Group of Eight

AUSTRALIA'S LEADING UNIVERSITIES

The University of Adelaide
The Australian National University
The University of Melbourne
Monash University
The University of New South Wales
The University of Queensland
The University of Sydney
The University of Western Australia

27 August 2007

Mr John Carter
Secretary
Standing Committee on Employment,
Workplace Relations and Education
PO BOX 6100
Parliament House
Canberra ACT 2600

Dear Mr Carter

Inquiry into the *Higher Education Endowment Fund Bill 2007 (Cth)*

When the *Higher Education Endowment Fund Bill 2007 (Cth)* (HEEF Bill) was introduced into the House of Representatives on 16 August 2007 the Go8 welcomed it as an historic step for Australia and its universities. Such a commitment represents a strong recognition of the importance of Australia's universities to the nation's future.

The Treasurer's 21 August 2007 announcement that the Government will commit a further $1 billion from the 2006-07 budget surplus was a further fillip for the sector. This additional investment represents a substantial boost to the Fund's seed capital—which will in turn, with prudent investment, hopefully see it produce greater levels of income sooner than was expected.

However, while the creation of the Fund and the prospect of further injections of capital into the future are welcome, the Go8 raises the following issues and concerns for consideration by the Committee as it prepares its report on the Bill.

The Group of Eight Limited

ABN 98 089 687 990

PO Box 4008 Manuka

ACT 2603 Australia

Telephone 02 6239 5488

Fax 02 6239 5808

http://www.go8.edu.au

1. The Fund must be viewed in context

While $6 billion is a large amount of money it needs to be viewed in the context of recent funding trends for Australia's public universities, the recurrent expenses and infrastructure challenges they now face, and international developments in public investment in higher education systems.

1.1 1996 budget cuts

In the 1996 Federal budget, university operating grants were cut by a cumulative six per cent in the forward estimates for the period 1997 to 2000 inclusive.[1] This amounted to a cut of some $850 million over these four years, with flow through effects for every subsequent year.

[1] Bell R. & Jackson K. (1998) *Higher Education Funding Amendment Bill 1998 (Cth) Bills Digest*, Parliamentary Library, p.4.

1.2 Compounding indexation shortfall

Also in 1995, the way that university block grants were indexed was reformed to remove any link with real increases in relevant wages. The arrangements that have applied since then have seen the notional salary component of university operating grants (75 per cent) indexed only by the Safety Net Adjustment applied to the lowest paid workers in Australia and the non-salary component (25 per cent) by the Treasury Measure of Underlying Inflation (subsequently the Consumer Price Index).

In 2004 the Go8 estimated that if Average Weekly Earnings were substituted for the 75 per cent Safety Net Adjustment component of the indexation formulae since 1997, this would have resulted in an extra $845 million in operating grants across the sector in 2003 alone.[2] The annual shortfall directly attributable to the indexation arrangements would now be approaching $1 billion dollars a year.

1.3 Ever increasing expectations for matching funds

In a recent report the Productivity Commission found that university block grants are under considerable pressure—not least because of the ever-increasing demands of competitive research schemes for matching funding from institutions.[3] In its submission to that inquiry the Go8 pointed out that this cost supplementation was estimated at $450 million per annum for the whole sector in 2003-04. It is now likely to be closer to $500 million annually with most of this burden being shouldered by Go8 institutions due to their relative success under competitive schemes.[4]

The Commission concluded that expenditure decision are generally better made directly by institutions than by the Governments because of the opportunity costs for institutions and decision makers alike, compliance costs and the reduction in the strategic capacity of institutions due to declines in the overall proportion of block grant funding in the system.[5]

1.4 Implications of funding pressures

A decade of funding pressure has manifested itself in the following ways:

1. large increases in student to staff ratios, with implications for quality of teaching and learning;[6]
2. reductions in academic salaries relative to average wages, with implications for the sector's ability to attract top talent;[7]
3. the deferment of essential expenditure on the maintenance of buildings and facilities, with long term consequences for the quality of essential infrastructure;[8]

---

[2] Gallagher M. & Mitton J (2003) *A Comparison of Different Index Values of the Salary Component for Higher Education Funding*, Unpublished, Australian National University.
[3] Productivity Commission (2007) *Public Support for Science and Innovation,* pp.517-518.
[4]Group of Eight (2006), *Submission to the Productivity Commission's Study of Public Support for Science and Innovation*, p.10.
[5]. Productivity Commission, *op.cit*., pp.XL raised concerns about the erosion of university block grants as a proportion of overall university funding. As a result, its key finding 12.1 read: '*Reductions in block funding levels would further limit the flexibility and discretion of higher education institutions to make meaningful strategic choices. Consequently, Australian Government block funding should not be reduced, either in absolute terms, or in relation to Australian Government competitive funding'*.
[6] Analysis of DEST Student and Staff data from 1996 to 2006 shows that in 1996 the student to staff ratio across the sector was 15:1 (15 Full Time Equivalent Students for every FTE Teaching Only or Teaching and Research Staff Member). By 2003 the ratio had grown to ratio 21:1. Since 2003, the average Go8 student to staff ratio has declined from 19.5:1 to 18.15:1 in 2006. This improvement can be largely attributed to the funding increases announced in the 2003 budget.
[7] Chapman B. (2001) *The Higher Education Funding Debate: Returns to Educational Investments, Current Pressures and Some Suggestion for Reform*, documents the consistent decline in academic salaries as a proportion of average wages from 1984 to 2001.
[8] According to DEST (2006) *Response to the Productivity Commission's Draft Research Report on Science and Innovation*, in 2005 Australia's universities reported 'deferred maintenance' expenditure (ie the level of maintenance

4. the pursuit of alternative sources of income, for example from full-fee domestic and international students;[9] and
5. the pursuit of various practices designed to increase productivity and reduce costs.[10]

1.5 International trends in public support for higher education systems

With Gross Expenditure on R&D at 1.8 per cent of GDP, Australia ranks fifteenth among OECD member countries for which the average is 2.3 per cent. If Australia was investing in R&D at the OECD average rate it would be spending $5 billion more each year on research than currently. In 2006 China became the world's second highest investor in R&D, spending some $170 billion, compared with Japan's $160 billion. The US leads with $410 billion while R&D spending by the European Unions totals $290 billion.
So, while the commitment of six billion dollars is significant and welcome, the $300 to $400 million it is expected to produce annually in the initial years, must be viewed in the context of the recurrent and backlog expenses Australia's universities face due to past funding cuts and punitive indexation arrangements, and alongside the huge investments in research and higher education systems being made by competitor countries.

2. Potential difficulties with the HEEF

As Vice-Chancellor of the Australian National University, Professor Ian Chubb has recently noted, there are numerous potential difficulties with the HEEF. These include:

- that in the absence of a commitment to the *Backing Australia's Ability* Science and Innovation package beyond 2011, the potential for the Fund to be used to substitute for several existing block funding schemes;
- that annual formula-based schemes could be replaced, in full or in part, with another burdensome periodic submission-based scheme, with new conditions attaching to payments, including matching funds and other compliance requirements; and
- that funding will be spread across all universities for all manner of capital works, if not skewed to regional institutions, with little thought given to strategic national priorities.[11]

Further, the Bill vests control over the selection and allocations of grants from the Fund to the Minister of the day. With such large amounts of public funding involved, the policy priority should be the achievement of clear, transparent and non-political mechanisms for allocating grants.

However, as introduced the Minister will determine who sits on the Fund's Advisory Board (ss.40(2 &3)), how the Board is to carry out its function and the processes by which it will operate (ss.40(4)), will decide which grants are funded (s.45) and the terms of any funding (ss.50(3)). There are risks under this model that funding allocations will be based on political factors rather than on the merits of individual proposals, or through any strategic consideration of the sector's infrastructure needs.

---

expenditure that should have been undertaken but was not due to insufficient funds) at $1.5 billion. In 2006 total deferred maintenance liabilities across Go8 universities alone have been estimated at $1.53 billion.

[9] For example, in 2005 Go8 universities earned revenues of $1.12 billion from international full fee paying students ($830 million) and from domestic full fee paying students ($292 million).

[10] The available evidence suggests that there have been substantial productivity gains in the performance of Australia's university sector over the last decade. Teaching productivity has increased, as indicated by higher student-staff ratios, higher rates of student completion and increased levels of student satisfaction. Research productivity and impact has also risen sharply. The volume of research output has increased significantly (from 15,191 weighted publications in 1995 to 43,853 in 2005). On this measure, total research output per academic staff FTE per year has risen from 0.5 to 1.3 and over the decade.

[11] Chubb I. (6 August 2006) *Putting Research on the Agenda*, Speech to the Education, Science and the Future of Australia, Public Policy Forum, Centre for the Study of Higher Education, The University of Melbourne, p.2.

In the interests of transparency and good governance, consideration should be given to making the following amendments:

- requiring that the Advisory Board's funding recommendations to the Minister to be made public; and
- requiring the Minister to make public his or her reasons for any departure from the Advisory Board's funding recommendations.

As a further measure to minimise the politicisation of the scheme, the announcement of grants should be limited to two fixed periods annually. Combined with the publication of clear guidelines setting out the purpose of the scheme and the processes that will be applied, such measures would go some way to ensuring transparency.

3. Ensuring the efficient allocation of funds

There are a variety of options available that could ensure the efficient and more strategic allocation of funds than appears to have been contemplated by the Government to date. For example, rather than distribute funds based purely on an application-based process, a significant proportion, say 50 per cent of funding available each year could be allocated as block grants to institutions, based on an independent assessment the total Asset Replacement Value (ARV) of the building and infrastructure stock of each institution. The remaining funds could then be allocated through a competitive application process.

Sound asset management would have institutions dedicating around four per cent of their ARV to maintenance activities (preventative and corrective maintenance, backlog maintenance and refurbishment) annually.[12] Currently, however, due to the budgetary pressures outlined above few Australian universities are able to dedicate such amounts for maintenance activities. In 2006, Go8 universities, with a combined estimated total ARV of $13 billion, dedicated approximately $291 million or 2.25 per cent of their total ARV on maintenance activities.[13] The total ARV of buildings and associated infrastructure across all Australian universities in 2006 is estimated at $26.5 billion.[14]

Therefore, in the early years of the Fund it will not possible to provide each institution with four per cent of its ARV annually as this alone would amount to $1 billion each year – well in excess of the 300 to 400 million dollars the Fund is expected to produce. However, pro rated allocations based on 1 per cent of institutions' ARVs ($265 million) annually would be feasible and would over time make a considerable difference. On current projections, such an approach would leave approximately $100 million available annually for allocation through a competitive process. Such an approach would have the benefits of:

- **certainty** - providing baseline funding certainty for institutions to allow them to rectify and maintain their existing capital. Over time this would free up additional funds for possible investment in new infrastructure;
- **transparency** - ensuring the allocations are targeted to institutions based on independently assessed measures of the replacement value of their capital stock and associated infrastructures;
- **efficiency** - in terms reducing workload for institutions in having to prepare complex applications and reducing the workload of the Advisory Board in terms of having to consider applications;[15] and

---

[12]Based on a 25 year asset refit/replacement timeframe.
[13] Tertiary Education Facilities Management Association (2007) *2006 Benchmark Report*, p.7.
[14] TEFMA, *op.cit.*, p.7
[15] The Productivity Commission has recently highlighted that expenditure decision are better made directly by institutions than by the Government because of the opportunity costs for institutions and decision makers, compliance costs and the reduction of the overall proportion of block grant funding in the system.

- **proportionality** - it would represent a balanced approach to the mix of attention that should be given by the fund to investment in existing as opposed to new infrastructure. While new investment is necessary, the more pressing challenge is for institutions to make-good their existing stocks.

4. Maintaining other infrastructure schemes

There are a variety of existing Commonwealth Schemes that directly or indirectly support investment in university capital and research infrastructure. These include the Institutional Grant Scheme (IGS) and Research Infrastructure Block Grant Scheme (RIBG) mentioned, but also include the National Collaborative Infrastructure Strategy (NCRIS) and many small schemes such as the Capital Development Pool (DEST), Linkage Infrastructure (ARC) and Enabling and Equipment Grants (NHMRC).

For the reasons outlined in this submission it is critical that the HEEF never be seen as a substitute for these important schemes which each serve specific purposes. The Go8 is therefore heartened by the Minister's recognition when introducing the Bill that funding for the HEEF is in addition to these existing infrastructure programs and will serve a very different purpose to these. In the Go8's view the purpose of the HEEF should be to provide institutions with an income stream to address the serious backlog maintenance challenges outlined in this submission, and for new capital and/or research infrastructure projects judged to be in the national interest through an open and transparent competitive process.

Summary

In summary, we propose that the following criteria should be applied to the operation of the HEEF:

1. HEEF funding is additional to and not a substitute for existing programs that provide funds for capital works and research infrastructure in universities;
2. HEEF funding is targeted to address critical backlog maintenance work at the discretion of institutions via allocations proportional to the total replacement value of the sector's capital stock – independently assessed;
3. additional HEEF funds should be allocated on a competitive basis according to clear and transparent guidelines, with priority given to projects of national significance;
4. there should be no requirement for matching funding from institutions; and
5. the compliance burden should be kept to a minimum.

Yours

Michael Gallagher
Executive Director