Full Economic Costs and Resource Allocation in the University

At recent information sessions on FEC, a number of staff sought information on how the introduction of FEC will impact on the resourcing of research projects, which do not fully cover full economic costs. The academic community will also be interested in how the contribution which their external research income makes towards University overheads and estate costs will be handled within the resource allocation model (RAM).

This article provides a brief introduction to this topic. Faculty secretaries and finance officers will be able to provide additional guidance. The broader issues surrounding the setting of Faculty budgets is covered in the 2006-07 Planning and Budgeting guidance, which was recently issued to all Faculties.

In order to better understand the concepts in this article, readers may find it useful to refer to the series of articles that appeared in the Newsletter over the last two years, explaining how FEC works. These can be found on the FEC project website at
http://www.gla.ac.uk/staff/fulleconomiccost/publications/index.htm

The key point to make at the outset is that the introduction of FEC comprises two elements; first, it is simply the use across the HE sector of a new costing methodology; second, it introduces the requirement to build in an additional element for sustainability. This is defined in the methodology as building in a component to replace and maintain our capital base (principally our estate), and adds approximately 9% to the cost of a grant or contract. In itself the introduction of FEC does not imply that it is more expensive for Universities to carry out research: the FEC costing approach merely makes the full costs of research transparent and shows the amount which would be required if we were able to achieve fully funded research to ensure the sustainability of this activity. In the case of some externally funded research the introduction of FEC will bring additional income into the University - for instance the Research Councils have an additional £120M per annum rising to £200M per annum next year to provide additional funding for existing volume. Research council projects, although only funded at 80% of FEC, in practice will bring a greater contribution to University overheads than under the previous funding regime.

Of course this does come at a price. Universities will increasingly have to demonstrate that they are operating on a sustainable basis, and in the medium term will need to be able to demonstrate that they are covering any 'FEC deficit' on externally funded research. This will need to be matched from RAE (QR) income, or from surpluses on other activities. In deciding how to handle FEC within the University's budgeting system in the immediate future, we had to strike a balance between not reducing research activities which make a contribution to overheads and estate costs, even though they do not recover 100% of FEC, and ensuring that these contributions are not used to expand research volume, which would drive us even further from long-run sustainability.

The key point for the individual researcher gaining external funding is the following. In the case of all externally funded research projects, PIs will be allocated an expenditure budget that will equate to 100% of the directly incurred costs as identified at the award stage. Typically directly incurred costs include Research Assistant salary costs, travel, consumables and equipment. This reflects the requirement for the PI to manage within the resources he or she identified as needed to undertake the activity. This is the case even for research council grants where 80% of each category of costs is covered. This should provide reassurance to the individual PI that, as far as the post-award management of externally funded research projects is concerned, it is 'business as usual'.

The other major area of interest is how the financial contribution which each grant makes will be handled by Finance The financial contribution is the difference between the price (income) from an externally funded research project and its marginal costs (the additional cost of actually carrying out the research project). The Faculties' I&E (Income & Expenditure) accounts will reflect the additional financial contribution recovered from research council grants, and contracts with government departments and private industry, and will not result in additional indirect and estate costs being attributed to Faculties. Thus in the short run the I&E accounts will provide a 'financial ledger' view of Faculties' actual income and expenditure incurred rather than a 'FEC cost ledger' view of both incurred and allocated costs.

The RAM will mirror what happens in the finance ledger by showing the financial contribution belonging to the Faculty. Before FEC, Faculties were credited within the RAM with the 'indirect cost recoveries' or 'overheads' earned through externally funded research. This general approach will not change in 2006-07. In the future the RAM will be changed to show both the income and the marginal costs of research.

What will change is the previous practice of attributing a minimum fixed proportion (10%) of 'overheads' to individual PIs, and any faculty specific policy of automatically allocating a larger proportion of indirect costs or salary recoups. This policy encouraged allocating additional expenditure to existing research and therefore runs directly counter to sustainability.

However, this does not mean that researchers should not be rewarded for attracting externally funded research, which maximises the financial contribution to overheads and estate costs. Indeed, Faculties have been asked to find the best way to incentivise Departments/Divisions/Research Groups, through their decisions on internal resource allocation (both pay and non-pay), in order to maximise this contribution to overheads. A report on FEC policy presented to the June 2005 meeting of SMG states that "Faculties will need to develop plans to influence decisions made by staff on which funders they will apply to for funds….but incentivisation of staff will be subject to local Faculty policy rather than being dictated by institutional policy."

Ultimately the common objective of all within the University has to be to maximise the financial contribution, balancing the objectives of academic excellence (which in RAE terms implies the retention of sufficient externally funded research volume) and the imperative of financial sustainability.

Faculties are best placed to make these judgements, as the key business units in the University.

Anton Muscatelli
Vice-Principal (Strategy and Advancement)