

Office for
Students



Annual TRAC 2016-17

Sector analysis

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Background

1. All UK higher education institutions are required to report Transparent Approach to Costing (TRAC) data annually by 31 January each year. TRAC data was first collected for academic year 1999-2000. Further education colleges and alternative providers of higher education are not required to submit TRAC data. TRAC data for 2016-17 was collected by the Higher Education Funding Council for England (HEFCE) on behalf of Research Councils UK and UK Research Councils, the Scottish Funding Council, the Higher Education Funding Council for Wales and the Department for the Economy (Northern Ireland) and these bodies are co-owners of the data, with the Office for Students and UK Research and Innovation.
2. 2016-17 is the second year in which TRAC reporting has been prepared under the new Higher Education Statement of Recommended Practice, applying Financial Reporting Standard (FRS) 102. This reporting standard introduced some significant changes in the way financial performance is reported, making comparison difficult between the latest results and historical TRAC data prior to 2015-16. Data for 2015-16 therefore formed the baseline for the start of a new time series of TRAC data. Analysis of the annual TRAC data for 2015-16 was published by HEFCE at www.hefce.ac.uk/data/year/2017/trac201516analysis/. Responsibility for reporting on TRAC data for 2016-17 has passed from HEFCE to the Office for Students.
3. This paper contains analysis of the 2016-17 sector aggregate data based on submissions from 131 higher education institutions in England and Northern Ireland¹. Aggregated data for 158 UK higher education institutions is provided in Annex B.

Key points

4. The annual TRAC return data for 2016-17 needs to be interpreted with caution. The sector aggregated position for higher education institutions in England and Northern Ireland showed a deficit of £1,033 million (excluding Research and Development Expenditure Credit (RDEC) income²), with 96.8 per cent of TRAC full economic costs recovered³. This compares with a small deficit in 2015-16 of £107 million (excluding RDEC), and a recovery of 99.6 per cent of full economic costs in 2015-16 (excluding RDEC income). This represents a deterioration on the previous year with a significant increase in costs of 6.9 per cent based on the full economic costs across all activities. This increase comprises:

¹ The analysis is based on 129 higher education institutions that were funded by HEFCE, and two higher education institutions funded by the Department for the Economy, Northern Ireland. Data for one institution in England is excluded from this analysis.

² The RDEC scheme was established by the government in 2013 to offer tax incentives to large companies to encourage greater investment in research and development. The scheme has now been amended so that universities and charities are unable to claim RDEC in respect of expenditure incurred on or after 1 August 2015. A number of institutions made claims to HM Revenue and Customs for eligible expenditure incurred in the period 2012-13 to 2014-15 and therefore included RDEC in their financial accounts for 2014-15, 2015-16 and 2016-17. (Some institutions did not receive payments for claims related to the period 2012-13 to 2014-15 until 2016-17). As the RDEC income is a large one-off financial benefit to the sector, we have shown two versions of the recovery on research activity and the sustainability gap figures, one including and one excluding net RDEC income.

³ TRAC full economic costs includes a sustainability adjustment: the margin for sustainability and investment. Further information is shown at Annex A.

- a. Staff cost increases of £725 million (a 4.7 per cent increase), other operating cost increases of £401 million (3.9 per cent) and a £176 million increase in depreciation (10.0 per cent).
 - b. A change in the method for calculating the sustainability adjustment. The approach used up to 2015-16 was based on two components of the sustainability adjustments (infrastructure adjustment and the return for financing and investment), which totalled £2,258 million (8.1 per cent of total expenditure) for 2015-16. However, the return for financing and investment component was based on factors that had not been revised since 2006, and thus understated the adjustment required for sustainability. The new approach to calculating the sustainability adjustment is the 'margin for sustainability and investment' (MSI), based on the six-year average 'earnings before interest, taxation, depreciation and amortisation' (EBITDA)⁴, which was £3,000 million (10.2 percent of total expenditure) for 2016-17, an increase of £742 million compared with 2015-16.
5. The change in the basis for financial reporting with the implementation of FRS 102 from 2015-16 makes comparison between years more difficult. (Reporting for 2014-15 and previous years was prepared on a different accounting basis). The changes lead to earlier recognition of income from donations, endowments and capital grants (in the year of receipt), with income recognised ahead of the expenditure which it supports. It also leads to potentially greater variability in income between years, making it more difficult to interpret the sector's and individual institutions' financial sustainability based on data for a single year. Nevertheless, institutions' operations and funding have not changed materially over the period 2014-15 to 2016-17.
 6. As an indication of the scale of the potential impact of these changes in financial reporting, total TRAC income for 2015-16 (£30,165 million excluding RDEC) included new donations and endowments, new capital grants and other material items totalling £1,308 million (4.3 per cent of the income). For 2016-17 total TRAC income included new donations and endowments, new capital grants and other material items totalling £942 million (3.0 per cent of income), with notable reductions in the levels of new capital grants from both government and non-government sources. The impact of expenditure items such as staff restructuring, reorganisation or property transactions on the sector's cost recovery was immaterial for the sector as a whole, totalling only £106 million (0.3 per cent of TRAC full economic costs) in 2016-17 (in 2015-16, £65 million, or 0.2 per cent of TRAC full economic costs.)

⁴ A margin for sustainability and investment is added to the costs reported in the consolidated financial statements to present the full economic cost. The MSI provides an institution-specific margin based on a six-year average of past financial performance and forecast performance. It is based on an agreed definition of the earnings before interest, taxation, depreciation and amortisation. The allocation of MSI to activities is based on the proportion of total expenditure allocated to the activity categories (teaching, research and other).

7. The sector aggregate TRAC data for higher education institutions in England and Northern Ireland presented in Table 1 and Figure 1 shows that:
- a. Publicly funded teaching shows a small deficit on a full economic cost basis – meaning that costs slightly exceed income, with 99.9 per cent of the full economic costs recovered. This is a deterioration from 2015-16.
 - b. Non-publicly funded teaching (primarily of overseas students) continues to generate a significant surplus: £1,200 million (27.0 per cent of income), representing a reduction of 5.6 per cent on the surplus of £1,271 million (29.5 per cent of income) in 2015-16.
 - c. Research continues to show a substantial deficit of £3,371 million, or £3,390 million after excluding the one-off benefits from RDEC. The latter represents a recovery of only 70.7 per cent of full economic costs. The underlying cost recovery (excluding RDEC) deteriorated from 74.1 per cent in 2015-16 to 70.7 per cent, and is notably lower than in 2010-11, when the recovery rate on research peaked at 77.8 per cent. Research income for 2016-17 is boosted by £519 million of income from new endowments, donations and capital grants.
 - d. For the first time in 2016-17, reporting of ‘Other activities’ is sub-divided into ‘Other (income-generating activity)’ and ‘Other (non-commercial activity)’. This shows that ‘Other (income-generating activity)’ achieved a surplus of only £60 million based on income of £4,795 million (1.2 per cent), while ‘Other (non-commercial activity)’ – from endowments, donations and capital grants – shows a substantial surplus of £1,107 million. In aggregate, ‘Other’ activities generated a surplus of £1,167 million (recovery of 123.5 per cent) compared with £1,113 million in 2015-16 (recovery of 123.6 per cent), but this is distorted by the reporting of new endowments, donations and capital grants received in the year. In 2016-17, these items totalled £191 million compared with £415 million in 2015-16. These funds will support expenditure arising in subsequent years such as investment in buildings, equipment and facilities.
 - e. Across all activities, the sector in England and Northern Ireland showed a deficit of £1,033 million (3.3 per cent of income), after excluding the RDEC benefit. This represents a deterioration from the previous year’s deficit of £107 million (0.4 per cent of income).

Table 1: TRAC income and full economic costs by activity, 2016-17 (higher education institutions in England and Northern Ireland) (figures in £M)⁵

	Teaching (Publicly funded)	Teaching (Non- publicly funded)	Research	Research excluding RDEC	Other (Income- generating)	Other (Non- commercial)	Other (Total)	Total	Total excluding RDEC
Income	12,602	4,437	8,191	8,167	4,795	1,330	6,125	31,355	31,331
TRAC full economic costs	12,612	3,237	11,562	11,557	4,735	223	4,958	32,369	32,365
Surplus/(deficit)	-10	1,200	-3,371	-3,390	60	1,107	1,167	-1,014	-1,033
Surplus/(deficit) as % of income	-0.1%	27.0%	-41.2%	-41.5%	1.2%	83.2%	19.1%	-3.2%	-3.3%
Recovery of full economic costs %	99.9%	137.1%	70.8%	70.7%	101.3%	596.8%	123.5%	96.9%	96.8%
Recovery of full economic costs % (2015-16)	102.4%	141.9%	74.7%	74.1%	data not available	data not available	123.6%	99.9%	99.6%
Included in income									
New endowments received	23	25	71	71	4	31	35	155	155
New donations	24	38	141	141	0	93	93	297	297
New government capital grants	70	9	209	209	18	2	21	309	309
New non-government capital grants	14	3	94	94	23	3	26	138	138
Other material items	22	3	3	3	15	1	16	44	44
Total income items	153	79	519	519	61	131	191	942	942
Total as % of income	1.2%	1.8%	6.3%	6.4%	1.3%	9.8%	3.1%	3.0%	3.0%
Total as % of income (2015-16)	1.5%	3.2%	7.2%	7.3%	data not available	data not available	7.1%	4.3%	4.3%

⁵ Definitions for this table can be found on the following page. Figures in this and subsequent tables may not sum because of rounding.

Definitions for Table 1

Publicly funded teaching: Teaching of higher and further education courses to home and EU students who were fundable by HEFCE or the Department for the Economy (Northern Ireland) or by the NHS, National College of Teaching and Leadership, or Education and Skills Funding Agency. Income includes student fees paid via the Student Loans Company.

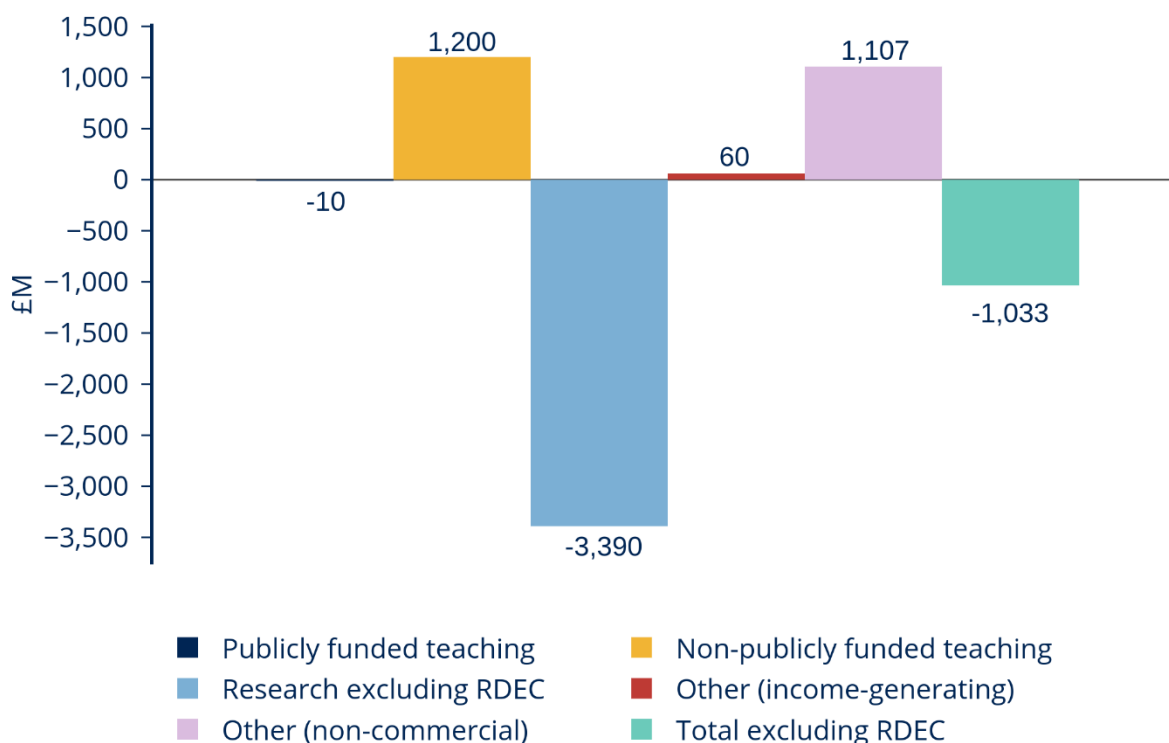
Non-publicly funded teaching: Teaching of students from outside the UK and EU; self-funded home and EU students and other commissioned courses (such as employer-specific 'closed' courses).

Research: All research activity (but not scholarship or staff development) commissioned and funded by external sponsors, or the institution's own-funded research activity. Public sponsors of research include UK Research Councils and other government departments. Other sponsors include UK charities, the EU, overseas governments, overseas charities and research carried out for commercial or industrial sponsors.

Other (income-generating): Includes commercial activities such as catering and conferences, commercially let facilities and residences; activities carried out through subsidiary companies such as publishing or commercial consultancy; knowledge transfer activity; and, for institutions with medical and dental schools, services provided to the NHS. (New sub-category reported for the first time in 2016-17.)

Other (non-commercial): Non-commercial activity such as investment and donations or endowments. (New sub-category reported for the first time in 2016-17.)

Figure 1: TRAC full economic cost surplus/(deficit) by activity, 2016-17 (higher education institutions in England and Northern Ireland)



8. Table 2 provides further analysis of research income and costs, analysed by research sponsor type. This shows that:
- a. Research Council funded research activity accounts for 20.1 per cent of total research costs, with a recovery of 71.8 per cent, after including £93 million of new capital grants (£50 million in new government capital grants and £43 million in new non-government capital grants).
 - b. Cost recovery on 'Training and supervision of postgraduate research students' continues to show the lowest recovery across the externally sponsored research activity, at 49.9 per cent. Postgraduate full-time equivalent student numbers as reported in TRAC decreased by 1.3 per cent from 82,625 to 81,535⁶.
 - c. Quality-related research funding from UK higher education funding councils, available to support all 'public good' research, totalled £1,626 million (materially unchanged from 2015-16 and prior years). This is insufficient to address the shortfall in the sector's 'public good' research portfolio, leaving research reliant on cross-subsidy from other income-generating activities and from non-publicly funded teaching.
9. In line with previous years, the sector continues to have a substantial level of activity that is not fully funded.
10. UK sector aggregate data is provided at Annex B.

⁶ Data does not include postgraduate students at institutions that apply dispensation from TRAC requirements.

Table 2: Research income and costs by sponsor type, 2016-17 (aggregate for England and Northern Ireland higher education institutions) (figures in £M)

	Recurrent research funding from the Funding Councils	Institution own-funded	Training and supervision of postgraduate research students	Research Councils	Other government departments	Other government departments excluding RDEC	EU	UK charities	Industry	Total research	Total research excluding RDEC
Income	1,626	367	1,027	1,664	872	848	631	1,038	965	8,191	8,167
TRAC full economic costs		2,159	2,056	2,318	1,116	1,112	967	1,709	1,236	11,562	11,557
Surplus/(deficit)		-1,792	-1,029	-653	-244	-263	-336	-671	-271	-3,371	-3,390
Surplus/(deficit) as % income		-488.1%	-100.3%	-39.3%	-28.0%	-31.1%	-53.3%	-64.6%	-28.1%	-41.2%	-41.5%
Recovery of full economic costs %		17.0%	49.9%	71.8%	78.1%	76.3%	65.2%	60.7%	78.1%	70.8%	70.7%
Recovery of full economic costs % (2015-16)		16.3%	51.8%	75.5%	83.1%	76.4%	68.0%	66.7%	78.8%	74.7%	74.1%
Included in income											
New endowments received	0	62	4	0	0	0	0	0	5	72	72
New donations	0	74	12	3	0	0	0	2	49	141	141
New government capital grants	1	75	16	50	35	35	8	15	10	211	211
New non-government capital grants	0	1	5	43	2	2	2	18	21	93	93
Other material items	0	1	1	0	1	1	0	0	0	3	3
Total income items	1	214	38	96	38	38	11	36	85	519	519
Total as % of income	0.1%	58.2%	3.7%	5.8%	4.3%	4.5%	1.7%	3.5%	8.8%	6.3%	6.4%
Total as % of income (2015-16)	0.5%	50.0%	4.0%	5.6%	4.0%	4.4%	4.4%	12.9%	9.4%	7.2%	7.3%

Notes to Table 2

'European Union' covers EU government bodies including the Commission. 'Industry' includes all other organisations such as UK industry, commerce and public corporations, EU non-government organisations (comprising EU-based charities, EU industry and any other EU source), overseas charities, overseas industry and other sources.

List of abbreviations

EBITDA	Earnings before interest, taxation, depreciation and amortisation
FRS	Financial Reporting Standard
HEFCE	The Higher Education Funding Council for England
MSI	Margin for Sustainability and Investment
RDEC	Research and Development Expenditure Credit
TRAC	Transparent Approach to Costing

Annex A: Derivations

Table 3: Derivation of TRAC full economic costs and sustainability gap (aggregate for higher education institutions in England and Northern Ireland)

	Total (£M)	Total excluding RDEC (£M)
Total income (derived from financial statements for 2016-17)	31,355	31,331
Total expenditure (derived from financial statements for 2016-17)	29,369	29,364
Operating surplus/(deficit) per audited financial statements	1,986	1,967
Target surplus for sustainable operations (EBITDA for MSI)	3,000	3,000
Sustainability gap (deficit)	-1,014	-1,033
Full economic cost (total expenditure plus target surplus for sustainable operations)	32,369	32,365

Notes to Table 3

1. The Research and Development Expenditure Credit (RDEC) scheme was established by the government in 2013 to offer tax incentives to large companies to encourage greater investment in research and development. The scheme has now been amended so that universities and charities are unable to claim RDEC in respect of expenditure incurred on or after 1 August 2015. However, a number of institutions made claims to HM Revenue and Customs for eligible expenditure incurred in the period 2012-13 to 2014-15, and therefore included RDEC in their financial accounts for 2014-15, 2015-16 and 2016-17. As the RDEC income is a large one-off financial benefit to the sector, we have shown two versions of the recovery on research activity and the sustainability gap figures, one including and one excluding net RDEC income.
2. The income and expenditure lines as reported in the financial statements are adjusted, where appropriate, in respect of pension costs, gains or losses on disposal of fixed assets, gains or losses on investments, share of surpluses or deficits in joint ventures and associates, taxation charges or credits and non-controlling interests, in line with the TRAC guidance.
3. The target surplus for sustainable operations is defined as 'earnings before interest, tax, depreciation and amortisation' adjusted as defined in the TRAC guidance requirements (section 3.2.4 and template at Annex 3.2a) to provide the 'margin for sustainability and investment' ('EBITDA for MSI')⁷.
4. The sustainability gap (deficit) is the difference between the actual operating surplus achieved and the target sustainability surplus to cover long-run costs (full economic costs).
5. Full economic cost is total expenditure derived from the financial statements, plus the target surplus for sustainable operations.

⁷ The TRAC guidance is available at www.hefce.ac.uk/funding/finsustain/trac/.

Annex B: UK figures

Table 4: Transparent Approach to Costing (TRAC) income and full economic costs by activity 2016-17 (UK higher education institutions) (figures in £M)

	Teaching (publicly funded)	Teaching (non- publicly funded)	Research	Research excluding RDEC	Other (income- generating)	Other (non- commercial)	Other (Total)	Total	Total excluding RDEC
Income	14,598	5,205	9,785	9,760	5,538	1,513	7,051	36,639	36,614
TRAC full economic costs	14,673	3,799	13,647	13,643	5,460	241	5,701	37,820	37,816
Surplus/(deficit)	-75	1,407	-3,862	-3,883	78	1,272	1,350	-1,181	-1,201
Surplus/(deficit) as % of income	-0.5%	27.0%	-39.5%	-39.8%	1.4%	84.1%	19.1%	-3.2%	-3.3%
Recovery of full economic costs %	99.5%	137.0%	71.7%	71.5%	101.4%	628.1%	123.7%	96.9%	96.8%
Recovery of full economic costs % (2015-16)	101.4%	141.2%	75.5%	74.6%	data not available	data not available	122.8%	99.4%	99.1%
Included in income									
New endowments received	24	32	73	73	4	33	37	166	166
New donations	26	49	153	153	2	115	116	344	344
New government capital grants	88	13	251	251	21	2	23	376	376
New non-government capital grants	20	6	124	124	24	3	27	176	176
Other material items	22	3	3	3	15	2	17	45	45
Total income items	180	103	604	604	65	156	221	1,107	1,107
Total as % of income	1.2%	2.0%	6.2%	6.2%	1.2%	10.3%	3.1%	3.0%	3.0%
Total as % of income (2015-16)	1.4%	3.0%	6.9%	6.9%	data not available	data not available	7.3%	4.2%	4.2%

Definitions for Table 4

Publicly funded teaching: Teaching of higher and further education courses to home and EU students who were fundable by HEFCE or the Department for the Economy (Northern Ireland) or by the NHS, National College of Teaching and Leadership, or Education and Skills Funding Agency. Income includes student fees paid via the Student Loans Company.

Non-publicly funded teaching: Teaching of students from outside the UK and EU; self-funded Home and EU students and other commissioned courses (such as employer-specific 'closed' courses).

Research: All research activity (but not scholarship or staff development) commissioned and funded by external sponsors, or the institution's own-funded research activity. Public sponsors of research include UK Research Councils and other government departments. Other sponsors include UK charities, the EU, overseas governments, overseas charities and research carried out for commercial or industrial sponsors.

Other (income-generating): Includes commercial activities such as catering and conferences, commercially let facilities and residences; activities carried out through subsidiary companies such as publishing or commercial consultancy; knowledge transfer activity and, for higher education institutions with medical and dental schools, services provided to the NHS. (New sub-category reported for the first time in 2016-17.)

Other (non-commercial): Non-commercial activity such as investment and donations or endowments. (New sub-category reported for the first time in 2016-17.)

Figure 2: TRAC full economic cost surplus/(deficit) by activity, 2016-17 (UK higher education institutions)

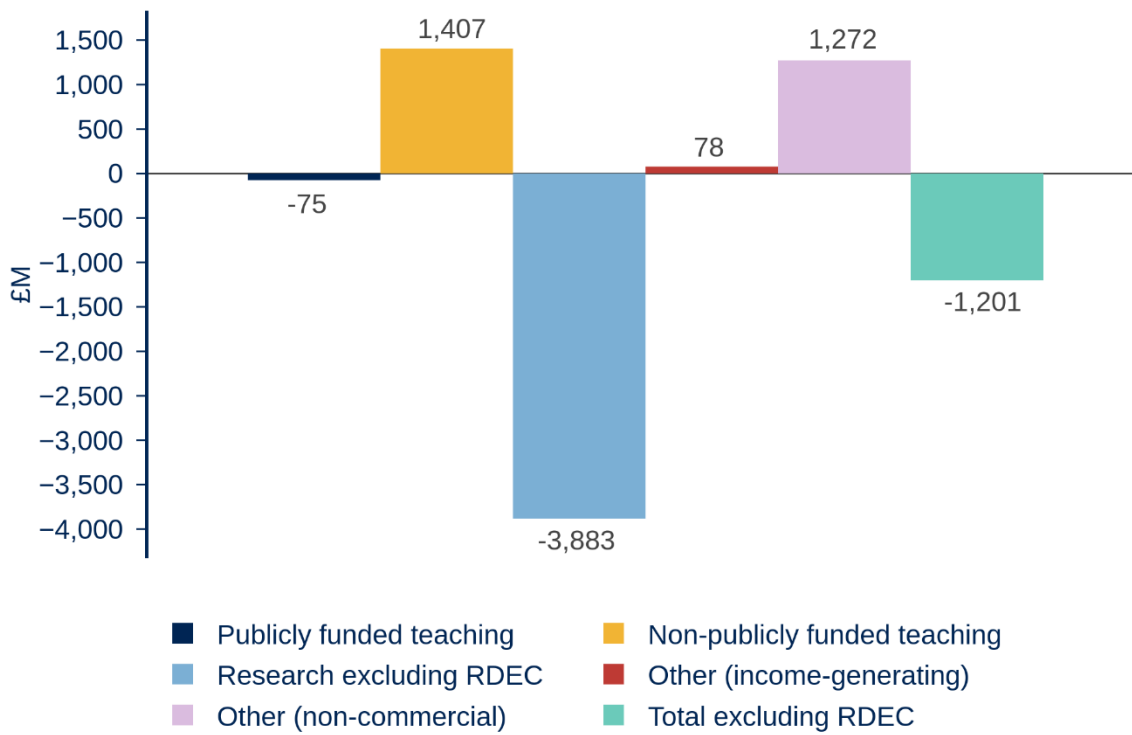


Table 5: Research income and costs by sponsor type, 2016-17 (UK higher education institutions) (figures in £M)

	Recurrent research funding from the Funding Councils	Institution own-funded	Training and supervision of postgraduate research students	Research Councils	Other government departments	Other government departments excluding RDEC	EU	UK charities	Industry	Total research	Total research excluding RDEC
Income	1,963	424	1,191	2,025	1,073	1,048	762	1,234	1,113	9,785	9,760
TRAC full economic costs		2,452	2,407	2,800	1,366	1,361	1,159	2,019	1,445	13,647	13,643
Surplus/(deficit)		-2,028	-1,216	-775	-293	-313	-397	-785	-332	-3,862	-3,883
Surplus/(deficit) as % income		-478.4%	-102.1%	-38.3%	-27.3%	-29.9%	-52.0%	-63.6%	-29.8%	-39.5%	-39.8%
Recovery of full economic costs %		17.3%	49.5%	72.3%	78.5%	77.0%	65.8%	61.1%	77.0%	71.7%	71.5%
Recovery of full economic costs % (2015-16)		16.6%	50.5%	76.4%	86.5%	78.2%	67.8%	66.2%	77.7%	75.5%	74.6%
Included in income											
New endowments received	0	62	5	0	0	0	0	0	5	73	73
New donations	0	74	12	3	1	1	0	4	58	153	153
New government capital grants	1	93	19	57	40	40	11	19	12	253	253
New non-government capital grants	0	3	6	57	9	9	4	21	22	122	122
Other material items	0	1	1	0	1	1	0	0	0	3	3
Total income items	1	234	43	117	51	51	15	44	98	604	604
Total as % of income	0.1%	55.2%	3.6%	5.8%	4.8%	4.9%	2.0%	3.5%	8.8%	6.2%	6.2%
Total as % of income (2015-16)	0.6%	46.8%	3.8%	6.1%	4.4%	5.0%	4.2%	11.5%	8.3%	6.9%	6.9%

Notes to Table 5

'European Union' covers EU government bodies including the Commission. 'Industry' includes all other organisations such as UK industry, commerce and public corporations, EU non-government organisations (comprising EU-based charities, EU industry and any other EU source), overseas charities, overseas industry and other sources.

Table 6: Derivation of TRAC full economic costs and sustainability gap (aggregate for UK higher education institutions)

	Total (£M)	Total excluding RDEC (£M)
Total income (derived from financial statements for 2016-17)	36,639	36,614
Total expenditure (derived from financial statements for 2016-17)	34,429	34,425
Operating surplus/(deficit) per audited financial statements	2,210	2,190
Target surplus for sustainable operations (EBITDA for MSI)	3,391	3,391
Sustainability gap (deficit)	-1,181	-1,201
Full economic cost (total expenditure + target surplus for sustainable operations)	37,820	37,816

Notes to Table 6

1. The Research and Development Expenditure Credit (RDEC) scheme was established by the government in 2013 to offer tax incentives to large companies to encourage greater investment in research and development. The scheme has now been amended so that universities and charities are unable to claim RDEC in respect of expenditure incurred on or after 1 August 2015. However, a number of institutions made claims to HM Revenue and Customs for eligible expenditure incurred in the period 2012-13 to 2014-15, and therefore included RDEC in their financial accounts for 2014-15, 2015-16 and 2016-17. As the RDEC income is a large one-off financial benefit to the sector, we have shown two versions of the recovery on research activity and the sustainability gap figures, one including and one excluding net RDEC income.
2. The income and expenditure lines as reported in the financial statements are adjusted, where appropriate, in respect of pension costs, gains or losses on disposal of fixed assets, gains or losses on investments, share of surpluses or deficits in joint ventures and associates, taxation charges or credits and non-controlling interests, in line with the TRAC guidance.
3. The target surplus for sustainable operations is defined as ‘earnings before interest, tax, depreciation and amortisation’ adjusted as defined in the TRAC guidance requirements (section 3.2.4 and template at Annex 3.2a) to provide the ‘margin for sustainability and investment’ (‘EBITDA for MSI’)⁸.
4. The sustainability gap (deficit) is the difference between the actual operating surplus achieved and the target sustainability surplus to cover long-run costs (full economic costs).
5. Full economic cost is total expenditure derived from the financial statements, plus the target surplus for sustainable operations.

⁸ The TRAC Guidance is available at www.hefce.ac.uk/funding/finsustain/trac/.



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