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Executive summary and recommendations

Executive summary

Introduction and background

Demands and expectations on universities both in teaching and research are growing rapidly. However public investment in Higher Education in the European Union member states is less than its competitors. The costs of universities' activities are rising and hence the financial sustainability of their missions will certainly be the primary issue of concern for universities in the 21st century. The first step in responding to these pressures is for universities to identify the real costs of their activities. The European University Association has conducted this project to examine European universities' progress towards this first goal and the relationship between this progress and individual universities' autonomy and accountability. The project has been undertaken with the support of the Directorate-General for Education and Culture of the European Commission.

Since 2005, EUA had been examining the issues of funding, autonomy and accountability through engaging its members, some 800 European universities in 46 countries and 35 national rectors' conferences, in launching an evidence-based debate on improving and updating funding structures. Conferences, workshops and projects assessed the status of system changes for funding and analysed various European funding and costing models.

The objectives of this study are to provide information and empirical data for the debate on financial sustainability from an institutional perspective, analyse the status quo of the development of full costing and the relationship between autonomy and accountability and financial sustainability.

The report addresses several parties and includes policy recommendations as well as practical advice for universities. The recommendations to universities, national governments, and European institutions are listed at the end of this executive summary.

Summary of Findings

Impact of Terminology

A major obstacle in comparing data has been the absence of a commonly understood terminology for finance, costing and accounting and costing systems in higher education in Europe. Financial data from each case study required detailed analysis to be sure of what was covered by certain terms used, or to take account of the varying financial contexts (differing tax regimes; depreciation; insurance rules, etc).

The institution-by-institution approach combined with a careful analysis of the results led to an in-depth understanding of how costing terms are interpreted in different countries, which revealed that financial terminology in the context of European Higher Education has to be used with caution. It is therefore necessary to work towards a more coherent terminology and be aware of possible (mis)understandings when debating this on a European level.

There are multiple reasons for this. The terminology of full costing in higher education in Europe has been influenced by various factors, such as the language and concepts for cost reimbursement used by European Commission Research Framework Programmes FP6 and FP7. Terms which, under FP6 and FP7, were specific to research projects are now being used to describe costs for overall activities, leading to confusion as to the precise definitions of these terms and what they really comprise in terms of costs.

Management costing and accounting theory, in particular Activity Based Costing (ABC) – a technique commonly used to establish full costing systems in Higher Education, has influenced the definitions but not yet achieved the common understanding and use in the higher education sector throughout Europe that they have in the business sector.

Advanced systems and their concepts and terms have had an impact as well. The Transparent Approach to Costing (TRAC) in the UK introduced a terminology with a very country-specific meaning

which can lead to misunderstandings when used in other countries. "Full economic costs", which is the term used in the UK, includes a special form of depreciation, the cost of capital employed and risk. The study found many examples of the "mis" use of the term "full economic cost".

The individual institutional ability to identify and allocate direct costs has influenced the understanding of what a direct cost is as well as the definition of cost objects.

National legislative differences across Europe affect costing and accounting practices and terminology. Different forms of depreciation, different terms in financial statements, different rules for property insurance in the public sector and the use of similar terms with different meanings make it extremely difficult to develop any standard terminology or comparability.

For the time being, EUA suggests adopting the term "full costing" to stand for the ability to identify and calculate all direct and indirect costs of a university's activities, including projects, in order to leave the necessary room for diversity in approaches.

Diversity

An analysis of costing and funding from an institutional perspective needs to take account of the great diversity among European universities and to cover their legal status, size, profile, ownership of property, governance, funding structure, costing structure and the level of autonomy. The findings of the study suggest that all these factors influence the development of full costing. It further allows universities that so desire to introduce full costing to identify others with similar structures for possible cooperation or for benchmarking purposes.

Status of development of full costing

The study shows that some countries or universities are well ahead of others in terms of the development of full costing systems. Development ranges from countries, such as the UK and the Netherlands, where a uniform but flexible system has been introduced in more or less all universities, to countries where none of the universities have developed full costing, such as Slovenia and Estonia.

Only certain universities have the necessary data available to introduce a full costing system – in fact

the amount of data available varied dramatically. The range encompassed everything from a lack of even basic information to very sophisticated databases covering students, courses, staff, staff time, estates and use of space. This is a very important factor because the quality of database and information systems influences the time, effort and investment needed for the implementation of full costing.

Another important factor for the development of full costing is the institutional context. National formal requirements, positive incentives or support for the development play a crucial role in progress towards full costing.

European Funding schemes that influence the design of costing systems need to be more aware of the range in the development of full costing in universities and should take this into account in the design of their rules of application and participation. Universities and countries which are not yet able to fully identify their costs need positive incentives to develop these models.

The role of external support

Support for the introduction of full costing was found to come at three different stages and was judged to be of the utmost significance for a successful outcome. It came as support for the development of the model, for the implementation of the model and in the form of post-implementation as funding on a full cost basis.

External support was found largely to come from national governments, national agencies responsible for the funding and/or organisation of universities, organisations representing all universities (e.g. Rectors' Conferences) and other external funding bodies.

Support can be found in the form of direct financial contributions but also through providing concrete consultancy for the development of full costing systems in the form of expertise. Advisory/consultancy support includes workshops, conferences, training, development of guidance materials, websites, exchange programmes, etc.

There is evidence that there is a positive relationship between the status of development and the level of support received. And countrywide coordinated development has many advantages in terms of increasing comparability and efficiency.

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In many cases, however, there is no external governmental support at any of the three stages and although there are countries where considerable progress has already been made to develop and implement full costing in universities, there is also a large number of countries with no countrywide coordinated development and a significant number of universities unable to identify the full costs of their activities.

Drivers for implementing full costing

There are many different drivers for the implementation of full costing, which exist on an institutional, national or European level. Often two or three of these drivers are behind the design, development and implementation of full costing systems.

At the start of the project it was assumed that the main driver behind the move to identify full costs was external competitive research funding, in particular the European Framework programmes for Research and Technological Development (FPs). The project revealed significantly though that currently the most important driver is the use of full costing as an institutional strategic management tool.

Nevertheless, European competitive research funding schemes play an important role. With their model of cost recovery they motivate universities to implement full costing while increasing the pressure on national competitive funding schemes to follow their example. National funding schemes that do not fund indirect costs provide no incentive for universities to establish models to identify these costs.

Benefits of full costing

Full costing provides benefits for universities, national governments and on a European level. Among the benefits for universities are: a more systematic approach to activity analysis and costing; a more efficient internal resource allocation; improved strategic decision-making based on better understanding of investment decisions; benchmarking possibilities within the sector and an enhanced ability to negotiate and price activities, which lead to higher cost recovery of project costs and contribute thus to financial sustainability.

On the national and European level full costing is vital to ensure accountability. It also builds up trust between government, funding agencies and universities and smoothes out the transition towards autonomy. It facilitates national government budget allocation, as universities can prove what they need on a reliable and verifiable basis. Full costing enables universities to act more efficiently and base their decisions on sound data, which, in turn, reassures the government that the funding provided is used appropriately. Robust costing systems can also help governments to benchmark their own achievement of objectives more effectively. Full costing is a tool that can enhance financial sustainability and in the long run create stronger and more competitive universities which helps strengthen the European Higher Education Area. Enhanced accountability will also build the case for simpler and less costly procedures in contract and grant funding applications for research and innovation.

Obstacles to implementing full costing

The picture emerging from the project shows that there are both internal institutional and external obstacles. Some of these do not hinder the process of implementing full costing as such but they add to the length and weaken the quality of implementation.

Among the most common institutional obstacles are resistance to change and towards a managerial approach in universities, concerns over time accounting and a lack of management and leadership commitment. To overcome these internal barriers it is necessary to raise awareness of the benefits of full costing among the top leadership and key academic and administrative staff of the university and to communicate effectively and extensively throughout the institution during the implementation of full costing.

The most common external obstacles are a lack of autonomy, legal barriers and a lack of trust between stakeholders, in particular between funders and universities. Universities also face a lack of external financial support with the implementation of full costing which is a costly process and a strain on financial, technical and human resources.

Finding solutions to these problems resides in the call for greater autonomy for universities and financial and other support in its various forms as identified through this project. An increased importance assigned to the development of full costing should also help in transforming attitudes from a "low cost culture" towards correct pricing for projects undertaken by universities.

The role of funding schemes

European and national funding schemes are major drivers in the development of full costing in European universities but play a curiously double role. The project found that certain aspects of the rules, implementation and interpretation of important funding programmes such as the European Commission Seventh Research Framework Programme (FP7) have created a situation, where this positive driver for change risks becoming a barrier for the implementation of full costing systems. A careful analysis of the current rules and how they are applied across a range of universities might be advisable prior to the 2010 mid-term review of FP7.

The current three possible forms of recovering indirect costs from FP7 (1: analytical accounting system for the most advanced, 2: a simplified method for a less complex system and 3: a flat rate for those costing systems where indirect costs are not identified to a sufficient extent) aim to take account of the different status and profiles of universities throughout Europe. The project findings suggest however that the first 2 models (analytical accounting system and simplified method) need to allow a wider scope for different methods of identifying the direct and indirect costs of projects. Increased communication on possible full costing systems would help to reduce the insecurity on the subject identified through this project within the higher education community.

One issue of increasing significance is that external competitive project funding usually only partly covers full costs even if these are identified. The analysis of project data suggests that more and more universities are becoming aware that their financial sustainability is at risk if they carry out projects that are not fully funded. This, in turn, increases the danger that the objectives of funding programmes, such as enhanced research capacity, innovation and economic growth will not be fully met if an increasingly large group

of universities refrain from application because they fear they will not recover the full costs of activities and projects undertaken.

The project's findings suggest that the majority of European universities and, in particular, universities from the new EU Member States will not be able to identify the full costs of their projects or activities in the next few years in a way that would enable European funding schemes to cover a higher percentage of indirect costs, without strong incentive and support both on European and national levels. The risk that they will only recover indirect costs at a flat rate of 40% for projects from 2010 onwards as opposed to the 60% available now and the possible threat of an even lower rate subsequently, may harm Europe's position in terms of global competition in the field of research and innovation.

EUA emphasises, therefore, that there should be further analysis of the current experience of universities with FP7 contracts/grants particularly before taking any decisions on flat rates for indirect costs recovery in order to avoid any potential competitive disadvantage. (US funding schemes, such as NSF funding, provide a higher percentage of funding of both direct and indirect costs). Given the status of development as revealed by this project, EUA further suggests providing support to help universities implement full costing.

EUA also re-affirms its position already made in its response to the European Commission Green Paper on "The European Research Area: New Perspectives" (2007) that a move towards full cost funding of research supported by external funding agencies is an essential condition to underpin the sustainability of universities' research missions.

The role of autonomy and accountability

The project showed that autonomy is one of the conditions that underpin the implementation of full costing. Universities with a greater autonomy, especially in legal and financial matters, have more room for decision making and understand the need to have the appropriate instruments, such as full costing, for managing this freedom. A lack of autonomy can, on the other hand, be an obstacle for implementing costing systems. The inability to influence, for example, the costs of human resources and facilities at the institutional decision-making level, makes it less vital to have tools for the identification of costs at hand.

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The project used the collected financial data from participating universities to see whether the degree of autonomy made a difference to a university's income and cost structure, and to explore some hypotheses put forward in the general policy debate on autonomy and funding.

To analyse further the relationship between autonomy and financial sustainability an aggregate legal and financial autonomy index was calculated which was constructed on the basis of 8 factors taking into account the different limitations imposed.

The total autonomy score and financial data indicate that more autonomous universities are better able to attract funds from different sources and that more autonomous universities are able to attract more international funding. The plan is to further explore this first step of the project's pilot sample with a larger sample of universities which could form the basis for identifying indicators of universities' autonomy and their benchmarking.

If autonomy is one side, then accountability is the other side of the coin. To be truly "accountable", universities have to fulfil targets, demonstrate quality and show what they have done with public and private funding. Full costing is one of the essential tools with which universities can prove to funders, students, taxpayers and society at large what their money is spent on. It is one of the key pillars of accountability.

The project revealed that there is a risk of accountability rules and procedures limiting autonomy or leading to complex bureaucratic reporting procedures. There need to be, of course, appropriate ways of showing expenditure of public and private funding. But the amount of data gathering and reporting for received funding, for example, needs to be proportional to the amounts received, and funding programmes should take more account of this in their rules of participation and requirements.

There are indications that, in general, requirements in funding schemes under the umbrella of accountability are too complex. The findings show that complex procedures do not necessarily provide a better proof of the correct use of received funding.

A university's flexibility can be restricted by an over-reliance on competitive funding sources. Competitive funding sources provide funding for particular projects or activities whereas a lump sum or block grant allows a university to shift resources internally according to its financial or strategic needs. Thus, too much reliance on competitive funding sources effectively limits financial autonomy. EUA calls for an open discussion on this issue of reaching the right balance between autonomy and accountability instead of simply introducing more and stricter rules.

Complexity

Full costing is a complex process that has to be implemented appropriately according to the specific needs and context of the university. It has to satisfy a number of different objectives and stakeholders, and it has to be flexible and robust enough to accommodate all these different needs through the provision of appropriate tools and administrative capacity. Therefore, it is important that universities themselves have long term goals and multiple purposes in mind when designing their system but it should not be made more difficult than necessary. Full costing is a means to achieve certain ends and not an end in itself.

One factor which significantly increases the complexity of full costing are the diverse requirements of external funding schemes, established to ensure accountability. Each funding scheme imposes different (sometimes conflicting) rules for institutions that make it difficult for them to establish well designed processes. This confusion calls for more coordination between national, European and international funding schemes and the need for the European Higher Education and Research community to share examples of best practice. EUA, for its part, is willing to act as a catalyst in this process.

Recommendations

Recommendations to universities

1. Start the process of full costing.
2. Understand the complexity and multiple purposes of costing systems and the requirements of stakeholders and then take account of these factors in the overall design.
3. Weigh up and then outline the multiple benefits of implementing costing systems and build awareness of these benefits within the university.
4. Use the costing system as an integrated strategic tool for planning and decision-making.

Recommendations to national governments

5. Recognise that universities need enhanced financial capacity to implement full costing.
6. Provide financial, technical, advisory and Human Resource support in implementing costing systems.
7. Grant universities the necessary autonomy to act independently.

Recommendations to European institutions

8. Work towards a coherent terminology and apply these terms in a consistent fashion.
9. Increase awareness on a European, national and institutional level of the multiple benefits of full costing (e.g. through follow-up activities of the Modernisation Agenda and European Research Area policy frameworks).
10. Recognise the variation in the status of development and ability to implement costing systems within European universities and provide further help and support to enhance this ability in managing European funding schemes.
11. Further simplify the rules for both FP7 and future European research funding programmes. Greater dialogue and analyses of existing rules and practices and how they are implemented should be fostered, involving representatives from universities and the relevant European institutions to allow for an optimum grasp of the situation, to achieve more efficiency in administrative procedures and to remove unclear or conflicting regulations at the 2010 review.

Recommendations to European institutions and national governments and other funders

12. Balance the need for accountability with less complexity of the information required in competitive funding schemes.
13. Work towards more coherent conditions for external funding requirements on European and national level.
14. Move towards funding on a full cost basis to contribute to financial sustainability and encourage other external funders to move in the same direction.

Recommendation to all parties

15. The term "full costing" should be adopted for the time being to stand for the ability to identify and calculate all direct and indirect costs for all of an institution's activities including projects.