Universities Scotland

The Sustainability of Scotland's Finances. Inquiry by the Scottish Parliament's Finance and Public Administration Committee.

September 2023.

Universities Scotland is a membership organisation working for the Principals and Directors of Scotland's 19 higher education institutions. We develop higher education policy and campaign on issues where our members have a shared interest.

Thank you for the opportunity to contribute to your inquiry. We have answered the questions as fully as possible but there are some we have not responded to as we do not feel best placed to offer comment.

1. **How should the Scottish Government's Budget 2024-25 and its future budgets respond to these challenges?**
2. **Does the Scottish Government's 'three pillars' strategic approach to managing the public finances adequately address the scale of financial pressures expected in the Scottish Budget 2024-25 and in the medium-term? Should the Scottish Government follow a different approach instead, and if so, why would that be more effective?**
7. **How should the Scottish Government start to address the forecast funding gap of 1.7% each year up until 2072-73?**
8. **How should the Scottish Government balance its short and long-term financial planning and where can improvements in this area be made?**

We have combined these four questions and offer the following view in response:

A focus on growth.

- The medium-term financial strategy (MTFS) projects a very stark gap between income and spending plans for the next few years. In this context, we welcome inclusive economic growth as one of the three "pillars" in the MTFS and what appears to be a greater prioritisation of economic growth with a purpose under First Minister Yousaf. Scotland's economy must grow to close the spending gap.
- Universities are key assets in the plan for sustainable economic growth, as defined in the National Strategy for Economic Transformation (NSET) and as identified in the new ten-year Innovation Strategy from June 2023. If the Scottish Government wants to boost economic growth, for the collective benefit of Scotland and to generate the resources to support public services and address poverty, they need to invest in universities' contribution. A dynamic wellbeing economy will be driven by high skills, research and innovation, and the attraction or talent and investment to Scotland. Universities are central to that.

- Regarding the NSET, universities are well placed to make a strong contribution to the ambition in the NSET, contributing across all five programmes of action from skills and entrepreneurship to new market opportunities and productive regions. The Innovation Strategy is closely connected to the NSET and is focused on building on Scotland's existing assets to achieve greater economic success. It will take additional public investment to deliver on both strategies, even with the willing support of stakeholders such as universities.
- Central to universities' ability to support economic impact in Scotland is their international reputation and reach around the globe; in all areas such as student recruitment, transnational education and research partnerships. This activity generates £1.94 billion of economic impact annually. This is entirely dependent on higher education's quality and excellence.
- Amongst a suite of competing priorities for funding, Scotland needs to invest in opportunities for growth and in scaling-up proven initiatives that lever in resources to grow Scotland's economy. Investment in university research and development generates an average economic return eight times the original investment.[1]
- There are many opportunities to improve Scotland's leverage potential from UK, European and international sources, if we have the right core investment in university research grants to protect our ability to compete successfully to bringing the resource into Scotland. The announcement of the UK's association to Horizon Europe offers Scotland's researchers the opportunity lead research teams again; this is an opportunity that we are keen to take full advantage of. Access to this funding stream was worth close to €900 million for Scotland over the period of the last multi-year Horizon programme, boosting the nation's innovation economy. In addition to Horizon, Scotland has scope to grow its share of competitively-won UKRI funding from the UK Government. At our peak, Scotland's universities were winning a 15.39% share of the UK total research funds available. By 2020-21 this had fallen to 13.25%. Each percentage point represents around £25 million gained or lost in value to Scotland and London Economics estimates there is a 12.7:1 economic multiplier on resources won from UKRI (exceeding the average multiplier figure for research income).[2] If Scotland can recover its competitive position back to a 15.4% share of UKRI funds, this would deliver an additional economic impact of at least £640 million to Scotland's economy.

A long-term approach

- Both the NSET and the Innovation Strategy look beyond the medium-term to delivery by 2030 and 2033 respectively. The Withers post-school reform proposals for skills and education also take a long-term view of change. The Scottish Government's investment decisions now have to look beyond the short-term however acute the pressures are in FY 2024/25.
- The ambitions within these Government-led and Government-commissioned strategies are both bold and strategic and whilst Scotland does not begin to deliver on those ambitions from a standing start, there needs to be a recognition that investment now and in the short term will take time to deliver that acceleration.

A requirement for creativity and greater collaboration in the current climate.

- Universities will make a budget case to the Scottish Government for 2024/25 that recognises the scale of the fiscal challenge. We intend to present a range of constructive proposals, including a modest level of investment in our core grants as well as some budget-neutral actions that the Scottish Government could choose to take in academic year 2045/25 and

[1] London Economics (2022) *The Economic Impact of Scotland's University Research*
[2] London Economics (2022) *The Economic Impact of Scotland's University Research*

beyond to allow universities to work more flexibly, and deliver more, within existing resources.

- We also recognise the imperative for collaboration across public, third and private sectors. Whilst this is heavily embedded practice in universities already, we have identified a range of opportunities for new or deeper collaborations that would support wider policy agendas as diverse as promoting entrepreneurship to mental health support services. This has been shared with the Scottish Government.
- Our approach, to calibrate our budget ask in recognition of the times, does not change the bigger reality of nearly a decade of real-terms cuts to core university grants which amounts to a major funding challenge that Scotland will need to address.
- Despite their ability to generate income from a range of competitive and private sources, universities are dependent on public funding for the core of service delivery to students and to our staff. Scottish Government investment in universities is the foundation that gives us the capacity to support students' learning and welfare, and to attract investment and jobs to Scotland.

Addressing tough choices and efficiency.

- One of the Scottish Government's three pillars is a relentless focus on the three critical missions. The MTFS is clear that this means: "*tough choices and targeting*". Universities have been on the receiving end of tough choices over the last decade, and again over the last year, in the form of the withdrawal of £20 million of planned investment in financial year 2023/24 (withdrawn in May 2023 after the Budget Bill was passed) which had indicated there would be a 2.53% cash increase to resource funding (teaching budgets).
- Looking back, there has been a steep erosion of university teaching and research grants in real terms (the teaching grant has been cut by 27% and the Research Excellence Grant has been cut by 31% in real terms between 2014/15 and 2022/23) which leaves the university sector with little further scope for "efficiencies".
- The Scottish Government's own data, in response to Parliamentary Question 01165 in 2021, shows that universities are the only part of the education sector (from early years to tertiary) to have seen a continuous real-terms erosion of funding since 2014/15. Every other level of education has seen a real-terms increase over this period. This leaves universities exposed when it comes to high rates of inflation and the prospect of further cuts.[3]
- Scotland's universities have led their own programme of efficiency and continuous improvement over the last ten years. As a sector in receipt of public funding, universities will always be committed to delivering best value for public investment. There is a lot of good practice in our universities and a decade of experience that higher education can share. Mapping our existing delivery against the five areas of public sector reform in the Scottish Government's 2022 resource spending review (RSR) shows a strong record of delivery. Some highlights include:

    - **Public Procurement.** The Advanced Procurement for Universities and Colleges (APUC) is a leader in collaborative procurement and secures over £25.5 million of savings every year, relative to market prices or, £13.1 million relative to prices previously paid. APUC agreements cover over 40% of the procurement spend of Scottish HE and FE.
    - **Digitalisation.** Jisc supports Scottish HE's efficiency with digital, data and technology services The savings and costs avoided by Scotland's higher education institutions collaboration through Jisc is estimated to be approximately £13.8 million per annum, based on 20-21 figures.

[3] Data from Scottish Parliament Question S6W 01165 (2021)

- **Maximising revenue.** Already, only 35.6% of universities' total revenue comes from public funding via the Scottish Government. The balance of public-private income Scotland's universities rely on has continuously shifted to far greater reliance on private revenue as public investment in university teaching and research has significantly declined in real terms since 2014/15. We are reaching a tipping point of geopolitical and market risk from forced reliance international tuition fee income, as cautioned by the Scottish Funding Council in 2022. Scotland's structural reliance on international fees has reached such an extent that the Funding Council forecast that this source of revenue will overtake Scottish Government funding as a percentage of the sector's total income in 2023/24, reaching 27% of the sector's average income, compared to 25% for SFC grants.[4]

Yet, universities' existing success in the efficiency agenda means only narrow margins of efficiency remain. It will be important that the Scottish Government's renewed reform agenda recognises universities' starting position and the scale of efficiency and reform already delivered. It is also important that we make the point, on behalf of our member universities, that their ability to maximising other sources of revenue is entirely based on excellence. This is essential to attract students, staff and competitively-won investment. Without sustainable and competitive levels of core public funding, our ability to maximise revenue streams will decrease, not increase.

3. Given the pressures on the capital budget, how should the Scottish Government prioritise its capital spend in the Scottish Budget 2024-25 and over the medium-term?

4. What are the implications of a declining capital budget, including on the productive capacity of the Scottish economy?

We have combined these two questions and offer the following view in response:

A declining capital budget has two principal effects on universities' contribution to a productive capacity:

I. **Research and innovation capital.** Since 2020 (for FY 2020/21) the Scottish Government and the Scottish Funding Council have made a change in accounting practice to classify funding for university research and innovation as capital funding as opposed to resource funding (as it had previously been). This means that cuts in capital funding reduce universities' capacity for research and innovation and reduce the ability to generate economic growth.

II. **Capital maintenance.** University estates have a major maintenance backlog and specific problems with building materials used in the late 20th century. Deterioration of the university estate risks our ability to attract talent and investment. Conversely, refurbishment of the state is a major opportunity for Scottish businesses – and a major opportunity to create more energy-efficient facilities.

To expand briefly on these points:

Research and innovation capital

[4] Scottish Funding Council data using HESA. The remaining 48% of income is derived from rest of UK fees, from UK and privately-won research grants and contracts (including UKRI), from conferences/events and other income generating activities and endowments.

SFC's Research Excellence Grant pays for the core research staff and facilities that enable universities to compete for research projects funded by business, charities, or UK and international funding bodies. As noted above, this has been cut by one-third in real terms since 2014/15.

This corresponds with a fall in the share of total UK Research Council resources won by universities in Scotland, including in disciplines very closely aligned to the sectors at the heart of the Innovation Strategy. In 2013-14 universities in Scotland secured 15.39% of the UK total but by 2020-21 this had fallen to 13.25%. Each percentage point fall represents around £25m. Such resources support internationally competitive researchers in Scotland that might otherwise be elsewhere in the UK or beyond. Those teams have a significant direct economic impact and are the foundation for innovation, company creation, Foreign Direct Investment etc. Such resources have a 8:1 economic impact. Returning Scotland's share to 2013/14 level would therefore now deliver around an additional £50m in funding with an economic impact of £400m.

On a specific point, we ask the Scottish Government to find the resources to match the UK Government's Department of Science, Innovation and Trade investment in HE Research Capital (HERC) otherwise Scotland's universities will lose out on the UK Government resource too. This resource must be match-funded. In 2023/24 it was worth a total of £34.9 million.[5]

Capital maintenance

The expansion of the university sector from the 1960s onward meant that buildings were constructed using the techniques available at the time, often with a finite design-life which has now been exceeded. Some of these included building technologies which have since been proven to have problems.

Of current high-profile interest, the safety concerns posed by the existence of unstable reinforced autoclaved aerated concrete (RAAC) in many public buildings, including some universities, make this an urgent priority for the Scottish Government.

We don't yet have an accurate picture of the extent of or cost of RAAC in higher education as not all higher education institutions have concluded their audit. As of early September, we know that 9 universities have RAAC. The full cost is not known but it a reasonable to suggest it will run to the £multi-millions. The Scottish Funding Council is collating data on the prevalence of RAAC in FE and HE. We will cooperate fully with the SFC's work to get reliable figures into the Scottish Government.

We have suggested to the Scottish Government that there could be benefit in forming local/regional collaborative taskforces of university, public and private sectors to respond to the challenges caused by RAAC. There are opportunities to share experience, access to specialist structural engineering advice and, where possible and appropriate, potential collaborative solutions to estates management during any necessary remedial works to avoid disruption to learners or other service users.

It's important to be clear that prior to the identification of safety concerns with RAAC, which will require significant resource to resolve, there was already a major issue of a backlog of investment in the university estate. Audit Scotland estimated the value of this backlog at £937 million based

[5] SFC. Final Funding Allocations. Para 50.

on data from 2018 (in 2018 prices). Of this, £139 million (in 2018 prices) was identified as "urgent".[6]

Public investment in HE capital in the period 2018/19 to 2023/24 has not come close to addressing that short-fall and the pressure facing universities regarding the estate has only grown. Last year, Universities Scotland made a modest bid to Scottish Government for a £60 million investment in a capital transformation fund that institutions could use flexibly to help attain net zero and to invest in high-quality digital innovation.[7] Instead, universities received a total of £17.46 million in capital funding from the Scottish Government.[8]

We hope there is at least some budgeted scope for expansion in SFC capital support for universities. Scottish Government's spring 2022 Capital Spending Review set out a Scottish Funding Council HE Capital budget of £359.4m for 2024-25[9]. This is £18.7m higher than the SFC's actual HE Capital budget in the 2023-24 budget.

6. The Scottish Government plans to address the budgetary implications of the expected long-term fall in population through growing the economy and tax base, public service reform, and an upcoming 'Addressing Depopulation Action Plan'. Are these the right priorities to address the implications of this fall in the population and, if not, how could the Scottish Government be more effective in this area?

We support the prioritisation given to growing the economy and see it as necessity given the MTFS projections of a gap in the Scottish Government's over the next few years and the direct connection between economic growth, the increased tax revenues generated by economic growth, and the spending power of the Scottish Government. Universities welcome both the National Strategy for Economic Transformation (NSET) from 2022 and the greater emphasis given to economic growth for a purpose in the 2023 *Fresh Start* policy prospectus. Universities are well placed to make a strong contribution to the ambition in the NSET, contributing across all five programmes of action.

We have not yet been directly involved in the Scottish Government's development of a plan to address depopulation and we note the inference in the *Programme for Government* that this could be specific to certain regions or locations within Scotland. However, we have had initial discussions with officials on the potential Talent Attraction and Migration Service, with the aim of attracting greater levels of talent to Scotland. Universities have a major role to play here. If they were supported by the UK Government in a more favourable immigration policy, or if greater devolution of immigration policy on a national/regional or sectoral basis were possible, universities would be able to maximise their role in inward migration of high-skill, working-age population in support of our demographics and the tax base. As the UK Government considers the evolution of its immigration policy in a post-Brexit context, we urge it to take a more nuanced approach that takes account of the different needs of parts of the UK.

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[6] Audit Scotland (2019) *University Finances* pg. 19
[7] Universities Scotland (2022) *Budget Case to the Scottish Government*
[8] Scottish Funding Council (2023) Final Funding Allocations Table 8. £17.46 million includes £3.8 million SFC "capital maintenance" and £17.46 million in research capital. HEIs receive an additional £17.46 million in "SIT research capital" from the SG if the SG can match-fund that amount.
[9] Scottish Government (2022) *Outcome of the Capital Spending Review* pg. 16

10. In follow-up to the Committee's inquiry on effective decision making, how can transparency be improved around how the Scottish Government takes budgetary decisions?

Transparency in Scottish and UK Government relations

- We agree with one of the Committee's summary findings that the opacity of the essential budgetary interactions between the UK Government and the Scottish Government pose a challenge to all those with an interest in understanding them. This poses direct and indirect challenges for the higher education sector as policy and funding relating to research, innovation and regeneration funding can be a mix of both reserved and devolved responsibility.
- There are many budgetary decisions taken by the UK Government, benefiting the English research and development sector, that create Barnett consequentials for the Scottish Government's block grant. We understand that the Scottish Government has full discretion about how to allocate those funds (there is no ring-fencing or correlation of investment) but it is impossible to get clarity from either Government on what sum is generated as the Barnett consequential to inform discussions and negotiations with the Scottish Government. A recent example, albeit with a positive outcome for universities, was an investment of £24.6 million which the Scottish Government made in university research in FY 2022/23, announcing it in mid-December of 2022. This funding was created as a direct consequence of a UK Government BEIS investment in research, to avoid adverse consequences on UK researchers following continued delays in finalising association to Horizon Europe. The total UK investment of £484 million was made with the direct intention of also supporting research in the devolved administrations. There was no certainty, for a few weeks of how much the consequential was for the Scottish block grant or that the Scottish Government would decide to allocate this resource to Scotland's universities (and in a context where the resource must be spent within that financial year, with only four months remaining).[10]

Post-budget scrutiny

- We welcome the Scottish Parliament's scrutiny of Scottish Government budgets in Chamber and in Committee and as pre-budget and post-budget exercises. However, we note that it is increasingly challenging to follow the flow of budget lines for higher education investment as published in budget documents given the lack of granularity and the immense complexity of funding formula and allocations received via the SFC (primarily) but also SAAS. There is also an increasing opacity to the Scottish Government's published figures for higher education spend.
- The 2023/24 budget was passed 21 February 2023 with a cash increase in the HE resource budget of £20 million relative to 2022/23.[11] Yet on 2 May, the SG informed universities, via the SFC, that the cash increase of £20 million was: "*not available for distribution and has been identified as a necessary saving*".[12] Universities were dismayed at this handling of the situation and at the decision taken 5 months after the initial budget announcement to Parliament.
- The year before (FY 2022/23) the loss of circa £7 million of funding from universities to cover the cost of graduate apprenticeships was not at all obvious from published budget statements

[10] Universities Scotland (2022) News item.

[11] Universities Scotland (2022). News item. The budget announcement for universities was a 2.53% cash increase to resource funding. We welcomed this in straightened financial times. This can be found in Table 7.08 in the SG budget document.

[12] Universities Scotland (2023) News item.

because in 2021/22 the cost of graduate apprenticeships was not covered by baseline resource funding but covered instead by COVID consequentials from the UK Government. The complete withdrawal of this funding for 2022/23 and lack of replacement funding from within the Scottish Government block budget meant that universities had no choice but to "absorb" the £7 million cut to honour the multi-year financial commitment of several hundred graduate apprenticeships as made to the apprentices themselves and to the business partners in this model.[13]

ENDS

[13] Universities Scotland (2021) News item.