed to HEIs seeking to recover at least the fEC of research projects, and it is suggested that UK-based companies are placing an increasing proportion of their research budgets overseas. The Review proposes that this issue be looked at in more detail (Recommendation 16).

### Europe and International

The Review notes that there is great interest world-wide in the UK development of TRAC-fEC, and the UK is seen as a leader in implementing policies to ensure a more sustainable research base.

Funding from the European Union provides 7.7% of total project-research funding, and funding from this source is growing at 6.7% annually in real terms. It therefore plays an increasing role in the UK research base. Despite recording a return of only 58% fEC on EU projects, HEIs obtain significant benefits from their involvement with European partners, particularly in building collaborations and networks.

The Review is encouraged by the extent to which the sustainability agenda is being promoted by the European Commission and European University Association. The UK should continue to stress the importance of sustainability and the need for better reimbursement in EU funded programmes.

The Review notes that Framework Programme 7 has a funding model which allows participants to be reimbursed at a percentage of their full costs, rather than direct costs with a fixed overhead as had been the case in previous years. This, in the longer term, has the potential to allow HEIs to participate on a more sustainable basis.

A derivation of TRAC has been developed to ensure that HEIs can take advantage of this if they wish to do so. However, due to Commission regulations this has become very burdensome. It is proposed that the Financial Sustainability Strategy Group and UUK lobby the Commission to reduce the burden of this model (Recommendation 17).

The Review recommends that the UK Research Office in Brussels and the FCO/DIUS Science and Innovation Network should keep UK funders aware of changes in the funding of indirect research costs in countries with significant research programmes (Recommendation 18).

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<sup>2</sup> As indicated in the Preface: when a lower-case 'f' is used in fEC it indicates the process of 'full Economic Costing'; when fEC is fully capitalised it stands for Full Economic Cost. Note that this category is actually 'Industry and Other' in the Transparency Review. - See footnote to table 3.

# 10. Recommendations

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1. The principle of providing additional investment in support of fEC while not building volume is a sound one, which is having a positive impact on the sustainability of the HE research base. This principle should continue to underpin the sustainability agenda.	20
2. The governance of sustainability should be strengthened throughout the HE sector.	20
3. Funding Councils should continue to strengthen the methodology used in the collection of Transparency Review statistics and consider publishing annual averages for TRAC Peer Groups.	20
4. DIUS should make greater use of Trigger Metrics and Transparency Review statistics in the Annual Reports on the Science and Innovation Framework (2004-2014), including reporting on progress towards the SIIF Goal of 'ensuring a financially sustainable level of activity by early in 2010 decade, avoiding over-reliance on non-research income and under-investment in research infrastructure'.	20
5. The review recognises the valuable contributions that sustainability frameworks, trigger metrics and the capital investment frameworks have had in promoting, incentivising and monitoring sustainability. It is recommended that these processes are now brought together to increase their impact and avoid duplication. Institutions should be encouraged to utilise appropriate KPIs to provide evidence of sustainability while reflecting the diversity of the sector.	20
6. A future Funding Council report to the Funders Forum on HEI Sustainability should comment on lessons learned from existing Sustainability Frameworks and give guidance to HEIs on their future revision and use, within the context of 'streamlined reporting' and the HERRG Concordat.	20
7. The Review concluded that an improvement is required that more clearly demonstrates the fEC contribution to the sustainability of the research base and which encourages efficient use of the funds. A working group should be established (with representatives of the Research Councils, the Funding Councils and UUK) to recommend to FSSG and DIUS: a) a light touch mechanism to provide reassurance about how fEC funding is used and how it contributes to sustainability; b) procedures to improve the transparency of the variations in the charge out rates between organisations, which might include the publication of such rates. The group should be required to report in no more than six months.	20
8. The TRAC Development Group, the Funding Councils and RCUK should examine issues relating to the accumulation of resources for maintenance and replacement of facilities and equipment. This should include examination of the use of depreciation in directly incurred and directly allocated costs, and any potential overlap of equipment access charges, QR, capital investment funds, and additional funding for infrastructure and equipment from other sources.	20
9. HEIs should continue their support for staff development activities, and should continue to develop ways to monitor implementation of the Concordat on Career Development of Researchers, and 'Roberts Funding Activities'. A subset of these metrics may serve as Trigger Metrics for 'staff sustainability', to be used alongside those for financial and physical sustainability.	23
10. RCUK should report on progress towards the harmonisation of Research Council grant rules and procedures on their website, and how this relates to commitments made in signing up to the HERRG Concordat.	29
11. Universities should monitor the percentage recovery of FEC from the project-research funding sources reported to HESA and use these as internal KPIs. These are in large part already submitted to HEFCE in Annual TRAC Returns. Publication by the Funding Councils of average percentage FEC recovery by funding source would alert the community to any trends that jeopardise sustainability.	33

12. When Government departments are funding research at HEIs, other than through competitive contracts where prices will be set according to market and other factors, they should continue to provide this funding on the basis of paying 100% fEC. In bidding for competitive research contracts, HEIs should formulate their bids with the aim of recovering 100% fEC, unless considerations related to the potential value of intellectual property, or other strategic reasons, justify recovery at a lower rate in a specific case. 33
13. The Review recognises the widespread support for charity research support funds and encourages the Funding Councils to ensure that the mechanisms for calculating these funds are transparent. The Review recommends that there needs to be a clearer understanding of the level of 'top-up' funding needed to bring percentage fEC recovery on charity research grants close to that paid by Research Councils. The charity research support funds are crucial to ensure that charitable funding in HEIs is sustainable, and Government should work with the Funding Councils and charities to achieve this. 38
14. The Association of Medical Research Charities should maintain a web-site which summarises overall approaches to payment of fEC in the charity sector and provides links to the detailed financial rules of their members. Charities are also encouraged to clarify the published versions of their rules regarding eligibility of directly allocated costs. 38
15. To facilitate contract negotiation with business, HEIs should a) develop a clear and explicit formulation of the factors to be taken into account when making decisions on the pricing of research which is funded by business or Government, and b) implement an appropriate level of delegated authority for negotiators. 41
16. Research should be conducted to examine the degree to which UK industry is contracting research overseas, and the degree to which research at UK universities is being contracted inward by overseas-based companies. This study would examine the reasons for these flows and for any trends that can be discerned in them. Such research should be eligible for support from the key departments concerned (FCO, BERR, DIUS) and ESRC, and involve parties such as UKTI which is responsible for overseas promotion of UK's attractiveness as a location for R&D. 41
17. UUK and the Financial Sustainability Strategy Group should work to reduce the burden of TRAC EC FP7 on the sector 46
18. The UK Government, HE agencies and bodies such as UUK should continue to ensure proactive dialogue and engagement with the European Commission and Parliament on the sustainability agenda. 46



RESEARCH  
COUNCILS UK

Research Councils UK  
Polaris House, North Star Avenue  
Swindon, Wiltshire SN2 1ET  
United Kingdom  
Tel: +44 (0) 1793 444420  
Fax: +44 (0) 1793 444409

[www.rcuk.ac.uk](http://www.rcuk.ac.uk)  
[info@rcuk.ac.uk](mailto:info@rcuk.ac.uk)