

OXFORD UNIVERSITY GAZETTE



THE UNIVERSITY'S RESOURCE ALLOCATION METHOD (RAM) (updated for 2002–2003)

SUPPLEMENT (2) TO NO. 4629

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Introduction

1. In 2001–2, the University introduced a new Resource Allocation Method (RAM) to govern the allocation of university resources to divisions/ODCE, and academic and non-academic services. The new method was described in supplement (1) to *Gazette* No. 4590, Wednesday, 20 June 2001. Since then, Council's Planning and Resource Allocation Committee (PRAC) has reviewed the new method, in the light of the experience of the first year, and also taking into account comments which have been received from within the University on its operation. As a result of this further consideration, some revisions have been introduced into the allocation method for 2002–3. The purpose of this note is to provide an updated account of the new Resource Allocation Method.

2. The paragraphs below set out the underlying principles, and main objectives, of the method, and give details of the formulaic and non-formulaic elements embodied within it. They highlight refinements to the method which have been made following the first year of its implementation.

3. Further details on any aspect of the method may be obtained from relevant staff of the Planning and Resource Allocation Section in the University Offices (and in particular Mr M.D. Sibly, telephone: 80303, e-mail: michael.sibly@admin.ox.ac.uk, or Mr P.F. Clark, telephone: 70078, e-mail: paul.clark@admin.ox.ac.uk, or Mrs V.M. Wood, telephone: 80678, e-mail: veronica.wood@admin.ox.ac.uk). Details can also be found on the Section's Web site, at <http://www/admin.ox.ac.uk/prac/>.

General principles

4. The RAM was introduced to complement the University's new governance and planning structures. It was intended to provide a transparent and consistent means of allocating the University's income to divisions, to whom responsibility for preparing academic budgets was devolved. Thus, whilst Council through the PRAC remains ultimately responsible for approving proposed divisional budgets, and for monitoring activity against them, responsibility for determining detailed spending decisions now rests with divisions. Details of the application of the method within each division may be obtained from the relevant divisional board secretariat.

5. Among other things, the design of the RAM is intended to encourage increases in the University's income, and its

most efficient use. This is achieved by allocating as much income as possible directly to divisions and ODCE, and building appropriate drivers into the formulaic allocation of the remaining funds.

6. Implementation of the RAM is also designed to link the allocation of income directly to planned academic activity, so that money flows according to the strategic academic priorities set by the University and the divisions. Operation of the RAM should be governed by these priorities, and the academic and managerial principles established by the University, rather than by the contingencies of a given financial situation. The RAM is concerned with the most effective and fair distribution of the University's income. It is not concerned with monitoring expenditure or the costs of different activities, although this may of course inform the future development of the RAM.

7. The RAM takes account of the way in which income comes into the University, but it is not simply an 'income as earned' model. The RAM thus also provides the University with a safeguard against fluctuations in the methods used externally to calculate the University's funding, and a means of mitigating the effects of external policies and methods of allocating funds which may not fit with its own strategic priorities. It gives the University the ability to move away, e.g., from the use of the HEFCE price bands and cost drivers in the distribution of income. It also allows the University to moderate the financial effects of external 'market' forces, by redistributing funds towards activities which it deems to be academically desirable, but which may not be financially self-sustaining (e.g., the support of important minority subjects). Thus, the RAM is a flexible tool which the University can adapt to maximise the use of its resources in the future, and take best advantage of new opportunities and circumstances. It is up to the University to decide how best to use this tool.

8. Following the first year of the operation of the new RAM (2001–2), there was a general desire for as much stability as possible in the operation of the method so that divisions, departments, and the services could adapt to it. At the same time, a number of points were identified where some adjustment was thought desirable, and these were considered and approved by Council during Hilary Term.

Details of the resource allocation method

9. The basic method by which income is allocated to divisions is as follows:

- (a) Estimate total University income.
- (b) Top-slice funds for certain specific purposes.
- (c) Directly allocate income where appropriate.
- (d) Agree service budgets.
- (e) Allocate the remaining funds by formula to the divisions/ODCE.
- (f) Adjust for differential academic salary costs.
- (g) Levy capital charge, and redistribute funds to divisions.
- (h) Levy infrastructure charge for service budgets.
- (i) Apply transitional arrangements (moderation).

Each stage is dealt with in more detail in the paragraphs below.

Estimate total University income

10. The starting point for resource allocation is to estimate total university income for the forthcoming year. For 2002–3, the estimated total is currently c.£362.6m.

11. This total is made up of income from a variety of sources. The two biggest elements are HEFCE grant (£126.9m in 2002–3), and income from research grants and contracts (estimated at £140.6m for 2002–3). Other significant components include income from university composition fees and from trust funds. It should be noted that whilst some elements in the total are known with a high degree of certainty (especially the HEFCE block grant), other elements are estimates, and the actual level of income is dependent on factors such as the level of student recruitment, and continued success in obtaining research grants and contracts.

Top-slice funds for specific purposes

12. The next step in the new method is to set aside from this sum the estimated total funds which are to be held centrally and are thus not available for distribution to divisions/ODCE, or for the funding of services. There are three principal elements here: the transfer to colleges of the college fee replacement income (£34.8m); the provision for central contingencies, reserves, or special initiatives, amounting in 2002–3 to approximately £3.6m; and a contribution to the services budgets which it has now been agreed should be met through a top-slice, rather than through the infrastructure charge, amounting in 2002–3 to some £11.7m. This last component of the top-slice is a new element in the RAM, introduced for 2002–3 onwards, and aims to provide for service costs which are not directly related to levels of use by members of the University. This leaves remaining income of approximately £312.5m for allocation in 2002–3.

Distribution of remaining income to divisions and Services

13. The method for distributing this sum comprises three distinct components:

- direct allocation** of a substantial proportion of total income to divisions/ODCE, and to services, on the basis that the income in question is clearly generated directly by the relevant unit;
- the **formulaic allocation** of remaining income to divisions/ODCE; and
- a **formulaic infrastructure charge**, to fund those elements of service budgets which are not covered by direct allocations to the services.

Directly allocated income

14. The **directly allocated income** (bullet point 1 above) consists of three principal elements:

(a) *All research grant and contract income*, including 100 per cent of overhead payments on such grants and contracts (totalling an estimated £140.6m for 2002–3). It should be noted that whilst the direct income associated with research grants and contracts is clearly earmarked and not available for other purposes, the overhead payments on such contracts are not earmarked. Although initially allocated directly to divisions/ODCE, these overheads are in part intended to support activities outside the departments or faculties which provide immediate support for research and therefore should be regarded as being available to contribute to the infrastructure charge for service budgets, dealt with below. Allocating all overheads to divisions/departments should act as a clear incentive to them to maximise overhead recovery rates.

(b) *Various other earmarked or directly earned sums*: these include, for example, income from a wide range of trust funds, earnings from trading activities, etc. A significant component of the funds under this heading (i.e. almost £13m) consists of funds which are earmarked for or earned by academic services or other service units.

(c) *Certain unearmarked general funds*, which the University is free to allocate as it wishes, but which are nonetheless being directly allocated to academic units because it is felt that this is the most appropriate way to treat them. The most important elements under this heading consist of income from tuition fees paid by overseas students, or income from tuition fees which is for other reasons being allocated directly to the host department (and in particular ODCE). The rationale here is that in those cases where the University is free to set the level of tuition fees itself, such fees should be directly allocated, so as to encourage divisions and departments to consider the level at which they are set, and to ensure all costs are recovered.

15. It is intended that the direct allocation to divisions, departments, and relevant services is not only simple, clear, and transparent, but will also act as a strong incentive to the relevant units to increase such income wherever possible, and to consider carefully how their costs relate to the income generated.

Allocate the remaining funds by formula

16. The second main step in the new method is the **formulaic allocation** of remaining income to divisions/ODCE. For 2002–3, the total available is approximately £98m. For 2002–3, exceptionally, it was agreed that an additional £8.4m ‘deficit’ funding should be added to the funds available for distribution through the formula, to allow the University to spend more than its projected income for the year. This funding should be viewed as non-recurrent. Thus, the *total* sum allocated to the divisions/ODCE through the formula for this year is £106.4m.

17. The formulaic allocations are based principally on (a) teaching-related criteria and (b) research-related criteria. Allocations of funds on this basis involve a series of linked steps. The first is to decide how to divide available resources between those to be allocated on teaching criteria and those to be allocated on research criteria. For 2002–3 the agreed ratio is 40:60 between teaching and research,

this ratio broadly reflecting the basis on which the funds are received from HEFCE.

18. **Teaching related funds** (approximately £42.6m in 2002–3) are then allocated pro rata to weighted full-time equivalent home/EU student load. The weightings primarily reflect differences in costs between different subject areas, and in the first instance the basis for these are the weightings used by HEFCE in its own block grant allocation formula (these are: 4.5 for clinical subjects; 2.0 for laboratory-based subjects; 1.5 for subjects with a laboratory or fieldwork element; 1.0 for all other subjects). An additional weighting of 1.05 is included for part-time undergraduate students. Oxford has also introduced a further weighting (of 1.25) to reflect the added costs of teaching postgraduate taught (PGT) students. It should also be noted that, because student load relating to postgraduate research students (PGR) in years 1–4 of their study are used both in the teaching component of the formula, and in the research component described below, there is *de facto* an additional weighting attributable to such students.

19. The **research related allocations** are more complex, but are designed to reflect both the basis on which funds are received by the University, and also the quality and volume of research activity in a particular subject area.

20. The principal component of the research-related allocation distributes funds pro rata to a measure of the volume of research activity, weighted to take account of quality (as reflected in the most recent RAE), and a relative cost band weighting (derived from HEFCE's own research-related cost band weightings). The funds distributed in this way for 2002–3 equal £47.9m. The core volume measure comprises numbers of staff returned as research active ('category A' and 'category A*' staff *in post*), in the most recent RAE, who are funded from general income or NHS-specific funds (this provision chiefly excluding those research-active staff funded from research grants and contracts, and some staff funded from endowments) and PGR load (weighted at $\times 0.15$). These numbers are then weighted by a quality factor derived from the most recent RAE ratings for the relevant department or unit, and by an appropriate HEFCE cost weighting, designed to reflect the differential costs of undertaking research in different subjects. The quality-related weightings used in Oxford are: RAE grade 4 = 2.0; RAE grade 5 = 3.0; RAE grade 5* = 4.0. Thus, no credit is given for RAE grades 3a or below (Oxford no longer has any such departments). The cost weightings are: 1.7 for high-cost laboratory and clinical subjects; 1.3 for intermediate cost subjects; 1.0 for all other subjects.¹

21. A significant proportion of the research-related block grant received from HEFCE is generated on the basis of the volume of external research grants and contract income received from UK-based charities; under the RAM, this funding (some £11.1m in 2002–3) is distributed pro rata to a two year moving average of UK-based charity research income, weighted for RAE-derived quality ratings, and HEFCE research cost band weightings.

¹ Following the RAE 2001, HEFCE reduced the cost band weighting for high-cost laboratory subjects from 1.7 to 1.6. It was agreed however, not to change the relevant weightings in the RAM in Oxford, and that the original weighting of 1.7 would be retained. HEFCE's rationale for making this change was not clear, and it was agreed that further analysis would be carried out before deciding whether or not to change to this part of the RAM. This decision was taken largely in the interests of maintaining stability.

22. Two other smaller sums are distributed on the following basis:

(a) some £4m is allocated pro rata to non-charitable UK research grant and contract income, again weighted for RAE-derived quality ratings and HEFCE research cost band weightings; and

(b) a further sum of some £842k in 2002–3, is distributed pro rata to the number of research fellows employed in a given department (using the same definition of what constitutes a research fellow as applied for the RAE 2001). This number is taken from the annual data return made to HEFCE, on the basis of which a part of the block grant for research is distributed. The number of research fellows is not weighted for either relative subject cost or quality. This element of the allocation is in recognition of the fact that, in the previous version of the RAM, there was no direct financial incentive for divisions to employ research fellows, as they attracted no formula allocation, but that they nevertheless contributed a considerable amount of academic prestige to Oxford, and it was thus desirable to encourage their employment.

23. The combination of these four components is designed to achieve an appropriate balance of incentives to generate additional research-related income, to reflect research quality, and to recognise differential costs. As with the teaching-related formula, use of externally derived quality and cost weightings is the subject of ongoing review.

Adjust for differential salary costs

24. The basic formulaic allocations on teaching and research related criteria derived from the above approach are then subject to two further modifications. The first of these is an adjustment designed to reflect the **differential costs** to departments and faculties of certain types of academic appointment—and in particular the relative costs of CUF/faculty lecturers, and university lecturers. This adjustment is intended to be financially neutral, and any plans to move academic posts from one category of appointment to another will need to be approved by PRAC and by Council, after consultation with colleges, as part of the annual planning and budgeting process. For 2002–3, £7.2m was generated by this means, and used to off-set the top-slice.

Levy Capital Charge

25. The second adjustment is made by the application of a **capital charge**. This is intended to provide an incentive to departments to be efficient in their use of space, and to ensure that they do not expand to larger premises without being exposed to the financial consequences which such expansion has for the University as a whole. It is also intended to put a price on the opportunity cost of using capital funds to invest in buildings rather than staff. The charge is initially set at £20 per square metre, and is to be levied on divisions pro rata to the area occupied, although some types of space are excluded from the charge (particularly recently constructed space funded from external donations, grants etc. from non-public sources).

26. The funds generated by the capital charge (about £3.2m for 2002–3) are redistributed to divisions formulaically on the basis of total research active staff numbers, weighted by research quality weightings, and student numbers (with 1.25 weighting for PGT students). This for-

mulaic reallocation of funds shares some of the same features of the main allocation formula, but is deliberately different in certain respects, notably in that it includes *all* students (i.e., Home/EU and Overseas), adopts different factors for the research-related allocation, and excludes any subject weightings (teaching or research).

Levy infrastructure charge for service budgets

27. The approach to setting and providing for service budgets involves several related steps. The first is to agree the level of the budget for each particular service. This is founded on an activity-based analysis, looking carefully at the costs which need to be incurred in order to deliver a particular level of service. Scrutiny of proposed service budgets was undertaken for 2002–3 by a sub-group of PRAC chaired by the Pro-Vice-Chancellor for Planning and Resource Allocation, and discussions were held both with the Pro-Vice-Chancellor for Academic Services and University Collections, and with the heads of the principal services themselves.

28. Once service budgets have been settled, the next step is to take account of the direct allocations of resources made to services, referred to in paragraph 14(b) above. In the case of a number of services, these directly attributable or directly earned allocations comprise a significant proportion of the relevant budget. For example, the combined budgets of the four museums when taken together total approximately £9.3m (excluding funding for specific projects). Of this, £1.6m is met through the RAM top-slice; £0.6m through the RAM infrastructure charge; and £7.1m from non-RAM formula sources.

29. The next step is to calculate the proportion of the agreed service budgets which cannot be met by such direct allocations, and then to provide funds for these through an infrastructure charge levied on *total* divisional income. This formulaic charge is based on a number of factors which are designed, in very broad terms, to repre-

sent proxies of usage of particular services. The principal drivers being used for 2002–3 are student load, staff load, and area occupied or maintained. The total volume of funds being provided for in this way for 2002–3 is approximately £49.8m. This is in addition to the £11.7m included in the top-slice, which is used to meet part of the costs of the service budgets.

30. A summary of all the steps described in paragraphs 10–29 above is provided in the flow-chart (opposite).

Transitional arrangements

31. The transitional adjustment is the means of moving divisions smoothly to their ultimate RAM positions. Funds are taken from ‘gaining’ divisions and redistributed to ‘losing’ divisions in a planned way, allowing all divisions to adjust their baselines over a period of time. It has been agreed by Council that gains and losses arising from the formula should be limited to plus or minus 2 per cent of formulaic income for 2002–3.

32. In essence, the transitional funding distributed to divisions once the RAM has been run is calculated by comparing the expected financial position in the current year with the projected position of the year for which allocations are being made. The additional funding to ‘gaining’ divisions is capped at plus 2 per cent, and the funds released as a result are used to support ‘losing’ divisions.

Further development work

33. Analysis and review of the implementation of the RAM, and its strategic implications for the University, is a continuing process. Detailed scrutiny of its operation will continue, with proposals for refinement and development being brought to PRAC and Council for approval. This will also seek to ensure that further changes take full account of the University’s emerging academic and financial strategies.

UNIVERSITY OF OXFORD RESOURCE ALLOCATION METHOD: SUMMARY DIAGRAM

