Commercialisation and Enterprise: History and Context

Many universities and colleges have for many years sought to generate income from non-governmental sources. Such sources of income include student accommodation, catering, consultancy, the use of sports facilities – and for some of the older institutions substantial endowments, sometimes in the form of property, and donations from alumni.

Mike Shattock in his book Managing Successful Universities (OU Press – 2003) reminds us that the generation of non-state funding has a long tradition in the UK, pointing out that in the 1930’s about one third of universities’ income was from student fees, one third from other private sources (mostly endowments and investments) and one third from the state (through the University Grants Committee). In 1980 the government permitted institutions to charge overseas students (those from outside the EU) full cost fees, which led to a greater awareness of the market in many institutions.

The importance of generating more commercial income was brought to the fore in the 1990’s, when there was a significant fall in funding per student, the “unit of resource.” Between 1989 and 1997 there was a drop of some 36% in the public funding of teaching in England, and it has been estimated that the unit of resource has fallen by 45% since the late 1980’s. This has led both to institutions themselves seeking to generate more income from non-governmental sources, known as ‘third steam’ or ‘third leg’ funding (in addition to the primary sources for teaching and research), and to policy initiatives from the Government and the funding councils to support such strategies.

Hefce began this third stream funding in 1999, with the launch of funds specifically to support institutions to increase their capability to respond to the needs of business and the wider community, where this would lead to wealth creation. The first such funding stream was the Higher Education Reach out to Business and the Community initiative (HEROBAC) – sponsored by the DfES and DTI, and this was followed by successive rounds of the Higher Education Innovation Fund (HEIF), principally provided by the Science Budget. The UK Research Partnership Investment Fund is another related initiative.

It was announced in June 2012 that a new National Centre for Universities and Business is to be established to strengthen relationships and help economic growth.

In Wales third mission activities have been supported by the HEFCW Third Mission Fund and the Welsh Development Agency Knowledge Exploitation Fund. The current arrangements are set out on the HEFCW web site.

In Northern Ireland the Department for Employment and Learning provides core funding for third stream activities through the Northern Ireland Higher Education Innovation Fund, supplemented by the Higher and Further Education Collaboration Fund ‘Connected’.

In Scotland some of the key priorities in the Horizon Fund for Universities are knowledge transfer and innovation; employability and skills development; and widening access.

The 2003 White Paper 'The Future of Higher Education' had as one of the two principal areas in which the Secretary of State felt that universities ‘had to improve’ the need for better progress in harnessing knowledge to wealth creation and helping to turn ideas into successful businesses. This confirmed the strong political steer to generate new sources of income.

Commercialisation Strategies

One of the characteristics of a financially healthy institution identified by Mike Shattock in ‘Managing Successful Universities’ (OU Press – 2003) is the ability to generate non-state funding. A diversified funding base can both help to cover shortfalls in
state funding and provide support for innovation and development – ‘seed corn’ funding. Institutions which have ambitions to remain successful will have to develop strategies to harness the potential of ‘third stream’ or commercial income. It is, however, important not to become over-reliant on income streams which might dry up.

A growing number of institutions now describe themselves as ‘business-facing’, meaning gearing their work increasingly to the needs of the local economy.

Most of the funding councils encourage the development of strategies for ‘third leg’ or enterprise activities. Such a strategy should be considered and approved by the governing body. One key aspect will relate to governance structures. If a company or companies need to be set up a board of directors will be required. The directors will have to understand their responsibilities under company law, and clear reporting lines must be in place.

Commercialisation strategies should address the structures required to deliver, manage and monitor work in this area, resourcing and may also need to cover:

- Consultancy conducted by staff
- Short and special courses, CPD work and other academic services
- Conference facilities, which can be related to student accommodation
- Campus services, such as shops and catering outlets
- Collaboration with industry and commerce, from joint work to more substantial developments such as science parks
- Fund raising from alumni and other contacts
- The possible development of spin out companies, licensing and the filing of patents
- Internationalisation and overseas ventures. Some institutions have established overseas campuses. There can be significant risks in overseas ventures

Commercialisation strategies will also set out the projects or activities to be supported by commercial income streams, such as student bursaries or scholarships, staff development work, enhancing facilities or specific capital projects.

**Governance Structures for Supporting Third Stream Work and Commercialisation**

An area which many institutions find difficult is that commercial ventures generally require a commercial structure, with substantial freedom to operate. The governing body (or its finance committee) will, however, expect to see a thorough investment appraisal and business plans, and regular performance data, and will expect the finance director to oversee such activities carefully.

Higher education institutions in the UK are charitable, and as the generation of commercial income may not be compatible with this charitable status, many institutions have established trading companies. In some cases there may be a holding company with subsidiaries. Some specific ventures are best managed through subsidiary companies (and there is guidance on this from Hefce). It is important that the relationship between the institution and any such companies is clear, and that they have sufficient independence to operate commercially. There may be issues, such as conflicts of interest, for governing bodies if members serve on the boards of subsidiary companies.

Some institutions may also have separate foundation trusts which may be used for fund-raising campaigns.

The governing bodies of some institutions have established specialist committees to monitor the development of commercial work. Such committees may need to have specialist expertise not already on the governing body. It is important that the role and remit of such committees, and any delegated powers, is clear.
It is also usual for there to be strong management oversight of commercial work by the executive. Some institutions give overall responsibility to a pro vice-chancellor (or equivalent officer), and many have established business development or enterprise functions, with appropriately qualified and experienced staff.

**Risk and Commercialisation**

Hefce guidance on risk management says that ‘the governing body should, as a minimum, ensure that there is an ongoing process for identifying, evaluating and managing the risks faced by the institution...’ In this it will be supported in particular by its audit committee. Commercial or trading activities may give rise to financial and reputational risks. These have to be balanced with the benefits of a more entrepreneurial culture.

It is also possible that there could be legal problems associated with consultancy, knowledge transfer work and the setting up of subsidiary or spin out companies if suitable professional expertise is not applied to their oversight. Collaboration with industry and commerce may raise HRM issues concerning remuneration or potential conflicts of interest, and could affect staff attitudes and behaviour. Contractual arrangements must be put in place clearly and in good time, and the governing body will wish to assure itself that this is the case. It is also important for insurance cover to be in place.

**Full Economic Costing**

Universities and colleges are being strongly encouraged to charge the full market price for their services (including research), and this encouragement is reinforced through the financial memoranda with the funding councils. Hefce sets out to the English institutions: ‘as part of ensuring its long term viability, an institution should know the full economic cost of its activities and use this information in making decisions. If it does not seek to recover the full cost, this should be the result of a clear policy set by the governing body and included in the financial strategy, and should not put the institution into financial difficulty. We expect our funds not to subsidise non-public activities’.

The funding councils, with Universities UK and GuildHE (formally SCOP), set up the Joint Costing and Pricing Steering Group in 1997 to help institutions to develop effective costing and pricing arrangements. One of the outcomes of the work of the JCP SG was the **Transparency Review** which developed the **Transparent Approach to Costing (TRAC)**, an activity based costing methodology for institutions. A set of TRAC guidance was published in 2005, both in the form of a non-technical overview and with detailed technical guidance. It can be applied both at institutional, or project/activity level. Hefce provides further guidance on financial sustainability and TRAC.

KPMG has undertaken a review of TRAC for Hefce, and a consultation on the future of the TRAC was launched in October 2012.

Two years after research councils began using full economic costs in the awarding of grants, Research Councils UK published a review of the process and a further review, chaired by Sir William Wakeham, resulted in **Financial Sustainability and Efficiency in Full Economic Costing of Research in UK HEIs**.

Following an extensive study JM Consulting have reported to the UK HE funding bodies on the calculation of research cost relativities based on the TRAC methodology.

In practice many institutions are not able to secure the full costs of their services, so commercial decisions have to be taken, in the light of market conditions, to maximise returns, often on a ‘cost plus’ basis.
Regionalisation

The 2003 White Paper 'The Future of Higher Education' asserts that 'the involvement of universities and colleges in regional, social and economic development is critical'. This can be in the form of knowledge and skills transfer, or through regeneration or other projects. Most institutions are also significant employers, which can have a big effect on regional and local economies. Regions it is argued are beginning to play a significant role in the global economy.

Significant contributions can be made to **Regional Economic Strategies** and other initiatives, academic, social and economic. Such partnerships can have a major impact on the institutional profile in the region. Links with schools and colleges, which may form part of a widening participation strategy, can also improve student recruitment.

In December 2009 the Department for Business, Innovation and Skills published 'Partnerships for Growth', a framework for the development of regional strategies in England, in particular related to economic development, innovation and skills. Local Enterprise Partnerships are now being developed. Higher education staff sit on the boards of almost all the partnerships and are using them to develop and strengthen links with business.

Hefcw has a clear regional strategy for the planning and delivery of higher education in Wales.

Governors may be involved with the development of regional strategies, or regional issues may be included in other areas of the corporate plan. Institutions in Scotland, Wales and Northern Ireland will also have to plan strategically in relation to their national agendas. The HEPI report Universities and Constitutional Change in the UK examines whether devolution in the UK has led to more distinctive HE policies in the devolved administrations.

The contribution of universities to their communities is well summarised in an article in The Times Higher Education (THE). The impact of changes in regional structures is examined in Beyond Bricks and Mortar Boards, published by UUK.

The SFC is proposing (September 2012) the establishment of a single knowledge exchange office in Scotland. Hefce publishes regional profiles of higher education in England.