Higher Education in the Age of Austerity

Part Two: Shared Services, Outsourcing and Entrepreneurship

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Executive Summary

Universities are facing testing times ahead. Direct public funding for higher education (HE) institutions (excluding research funding) will fall by 40%, from £7.1 billion to £4.2 billion, by 2014-15. Direct grants for teaching will no longer be available for most courses; instead, funding will follow the student, with higher tuition fees constituting the majority of institutional income. These changes will have profound ramifications for the country's HE sector, perhaps the most significant of which will be to create a far more competitive environment for higher education institutions, which will no longer be able to rely on an annual block grant to fund teaching irrespective of quality or student satisfaction. Universities will become ever more conscious of the need to improve the quality of their core functions of teaching and research, and will be driven to seek efficiency savings, especially in non-core functions, by the desire to outdo their competitors on value and price. As a result, institutions will need to devote more attention than ever to how they can most efficiently manage limited resources, maintain the quality of infrastructure, facilities and services in an affordable fashion, and raise additional funds from external sources.

Shared Services

In its simplest formulation, the term 'shared service' refers to organisational collaboration in service provision. The chief rationale for the use of shared services is that they can produce both efficiency savings and improvements in service quality. The Shared Services Advisory Group estimates that successful use of shared services can produce a 30-50% cost reduction in the private sector and 20-30% in the public sector. Unfortunately, the use of shared services is still relatively rare within UK higher education. A September 2008 report by the Joint Information and Systems Committee (JISC) found that only 26% of HE institutions reported themselves to have any shared services at all, compared to 30% of

further education institutions.[1] Additionally, only 3% of HE institutions were found to have a shared service in finance, human resources, timetabling or student records.

However, there are numerous examples of successful shared services projects, such as Manchester Student Homes (MSH). MSH is an example of collaborative service provision undertaken at local partnership level. Typically, every university has an accommodation office which provides information and assistance for students looking for a place to live, either in purpose built residences or the private sector. The University of Manchester and Manchester Metropolitan University have engaged in a collaborative effort to provide this same information and support through a single office, thereby reducing administrative costs. The result has been the creation of Manchester Student Homes, owned and funded by the two universities and their respective student unions. MSH is now the sole official provider of advice and guidance to students seeking accommodation in the city.

The challenge for the HE sector is to make wider use of innovative and effective shared service arrangements such as MSH. The key obstacle to wider shared service usage in higher education relates to VAT liability. All universities in the UK are designated as 'eligible bodies' under the VAT Act 1994, meaning that supplies made by these institutions are exempt from VAT. However, when universities buy in services, whether from a private source or from another university, a new VAT liability is generated which cannot be recovered. As a result, any efficiencies achieved would be required to generate a saving in excess of the current rate of VAT.

One possible way to overcome the VAT issue would be for the Government to adopt a scheme similar to that of the "contracted out service provision" that is currently used in the NHS and other government departments. The provision was created in order to remove disincentives to shared services during a drive for greater efficiency- a rationale that applies equally to higher education today- and has enabled the creation of programmes such as NHS Shared Business Services, which has operated since 2005. The National Audit Office forecasts that the scheme will deliver net savings of £250 million over eleven years.

In addition, the EU's Principal Directive on VAT currently allows for shared services to be exempt from VAT if both the parties involved are already exempt themselves. Although this is a mandatory provision, it has not yet been implemented in UK law. However, in June 2010, HMRC announced that it would be launching a formal consultation on the implementation of Article 132(1)(f) in the autumn of 2010. We hope that the potential for achieving long-term improvements in efficiency and service quality through the use of shared services is taken into full account during the consultation process.

The VAT issue aside, the chief obstacle to usage of shared services within UK higher education is a lack

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[1] 'JISC Study of Shared Services in UK Further and Higher Education. Report 4: Conclusions and Proposals', Report for JISC by Duke & Jordan Ltd et al, September 2008, available at http://www.jisc.ac.uk/media/documents/programmes/jos/jisc_shared_services_report_4%20.pdf. Accessed 31/05/12

of enthusiasm among senior managers. The JISC survey found that fewer than 50% of institutional managers would 'readily consider' a shared service in any area of administrative operation, with the number dipping below 25% in finance, timetabling, and customer relations. Much of this reluctance derives from the distinct culture of UK higher education. British universities are among the most autonomous in the world and are rightly protective of their independence, but this can lead to reluctance among managers to establish major partnerships with other institutions which may entail the loss of a degree of control over services. In addition, universities operate in a more collegiate manner than conventional businesses and management teams have to take into account a range of interests within each institution, making it more difficult to enact major changes to business procedures.

Despite these obstacles, there is still good cause to be optimistic that shared services can make a sizeable contribution to making UK universities more competitive in the future and allow for the utilisation of savings in support of teaching and research. Institutions are likely to resist heavy-handed attempts to impose shared service usage from the top down; shared services in UK HE will develop through bottom-up initiatives as administrators begin to see for themselves the benefits that can accrue from a properly managed shared service programme. In an environment of variable tuition fees and limited direct funding, institutions will need to become as efficient as possible in order to survive and succeed. We therefore expect institutions to examine the possibility of shared service provision increasingly closely in the coming years. **The Government could accelerate this process by addressing the issue of VAT liability, and we recommend that it examine this option when the public finances allow.**

Outsourcing: Accommodation and Facilities Management

Between 2003-4 and 2007-8, university estate maintenance costs rose by 33.9%, from £23.67 per square metre to £31.69. However, despite these levels of investment, too many university facilities remain below-par. HEFCE estimates that of the 25.6 million square metres of UK HE estate, one third (8.6 million square metres) is unsuitable for the needs of its users; approximately 24% of the UK's higher education estate was constructed before 1940 and much of it is now well past its design life. HEFCE estimated in 2007 that to address the situation will cost in excess of £3.8 billion in maintenance expenditure, with a further £2.2 billion per annum required in capital expenditure. This problem is clearly one that has not been adequately addressed and will worsen over time unless action is taken now.

Given the fact that capital expenditure by the Department of Business, Innovation and Skills will fall by 44% over the next four years, universities should not expect the cost of construction and renovation work to be covered by public funding in the future. Instead, they can and should look to the private sector to provide this support. Alternative models of funding can enable universities to find ways of

ensuring the redevelopment of their campus facilities at minimum cost and risk to themselves.

By means of deals in which the private sector partner makes the required investment and accepts the demand risk, a number of universities across the country have already been able to address the need for real improvements in the provision of student accommodation facilities, in spite of fiscal constraints. Partnership with accommodation providers such as the University Partnerships Programme (UPP) and UNITE allow the university to benefit from renewed investment in facilities, using funds raised from private sources. Higher education is seen as a relatively stable long-term investment, so that lending against such projects is not hard to come by, even during periods of recession.

In the case of a typical UPP transaction, the university will grant a head lease on university land to the private provider. A Special Purpose Vehicle (SPV) is created specifically for the purpose, operating as the project company. Typically the university will receive a capital sum ranging from £10- 50 million. Rents are then either collected by the private provider or passed on to it after collection by the university. The university may receive an annual percentage of the rents passing, to fund marketing and allocation of the accommodation. Deals of this type usually last between 35-50 years. Private operators pursuing long-term partnership models will typically invest in the quality of the facilities, improving the quality of the estate, and usually accept void risk until the point that a residential agreement has been signed with the student. The benefit of such models is that they allow crumbling facilities to be renovated through private investment, improving the student experience and reducing the existing risk profile of the institution without affecting universities' capital budgets. Facilities are then managed by specialist companies, allowing the university to concentrate on its core functions. Outsourcing companies bring specialised skills and expertise, allowing them to produce real improvements in service quality, and significant economic efficiencies.

Outsourced facilities management need not be limited to accommodation. Other elements of the physical estate such as lecture theatres and catering halls can benefit from sustained long-term investment through engagement with the private sector. However, although student term-time rental accommodation is exempt from VAT charges, for a wide range of outsourcing services this does not apply. As a result, outsourcing services to the private sector presents real challenges with regards to VAT, as it does with the delivery of shared services between universities.

We would welcome the prospect of legislative reform aimed at extending a VAT exemption to outsourcing arrangements between universities and facilities providers. Over the long-term, such a measure would increase the competitiveness of a sector crucial to the UK's future prospects, but given the country's fiscal constraints it is understandable that the Treasury is unwilling to make such an exemption at the present time. Encouragingly however, some private companies are in the process of working within the confines of existing tax legislation to deliver a service unencumbered by VAT liability, without the need for any legislative reform.

This can be achieved through a mechanism known as a Joint Venture Partnership (JVP), the details of which in many ways mirror the arrangements for outsourcing of accommodation that are described above. A joint Special Purpose Vehicle (SPV) is created, incorporating the partnering university, which holds a 51% shareholding, and the private sector provider, holding the remaining 49%. Critically, it is then possible to register the SPV for VAT within the same University VAT group, enabling the institution to outsource the provision of non-core services without creating a new VAT liability.

The British Universities Finance Directors Group estimates that universities spend around £9 billion p.a. on goods and services. The experience of industry providers in the transferring of the provision of such non-core services indicates that as much as 30% could be saved if such a model were adopted, equating to potential sector-wide savings of £2.7 billion per annum. **Universities should explore the possibility of developing similar arrangements with external providers in order to work around the VAT issue without the need for legislative change.**

IT outsourcing

The traditional model of provision of IT services in the higher education sector is one in which individual institutions own, operate and provide IT services at all levels. However, universities are increasingly revisiting the issue in their search for efficiency of service provision. Many HEIs have begun to farm out the provision of their IT systems to third party specialists, most commonly Google and Microsoft.

The benefits of handing over these services to the private sector are clear:

- University e-mail systems can be provided free of charge by third party specialists. Both Google and Microsoft now host student email systems for free. UCL reported that it saved £250,000 by adopting Microsoft's live@edu email service in 2010;

- Email provision by companies such as Google and Microsoft includes a range of additional applications which are not usually found on email services provided in-house;

- By using remote 'cloud computing', in which computing resources are stored remotely and shared via the internet rather than on local servers, universities have no need to maintain large, expensive and power-hungry servers on their campuses;

- Cloud-based systems usually offer considerably greater storage capacity than those hosted on local servers;

- Using cloud-based systems managed by external providers negates the need for universities to regularly upgrade their own IT infrastructure to keep pace with demand, releasing long-term savings;

- Outsourced computing systems are more flexible than those provided in-house as the level of usage can be altered to reflect peaks and troughs in demand.

However, universities have tended to be deterred by the following considerations:

- Often in-house systems have been installed at considerable expense, so managers feel reluctant to scrap them outright;

- The HE sector has not yet fully met the challenge of costing IT systems and it is therefore more difficult for managers to make reliable estimates of the potential cost savings achievable through outsourcing such systems;

- Concerns over data security and privacy make some universities hesitant to use external providers for services that involve the storage of personal data, such as email systems. In addition, data protection requirements prohibit certain kinds of data from travelling outside an institution's jurisdiction. These can be problematic in relation to cloud-based solutions which are not normally geographically defined;

- Although specialism and economies of scale should imply that external suppliers of computing systems are more proficient than university departments, such systems have been known to fail on occasion.

As budget cuts begin to bite, institutions must be willing to look upon the private sector as a potential ally rather than with suspicion. **By embracing the offerings of private companies, the HE sector can reduce its costs, focus its attention on its core functions and provide a better, more cost-effective service for its students and staff.**

Entrepreneurship and 'spin-offs'

Entrepreneurship in the university sector takes a number of forms. Often it involves the utilisation of an institution's intellectual capital in innovative partnerships with private industry, particularly in the area of high-technology enterprise. Engagement with business can produce commercial returns, as well as fostering a culture of entrepreneurialism and creating strong links between the university and the private sector. Institutions with a strong track record of entrepreneurialism, such as the University of Hertfordshire, have put engagement with business at the heart of their operations, and have consequently benefited from a number of innovative commercial projects, ranging from a high-tech Biopark to a local bus service.

One way for universities to generate income from commercial sources is by using 'internal outsourcing'. In cases where an institution has strong reasons for deciding against outsourcing a service, it may instead make use of internal outsourcing where, instead of bringing in an outside organisation to

provide a particular service, the university takes an in-house service and turns it into a separate business. This solution allows the newly-formed company to look beyond the university as sole customer, and seek business elsewhere. An example is the Uno bus service, owned by the University of Hertfordshire, which developed it from a bus service for students to an established local company serving the wider community- hence its slogan 'the university bus for everyone'

Another potential source of commercial revenue for universities is the creation of 'spin-off' companies, usually in high-technology fields, making use of an institution's research expertise and capacity for technological innovation. The University of Edinburgh alone was involved in the creation of 40 new businesses in the academic year 2009-2010, which have already raised £3 million in external funding. Nine of the new businesses were created by academic staff, 19 by students, and 12 by entrepreneurs from outside the University who constructed their business through Edinburgh Research and Innovation (ERI), the University's technology transfer office (TTO). While some TTOs are very successful, too many are ineffective: a 2008 review found that only around 6% are active in developing spin-off companies, licensing, or filing patents. Policy Exchange recommended in a previous Research Note, *Innovation and Industry: the role of universities* that Government funding for TTOs, currently disbursed through the £150 million Higher Education Innovation Fund, should be restricted to TTOs that can demonstrate strong outcomes. Other institutions could then buy in expertise from these larger TTOs.

One difficulty with the creation of spin-off companies is the raising of capital in a project's early stages. Venture capitalists are often unwilling to take risks on promising technologies which nevertheless require considerable work before they are ready for commercialisation. The Government can therefore play an important role in providing proof-of-concept funding to allow projects to progress to a more commercially appealing stage. As Policy Exchange noted in *Innovation and Industry: the role of universities*, there are currently far too many disparate sources of such funding: up to 55 different funds exist, amounting to around £40 million in total. These funds should all be rationalised and should be distributed by the Technology Strategy Board (TSB), a body established in 2007 to promote 'technology-enabled innovation' in the UK, and funded to the tune of around £200 million per annum. We endorse the recommendation made in *Innovation and Industry: the role of universities* that the TSB should act as a vehicle to distribute proof-of-concept funding to innovative spin-off projects in their early stages.

While such changes should help simplify the system of public support for commercial innovation and business engagement within the HE sector, the main driver of change will be universities themselves. It is of crucial importance to the UK's HE sector that universities diversify their income streams, and make full use of the expertise and intellectual capital that they possess. Those institutions that are able to maximise the commercial potential of their resources will achieve a vital head-start in the newly competitive environment in which universities will find themselves. **It is of vital importance that institutions continue to develop ways to engage constructively with business and exploit to the full the commercial potential of their resources and ideas.**

Recommendations:

1) The Government should consider creating a 'contracted out services provision' for higher education, similar to that enjoyed by the NHS. This would remove a significant barrier to the outsourcing of services, allowing universities to concentrate on their core functions of teaching and research.

2) Alternatively, the Government should implement the EU VAT Directive on shared services. This will remove the significant tax barrier which is a current disincentive to HEIs collaborating to reduce costs. If immediate implementation is fiscally unrealistic, the Government should aspire to implement the Directive when future circumstances allow.

3) In the meantime, it is incumbent on universities to explore methods of working within the confines of existing tax legislation to deliver a service unencumbered by VAT liability, without the need for any legislative reform.

4) Universities must make a concerted effort to reduce their reliance on Government funding for support. All institutions must give due consideration to increasing their level of engagement with private business in order to diversify their income streams, and seek to take a more entrepreneurial approach to generating revenue from commercial sources.

5) We endorse the recommendations made in *Innovation and Industry: the role of universities* that funding for early-stage technological ventures should be unified through the Technology Strategy Board, and that public funding for technology transfer should be limited to a small number of high-quality TTOs.

Introduction

Universities are facing testing times ahead. The budget of the Department of Business, Innovation and Skills (BIS) is to be reduced by 25% over the next four years as part of the Government's drive to reduce the fiscal deficit. This will result in swingeing reductions in the funds allocated to universities through the Higher Education Funding Council for England (HEFCE), which constitutes over 30% of the higher education (HE) sector's total income.[2] Direct public funding for HE institutions (excluding research funding) will fall by 40%, from £7.1 billion to £4.2 billion, by 2014-15.[3] Although taught courses in Science, Technology, Engineering and Maths (STEM) will continue to receive public funding at a comparable level to now, direct grants for teaching will no longer be available for most other courses. Instead, HE funding will follow the student, with higher tuition fees constituting the majority of institutional income. These changes will have profound ramifications for the country's HE sector.

Perhaps the most significant effect of these reforms will be to create a far more competitive environment for higher education institutions, which will no longer be able to rely on an annual block grant to fund teaching irrespective of quality or student satisfaction. As the Browne Review of higher education funding noted, the system of funding limited HE places via block grants means that 'year on year institutions are secure in knowing that they can fill their own student places no matter the competition from other institutions, and obtain guaranteed HEFCE funding as well as charge the maximum fee to all students'.[4] The move away from grant-based funding, as proposed by Lord Browne's review, will bring an end to this security. Instead, universities will rely very heavily on tuition fees as a chief source of income, and will therefore stand or fall on their ability to attract prospective students. As competition for students becomes fiercer, universities will become ever more conscious of the need to improve the quality of their core functions (teaching and research), particularly teaching. At the same time, in an environment of variable tuition charges, universities will be driven to seek efficiency savings, especially in non-core functions, by the desire to outdo their competitors on value and price. As a result, institutions will need to devote more attention than ever to how they can most efficiently manage limited resources, improve the quality of infrastructure, facilities and services in an affordable fashion, and raise additional funds from external sources. There is considerable scope for improvement in these areas; a survey of vice-chancellors by PA Consulting found that '80% referred to deficiencies in their resource management systems as a basis for encouraging enterprise and/or efficiency'.[5]

One option for the sector is to consider outsourcing the provision of certain services to specialist companies, in order to allow universities to focus more strongly on their primary functions. An

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[2] Higher Education Statistics Agency, Finances of UK Institutions 2008-9, at
http://www.hesa.ac.uk/index.php?option=com_content&task=view&id=1900&Itemid=239
[3] Department for Business, Innovation and Skills website,
http://nds.coi.gov.uk/content/Detail.aspx?ReleaseID=416110&NewsAreaID=2, accessed 25/10/10
[4] Lord Browne of Madingley et al, *Securing a sustainable future for higher education*, 12 October 2010
[5] PA Consulting, *A passing storm or permanent climate change? Vice-chancellors' views on the outlook for universities*, 2010

increasing number of institutions already make use of private companies such as UPP, UNITE, Compass and Sodexo, but they remain in the minority. Private companies can provide the capability to improve the student experience of these services at a reduced cost to the institution both in terms of expenditure and risk profile, freeing both funds and staff for teaching purposes.

As well as reducing costs by transferring the running of services to an external provider, universities could seek to make additional savings through collaborative working with other institutions. Functions such as human resources management are common to all universities and do not need to be performed individually by each and every institution. Indeed, institutions working together could outsource services in groups of institutions or consortia, generating both greater purchasing power and savings. Such services could be provided on a shared basis, helping to avoid unnecessary duplication and achieve savings through the realisation of economies of scale. It is estimated that universities spend approximately £700 million on Human Resources and Finance each year,[6] and costly backroom services such as these are a prime target for shared provision. Additionally, universities could examine whether shared services could be suitable in less conventional areas such as printing, campus management, timetabling and professional training.

Finally, universities should seek to move towards diversifying their income by making the most of their unique resources. Universities are repositories of knowledge and ingenuity, and they should seek to tap into the resourcefulness and creativity of their students and staff in order to pioneer entrepreneurial ventures. There is currently no reason why a university cannot buy up or start a business, run it at a profit and reinvest the revenue into teaching and research activities.

Shared Services

What are shared services?

In 2006 HEFCE noted that 'the traditional definition of a shared service concentrates on bringing together 'back office' functions... into a separate organisation.'[7] However, as organisations pursue innovative collaborative arrangements to secure efficiencies and improve standards in different operational areas, a broader definition is required to encompass them. Hence, in its July 2006 report on shared services to HEFCE, KPMG defined the term 'shared service' as referring loosely to the provision of services in a 'combined or collaborative function, sharing processes and technology'.[8] A still broader definition was produced by the Joint Information and Systems Committee (JISC) in 2009, which defines

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[6] 'Shared Services in the Higher Education Sector', Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10
[7] HEFCE Circular Letter 20/2006, 10 August 2006, available at http://www.hefce.ac.uk/pubs/circlets/2006/cl20_06/. Accessed 29/09/10
[8] Shared Services in the Higher Education Sector, Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10

shared services as 'institutions cooperating in the development and delivery of services, so sharing skills and knowledge, perhaps with commercial participation'.[9]

In its simplest formulation, therefore, the term 'shared service' refers to organisational collaboration in service provision. This collaboration can take a number of forms: for example, an outsourcing arrangement in which two or more institutions purchase services jointly from an external supplier would be classed as a shared service. However, not all shared services need necessarily involve a private sector provider. To use higher education as an example, the term could equally refer to an arrangement where one university provides a service to others, or where the support functions of two or more universities are combined into a single, separate organisation, which then provides the service jointly to the institutions involved. Additionally, the term shared services can be applied to national consortia that serve the needs of a large number of individual institutions. In the higher education sector, shared services are most commonly found in (but are not limited to) back-office services such as estate management, human resources, library management, virtual learning environments, timetabling, finance and student records,[10] as well as procurement, printing and data management.

The chief rationale for the use of shared services is that they can produce both efficiency savings and improvements in quality. There is no fundamental reason why universities should provide all their backroom functions internally or purchase them on an individual basis. While there is currently little in the way of quantifiable information on savings achieved, shared services tend to be cheaper due to the cost-saving benefits of economies of scale, increased procurement power driven by capacity and the ability to standardise, and increased opportunities for specialisation in service delivery.[11] The Shared Services Advisory Group estimates that successful use of shared services can produce a 30-50% cost reduction in the private sector and 20-30% in the public sector (in which savings are more difficult to achieve due to lesser flexibility in areas such as staff terms and conditions).[12] The Confederation of British Industry (CBI) estimates that savings of 20% could be 'readily achieved' through increased shared service usage in higher and further education.[13]

How prevalent is the use of shared services within UK higher education?

The use of shared services is still relatively rare within the UK higher education sector. A September 2008 report by the Joint Information and Systems Committee (JISC) found that only 3% of HE institutions

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[9] JISC Infonet, 'What are Shared Services?', 2009, available at http://www.jiscinfonet.ac.uk/infokits/shared-services. Accessed 19/10/10

[10] Ibid.

[11] Shared Services in the Higher Education Sector, Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10

[12] Ibid.

[13] Confederation of British Industry, *Time for action- Reforming public services and balancing the budget*, May 2010

have a shared service in finance, human resources, timetabling or student records[14] - the types of back office functions that are conventionally regarded as among the most suitable areas for shared provision. This compares poorly with the further education (FE) sector, in which 17% of institutions have a shared service in one or more of these areas. Overall, only 26% of HE institutions reported themselves to have any shared services at all, compared to 30% of FE institutions.[15] The private sector is considerably further ahead in the development of shared services; a study conducted as long ago as 2001 found that 90% of Fortune 500 and European 500 companies had already implemented or planned to implement shared service arrangements.[16]

The reasons for the relative scarcity of shared services in UK HE are discussed below. However, it should be noted that in recent years efforts have been made to increase their usage within the sector. Part of this push has come from top-down encouragement by the Government via HEFCE, following recommendations made in the 2004 Gershon Review of efficiency in the public sector[17] and the Cabinet Office's 2005 report *Transformational Government: Enabled by Technology*,[18] which both called for the development of a culture of shared services in the public sector. Although universities are not technically public sector organisations, HEFCE sought to encourage them to 'take advantage of such opportunities to improve services and release resources to support teaching and research.'[19] In response, individual institutions have carried out a number of feasibility studies identifying possibilities for shared services in a number of areas including human resources, estates management, procurement, research management and computing.

One such study examined the feasibility of developing a 'national shared digital research data service'[20] for UK HE in order to meet a 'developing need in the UK for a systematic methodology for the storage, access, security and archiving of the great mass of academic and scientific research publications, papers and supporting data now being made available in digital or computerised form'.[21] This project, known as the UK Research Data Service (UKRDS), has now been developed beyond the interim planning phase which was completed in June 2010. The report produced following completion of the planning phase

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[14] Joint Information and Systems Committee, *Study of Shared Services in UK Further and Higher Education, Report 4: Conclusions and Proposals*, September 2008
[15] Ibid
[16] Bywater Consulting, *Realising the potential of shared services*, 2001
[17] Sir Peter Gershon, *Releasing resources to the front line: Independent review of public sector efficiency*, July 2004, available at http://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/efficiency_review120704.pdf. Accessed 11/10/10
[18] Cabinet Office, *Transformational Government: Enabled by Technology,* November 2005, available at http://www.cabinetoffice.gov.uk/media/141734/transgov-strategy.pdf. Accessed 16/09/10
[19] HEFCE Circular Letter 20/2006, 10 August 2006, available at http://www.hefce.ac.uk/pubs/circlets/2006/cl20_06/. Accessed 29/09/10
[20] Universities and Colleges Information Systems Association, 'Shared Services', 2 March 2010, available at http://www.ucisa.ac.uk/members/activities/sharedservices.aspx. Accessed 29/09/10
[21] UK Research Data Service, 'Proposal and Business Plan for the Initial Pathfinder Development Phase', May 2010

recommended that the project should proceed and 'lead to the establishment of long-term co-ordinated support for the rollout and maintenance of a nationally coherent approach to research data management at UK Higher Education and Research Institutions.' It also noted that the cost of the three-year development phase will come to only £9 million, which compares with US$100M over five years for the National Science Foundation's Datanet initiative in the US, and A$78M over three years for the Australian National Data Service. The UKRDS is expected to generate a return on investment through its facilitation of shared services, as well as through storage efficiencies and new research made possible by new opportunities for the recombination of data.

The top-down drive to improve shared services in UK HE has had some effect, and HEFCE funding for 2010/11 included £20 million for the further development of shared services in the sector.[22] However, it is important to note that the chief driver of shared services is bottom-up, deriving from the desire of individual institutions to improve the quality of their services, as noted by the JISC in their September 2008 report. The JISC surveyed institutions to assess the relative importance of drivers towards shared services and found that the two most important were 'continuity and resilience' of service and quality of service, followed by cost savings and 'releasing staff for more customer facing activities.'[23] This has led to a number of collaborative arrangements in service provision, ranging from local collaboration between individual institutions to the formation of national shared service organisations.

Examples of bottom-up cooperation include The Bloomsbury Consortium (TBC), a voluntary, collaborative arrangement in academic and administrative matters between specialist colleges of London University (namely Birkbeck, the School of Oriental and African Studies, the Institute of Education, the School of Pharmacy, the London School of Hygiene and Tropical medicine and the Royal Veterinary College).[24] The consortium was formed in 2004 and has since embarked upon a number of collaborative initiatives, including the Bloomsbury Learning Environment (BLE). This involves the shared use of an online learning platform known as 'Blackboard',[25] which allows students to access course materials and submit assessments via the internet, and which is in widespread use in UK universities. The BLE represents the first time that Blackboard has been implemented on a cross-institutional basis in the UK;[26] it enables each institution to have its own unique interface with the system, but all under a single licence. There are numerous benefits to this arrangement, including cost savings on licence fees,

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[22] HEFCE News, 24 June 2010, available at http://www.hefce.ac.uk/news/hefce/2010/umf.htm. Accessed 12/09/10

[23] Shared Services in the Higher Education Sector, Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10

[24] 'The Bloomsbury Colleges Report', 2009, available at http://www.bloomsbury.ac.uk/news/tbcreport. Accessed 07/08/10

[25] See www.blackboard.com for more information

[26] 'The Bloomsbury Colleges Report', 2009, available at http://www.bloomsbury.ac.uk/news/tbcreport. Accessed 07/08/10

shared technical support, and collaborative funding opportunities.[27] The Bloomsbury Consortium continues to explore other potential opportunities for collaboration, particularly in the areas of purchasing and procurement, as well as other potential projects including a shared student learning space and a shared resource register for personnel, equipment and facilities. The consortium has already made use of joint tendering in catering, cash carrying, and occupational health,[28] and states that the shared service arrangements agreed so far 'have led to either savings or to improved services for the same outlay.'[29]

The Bloomsbury Consortium's exploration of shared procurement reflects the fact that this is one of the most common areas for shared service provision in UK HE. HEFCE estimates that collaborative purchasing arrangements now cover 15-20% of institutional spend- a significant total, bearing in mind that higher education and research institutions in the UK spend over £5 billion per year on the procurement of goods and services.[30] Nearly all UK HEIs are voluntary members of one or another of the six regional purchasing consortia, such as the Southern Universities Purchasing Consortium, which reported a return of £48 for every £1 received in membership fees in 2004-5, or the North Western Universities Purchasing Consortium Ltd, which produces an average of 10% savings on contracts for its members.[31]

The above examples demonstrate that there are already a number of successful and productive shared service arrangements already in place in UK HE, ranging from smaller, local partnerships to national consortia. There are also other examples of long-standing collaborative arrangements within UK HE: universities have long used a shared admissions system (UCAS) and subscribe to umbrella organisations such as the Quality and Assurance Agency (QAA) and the Higher Education Statistics Agency (HESA). However, shared service penetration remains low in comparison to other sectors, so there is still an enormous amount of room for it to expand. For this to happen, a number of obstacles need to be overcome.

What are the obstacles to wider use of shared services in UK higher education?

The key obstacle to wider shared service usage in higher education relates to VAT charges. All universities in the UK are designated as 'eligible bodies' under Group 6 (Education) of Schedule 9 of the VAT Act 1994, meaning that supplies made by these institutions are exempt from VAT.[32] The University pays VAT on most of the goods and services it receives but can only recover a small percentage (if any)

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[27] Ibid

[28] Ibid

[29] Ibid

[30] Shared Services in the Higher Education Sector, Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10

[31] Ibid

[32] Strathclyde University, 'Detailed VAT information', http://www.strath.ac.uk/finance/financialservices/valueaddedtaxvat/detailedvatinformation/

of VAT via partial exemption recovery rules. Therefore, when universities buy in services (rather than providing them in-house), VAT is payable and the majority cannot be reclaimed. Accordingly, were a group of institutions to share a service, they would all have to pay VAT to the service provider, including in cases where one university was providing the service to others. If a group of institutions formed a consortium established as a separate legal entity in order to provide a shared service, the arrangement would still attract VAT payment for services to institutions. As a result, any efficiencies achieved would be required to generate a saving in excess of the current rate of VAT, which presently stands at 17.5% but will rise to 20% on 4th January 2011. This places universities in a different position to, for example, local authorities or government departments, which can reclaim VAT on shared services as a result of measures intended to remove disincentives to outsourcing and shared provision, and to prevent VAT becoming a cost on local taxation.[33]

VAT liability for shared service provision represents a serious obstacle to the expansion of shared services in HE. The JISC's 2008 survey of vice-chancellors found VAT liability to rank as the second most significant inhibitor to shared services within the sector, behind problems with forming effective partnership arrangements.[34] Worryingly, the VAT obstacle has the effect of preventing many institutions from giving genuine consideration to the potential benefits of collaborative service provision, acting as an 'inhibitor to serious discussion within institutions regarding the introduction of shared services'.[35] This supports the impression we gained from a number of vice-chancellors who all identified VAT as a primary obstacle to progress on shared service provision within the sector.

In a period of wide-ranging government spending cuts, the Treasury is unlikely to look favourably on pleas from the higher education sector for a VAT exemption on the purchase of shared services. However, as a 2007 report by the National Audit Office noted, the 'potential benefit from removing the VAT barrier for higher education and further education bodies is believed to be tens of millions of pounds per year.'[36] It may be that the Treasury currently has no option other than to prioritise achieving planned short-term spending cuts over the potential long-term savings that could be achieved through increased use of shared services, but we argue that it should aspire to change the VAT situation when circumstances become more favourable. The competitiveness of the UK's higher education sector is of paramount importance to the economy and the effect of VAT on the viability of shared service provision should be seen as an ongoing problem.

One possible way to overcome the VAT issue would be for the Government to adopt a scheme similar to that of the "contracted out service provision" that is currently used in the NHS and other government

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[33] National Audit Office, *Improving corporate functions using shared services*, House of Commons Stationery Office, 26 November 2007

[34] Joint Information and Systems Committee, *Study of Shared Services in UK Further and Higher Education, Report 4: Conclusions and Proposals*, September 2008

[35] Ibid

[36] National Audit Office, *Improving corporate functions using shared services*, House of Commons Stationery Office, 26 November 2007

departments. Under section 41 (3) of the VAT Act 1994, NHS bodies and government departments are able to recover VAT paid on certain contracted-out services. The provision was created in order to remove disincentives to shared services during a drive for greater efficiency- a rationale that applies equally to higher education today- and has enabled the creation of programmes such as NHS Shared Business Services, which has operated since 2005. The National Audit Office forecasts that the scheme will deliver net savings of £250 million over eleven years, while customers of NHS Shared Business Services are guaranteed initial gross savings of not less than 20% in the cost of the services provided.[37] If a similar provision were to be applied to higher education it would have to be carefully defined to avoid confusion in the sector, particularly with regard to which services would be eligible for the provision. In addition, it would probably have to be limited to the higher education sector only (excluding other sectors such as further education and non-departmental public bodies which face similar problems) in order to minimise the initial cost to the Treasury.

In addition, the EU's Principal Directive on VAT currently allows for shared services to be exempt from VAT if both the parties involved are already exempt themselves. Article 132(1)(f) of the Directive lists certain VAT exemptions that may be made in the public interest, including 'the supply of services by independent groups of persons, who are carrying on an activity which is exempt from VAT or in relation to which they are not taxable persons.' Although this is a mandatory provision, it has yet not been implemented in UK law. However, in June 2010, HMRC announced that it would be launching a formal consultation on the implementation of Article 132(1)(f) in the autumn of 2010.[38] We hope that the potential for achieving long-term improvements in efficiency and service quality through the use of shared services is taken into full account during the consultation process.

The VAT issue aside, the chief obstacle to usage of shared services within UK higher education is a lack of enthusiasm among senior managers. The JISC survey found that fewer than 50% of institutional managers would 'readily consider' a shared service in any area of administrative operation, with the number dipping below 25% in finance, timetabling, and customer relations.[39] Much of this reluctance derives from the distinct culture of UK higher education. British universities are among the most autonomous in the world[40] and are rightly protective of their independence, but this can lead to reluctance among managers to establish major partnerships with other institutions which may entail the loss of a degree of control over services. In addition, universities operate in a more collegiate manner than conventional businesses and management teams have to take into account a range of interests

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[37] National Audit Office, *Improving corporate functions using shared services*, House of Commons Stationery Office, 26 November 2007

[38] HMRC, Tax consultations announced at Budget (June 2010), available at http://www.hmrc.gov.uk/consultations/cons-announced-budget-june2010.pdf. Accessed 19th October 2010

[39] Joint Information and Systems Committee, *Study of Shared Services in UK Further and Higher Education, Report 4: Conclusions and Proposals*, September 2008

[40] Lord Browne of Madingley et al., *Independent review of higher education funding and student finance*, 12 October 2010.

within each institution.[41] This can make it more difficult to enact major changes to business procedures, and leads to concern among some managers that partnership arrangements may be overly dependent on the support of senior individuals within an institution, and may fail when those individuals cease to be involved.[42]

Furthermore, it should be remembered that universities are in competition with each other to attract and retain students, and that this competition will become more intense once funding through tuition charges replaces the bulk of direct state funding for the sector. In the private sector, most shared service programmes are internal schemes implemented in a decentralised organisation, while public sector services are rarely shared between competing organisations.[43] Universities are likely to be unwilling to share a service if they believe that they currently gain a competitive advantage from it. Institutional managers therefore need to be convinced that a shared service can deliver real improvements in service quality and/or significant savings before they will pursue it.

Finally, moving to shared service provision for important administrative functions always carries an element of risk, and universities are traditionally risk-averse institutions. The transition to a shared service is likely to require initial changes to processes which will carry some up-front costs. The smooth, reliable operation of administrative systems is clearly of paramount importance to universities and managers are cautious of major changes in these areas. In order to commit to shared services, institutions need to be convinced of their benefits- and these can be difficult to gauge, particularly when only around 20% of administrative systems in the sector are fully costed, according to the JISC survey of managers.[44]

Despite these obstacles, there is still good cause to be optimistic that shared services can make a sizeable contribution to making UK universities more competitive in the future. As noted above, there are already examples of successful shared service schemes in the sector, and despite operating in an increasingly competitive environment British universities retain a culture of openness and cooperation which should assist in the development of partnerships. Institutions are likely to resist heavy-handed attempts to impose shared service usage from the top down; shared services in UK HE will develop through bottom-up initiatives as administrators begin to see for themselves the benefits that can accrue from a properly managed shared service programme. In an environment of variable tuition fees and limited direct funding, institutions will need to become as efficient as possible in order to survive and succeed. We therefore expect institutions to examine the possibility of shared service provision

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[41] 'Creating partnerships in higher education- shared services within HE', available at http://www.he-sharedservices.co.uk/SS_within_HE.html. Accessed 15/10/10

[42] Joint Information and Systems Committee, *Study of Shared Services in UK Further and Higher Education, Report 4: Conclusions and Proposals*, September 2008

[43] *Shared Services in the Higher Education Sector*, Report for HEFCE by KPMG, July 2006, available at http://www.hefce.ac.uk/pubs/rdreports/2006/rd15_06/rd15_06.pdf. Accessed 15/09/10

[44] Joint Information and Systems Committee, *Study of Shared Services in UK Further and Higher Education, Report 4: Conclusions and Proposals*, September 2008

increasingly closely in the coming years. **The Government could accelerate this process by addressing the issue of VAT liability, and we recommend that it examine this option when the public finances allow.**

Case Study: Manchester Student Homes

Manchester Student Homes (MSH) is an example of collaborative service provision undertaken at local partnership level. Typically, every university has an accommodation office which provides information and assistance for students with regards to finding a place to live. The University of Manchester and Manchester Metropolitan University have engaged in a collaborative effort to provide this same information and support through a single office, thereby reducing administrative costs. The venture is jointly overseen by the two institutions.

The result has been the creation of Manchester Student Homes, owned and funded by the two universities and their respective student unions. MSH is now the sole official provider of advice and guidance to students in the city with relation to private sector accommodation. The establishment of MSH has brought numerous benefits typical of a shared approach such as administrative efficiencies and those driven by capacity, including the implementation of a landlord code of standards driving up the quality of accommodation available to students across Manchester.[45] In addition, MSH provides a student welfare service, and will check contracts before signing for no fee. MSH also runs an impartial mediation service to help settle any disputes between landlords and tenants.

Outsourcing: Accommodation and Facilities Management

Maintenance of the physical estate can constitute a major drain on a university's resources. Lecture theatres, laboratories, classrooms, administration blocks, halls of residence and refectories all require significant capital for construction and constant investment in their maintenance. For 2010/11, expenditure on administration, premises, residences and catering represented £4.79bn or 19.2% of total annual expenditure across the sector.[46] Between 2003-4 and 2007-8, estate maintenance costs rose by 33.9%, from £23.67 per square metre to £31.69.[47] However, despite these levels of investment, too many university facilities remain below-par. HEFCE estimates that of the 25.6 million square metres of UK HE estate, one third (8.6 million square metres) is unsuitable for the needs of its users.[48]
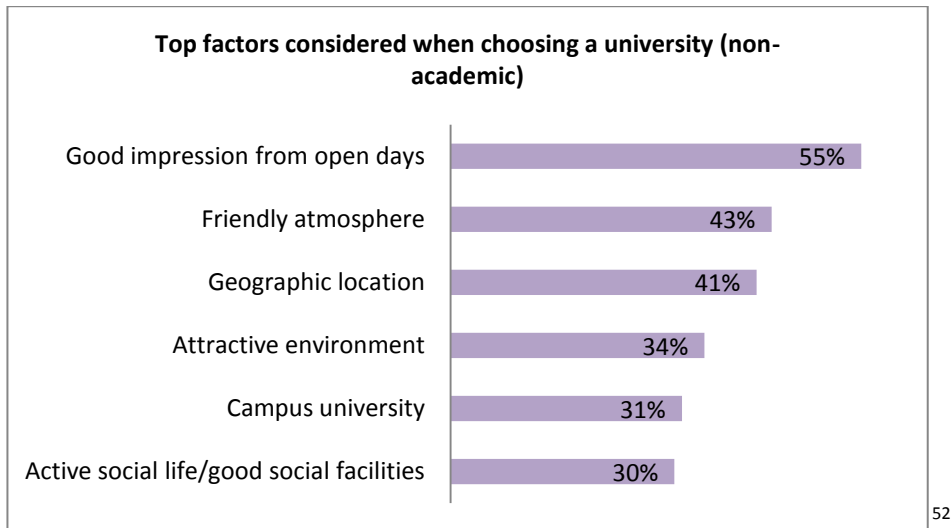
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[45] Manchester Student Homes website, http://www.manchesterstudenthomes.com/
[46] Higher Education Financial Yearbook 2010/11
[47] HEFCE, *Performance in Higher Education Estates: EMS Annual Report 2007,* April 2010, available at http://www.opdems.ac.uk/_files/EMS%20Annual%20Report%202007.pdf. Accessed 27/09/10
[48] Ibid

A university's facilities play an important role in attracting students and are important in reducing institutional non-completion rates.[49] Students are drawn to pleasing environments where modern, high-quality facilities are offered for their learning, accommodation and recreation. The Sodexo University Lifestyle Survey found that over a third of prospective students take the attractiveness of the university campus (including architecture and campus layout) into account when choosing which university to attend.[50] This would indicate that the investment that has been made in new buildings on university campuses has been a significant factor in increasing the popularity of those institutions.[51]

Top factors considered when choosing a university (non-academic)

Factor	Percentage
Good impression from open days	55%
Friendly atmosphere	43%
Geographic location	41%
Attractive environment	34%
Campus university	31%
Active social life/good social facilities	30%

[52]

Naturally, investment in a university's physical estate has the effect of diverting funds away from its core functions of teaching and research, but it is self-evidently in universities' interests to construct, maintain and manage their built estate in the most efficient and cost-effective manner possible.

A Shortage of Facilities

Over the past ten years there has been a massive increase in the number of students enrolling on UK courses. Indeed the number of total enrolments has risen by 30.3% over the past decade. For the academic year 2009-10 the number of university applications rose by a staggering 22.9% on the previous year, while the number of international applications increased by 28.7% in the same year.[53]

Given this context, it is easy to understand universities' desire to add capacity in order to meet this rising demand. The problem is exacerbated by the failure to have properly invested in the maintenance and renovation of existing physical infrastructure. Approximately 24% of the UK's higher education estate was constructed before 1940, and is now well past its design life. HEFCE estimated in 2007 that to

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[49] *Improving student achievement in English higher education,* Report by the Comptroller and Auditor General, HC 486 Session 2001-2002: 18 January 2002, pp.14-28

[50] The Sodexo University Lifestyle Survey 2010

[51] Ibid.

[52] Ibid

[53] UCAS website, 'Application numbers hit record highs for the fourth year running', 8th February 2010, http://www.ucas.ac.uk/about_us/media_enquiries/media_releases/2010/080210

address the situation will cost in excess of £3.8 billion in maintenance expenditure, with a further £2.2 billion per annum required in capital expenditure.[54] This problem is clearly one that has not been adequately addressed and will worsen over time unless action is taken now.

Given the fact that capital expenditure by the Department of Business, Innovation and Skills will fall by 44% over the next four years,[55] universities should not expect the cost of construction and renovation work to be covered by public funding in the future. Instead, they can and should look to the private sector to provide this support. Alternative models of funding can enable universities to find ways of ensuring the redevelopment of their campus facilities at minimum cost and risk to themselves.

Alternative arrangements

There is currently a market for the outsourcing of property development and facilities management. By means of the process set out below, which involves the private sector making the investment and taking the demand risk, a number of universities across the country have already been able to address the need for real improvements in the provision of student accommodation facilities in spite of fiscal constraints.

The arrangements designed to ensure the provision of privately constructed and managed accommodation facilities vary between different universities and providers. It should be noted that term-time student rental income is exempt from VAT regardless of the organisation to which it is paid, so VAT eligibility is not an issue with regard to the following model. The model described below is as used by accommodation providers such as UPP, which currently provides over 20,000 student rooms across 11 universities in the UK:

1. A Special Purpose Vehicle (SPV) is created, incorporating the partnering university and the service provider. With the creation of an SPV, access to non-recourse financing can be secured from lenders, solely against the project rather than any other of the universities assets, ensuring that no financial liability can fall back onto the institution. The University then grants a lease to the SPV for a particular piece of land for development of an existing university property or the construction of new campus infrastructure. In return for granting the lease, the University can expect a capital receipt for reinvestment and a new residence which will revert to the University at the end of the lease period. The value of any capital receipt is based on a

[54] HEFCE, *'Performance in Higher Education Estates: EMS Annual Report 2007'* http://www.opdems.ac.uk/_files/EMS%20Annual%20Report%202007.pdf
[55] Department for Business, Innovation and Skills website, http://nds.coi.gov.uk/content/Detail.aspx?ReleaseID=416110&NewsAreaID=2, accessed 25/10/10

net present value calculation of future cash flows, modelled on the basis of a discount rate reflecting project risk.[56]

2. The SPV signs a corresponding under-lease back to the University, ensuring construction costs are recoverable for VAT purposes. The under-lease also enables the University to continue to market the accommodation as if it were its own and to control the allocation of students. For continuing to promote the accommodation and collect the rent, the University receives a fee typically between 2-4% of rents passing. There are a number of advantages in the University continuing to collect rents. The University is able to make use of resources in its accommodation offices to do so, and is best positioned to chase unpaid fees, while this approach also minimises data protection issues.

3. A transaction of this type would usually involve entering into an agreement with a university on a long-term basis, with the usual length of the concession running for somewhere between 35 and 50 years. Once created, the SPV itself finances the project, at no expense or recourse to the taxpayer. Historically, institutional investors have been attracted to the profile of low risk and a steady income stream which a portfolio based on a universities rental accommodation presents.

4. On the transfer and/or completion of the construction of the accommodation, operational management passes to a facilities management company, under contract to the SPV. A service level agreement is put in place which passes operational risks, including availability, performance and cost overruns to the private service provider.

How do outsourced models of accommodation provision address the quality of the student experience?

The quality of the student experience is vital to the competitiveness of any university, and models of outsourced accommodation and facilities provision can contribute towards improving it. Most obviously, the quality of the residential and academic estate is improved. Survey data suggests that the quality of buildings has a significant effect on the performance of postgraduate and undergraduate students, as well as academic staff, and is linked to overall satisfaction rates and level of happiness.[57] In addition, the outsourcing model described above provides an extra income stream to the university for reinvestment into core services. Finally, accommodation providers typically offer free or heavily subsidised accommodation for University Wardens and pastoral care staff, who are able to have direct input into the day to day operation of the residences.

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[56] One university we consulted reported that they received a lump sum in excess of £15 million which it could then invest into the delivery of its core functions.

[57] Commission for Architecture and the Built Environment, *Design with distinction: the value of good building design in higher education*, March 2005. Available at http://www.cabe.org.uk/files/design-with-distinction.pdf. Accessed 22/10/10

Case Study: University of Exeter

The University of Exeter established a partnership with UPP in 2009 as part of its on-going £450 million investment programme, which also includes a £48 million redevelopment of the centre of the Streatham Campus, a £25 million investment in the Business School and £18 million for new facilities for Biosciences. The forty-year partnership with UPP will enable the University to concentrate its funds on academic investment whilst also being able to improve and increase its student accommodation stock.

The transaction saw £133m invested in the University, and construction, operational and lifecycle risk was transferred from the University to UPP. UPP now saves its 11 university partners a total of £172m in lifecycle costs. The value of the construction contract is £77 million and construction will take place over three years from financial close, with the final phase due for completion in 2012/13. The transaction, the result of a competitive bidding process, also generated a capital receipt for the University of Exeter for investment in the provision of its core teaching and research functions.

Managing Risk:

Rent: One of the key concerns with respect to contracting accommodation from the private sector relates to rental value, and the risk that a company will fail to take into account the situation of students, who are already saddled with a large amount of debt, when setting rents. A university, on the other hand, can charge rent levels at affordable, subsidised rates. However, affordability is key to the success of outsourced accommodation projects, and this is reflected in the deals that are struck. In many cases, rent levels are agreed annually between the company and the university on the basis of detailed price point analysis, and are set at a lower rate than the market would otherwise determine. Occupancy is the key discipline from the point of view of the accommodation provider and is best secured through partnership with the University.

Construction Risk: Where new accommodation is involved, it is the construction phase which presents the greatest risk to the overall project. By passing design, planning and construction risk to the private sector provider, the University mitigates the considerable risks involved in developing infrastructure on an in-house basis such as cost overruns and delayed delivery.

Operational Risks: If the University were to manage its own accommodation in-house, it would be entirely responsible for the costs of maintaining the buildings and facilities as well as the administration of the site. Outsourcing such management to a third party company allows the university to reduce its exposure to risk, as the service provider bears all operational and lifecycle replacement risks and costs. At the end of the lease, the ownership of the land and/or property reverts back to the University, having met the requirements of a pre-agreed hand-back provision. This arrangement ensures that the partnering company keeps its end of the bargain by making the necessary investment in maintenance and upkeep.

Residential Demand Risk: Using this particular model, the University will collect the rent from the students in the same way that it would normally. The difference is that the money is then passed to the SPV. If a room should be left vacant up until the beginning of the academic year it is the responsibility of the service provider to make up the lost revenue. The service provider holds this risk until the student signs a residential license agreement; should the student then drop out or vacate the accommodation for any other reason, the University is responsible for 'back filling' the accommodation, typically through a residential waiting list held by the University. It should be borne in mind that were the University to provide accommodation solely in-house, not only would it incur a loss on any vacant rooms, but it would also be forced to cover the costs of construction, redevelopment, management, maintenance and administration of the halls. It makes sense, therefore, to pass these costs onto a third party company.

Snapshot overview- UNITE[58]

Another large developer and manager of higher education facilities and accommodation is UNITE, which currently supplies over 40,000 bedrooms in 24 cities in the UK. UNITE acquires the land and manages the project from start to finish, without direct management input from the university involved. UNITE specialises in off-campus and city centre locations and collects rent directly from students, rather than through the university accommodation office. The occupancy rate stands at around 97-98%.

UNITE began life as a conventional property developer, moving into university accommodation after seeing that universities were either unable or unwilling to make the necessary investments in the upkeep and expansion of their accommodation facilities. UNITE began a programme of 'land grab' in university cities, purchasing sites which could potentially be used for halls of residence, and beginning to redevelop them from 1995 onwards. 90% of these rooms have been fully built by the company. UNITE then lets the new accommodation directly to students, usually with the assistance of the university accommodation office in promoting the facilities to students.

More recently, UNITE has begun to explore options to move towards a model whereby it acquires the leasehold on current student property at a university, in return for which the institution receives a capital sum. Usually, UNITE then carries out a degree of capital works (on which VAT is usually recoverable with the right corporate and lease structures in place) before entering directly into Assured Shorthold Tenancy agreements with individual students. UNITE and its investors take the demand risk in this instance, rather than the university, although typically a range of covenants are entered into with the university in order to ensure that the demand risk profile of the investment does not change over time as a result of changes in the university accommodation strategy. As the leaseholder, UNITE also bears lifecycle operational and maintenance risk, subject to a service provision agreement made with each university on a case by case basis.

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[58] Information from UNITE

Outsourced facilities management need not be limited to accommodation. Other elements of the physical estate such as lecture theatres, laboratories, catering halls and classrooms can all benefit from sustained long-term investment through engagement with the private sector. However, although student term-time rental accommodation is exempt from VAT charges, for a wide range of outsourcing services this does not apply. As a result, outsourcing services to the private sector presents real challenges with regards to VAT, as it does with the delivery of shared services between universities. Clearly the simple application of the EU Directive on VAT does not apply as both parties are not already exempt from VAT in their own right. VAT liability would continue to arise if the employment related provision of a service was transferred from a university to a private company.

Snapshot overview: Sodexo

Sodexo provides catering and facilities management services to around 25 higher education institutions in the UK. Its model varies from case to case, with key criteria of operation, performance management requirements and investment requirements established with each client on an individual basis. Commonly, these models involve a share of risk and reward, whereby Sodexo will place its earning potential at risk in return for a share of upside performance. Contracts usually last for 3-5 years, often with an additional 2 year option; for contracts with a more substantial initial investment the term may extend to ten years.

The Sodexo model gives its clients access to capital sums to upgrade and refurbish their catering operations, which in turn will boost revenue and productivity, and impact on utility and space costs. It also delivers back-office savings; because Sodexo administers the entire catering and facilities management function there is a reduction in support activity within the institution, whether in account management and procurement, or in staff training and HR. In order to ensure that it keeps up to date with students' needs, Sodexo conducts a biennial Student Satisfaction Survey which informs its service provision.

Catering contracts such as those of Sodexo are usually structured in such a way as to permit the continuation of the VAT exemption that applies to food sales to students. However, VAT is charged on other aspects of service delivery including cleaning materials, sundry supplies and the provider's fee. This sum of VAT is non-recoverable and must therefore be mitigated by improved performance. In operations where Sodexo provides additional services up to a full facilities management package, then the issue of VAT becomes much more significant. In these operations the tax is applied to the whole of the service billing, thus rendering it essential to deliver at least a 20% efficiency saving on the self-delivered business

We would welcome the prospect of legislative reform aimed at extending a VAT exemption to outsourcing arrangements between universities and facilities providers. Over the long-term, such a measure would increase the competitiveness of a sector crucial to the UK's future prospects. However,

given the country's fiscal constraints, it is understandable that the Treasury is unwilling to consider such an exemption at the present time due to concerns over the loss of tax revenue, and fears that setting a precedent could open the floodgates to other industries and sectors that feel they should also be considered for "special treatment". Encouragingly however, some private companies are in the process of working within the confines of existing tax legislation to deliver a service unencumbered by VAT liability, without the need for any legislative reform.

This can be achieved through a mechanism known as a Joint Venture Partnership (JPV), the details of which in many ways mirror the arrangements for outsourcing of accommodation that are described above. A joint Special Purpose Vehicle (SPV) is created, incorporating the partnering university, which holds a 51% shareholding, and the private sector provider, holding the remaining 49%. Critically, it is then possible to register the SPV for VAT within the same University VAT group, enabling the institution to outsource the provision of non-core services without creating a new VAT liability.

The British Universities Finance Directors Group estimates that universities spend around £9 billion p.a. on goods and services. The experience of industry providers in the transferring of the provision of such non-core services indicates that as much as 30% could be saved if such a model were adopted, equating to potential sector-wide savings of £2.7 billion per annum. **Universities should explore the possibility of developing similar arrangements with external providers in order to work around the VAT issue without the need for legislative change.**

Outsourcing: Information Technology Services

Universities have traditionally been reluctant to outsource their IT systems to third parties, preferring instead to provide these systems in-house. The traditional model of provision of IT services in the higher education sector is one in which individual institutions own, operate and provide IT services at all levels.[59] The chief reasons for this are discussed below but include concerns over data security and the difficulty of making accurate estimates of potential cost savings. However, universities are increasingly revisiting the issue in their search for efficiency of service provision. Many HEIs have begun to farm out the provision of their IT systems to third party specialists, most commonly Google and Microsoft.

The benefits of handing over these services to the private sector are clear:

- University e-mail systems can be provided free of charge by third party specialists. Both Google and Microsoft now host student email systems for free. Manchester Metropolitan University claims to have been able to save a "six figure sum" by choosing the Live@edu service through

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[59] Wilbert Kraan and Li Yuan, 'Cloud computing in institutions: a briefing paper', Joint Information and Systems Committee, March 2010, available at
http://wiki.cetis.ac.uk/images/1/11/Cloud_computing_web.pdf. Accessed 28/10/10

Microsoft.[60] It is estimated by the JISC that the University of Westminster saved close to £1 million by taking advantage of free data storage and email from Google.[61] UCL reported that it saved £250,000 by adopting Microsoft's live@edu email service in 2010;[62]

- Email provision by companies such as Google and Microsoft includes a range of additional applications including calendar, document sharing and instant messaging applications which are not usually found on email services provided in-house, and are regularly updated;

- By using remote 'cloud computing', in which computing resources are stored remotely and shared via the internet rather than on local servers,[63] universities have no need to maintain large, expensive and power-hungry servers on their campuses. This greatly lowers administration costs and reduces energy consumption;

- Cloud-based systems usually offer considerably greater storage capacity than those hosted on local servers;

- Using cloud-based systems managed by external providers negates the need for universities to regularly upgrade their own IT infrastructure to keep pace with demand, releasing long-term savings;

- Outsourced computing systems are more flexible than those provided in-house as the level of usage can be altered to reflect peaks and troughs in demand. For example, September enrolment requires significant IT capacity which will not then be needed for the majority of the rest of the year.[64] Rather than have expensive internal IT systems lying dormant, it is more efficient to use flexible outsourced computing where extra capacity can be rented when necessary.

However, universities have tended to be deterred by the following considerations:

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[60] Hannah Fearn, 'Outsourcing grows as institutions find silver lining in cloud computing', *Times Higher Education*, 8 April 2010, http://www.timeshighereducation.co.uk/story.asp?sectioncode=26&storycode=411114. Accessed 03/10/10

[61] Joint Information and Systems Committee, 'Outsourcing email and data storage at University of Westminster', December 2008, available at https://www.ucisa.ac.uk/en/members/activities/~/media/Files/members/activities/outsourcing/CS%20Westminster%20v1%2002%20AB%20pdf.ashx. Accessed 28/10/10

[62] Computing.co.uk, 'Universities opt for Microsoft's cloud email service over Google Mail', 4th May 2010, available at http://www.computing.co.uk/computing/news/2262403/univeristes-opt-microsoft. Accessed 27/10/10

[63] Cloud computing definition from Macmillan Dictionary, available at http://www.macmillandictionary.com/buzzword/entries/cloud-computing.html. Accessed 26/10/10

[64] Wilbert Kraan and Li Yuan, 'Cloud computing in institutions: a briefing paper', Joint Information and Systems Committee, March 2010, available at http://wiki.cetis.ac.uk/images/1/11/Cloud_computing_web.pdf. Accessed 28/10/10

- Often in-house systems have been installed at considerable expense, so managers feel reluctant to scrap them outright;

- Costing of IT services is a difficult task as it involves three interacting variables: people, processes and technology.[65] The HE sector has not yet fully met the challenge of costing IT systems and it is therefore more difficult for managers to make reliable estimates of the potential cost savings achievable through outsourcing such systems;

- Concerns over data security and privacy make some universities hesitant to use external providers for services that involve the storage of personal data, such as email systems. All cloud computing involves the processing of data on shared systems, and the transportation of that data via the internet.[66] This therefore leads to concerns about the vulnerability of these systems to illegal access. In addition, data protection requirements prohibit certain kinds of data from travelling outside an institution's jurisdiction.[67] These can be problematic in relation to cloud-based solutions which are not normally geographically defined;

- Although specialism and economies of scale should imply that external suppliers of computing systems are more proficient than university departments, such systems have been known to fail on occasion.

The above issues are far from sufficient to outweigh the benefits of IT outsourcing. However, the issue of data protection in particular is one that should be taken seriously. Oxford University decided against outsourcing its new email service, launched in 2009, due to concerns that emails from the University might be held on servers in countries outside the European Economic Area.[68] This led to concerns that the security of the stored data could not be adequately assured. However, the increased usage of outsourced IT services in the HE sector demonstrates that these concerns can be overcome. When three major UK universities (UCL, Manchester Metropolitan and Royal Holloway) adopted Microsofts live@edu email service in 2010, they did so on the basis of clear assurances made regarding the security of the system. Microsoft was able to assure the universities that emails would be stored in Dublin, assuaging data protection concerns. UCL's IT Director was quoted as saying 'Data protection was a major factor for us. Microsoft could tell the university exactly where its data would be held and that it would

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[65] Comment from the Joint Information and Systems Committee
[66] Wilbert Kraan and Li Yuan, 'Cloud computing in institutions: a briefing paper', Joint Information and Systems Committee, March 2010, available at
http://wiki.cetis.ac.uk/images/1/11/Cloud_computing_web.pdf. Accessed 28/10/10
[67] Ibid
[68] Joint Information and Systems Committee, 'Outsourcing email and data storage at Oxford University', December 2008, available at
https://www.ucisa.ac.uk/en/members/activities/~/media/Files/members/activities/outsourcing/CS%20OxfordUni%20v1%2002%20AB%20pdf.ashx. Accessed 28/10/10

keep the content of all emails private.'[69] Where such assurances are not available, universities may consider outsourcing only non-critical systems at first, and going further only when the provider has demonstrated its competence in relation to data security.

With regard to reliability and performance, there have been cases in the past in which outsourced computing systems have failed. However, providers are strongly incentivised to provide a reliable system in order to retain custom and, as the JISC notes, it is reasonable to expect failures to become considerably rarer as cloud computing develops. In addition, strong Service Level Agreements between the institution and the provider can help to mitigate any risk.[70] It should also be noted that internally-provided computing systems are far from immune to failure themselves.

As budget cuts begin to bite, institutions must be willing to look upon the private sector as a potential ally rather than with suspicion. **By embracing the offerings of private companies, the HE sector can reduce its costs, focus its attention on its core functions and provide a better, more cost-effective service for its students and staff.**

Case Study: University of Birmingham[71]

The University of Birmingham developed an online payment system which enables students to register for modules and make payments for tuition fees and university accommodation fees over a secure internet system. Not only is this far more convenient for students, it also saves the university time and money through not having to employ temporary staff to cover peak times such as the beginning of the academic year. Since the system went live in 2001, it has successfully processed over £36 million worth of payments.

The University has also worked in collaboration with WPM Education, a provider of online payment systems to the education sector, in order to develop the "e-shop" system. This online resource allows students to pay for university services such as field trips, short courses and other services. The "e-shop" has produced small value payment savings of over £1 million over a single academic year (2007-08). This is set to improve as students become more aware of the easy accessible system and take advantage of its convenience.

As well as saving the University money, the "e-shop" system has proved to be a source of income as over 60 institutions across the UK HE sector have bought into the product.

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[69] Computing.co.uk, 'Universities opt for Microsoft's cloud email service over Google Mail', 4th May 2010, available at http://www.computing.co.uk/computing/news/2262403/univeristies-opt-microsoft. Accessed 27/10/10

[70] Wilbert Kraan and Li Yuan, 'Cloud computing in institutions: a briefing paper', Joint Information and Systems Committee, March 2010, available at http://wiki.cetis.ac.uk/images/1/11/Cloud_computing_web.pdf. Accessed 28/10/10

[71] Russell Group Papers, *'Staying on top: The challenge of sustaining world-class higher education in the UK',* Issue 2, 2010

Case Study: Leeds Metropolitan University[72]

By July 2007, the e-mail system that was being used by Leeds Metropolitan University was in dire need of updating. The system had originally been created in a time when few students had access to the internet either at university or in their accommodation, and consequently the specifications had become seriously outdated. The University's system only allocated a small amount of disk space to each user account and did not have features common to third party systems, such as calendars, task managers or other office applications.

Added to these problems was the growth in demand for a fully comprehensive e-mail server. Students and staff were beginning to make far greater use of online resources for teaching and research, using digital photographs and recordings in their work and were submitting coursework online. The aged University email system struggled to handle these files, so students turned instead to third party offerings such as Yahoo Mail and Hotmail, which not only sported numerous additional features but also offered users gigabytes of disk storage space. The trouble was that these third party systems were not always compatible with the University's in-house network and messages were either not being delivered on time or were not being delivered at all. It therefore became clear that an entirely new system was required.

The first stage was to establish the precise needs of staff and students. This was done through numerous focus groups and informal conversations with key member of the student community, academics and administrative staff. Once this was completed, private-sector solutions could be assessed against the stated requirements of the faculty and student body. In the end GoogleMail was selected as the new email provider.

The system went live in February 2008 and after a mere four weeks over 3,000 Leeds Met students had signed up to GoogleMail. During the summer of 2008, a further 30,000 accounts were created, one for every student that would attend the University in the coming academic year. It was essential throughout the course of the project that there was an ongoing dialogue between Leeds Met, Google and the other key stakeholders, namely the staff and students who would be making use of the system. It is a testament to the strength of this partnership that the lines of communication were kept open so that the scheme worked so well.

Entrepreneurship and 'spin-offs'

Entrepreneurship in the university sector takes a number of forms. Often it involves the utilisation of an institution's intellectual capital in innovative partnerships with private industry, particularly in the area of high-technology enterprise. Universities are repositories of knowledge and expertise, and

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[72] Joint Information and Systems Committee, *Outsourcing Email and Data Storage*, December 2008

engagement with business can produce commercial returns, as well as fostering a culture of entrepreneurialism and creating strong links between the university and the private sector. Institutions with a strong track record of entrepreneurialism, such as the University of Hertfordshire, have put engagement with business at the heart of their operations, and have consequently benefited from a number of innovative commercial projects, ranging from a high-tech Biopark to a local bus service.

Universities can also generate income from commercial sources using 'internal outsourcing'. So far in this report we have looked at the possibility of an HEI outsourcing a product or service altogether. Although this does bring the considerable benefits of having a specialist company bringing in its own skills and expertise, not to mention significant cost savings, there are some potential drawbacks. In the first place, reducing expenditure is gained at the expense of losing a particular ongoing revenue stream, such as income from students for rental accommodation. In addition, the University loses a degree of control over that particular service by handing over its operation to a third party. In cases where an institution has strong reasons for deciding against outsourcing a service, it may instead make use of internal outsourcing where, instead of bringing in an outside organisation to provide a particular service, the university takes an in-house service and turns it into a separate business.

This solution allows the newly-formed company to look beyond the university as sole customer, and seek business elsewhere. As a result, it is possible to turn an unprofitable product or service into one that can produce a high turnover, allowing any profit to be fed back into the university. An example is the Uno bus service, owned by the University of Hertfordshire, which developed it from a bus service for students to an established local company serving the wider community- hence its slogan 'the university bus for everyone'.[73]

Case Study: University of Hertfordshire- *Uno* **Bus Service**

In 1992 the contract to run the bus service in Hatfield was open for bidding. The private companies that submitted bids were proposing to charge rates that were far too high for the local community. The University took the unusual step of entering the race and succeeded in securing the contract to run the town's bus service.

The company began life as *UniversityBus* and was set to provide transport links primarily to and from the University and to the surrounding local areas. Transport routes were opened up to include links from Hatfield to London. The bus company itself has since undergone a massive transformation and has become *Uno*, an established company with a brand that is recognised throughout the town.

In addition to providing a valuable service to the community, the University has been able to reduce the fares specifically for students attending the University, improving value for money for the student community.

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[73] Uno Bus Service, http://www.unobus.info/. Accessed 02/11/10

One of the keys to the success of this operation is that the company is run at arm's length from the University and maintains a quasi-autonomous status. This allows it the freedom to manoeuvre and be flexible in its business approach without interference or micromanagement from the University's governing body. The interests of the company come first and any benefits that are gained can then be passed on the University of Hertfordshire.

Making over 2,300,000 passenger journeys each year[74], *Uno* has managed to provide an annual turnover over £75 million.[75] The profits from this enterprise are then used to cross-subsidise the University itself. It is through such business interaction and entrepreneurship that the University has reduced its reliance on HEFCE funding. In fact, in 2009 the University of Hertfordshire relied on taxpayer support through HEFCE for less than a third of its total income.[76]

Entrepreneurial universities can also make use of the expertise they possess to manage external projects at a profit. Cornwall Country Council recently awarded the University of Plymouth a 25-year contract contract to manage the £12 million Pool Innovation Centre, which opened in June 2010. The centre is a modern business park, the first of its kind in the county, which aims to attract innovative companies to its 49 available offices.

Another potential source of commercial revenue for universities is via the creation of 'spin-off' companies, usually in high-technology fields, making use of an institution's research expertise and capacity for technological innovation. The University of Edinburgh alone was involved in the creation of 40 new business in the academic year 2009-2010, which have already raised £3 million in external funding.[77] Nine of the new businesses were created by academic staff, 19 by students, and 12 by entrepreneurs from outside the University who constructed their business through Edinburgh Research and Innovation (ERI), the University's technology transfer office (TTO).[78] The majority of leading institutions now have such offices, aimed at connecting commercial investors with an institution's reserves of expertise. They also seek to generate income through commercial licensing of new technologies developed by academics and students.

Some TTOs, including ERI, Imperial College's Imperial Innovations (which raised £66 million after being listed on the stock exchange in 2006), and Oxford's Isis Innovation (which spun out 65 ventures between 1999 and 2009) are highly successful. However, too many are ineffective: a 2008 review found that only around 6% are active in developing spin-off companies, licensing, or filing patents.[79] Policy Exchange

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[74] http://www.herts.ac.uk/about-us/working-with-the-community/home.cfm
[75] Private information
[76] University of Hertfordshire Annual Report 2009
[77] Hannah Fearn, 'Edinburgh creates record number of spin-offs', *Times Higher Education*, 19 October 2010
[78] Ibid
[79] Paul Wellings, *Intellectual Property and Research Benefit,* Department for Innovation, Universities and Skills, September 2008.

recommended in a previous Research Note, *Innovation and Industry: the role of universities,* that Government funding for TTOs, currently disbursed through the £150 million Higher Education Innovation Fund, should be restricted to TTOs that can demonstrate strong outcomes. Other institutions could then buy in expertise from these larger TTOs.[80]

Case study: Imperial Innovations

Imperial Innovations, founded in 1986 as a wholly-owned subsidiary over Imperial College, was one of Europe's first Technology Transfer Offices. It is now one of the UK's leading technology commercialisation companies, having been listed on the AIM stock exchange in 2006. The initial listing raised £26 million and a further £40 million of investment was raised over the next three years.

Despite now being a successful company in its own right, Imperial Innovations still works in close partnership with its former owner, and invests mainly in businesses based on the intellectual property from Imperial College, although it also seeks out other commercial opportunities. Its business model is to invest at seed stage, and it provides businesses with invaluable access to laboratories, equipment and office space at its Incubator site at Imperial College.

Imperial Innovations now has equity holdings in over 80 different companies.[81]

One difficulty with the creation of spin-off companies is the raising of capital in a project's early stages. Venture capitalists are often unwilling to take risks on promising technologies which nevertheless require considerable work before they are ready for commercialisation. This issue has been exacerbated by the economic recession, as investors and venture firms have focused on keeping existing ventures above water, rather than seeking out new projects.[82] The Government can therefore play an important role in providing proof-of-concept funding to allow projects to progress to a more commercially appealing stage. As Policy Exchange noted in *Innovation and Industry: the role of universities*, there are currently far too many disparate sources of such funding: up to 55 different funds exist, amounting to around £40 million in total.[83] These funds should all be rationalised and should be distributed by the Technology Strategy Board (TSB), a body established in 2007 to promote 'technology-enabled innovation' in the UK, and funded to the tune of around £200 million per annum. We endorse the recommendation made in *Innovation and Industry: the role of universities,* that the TSB should act as a vehicle to distribute proof-of-concept funding to innovative spin-off projects in their early stages. In addition, we welcome the recent announcement that the TSB will oversee the formation of a network of

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[80] Anna Fazackerley, Martin Smith and Alex Massey, *Innovation and Industry: The role of universities*, Policy Exchange, November 2009

[81] Information from Imperial Innovations, http://www.imperialinnovations.co.uk/index.php. Accessed 02/11/2010

[82] Richard Tyler, 'University spin-off activity collapses', *Daily Telegraph,* 31 December 2009

[83] Anna Fazackerley, Martin Smith and Alex Massey, *Innovation and Industry: The role of universities*, Policy Exchange, November 2009

technology and innovation centres, aimed at bridging the gap between universities and business, and funded to the tune of £200 million.[84]

While such changes should help simplify the system of public support for commercial innovation and business engagement within the HE sector, the main driver of change will be universities themselves. It is of crucial importance to the UK's HE sector that universities diversify their income streams, and make full use of the expertise and intellectual capital that they possess. The coming market-based reforms to higher education make this imperative even more pressing. Those institutions which are able to maximise the commercial potential of their resources will achieve a vital head-start in the newly competitive environment in which universities will find themselves. **It is of vital importance that institutions continue to develop ways to engage constructively with business and exploit to the full the commercial potential of their resources and ideas.**

Case Study: University of Hertfordshire BioPark[85]

The University of Hertfordshire is leading the way in engaging with specialist businesses through the setting up of the BioPark.

Established in February 2006, the BioPark is a thriving research and development centre with equipped laboratories, conference centres and meeting rooms. Biopharmaceutical and biomedical companies have been encouraged to move into this cluster and share their knowledge and expertise, developing strong links between the University, research institutes and private enterprise. The BioPark was established using £8 million of funding provided by the East of England Development Agency, which allowed the University to buy the former Roche Products Base in Welwyn Garden City. This 100,000 square foot centre was then converted in order to house the new BioPark.

This project is run on a commercial basis and is managed by Exemplas, a local business which the University acquired on behalf of the University itself. Any profits that are made are reinvested into the University. Not only does the University benefit from an additional income stream, but the local economy receives a boost thanks to the increased business activity in the community.

As of June 2010, 93% of the space in the BioPark had been let, and there are plans for further expansion, with a further £2.2 million investment planned by the University and its partners[86].

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[84] Technology and Strategy Board website, available at
http://www.innovateuk.org/deliveringinnovation/technology-and-innovation-centres.ashx. Accessed 3/11/10
[85] University Alliance, *Efficiency, leadership and partnership: an approach that delivers shared economic priorities*, June 2010
[86] Ibid

Recommendations:

1) **The Government should consider creating a 'contracted out services provision' for higher education, similar to that enjoyed by the NHS. This would remove a significant barrier to the outsourcing of services, allowing universities to concentrate on their core functions of teaching and research.**

2) **Alternatively, the Government should implement the EU VAT Directive on shared services. This will remove the significant tax barrier which is a current disincentive to HEIs collaborating to reduce costs. If immediate implementation is fiscally unrealistic, the Government should aspire to implement the Directive when future circumstances allow.**

3) **In the meantime, it is incumbent on universities to explore methods of working within the confines of existing tax legislation to deliver a service unencumbered by VAT liability, without the need for any legislative reform.**

4) **Universities must make a concerted effort to reduce their reliance on Government funding for support. All institutions must give due consideration to increasing their level of engagement with private business in order to diversify their income streams, and seek to take a more entrepreneurial approach to generating revenue from commercial sources.**

5) **We endorse the recommendations made in *Innovation and Industry: the role of universities* that funding for early-stage technological ventures should be unified through the Technology Strategy Board, and that public funding for technology transfer should be limited to a small number of high-quality TTOs.**

The work of the Education unit at Policy Exchange

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