JCPSG

Joint Costing and Pricing Steering Group

Pricing Toolkit for the Higher Education Sector

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Foreword

The Joint Costing and Pricing Group has, throughout its work for the Higher Education sector, emphasized the importance of the integration of financial and academic considerations in both strategy and decision making. Previous work has focused on the role of Costing as a method and as a discipline, and this has spilled over into work to meet the requirements of the Transparency Review set by Government. Costing is however only one dimension and the Toolkit presented here extends the range to issues of Pricing.

Higher education institutions in the UK have gone through a substantial period of organizational change and it is likely that this process will continue for years to come. As a consequence of such changes, universities and colleges have had to diversify their range of activities and seek new activities and markets both in the UK and overseas.

To ensure that each institution meets its strategic objectives and maintains its financial viability, it is vitally important that the financial aspects of its various activities are addressed adequately. Costing methods are designed to help institutions obtain robust data on the costs of their activities. This Pricing Toolkit seeks to assist them in setting prices for the provision of services on a proper basis, where they have discretion to do so, since pricing decisions can have a major impact on the achievement of strategic objectives and on financial performance.

The toolkit emphasizes that pricing decisions can often be complex in nature and a range of different factors, not just costs, need to be taken into account. Thus to make effective pricing decisions an institution may have to obtain additional information about markets, customers and competitors and to thoroughly analyze that data. Throughout the toolkit there are many case studies that illustrate the various aspects of pricing in a higher education setting to assist with this process.

We hope that the material in this toolkit will be of use to all academic and support service managers, not just contract and finance officers, and will be disseminated widely throughout the institution.

We are indebted to the many people in universities and colleges who assisted with the development of the material, and in particular to Lisa Blackshaw (National Co-ordinator for Costing and Pricing), John Clements (Oxford University) and David Halton (The University of the West of England, Bristol) who took the work forward on behalf of JCPSG.

Professor David R. Westbury
Chair, Joint Costing and Pricing Steering Group.

Contents

Module 1 Introduction

Aims

By the end of this module you should understand:

- what is meant by pricing;
- the current culture of pricing in higher education (HE).

Structure of this module

This module aims to give the reader a brief and general introduction to the subject of pricing and its relevance to higher education institutions (HEIs) and their markets.

1.1 Pricing in markets

Understanding the factors that influence how a market behaves is critical to reaching informed pricing decisions. This handbook is designed to help the reader understand those factors and make a judgement about how far they should be used to contribute to effective pricing decisions. Economic theory explains the relationship between pricing and the marketplace. This module does not attempt to explain these relationships in technical theory terms; however, it applies basic economic theory to relevant HE markets to demonstrate the impact on price.

There are different types of market depending on the nature of the provider, the buyer and the nature of the good or service. For example, when an HEI lowers the price that it charges for a good or service it may expect the demand to increase. Likewise if the price was increased it may expect the demand to decrease. However, the response to the change in price will vary depending on how sensitive the market is to price changes. When an HEI takes a pricing decision it should understand the price sensitivity of the market that it is operating in to anticipate the buyer’s reaction.

When making a pricing decision HEIs will need to consider other factors that may contribute to the price sensitivity of the market. Some of these factors are internal and within the HEI’s sphere of control. Some factors are external and largely outside the HEI’s sphere of control. Examples of these factors are listed in the table overleaf.

Internal and external factors affecting price

Internal factors	External factors
Costs – clearly these will vary from HEI to HEI as will the approach to their calculation. Some of these will be within the control of an HEI, such as staff, and others may be imposed, such as the cost of specialist equipment.	*Competitors* – clearly the competitive intensity will affect how the market behaves. In some areas (for example, very specialist research remits) an HEI may well be the only provider. However, in other areas an HEI may find itself in direct competition with others who appear to provide a similar or the same service or goods.
	Another example could be where a competitor introduces a new product or service into the market which effectively leaves another HEI's product/service obsolete. In this scenario the prices of those other product/services may well fall quickly.
Corporate strategy – HEIs may well differ in their approach to cost recovery and the generation of profit or surplus. For example, some HEIs may be quite aggressive in their desire to capture market share and may well be prepared for a period of time to introduce low prices in the market which do not even cover costs.	*Political and legal* – both government policy and law will influence pricing decisions. For example, health and safety legislation will mean increased costs that may be passed on to the consumer. A national policy initiative to widen access to education will influence market behaviour and the prices that can be charged.
	Customers – understanding customer demand can be a difficult task and there are many influencing factors. However, generally it is true to say that where there is excess demand (i.e. demand exceeds supply) then prices are likely to rise and vice-versa.

1.2 Examples of market factors specific to the HE sector

Examples of these, discussed below, are:

- government funded student places;
- overseas student fees;
- MBA fees;
- admission points;
- research contracts.

1.2.1 Government funded student places

The Government funds universities and colleges for the provision of higher education places. However, both the full-time undergraduate tuition fee and the planned number of student places are set by Government. These are examples of government involvement in the market. In this context the HEI has constraints over some of its income levels, regardless of shifts in demand, supply or cost.

If the funding provided by Government does not meet the costs of teaching students then HEIs will need to respond, for example, by:

- cross-subsidy against other activities in the HEI;
- reducing costs; or
- changing the nature of the service delivered.

1.2.2 Overseas student fees

HEIs set fees in the overseas market. It is a market where there are a large number of buyers and sellers; there is little perceived variance in the service that will be provided between groupings of HEIs, and increasingly the overseas student has information about the options available. As this is a price sensitive market the HEIs charge very similar prices that are based on what the market will stand and on what the competition is charging. Without distinct product differentiation (the buyer recognizing clear levels of benefit and different benefits between the HEIs on offer) it may well follow that an increase in price will lead to a direct decrease in demand.

1.2.3 MBA fees

Some MBA courses may be viewed in the market as elite. In this market the fees can be set above those of other providers of MBA courses. This may not be as a consequence of higher costs, although costs may be a factor. In this 'elite' market a price increase would not be likely to result in clients choosing other providers of MBA courses. There will, however, be a ceiling on the price that a buyer will be willing to pay, and the HEI will need to be aware of that price.

1.2.4 Admission points

Price can sometimes refer to factors other than money. In this example the price is the level of admission points needed to qualify for admission to an undergraduate course, as published in the HEI's prospectus. In this market the student will compare HEIs and draw assumptions from the level of points required. Experience shows that students relate the level of points to the quality of the course. Subsequently an increase in price (from 16 to 20 points) could result in an increase in demand, and vice-versa.

1.2.5 Research contracts

When HEIs are competing for research contracts they may not know the price that their competitors will propose. In this market the HEI must attempt a best guess of what the competitors will charge. Additionally, and importantly, the HEI must ensure that its offer accounts for any difference in price by differentiating its research from that of the competitor, otherwise the market will decide on the lowest price.

1.3 Setting the right price

HEIs are not organisations that measure success by annual profit, although they do need to achieve certain financial objectives. However, in order to fulfil their diverse missions relating to the provision of and excellence in learning, teaching and research they recognise the imperative to be financially stable, and as such to operate increasingly like a business.

Successful pricing activity means that the HEI has maximised income from sales of a given good or service with a view to securing further sales. There are adverse consequences of setting the incorrect price:

- if a project is under-priced, then goods or services will be sold for less income than could have been achieved, or at worst, a loss;
- if the goods or services are over-priced, customers may be disinclined to enter into a buying contract with the HEI. Alternatively, they may have expectations, based on assumptions about price relative to quality and quantity, that exceed the reality, therefore dissuading the buyer from further purchases.

Over- or under-pricing can occur for a number of reasons and there are occasions when it is a deliberate part of an overall pricing strategy. However, when it is not done deliberately it may have serious implications for the success of the organisation.

1.3.1 Pricing implications

An accumulation of lost opportunities through inappropriate pricing could affect the financial health of the department and will eventually become an issue for the HEI. Pressure grows to make up the income from other sources, or to cut costs. Loss of income in one business area may lead to over-pricing in other areas to make up the difference, with undesired consequences.

Income can also be affected because the time and costs required to complete a project to the necessary standard have been underestimated, or because proposals have been unsuccessful, due perhaps to over-pricing. The impact of not receiving income as projected may be such that other projects are prevented from accessing the funding they need for completion.

1.3.2 Specific UK HE pricing issues

There are certain factors specific to higher education that need to be recognised and taken account of during the pricing process.

- Funding – as already noted, HEIs are not in control of prices for certain services. Specifically full-time undergraduate tuition fees are set by Government, and HEIs cannot charge the student over and above that amount.
- Under-pricing – HEIs do have control over the price of many other activities, for example: overseas student fees; research consultancy; professional courses or catering; and conference facilities. Historically the HE sector has under-priced its services, particularly in relation to research activities. This has been due in part to the intellectual culture of knowledge sharing as well as ineffective costing methods.
- The HE sector now finds itself in a situation where many HEIs are under-pricing many of their activities. This has two consequences: first an HEI cannot ignore the under-pricing of its competitors when setting a price, even if the price has been set against accurate costing figures and demand studies; and second the buyers in the market have come to accept the sector’s low price and may now perceive an increase in price as ‘unfair’, and be unwilling to pay the true price of the service. The solution to these problems needs to come from the sector, and in the meantime the individual department, unit or HEI needs to take this culture into account.

Module 2 Strategic pricing and marketing strategy

Aims

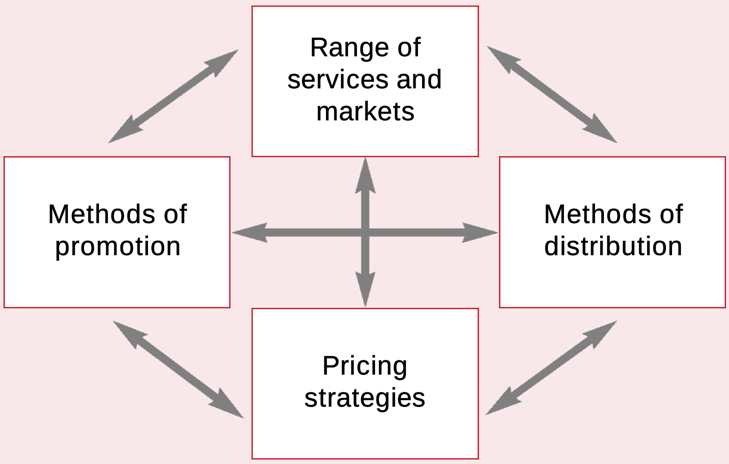
By the end of this module you should be able to understand and apply:

- the component parts of a marketing strategy;
- the strategic role of pricing in a corporate strategy.

Structure of this module

Having developed strategic objectives as part of its corporate planning process and undertaken market research where appropriate, HEIs need to prepare a marketing strategy which will both complement and supplement the other aspects of its corporate strategy. A strategic view of its pricing policy is a key component of such a marketing strategy and will be addressed in this module.

The module outlines the four key components of a marketing strategy, which is often referred to as the marketing mix. It then considers the relationship between pricing policy and the other elements of the mix. These components are illustrated below:



The marketing mix will vary between the type of service being considered and the identified market segment. Each of these aspects of the marketing mix will be considered in turn.

2.1 Range of services and markets

In developing a marketing strategy, HEIs need to give considerable thought to the wide range of services that they offer and the relationships with the markets. There is bound to be a combination of existing services which will have been around for some time and services which are newly developed. Similarly there will be a combination of existing markets in which the HEI is involved and new markets which it wishes to penetrate. This is illustrated in the following diagram.

Products and existing and new markets

		MARKETS	
		EXISTING	NEW
PRODUCTS	NEW	A	B
	EXISTING	C	D

In terms of marketing the HEI can be faced with four possible options and these are discussed below:

A. Marketing existing products in existing markets – this involves either continuing to market products to the existing customer base or to new customers within the same market segment. Thus it is a strategy of market maintenance or market penetration. In the case of an HEI department this implies the ongoing marketing task undertaken, each year, of marketing the existing range of courses to the main market which may be the 18 year old school leaver.

B. Marketing existing products in new markets – this is often referred to as a strategy of market development. An HEI department might decide to market its existing range of educational activities in another country or to a new client base such as the unemployed.

C. Marketing new products in existing markets – this is a strategy of product development and involves ‘selling-on’ to existing customers. Thus an HEI department which already provides a wide range of training courses to local employers might try to diversify and offer market research and consultancy activities to that same range of employers.

D. Marketing new products in new markets – this is the most risky and probably most time consuming approach but also the one most likely to give the greatest return. Thus, an HEI department which traditionally has focused its activities around full-time degree courses might decide to try and market short-term training courses to local employers. This approach implies both a new product and a new market.

The above options are not mutually exclusive and HEIs might pursue several approaches simultaneously. The HEI will also need to continually consider its competition in this matrix, for example, a market may be expanding and therefore competition may not be an important issue as demand is increasing with supply. However, in a static or shrinking market competition becomes a crucial factor to consider as the HEI attempts to increase its market share at the expense of others. It must also be recognised that each option will require a differing degree of commitment to new product development and a differing approach to the other elements of the marketing mix.

2.2 Methods of service distribution

Marketing has sometimes been defined as the process of getting the right goods and services to the right place at the right time. This raises the key issues of:

- where goods and services should be made available to the customer;
- the logistical process of distributing the goods and services to the place where they can be acquired by the customer.

Consider, for example, the marketing of personal computers. These may be marketed (and purchased) through specialist computer stores, large chain retail outlets or by mail order direct from the manufacturer. From the point of view of the manufacturer each of these distribution options will have implications for both sales volumes and revenues, costs and distribution processes. Hence an evaluation of these factors is required before any decision is made.

Such distribution considerations are relevant to HEIs as the following examples illustrate:

Courses – educational courses may be delivered in a number of different ways each with different logistical and cost implications:

- traditional attendance based courses;
- open learning courses;
- outreach courses;
- Internet based courses.

Publications – an HEI may produce and market a variety of publications on, for example, research issues. These publications may be distributed directly by the HEI or through some third party commercial organisation.

Sometimes distribution methods are evaluated purely on the basis of cost. This is a mistake, and a full financial evaluation needs to be undertaken taking account of the likely outcomes (for example, sales volumes and revenues) arising from each approach as well as the costs involved.

2.3 Promotion

Promotion is effectively concerned with communicating information about the organisation and its products and activities to its potential and existing customers. For this reason it is sometimes referred to as marketing communications. It comprises four types of activity which will have different degrees of applicability in HEIs in different situations. These four types of activity are:

Advertising: some form of mass communications in the various forms of media (newspapers, TV, radio) which is paid for by the HEI undertaking the advertising. The advertising can concern the HEI itself or focus on specific services or activities. The potential role of the Internet in marketing HEI services should also be borne in mind.

Sales promotion: this can comprise a number of disparate activities concerned with promoting the HEI as a whole and/or its services and activities. Examples might include:

- exhibitions;
- recruitment fairs – overseas and home;
- display materials;
- mail shots;
- prospectus;
- faculty handbooks;
- web pages.

Public relations: this can involve, for example, editorial comments, news stories, or letters related to the HEIs. This information is presented to the audience, free of charge, through mass media communication. Because the channel of communication is not paid for the HEI has less control over the style, content and presentation of the message than when promoting through other means. The main purpose of public relations activity is to keep the HEI in the audience's mind and to ensure that any news is presented in the most positive manner. Therefore it is common practice for an HEI to have public relations personnel who maintain relations with media to promote stories into the media and to manage any possible 'bad press' before it reaches the audience.

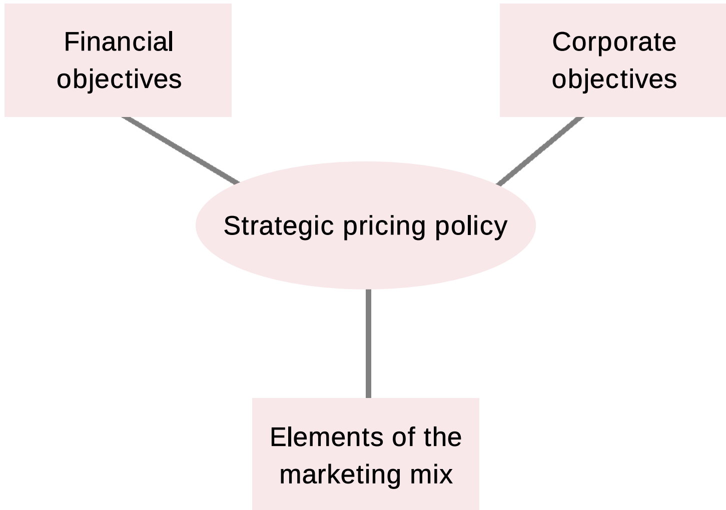
Individual staff actions: in a commercial organisation there will usually be a team of salespersons whose job it is to sell the company's products. Similar operations can be identified in HEIs, although the individual's roles are often not exclusively to do with promotion; examples are:

- international office;
- commercial liaison office;
- schools liaison;
- other opportunities – members of staff in HEIs can 'sell' the HEI in various ways, including during the student visit or interview process, networking activities at given opportunities.

2.4 Strategic pricing policy

Strategic pricing policy means having a longer term view of the pricing of services and products being delivered by the HEI. It should come out of the HEI's corporate strategy and should aim to enable achievement of the HEI's overall strategy. Strategic pricing policy should lay down guidelines for pricing against which individual pricing decisions should be assessed. As well as the HEI's strategic direction the pricing policy decision needs to be considered in relation to other factors (see following diagram).

Financial and corporate objective relationship



A strategic pricing policy cannot be determined in isolation but must take account of and be integrated with the other factors illustrated in the above diagram. Two key aspects detailed below are:

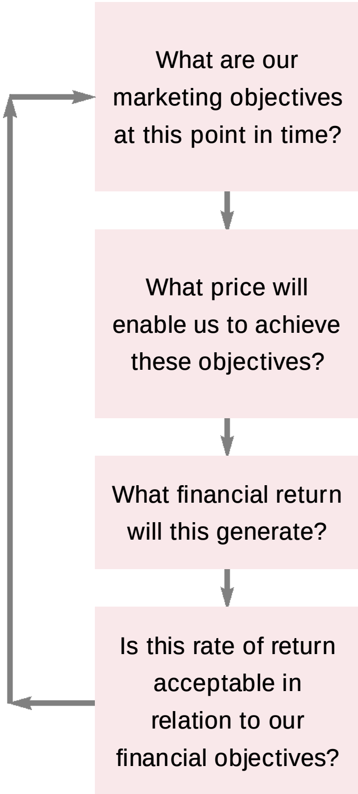
- the relationship between financial objectives and corporate objectives;
- pricing and the marketing mix.

2.4.1 Financial objectives and corporate objectives

In establishing a strategic pricing policy there can be a trade off between achievement of financial objectives and achievement of corporate objectives. Short-term financial returns from a service will be heavily influenced by the price charged and, in general terms, the higher the price the higher the return and vice-versa. However, the price charged will also have an impact on certain strategic objectives, such as market share, rate of sales growth. In general terms the likelihood is that the lower the price the higher the rate of sales growth/market share and vice-versa, although people will pay higher prices for high quality as this relates to the perceived value that they receive; this is explored further in Module 3. The price charged must reflect the balance between financial and corporate objectives; in some cases achievement of the corporate objectives might be paramount and justify a negative financial return – a loss leader. In some HEIs, particularly the smaller colleges, the option of sustaining a loss leader for any period of time may not be a practical option due to the scale of their operations.

Overall, HEIs need to address the questions shown in the diagram below in relation to each service:

Financial and corporate objectives flow diagram



This iterative process needs to be followed until a suitable balance between financial return and corporate objectives is achieved.

2.4.2 Pricing and the marketing mix

A strategic pricing policy will need to take into account other elements of the marketing mix, and the pricing policy must be co-ordinated with policy in these other areas. The following examples illustrate this point:

- A pricing policy will need to take account of the nature of a particular service, the position in the market and the stage in the life cycle of the service being considered. If an HEI has just launched a new course or undertaken a new activity and it is within its control to set the price, then the need for growth and market penetration might be so important as to justify a low or even negative financial return resulting from a low sales price. As the project matures, sales growth might be seen as less important and so the price charged will be such as to produce high financial returns.

Case study A: Pricing for market penetration

The engineering faculty of Alderwood University wishes to expand the range of consultancy services it provides to manufacturing industry in the local area. Although it feels it has the necessary staff expertise and other resources it has a very limited track record in delivering such services and so lacks credibility among local companies. Hence it has made a policy decision to price its consultancy services at a very low level such that it barely covers the marginal costs involved. It anticipates that by adopting this approach it will attract a fair degree of business and thus build up its statement of experience. However, the finance director of the university is very concerned about this approach. The FD fears that once the policy is in place potential clients will expect a continuation of this low pricing policy and university departments will wish to continue with the policy into the foreseeable future, or that the low price may be perceived as reflecting poor quality. Hence he has insisted that the low pricing policy be adopted initially for a six month period. At the end of this period the pricing policy will be reviewed with the aim of moving towards a more realistic pricing policy.

- Pricing policy needs to take account of distribution policy. The price that can be charged for a particular service will be influenced by the distribution channel chosen and the market conditions relating to that distribution channel.

Case study B: Pricing using different distribution approaches

The education faculty of the University of Elmdale offers a taught doctoral course (Ed.D) in education policy and management. The current course, which is offered on a part-time and a full-time basis, requires substantial periods of attendance at the university. It is one of the few HEIs in the country which offers such a course and thus is able to charge premium fees for the course.

The university is now considering offering the same degree course on a distance learning basis using the Internet to deliver curriculum materials. In offering such a course it will be competing with a number of prestigious universities in the USA, Australia and South Africa. Consequently the ‘going rate’ for such a Ed.D degree is less than the price of the current attendance mode course. Thus in fixing a price for such a distance learning course the University has to strike a balance between setting a price based on the ‘going rate’ and charging a premium rate which relies on the preference of potential students for a British degree. However, in setting a differential price for the distance learning course, consideration should also be given to the potential impact on demand for the traditional course.

- Pricing policy needs to be co-ordinated with promotion policy. Thus if an organisation was launching a promotion initiative then it may be appropriate to offer some special pricing initiative to support the thrust of the promotion activity.

Case study C: Promotion through a partnership initiative

Blackwell College of Higher Education has a substantial amount of student accommodation on campus. Like most HEIs it wishes to market this accommodation to tourists and holiday makers during the summer months. In recent years it has had some difficulty in achieving reasonable occupancy rates during July and August and needs to take some actions to alleviate the problem. Consequently it has entered into a partnership arrangement with a nearby theme park to market a joint package of college accommodation, meals and theme park entry. This package is to be heavily marketed in suitable magazines, with a special offer of a reduced price for those who place a firm booking prior to the end of the year.

Module 3 Key pricing factors

Aims

By the end of this module you should be able to understand:

- the key factors involved in pricing decisions and their inter-relationship;
- the types of data and information needed to inform pricing decisions;
- how HEIs can make best use of the information that is available to them;
- how to analyse the data so that it can help develop an effective pricing strategy.

Structure of this module

This module explains the five key factors that should be assessed in developing pricing strategies and decisions:

- an HEI's corporate strategy; (3.2)
- customers; (3.3)
- costs; (3.4)
- competition; (3.5)
- other factors. (3.6)

The module begins with an introduction then addresses each of the five factors. For each factor the context and background is discussed in an overview section followed, where appropriate, by sections on data collection and data analysis. The purpose of this module is to give practical, operational advice about what information and analyses HEIs ideally should have to hand during pricing discussions and (in the real world) how HEIs can make best use of the limited information they may actually possess. It may make sense to think of the sections as five mini-modules and look at them individually in the first instance.

3.1 Pricing factors

Module 2 described how price is part of the marketing mix and should be considered as an element of an HEI's strategic marketing planning. This module looks at price in more detail and examines the key factors that should be assessed to enable an HEI to price its goods and services effectively.

An overriding principle that should be made clear at the start is that costs are only one component of an effective pricing strategy. Traditionally within higher education the costs (however calculated) of a service have been the main determinant of its price. The more strategic approach, which starts from an appreciation of the HEI's strategic position and the value customers attribute to a particular offering, is not adopted in many HEIs.

For example, the following illustration of pricing the hire of conference facilities for the summer vacation represents a common scenario.

Case study: A traditional cost driven approach to pricing

The University of Midchester uses its premises during the summer vacation to attract residential conferences. This has led to a situation where in recent years the halls of residence and lecture and seminar facilities have been up to 50% utilised during the summer recess generating 'surplus' income to the University. However, during the last summer, bookings fell and the University is not entirely sure of the reasons for this. There is a perception that price may be a factor and a reduction may therefore help recover their position in the conference market. The Director of Finance is currently assessing options and calculating the break-even position that the University must achieve to cover its costs. Meanwhile the Head of Marketing and Promotions is pondering whether to change the design image and brand of the University's promotional material to capture more of this particular market.

This scenario is effectively driven by financial implications. However, while the importance of covering costs is clear, a focus just on the income and expenditure account to determine price could mean the University either fails to recover its declining share of the market or experiences a considerable reduction in profitability of these activities. A strategic pricing approach should not ask 'What price do we need to charge to cover our costs?', rather 'What costs can we afford to incur given the price sensitivity of the market and still make a profit?'.

In this example a price reduction may generate a stable or even improved position in the short term, but in the longer term failure to understand the value customers place on the service, and the ingredients that make up that perception of value, may well result in a weaker position for the University in this market.

For example

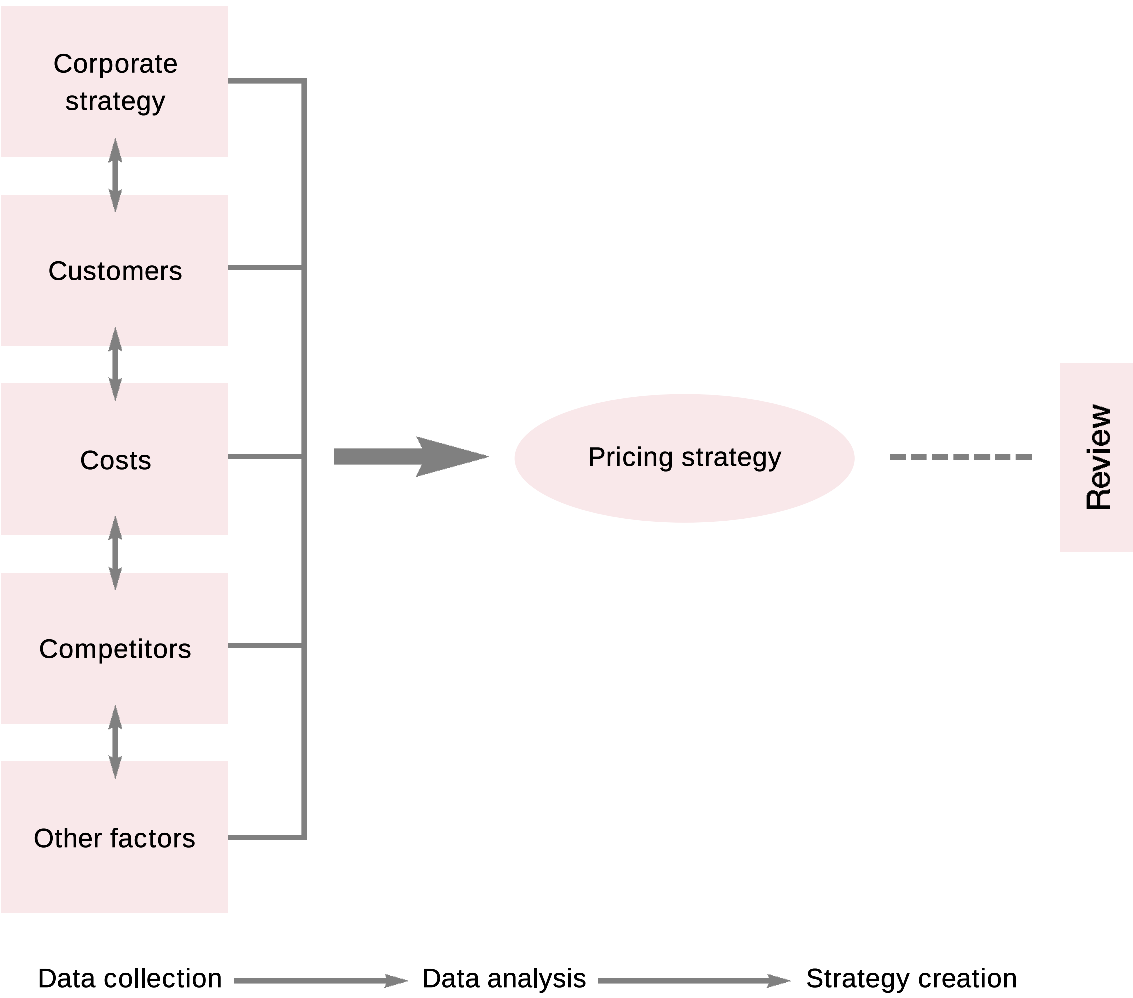
- Is the recent decline the result of a financial decision made by purchasers to go elsewhere or are there other factors involved such as quality, image or other non-financial attributes?
- Would some customers actually be prepared to pay substantially more for the facilities if they could be convinced that there is a prestige image attached or a longer-term contract that reduced their effort and costs in switching between suppliers?

Another way of demonstrating the difference between cost driven pricing and strategic pricing is to replace the question of 'What price will our customers pay?' with 'What is the real value of this service to our customers and how can we better communicate that value in order to justify the price?'

To reach a strategic approach to pricing, it is important that HEIs are able to strengthen the relationship between marketing and finance – that is, a balance between reflecting customer value and the need to cover costs and, in most circumstances, generate some surplus.

The combination of these factors should be considered in all pricing decisions, although clearly the scale of analysis will depend on the importance of the decision to be taken. The correct pricing decision of a one day seminar will not warrant the same attention as that of a new postgraduate qualification, and in some minor cases a decision based purely around the direct costs of an activity may be appropriate. The key factors are illustrated in the following diagram.

Key factors in pricing



Within each factor HEIs should be looking to collect key data and analyse this to help determine the correct pricing strategy. The following sections of this module explore the types of data to be collected and analysed while Module 5 looks at the alternative pricing strategies that can be employed once this knowledge has been gathered.

3.2 Corporate strategy

In any organisation every decision taken should be in support of its overall strategy. Pricing methods are not an exception to this. An HEI's overall strategy should, therefore, govern the approach to pricing in practice.

The HEI should have a long-term vision which outlines the direction the organisation wants to go and what it is trying to achieve. Educational HEIs are of course not in the world of setting simple 'bottom line' visions, and it is more likely that their vision will be characterised by an aspiration to improve quality, access, the learning experience of their students and development of their research capability. For example, an HEI may have, within its vision, an aspiration to increase the proportion of local ethnic minorities in its student population.

To support the vision, an HEI should have in place a mission statement which is designed to articulate the overall approach to be taken to achieve the vision. For HEIs, the mission might be geared towards quality, the nature of service delivery, the use of technology and attracting, retaining and developing staff.

The corporate strategy sets out how the HEI will achieve its mission and, therefore, its vision. It should be a detailed document which contains measurable objectives over (typically) a five year period. Importantly, it is from this document that individual faculties and business units will be able to determine their own plans and priorities and, specifically, the pricing methods needed to achieve these. Within the corporate strategy there will be a number of sub-strategies such as:

- marketing strategy;
- financial strategy;
- research strategy;
- teaching and learning strategy;
- pricing strategy.

It is important, therefore, that pricing decisions are not made in isolation of the 'big picture' and all staff involved in pricing decisions must understand the overall aims and direction of their particular HEI, so that these decisions are not in conflict but actually support the organisation in realising its objectives and vision. Often this potential conflict only materialises some time after the (incorrect) pricing decision has been made – as it becomes increasingly clear that the HEI's ability to deliver a particular strategic objective is constrained.

Case study: The influence of strategic objectives

Hightree University is based in an urban location and has being looking at ways it can increase the intake of undergraduate students from within its own locality, and particularly to increase participation among those who currently attend the local further education (FE) colleges on FE courses. The University has set out a strategic objective to this effect and aims to increase intake from these students by 10% over the next three years.

As part of the implementation of this objective, it has decided to provide access teaching at the local FE colleges. The provision of teaching will incur some cost to the University in staff time, travel and the preparation of materials. It has been decided that in order to attract these potential students it would be inappropriate to charge the colleges the full cost of providing the teaching. However, through the guidance offered to these potential students during the course, it is hoped that in the longer term a number of them will go on to enter the University on an undergraduate programme.

The price therefore has in effect been set below cost in order to fulfil the overarching strategic objective.

Note: this is a fairly straightforward example of how a strategic objective governs a pricing decision. However, the position would be different in the above HEI if it had also set itself an objective of improving its financial health. The decision to set the price below cost would work against this latter objective.

There will probably always be tension between strategic objectives which often materialises at the moment when a pricing strategy needs to be agreed. A common example is the ‘loss leader’ price which aims to achieve greater growth in longer-term market share while sacrificing short-term profitability.

There is no simple solution to resolving the tensions that may appear to exist between an HEI’s strategic objectives. However, there are some important factors that need to be taken into account in order to try and reach a balance:

- All staff should be aware of the HEI’s vision, mission and strategic aims, and not just those which may have a direct impact on themselves or their department.
- Strategic objectives do not all have to be implemented at the same time and at the same pace. It may be necessary to balance between a need to capture market share in a particular area in years one and two of the strategic plan against the need for a reasonable financial return from this activity, which can be the focus of years three to five of the plan.
- In order to ensure congruence between the HEI’s strategic plan and pricing decisions, it is important for the internal management arrangements to be sufficiently robust. This is explored in greater detail in Module 5.
- Wherever possible a pricing strategy should be prepared and adopted. This should seek to translate the HEI’s corporate (overall) strategy into pricing aims and objectives. This should reduce the risks of inappropriate pricing decisions being made.

Pricing, therefore, is not determined purely by numbers. There are a variety of other internal and external factors that should be taken into account in order to bring about an improved understanding of the pricing environment.

3.3 Customers

The wide range of HEI activities that involve pricing decisions mean that there is a significant range of customer groups who experience the effects of these decisions. Listed below are some examples of broad customer groups:

- home/EU undergraduate students;
- international undergraduate students;
- postgraduate students (taught and research);
- research sponsors (private, charitable, government);
- commercial organisations (including small and medium-sized enterprises, global corporations);
- individuals (for example, purchasing books, digests or specific services).

Within each of these broad customer groups there will be a variety of factors that influence and determine any particular purchasing decision. Price is of course only one of these elements. Understanding these factors, and specifically how a customer may react to a certain price, is a complex task.

3.3.1 Pricing and customer decisions

It is often assumed that HEIs know exactly how their prospective customers will react to different price levels for goods and services. This section is aimed at helping HEIs understand how customers use price in their purchasing decisions, and gives guidelines on the key questions that should be addressed in forming this judgement.

The key to understanding customer purchasing decisions is the comparison between price and the perceived future benefits which will arise from their purchase. For each purchasing option, customers will assess the relative price and relative benefits to be derived. In other words it is on the combination of price and benefits, rather than just on price alone, that customers' buying decisions are made.

A good example of this within higher education is the wide range of prices charged by different HEIs for (full-time) MBA degrees. If students' choices were purely on a price basis then all HEIs' prices would have rapidly converged to a common value. This they clearly have not done: in fact, prices for apparently similar programmes vary in the ratio 3:1. This differential has to be supported by different views within the group of prospective students as to the career and other benefits of the different programmes.

Understanding the value a customer attributes to a commodity is critical to determining price. Unfortunately reaching this understanding can be difficult, particularly for non-commercial organisations who do not have extensive marketing or market research budgets to call upon. However, in considering how to approach this problem the following practical examples of different influencing factors may help develop an informed judgement about the value a customer assigns to a particular offering. These examples are often referred to as factors affecting price sensitivity and are as follows:

- **Substitutes** – clearly in many cases the price of a substitute will be a major factor in purchasing decisions (even if the customers' perception of a suitable substitute is flawed).

  For example, in addition to the full-time MBAs described above there are many distance learning MBAs available in the UK today. Taking a distance learning MBA often does not represent the same level of economic investment as full-time study, since the student can continue in employment. Moreover it is more difficult to assess the quality of the provision being offered. In contrast to full-time MBAs, therefore, the decision on which distance learning MBA to choose may be heavily influenced by price comparison even if in fact the quality varies significantly. In this scenario HEIs may need to influence the customer about their perceptions of substitutes rather than look to cutting their own price.

- **Uniqueness** – one of the ways HEIs can influence customers is by persuading them that their offering is unique and not comparable with what appear to be similar offers available on the market. Sticking with the MBA example, a trawl through advertisements at certain times of year demonstrates this in practice as universities and colleges attempt to influence customers' views that their particular MBA is unique and therefore can be differentiated from (often lower priced) alternatives. In effect this is ensuring the key features of an offering are converted into value. In the commercial world each company spends vast amounts of money re-branding its products in an attempt to persuade buyers it is somehow different from alternatives.

- **Transfer costs** – this is the cost (or perceived cost) to the customer of transferring their business to another supplier. Cost here should be understood in the widest sense (including inconvenience and disbenefit, as well as financial costs). For example, a commercial research sponsor may consider it to be a time-consuming and costly exercise to break a research relationship with an HEI and go back to square one and test the market, and therefore may be inclined to remain with a preferred provider assuming it is content with the work. Transfer costs clearly apply to some HEI activities, but not at all to others: there is evidence, for example, that many students regard the transfer cost of moving to a different HEI for postgraduate study as zero or even negative (that is, they positively want to move HEI).

- **Price-quality relationship** – in some cases customers are less sensitive to a price if they perceive that the higher price is a signal of quality. In effect they are prepared to pay a premium for perceived greater end-benefits. This is at the root of the differential prices for full-time MBAs discussed above.

  Setting high prices can also deliberately limit the number of customers if HEIs so desire. Thus an HEI with a popular postgraduate taught programme which cannot be expanded (due to space or staffing constraints) may set high prices in order to reduce the number of applicants to a manageable level.

- **Proportional effect** – for some overseas students the fees payable to a UK higher education institution may account for a significant proportion of their total disposable income. In such a case they are more likely to be sensitive to price and living expenses. Conversely some of these students may have their fees paid for by a relative or third party (for example, a sponsor) and, therefore, one can assume they may have a differing degree of price sensitivity to, for example, accommodation or travel costs.

- **End benefit** – the value a student assigns to a short course may be in relation to the expected benefits (for example, job opportunities or career advancement), and therefore it is possible that their first consideration will not necessarily be the price of the course. An example of this in practice is the advertising for some postgraduate courses in which an HEI argues that someone completing the qualification will earn substantially more as a result.
- **Fairness** – often customers will have a perception of what constitutes a fair price or price range. Academics who, for example, are priced for consultancy work at a level which a customer perceives to be unreasonable may be less likely to receive commissions even if the buying organisation has significant resources at its disposal. The concept of fairness is, of course, notoriously difficult to define.

These are some examples of factors which may affect a customer's judgement about their perceived value of a service offered, and serve to demonstrate that pricing decisions need to be based on a much broader foundation than costs.

3.3.2 Data collection

Given the complex nature of accurately determining customer value, what is the key data that HEIs need to collect on their customers in order that at least an informed judgement can be made? The seniority of person required to make that judgement or decision will depend on the size or impact of the decision.

Managers and academic staff should look to collect at least the following information in order to begin to reach an understanding of their customer base. This information does not of itself answer any of the questions raised above, but is a prerequisite to considering them.

Customer related data collection

Customer base (existing and prospective)	Profile	Possible sources of information
Individuals	• age; • place of residence; • social characteristics; • ethnicity; • sex; • employment status; • employment sector; • fee payer.	• student information system; • UCAS; • information extracted from enquiries and applications; • HEI's market research resources.
Commercial organisations	• size (turnover, employees); • profitability; • main markets/key areas of business; • mission; • industry trends.	• local labour market intelligence; • business organisations (for example: chambers of commerce; professional associations); • commercial organisations who sell information on companies or industry sectors (for example: via the Internet); • annual report; • HEI's market research resources.
Charitable organisations	• aims and objectives; • size (donations, staff); • key areas of business (research interests); • sector trends.	• previous knowledge; • academic networks; • annual report.
Government departments	• budget size (research budget size); • previous activity; • current trends and issues.	• previous knowledge; • government; • annual report/corporate plan.

Clearly within these broad ranges of customers HEIs will need to segment particular groups (for example, for individuals: part-time, full-time, subject area, domestic, overseas, USA, school leaver, mature).

Once the customer base is identified and accurately understood, HEIs can focus upon the factors influencing price sensitivity and customer benefit perceptions. Often HEIs do not have vast amounts of information available to help them with this task, and where internal information is limited consideration may need to be given to commissioning market research which measures buyer behaviour.

The types of information needed to identify influencing factors are summarised below:

Influencing factors relating to customers

Influencing issue	Possible sources of information
• Alternatives that customers are faced with when making their purchase.	• Advertising by other HEIs. • Local knowledge and research. • Survey of current/previous customers.
• Attributes that customers consider important when making their purchase.	• Survey of current/previous customers.
• The importance of prestige or image to the customer.	• Often local judgement is as reliable as surveying customers.
• The end-benefits that the customers desire.	• Alumni – destinations of previous students. • Survey of current/previous customers.
• The price range that the customers consider fair.	• Difficult to ascertain – local judgement may be the best source.

If an HEI is able to provide information in response to these issues then its understanding of customers is considerably enhanced and its pricing strategy will, therefore, become more robust. Clearly in practical terms HEIs should not overlook their own staff's knowledge and perceptions of their customers, particularly if commissioning market research is not feasible.

Once the information has begun to emerge on customers and the factors influencing their perceptions about the value of an offer, HEIs need to conduct careful analysis in order that this information becomes knowledge which can successfully influence the pricing strategy.

3.3.3 Data analysis

The outcome of the data collected about an HEI's potential customers could be usefully analysed to answer the following questions. These questions need to be answered for each type of product or service offered for which a price can be set (for example, postgraduate programmes, research projects, conference facilities, catering):

- Who are our customers (either as a broad group or segments within a group)?
- What are the customers' objectives from the purchase?
- What appear to be the main factors influencing their sensitivity to price?
- Could marketing be used to change or strengthen the influencing factors on price sensitivity?
- Are customers' needs fully met by the offer? Where are the gaps and what are the implications of addressing these?

It is important that this analysis of customers is now taken forward to contribute to the overall formulation of a pricing strategy.

3.4 Costs

We have emphasised throughout this document that the costs of a product or service should be just one of a number of factors which will influence a pricing decision. Nevertheless, it is the case that the costs of a product or service are very relevant to pricing decisions. This section will discuss various aspects of costing as they affect pricing decisions. However, this section does not attempt to provide a full discussion of costing issues, and readers are referred to the JCPSG training material: 'Costing and Pricing for Decision Makers in Higher Education – User Guide, June 1999, which is available on the JCPSG website.

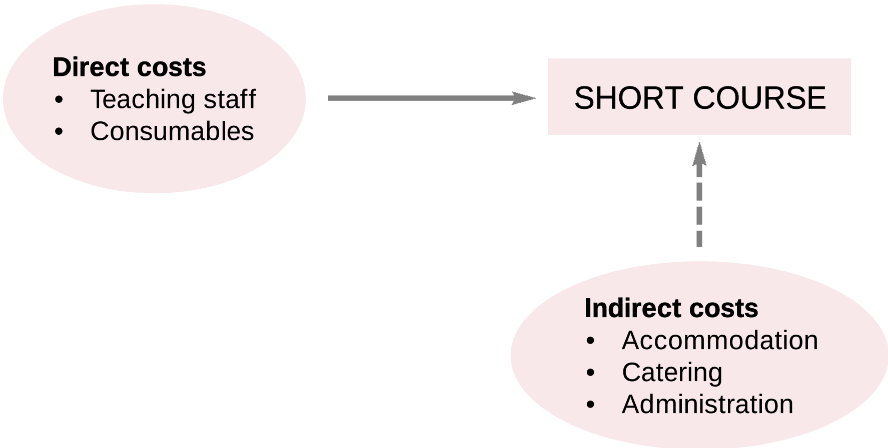
This section covers the following:

- pricing decisions and total costs;
- pricing decisions and marginal costs;
- the use of contribution and break-even analysis;
- internal transfer pricing;
- data collection;
- data analysis.

3.4.1 Pricing decisions and total costs

A general rule to be applied when making pricing decisions is that the price should be set by reference to the total costs of the activity being considered. Total costs are the sum of direct costs and indirect costs of an activity, as shown below using a short course as an example:

Direct and indirect costs



Direct costs are the most familiar and easily comprehended. They are those costs which can be directly allocated to the activity in question. In the above example, these would be teaching staff time and consumables costs, such as stationery.

Indirect costs are those costs which cannot be directly allocated to a particular activity (because of a lack of information) but a share of which needs to be attributed to the activity by some means of apportionment. Using the above example, indirect costs would be the costs of teaching accommodation, catering costs and a share of administrative costs of the HEI. Indirect costs can be apportioned to activities using suitable cost drivers. Examples of the use of such drivers include:

Cost drivers

Type of indirect cost	Cost driver
Library costs	Numbers of students
Estates costs	Floor area occupied
Personnel costs	Numbers of staff

It is for the individual HEI to devise an appropriate model for apportioning its indirect costs to its activities, after consideration of its own strategy and of the behaviours it wants to encourage. In terms of the HEI's own approach to apportioning indirect costs (i.e. its internal indirect cost recovery rate), it is clearly unnecessarily complex to apportion these indirect costs down to the level of individual grants and projects (for example, 1/500th of the playing fields, 1/2000th of the Principal's car), so broad-brush assumptions are made, resulting in a general indirect cost recovery rate. The rate will be set at an HEI level, with regard to strategic and other factors for each 'product line': research grants, consultancy, catering etc. The University will want to be sure that the rate it set for indirect cost recovery on a project or activity is achievable in the marketplace and is the most strategic way of allocating the indirect cost burden. The information generated from the Transparency Review will help HEIs understand their cost structures better and therefore make those sorts of decisions more effectively. A principle to consider is to have as few different indirect cost recovery rates as possible, otherwise staff will find pricing and costing confusing and may make mistakes.

However, whatever the approach to apportioning indirect costs to activities used by the HEI, there are often limitations laid down by the 'customer' as to the amount of indirect costs they are prepared to pay for in the price. The argument is often made that HEI indirect costs are already financed by public funds and so should not be paid for a second time. Thus, although the HEI may wish to get the 'customer' to agree to a particular price, the customer may wish to see an analysis of the costs of the proposed activity and may limit the amount of indirect costs for which they are prepared to pay. This is particularly the case in relation to the pricing of research contracts, and the following table summarises the contributions to indirect costs that sponsors are currently willing to see included in their prices.

Limitations on indirect cost contribution rates

Sponsor	Indirect cost contribution from sponsors
Research grants funded by Research Councils	46% direct staff costs
Research grants funded by the European Union	Circa 20% of all direct costs
Teaching company schemes	Typically 46% of 60% of staff costs
Charities and voluntary organisations	No indirect costs allowed in pricing

Individual sponsors may also be willing to accept specific, rather than general, contributions to indirect costs, for example, 10 hours of personnel time for every job created, 10 hours of library time for every PhD student, any capital equipment required. To this extent, prices for research grants funded by the Research Councils and the European Union, as well as teaching company schemes, are sponsor-determined, with little discretion open to the HEI to justify higher indirect cost contributions on the basis of actual costs. The results are also usually audited by the sponsor, with clawback possible if costs are not in line with budget.

Under the current system, sponsors have no way to be sure whether the amount of indirect costs they are paying for is too much or too little in relation to the indirect cost base of a particular HEI, and therefore whether value for money is being achieved. Meanwhile, the HEI may be experiencing difficulty covering its indirect costs and may want the rate of payment increased. The Transparency Review already mentioned seeks to address this point by apportioning indirect costs to activities using simple drivers. Given the greater transparency of costs one possible result of the Transparency Review may be an agreement to raise, or lower, the rates for indirect cost contribution. Thus, for example, charities may be willing to contribute towards indirect costs if they can be justified. There will also be a need for HEIs to justify higher-than-average levels of central indirect costs. In other words, the connection between cost and price is becoming much closer, in an effort to achieve greater accountability.

It is important to ensure that all relevant costs are taken into account before making a pricing decision. Often, staff are conscious only of the direct costs and fail to understand that it is important to incorporate a proportion of the indirect costs in order that the income generated will contribute to indirect costs and profit. However, saying that prices should be related to total costs does not mean that the price must equate to the total cost, and three scenarios are possible:

- **Price is greater than total cost** – this implies the generation of a surplus or profit on the activity, which will then be available to fund future development activities of the HEI. The amount by which price should exceed cost (and hence the element of surplus) must be set in reference to the HEI's financial strategy and the overall financial surplus the HEI wishes to achieve.
- **Price is less than total cost** – this implies a planned deficit on the activity which presumably is based on the idea of a 'loss leader'. Again, the amount by which price should be set below total cost (and hence the element of subsidy) must be set by reference to other elements of the pricing decision such as competition and corporate objectives
- **Price equals total cost** – in this case there is neither a surplus or a subsidy.

However, the pricing decision may be more complex than this, and variations in pricing may be applied to different types of customer and different markets. Thus, for one customer type the price may be set in excess of total costs while for another customer type the price may be set below total cost for strategic marketing reasons.

Case study: Pricing and total costs

The economics faculty of Campshire University produces a briefing service to local organisations about European Union developments. Each organisation pays an annual subscription and receives 12 monthly bulletins and a telephone advisory service. The university has calculated that the total costs of providing this service (incorporating a share of central indirect costs) is £800 per client. To achieve maximum coverage from local organisations it has applied the following pricing policy:

- Private companies – £1,200 per annum (50% on cost)
- Local authorities – £1,000 per annum (25% on cost)
- Chambers of trade/commerce – £600 per annum for the first year only

Currently there is little involvement from chambers of trade/commerce, and so it has been decided to offer the service at below total cost for one year only in order to stimulate demand.

Case study: Marginal cost pricing

The print room of Oakdew University provides services to all departments in the University and generates 10 million units of work per annum. The following cost information is available about the print room:

Total costs of production:

	Total costs £	Unit cost p
Materials	25,000	0.25
Labour	75,000	0.75
Variable indirect costs	20,000	0.20
Fixed indirect costs	10,000	0.10
Total	130,000	1.30

The print room has been asked by a private company to submit a tender for a once-off contract to undertake 300,000 units of work and it needs to decide what price it should charge for the work.

The total costs (including indirect costs) would amount to £3,900 (300,000 x 1.3p).

However, the head of the unit feels that since this is a fairly small (3% of total workload) contract which is once-off then it is appropriate to base the price on the marginal costs. These are calculated as follows:

Marginal costs of production:

	Marginal *costs per unit*
Materials	0.25
Labour	nil
Variable indirect costs	0.20
Fixed indirect costs	nil
Total	0.45

Thus the marginal costs of undertaking this contract would amount to £1,360 (300,000 x 0.45p)

The following points should be noted:

- Fixed indirect costs are by definition non-marginal.
- Since there is slack capacity in the unit, it is assumed that the additional work can be undertaken by the existing staff, and thus the marginal labour costs of this contract are nil. In other circumstances it may have been necessary for overtime to have been worked or temporary staff recruited, and in this case there would have been a marginal labour cost.

3.4.2 **Pricing decisions and marginal costs**

In certain specific circumstances it is appropriate and acceptable to base pricing decisions on the marginal costs of an activity rather than the total costs of that activity. The marginal costs of an activity are synonymous with variable costs and are the additional costs that an HEI would actually incur if it undertook the activity. However, the marginal (or variable) costs of an activity must not be thought to be synonymous with the direct costs of an activity. For example, teaching costs associated with a short course may, effectively, be fixed in nature even though they are directly attributable to the activity.

Marginal cost pricing (i.e. the setting of prices by reference to the marginal costs rather than the fixed costs of an activity) must be treated with caution. If all activities were priced on the basis of marginal costs then there is a risk that insufficient revenues would be generated to finance the indirect costs of the organisation. Thus marginal cost pricing should only be undertaken in the following circumstances:

- The proposed activity is for a once-off contract which is fairly short-term in nature. Thus it is not applicable to ongoing activities.
- Pricing the activity at marginal cost will not affect the price charged for the mainstream provision of the same activity. This implies that an activity might be provided in some other geographic location.
- The proposed activity is a fairly small proportion of the existing workload of the department.

As with total costing, saying that prices should be related to marginal costs does not mean that the price must equate to the marginal cost, and again three scenarios are possible:

- Price is greater than marginal cost – the excess of price over marginal cost means that the activity will be making a ‘contribution’ (see next section) towards the fixed costs of the HEI.
- Price is less than marginal cost – this would seem an unwise pricing decision since the price charged is less than the additional costs that will be incurred in undertaking the activity.
- Price equals total cost – in this case there will be zero contribution towards fixed costs.

3.4.3 Contribution and break-even analysis

The concept of contribution and break-even analysis is an important one in making pricing decisions. It recognises that pricing decisions are dynamic in nature, and recognition must be made of the relationship between demand for a product and its price.

The term contribution is short for contribution to fixed costs and is calculated as follows using the data from the EU briefing service from the earlier example:

Calculating contribution to fixed costs

	Private companies	Local authorities	Chambers of trade/commerce
	£	£	£
Income	1,200	1,000	600
Marginal (variable) costs	700	700	700
Contribution to fixed costs	500	300	(100)
Number of clients	30	6	1
Total contibution	15,000	1,800	(100)

Thus, the total contribution being generated amounts to £16,700. Given that fixed costs are by definition fixed, then the profit generated by the activity will depend on the level of contribution being generated. Thus, if the fixed costs attributed to this activity were £14,000 then the profit generated would be £2,700.

However, since demand is inextricably linked to price then different price levels will generate different levels of demand and thus different levels of contribution. This is illustrated in the case study shown below.

Case study: Contribution analysis

The business studies department of Woodchip University has recently published a guidebook to doing business in Eastern Europe and wishes to sell this document to commercial firms. However, it is unsure what price to charge for the service. The following cost data is available about the product:

- Marginal costs of each unit = £5
- Total fixed costs associated with the activity = £1,000

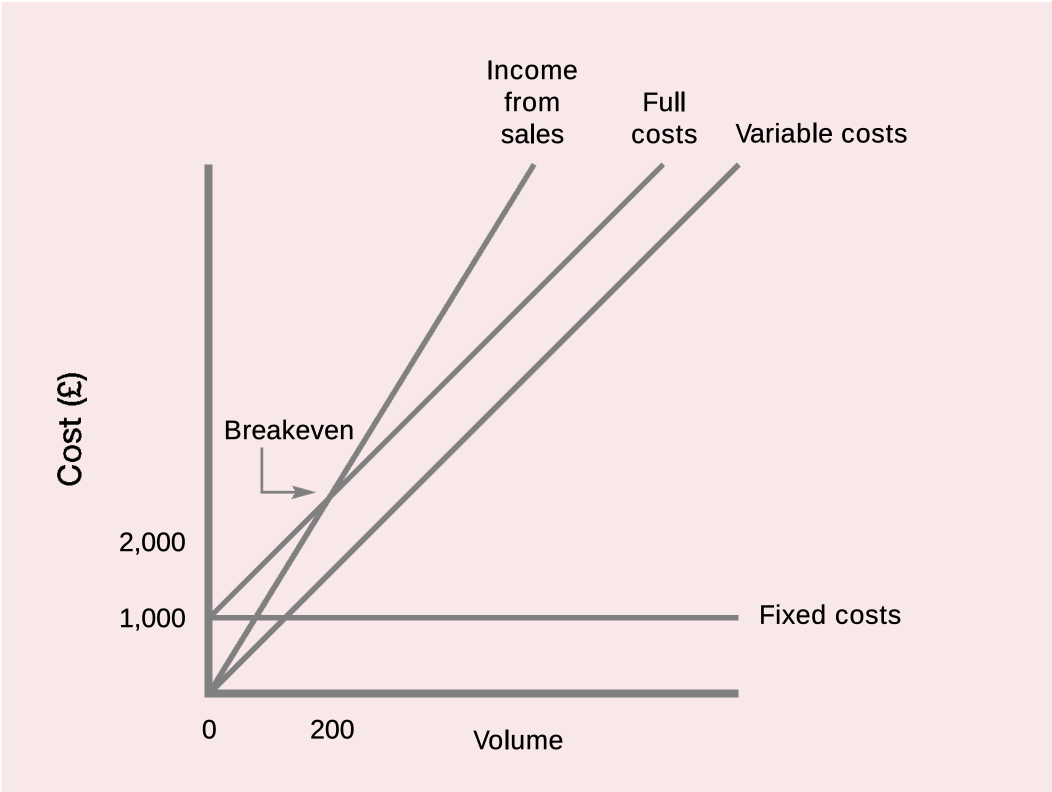
The marketing department of the university has undertaken some market research and has prepared estimates of demand for the guidebook at various prices. The results of this are shown below:

Price	**Sales volume**	**Income**	**Marginal costs**	**Contribution**	**Fixed costs**	**Profit**
£	£	£	£	£	£	£
10	200	2,000	1,000	1,000	1,000	Nil
12	180	2,160	900	1,260	1,000	260
14	130	1,820	700	1,120	1,000	120
17	80	1,360	400	960	1,000	(40)

Thus the maximum contribution will be generated at a selling price of £12.

Break-even analysis aims to identify the point at which a particular activity will financially break even, and in the above example it can be seen that the break-even point will be achieved at a price of £10 per guidebook. The break-even point is also illustrated in the following diagram.

Break-even analysis



3.4.4 Internal transfer pricing

Transfer pricing is relevant where there are individual departments within an HEI which perform services for other departments and have the role of *cost centre*, meaning that they have been given devolved responsibility for both income and costs and have a responsibility to generate surpluses for the HEI. An example might be a printing service. The printing service may feel that its self-interest demands that it charge fellow departments high prices for printing work in order to generate surpluses. However, this would not be in the interests of the organisation as a whole. Individual departments that did a lot of printing may begin to investigate outside sources of printing services which offered cheaper rates then the internal service. Eventually, the printing service might not have enough business to be viable and might be closed, with the resultant loss of jobs. However, departments which only did small amounts of printing would then find themselves forced to pay higher prices than previously for external contractors to undertake their uneconomic orders. They may not even be able to find a contractor willing to undertake the work at all, which might impact on the quality of their administration and marketing. The HEI, taken as a whole, would be worse off.

Equally, departments which felt it was in their self-interest to secure low rates should consider that this could also lead the service department to be closed down, for failing to cover its costs, which is again not in the interests of the department or the HEI as a whole.

The aim, then, is to set a transfer price which encourages profit centre managers to make sound decisions which are in the organisation's overall interests. However, as a preliminary point, it should be noted that a decision is only as sound as the management information on which it is based, which should give the full picture. If an external market exists for the product, this can be used as a source of information in setting the transfer price. If there is no market, costs of production will have to be used in setting the transfer price. This is discussed further below.

- **Where an external market exists:** the transfer price is the market price. The ordering department pays the same as it would pay if there were no internal provider and the supplying department makes the same income it would make if selling to an external customer. This is the opportunity cost of buying from/selling to the internal department rather than an external body. However, finding an identical comparator product to price can be difficult – for example, if a private supplier has surplus capacity, it may be offering a lower price than usual. Also the market price has to be adjusted to strip out selling and distribution costs which would not be incurred by an internal relationship.
- **Cost-based transfer pricing:** if the supplying department – in this example, printing services – has surplus capacity, then it should be willing to take any business which simply covers its variable costs. However, it should be recognised that it will be failing to cover its fixed costs, so this cannot be a long-term cost option. If it is busy, then it should build in a surplus element. The main methods of calculating how much that surplus should be are:
  - variable cost plus – but unless the 'plus' covers fixed costs, the supplying department will still be making a loss on the transaction;
  - variable cost plus a regular lump sum towards fixed indirect costs. This would be most suitable where there was a continual relationship;
  - full costs – this is likely to produce problems with regard to decision making as printing services' fixed costs will now be seen as part of the ordering department's variable costs:

Calculating total variable cost

	Printing dept.	Ordering dept.	Total
	£	£	£
Transfer-in price		70	
Variable cost	40	20	60
Mark-up/contribution	30	10	
Price	70	100	

Here, the ordering department might see its variable cost as £90 (£70 transfer-in + £20 variable costs). In actual fact, it should accept any business that brings in income over £60, which is the total variable costs of the organisation as a whole (assuming it has surplus capacity).

- **dual pricing:** variable costs are used for decision making and full costs for performance evaluation of the supplying department i.e. it is made to appear to be covering its fixed costs on the transaction. Such a system is probably too complex for most HEIs.

  In practice, the transfer price may well come down to a negotiation. The HEI should try to ensure a level playing field for such negotiations between the ordering and supplying departments and to ensure that no blame attaches to supplying departments which knowingly take losses in the interests of the whole organisation. Factors to take into account include surplus capacity and the strategic importance of the order to the HEI as a whole.

3.4.5 Data collection

Good quality management information is crucial if an HEI is to understand and learn from its historical performance and reconfigure its costing and pricing strategy accordingly. A key source of data is budgets. The HEI will have budgets and cost data at both an HEI and a departmental level, and will compare budgets with actual performance throughout the year.

At the project level, the best information comes from a continuing relationship, for example, a conference or short course which is held every year, as trend information can then be built up – who the attendees were, what worked, what failed to work. With research grants or consultancy assignments, the issues are likely to be unique and non-recurring, as each assignment may well be for a new client, with a different product and different staff every time. Nevertheless, general lessons in terms of both price-setting and project management can be learned. In terms of price-setting, a record should be kept of the prices submitted for bids both won and lost, and reviews of failed bids should be carried out to see what can be learned from them. Project management is often the key to making a profit rather than a loss, and post-project evaluations are therefore recommended for all types of assignment.

In terms of information necessary to produce a cost-based price for a project, the following are the main facts which should be collected:

- staff time inputs;
- staff grades and types;
- staff incentive schemes;
- equipment needs;
- student numbers (where relevant, for example, marking time per script);
- when the work takes place (if outside normal working hours, overtime may be payable. Some HEIs will also charge differently for space depending on whether it is term time or not);
- where the activity takes place (if it takes place at a client’s premises, then no room rental is needed. If it takes place overseas, then an allowance might be added for the services of the Overseas Office);
- the level that the HEI has set for indirect cost recovery;
- the terms and conditions set by the sponsor (for example, some sponsors will allow the inclusion of certain indirect costs such as 10 hours of Personnel Office time for each job created, 10 hours of library time per PhD student);

- if the HEI has a partner, for example, in running a short course overseas, there may be specific contractual arrangements in place relating to the sharing of costs;
- inflation, if the project lasts longer than one year;
- whether a course is credit-bearing or not, since a credit-bearing course should take a share of the costs of the Accreditation function;
- and of course, the design, and hence costs, of the course will be guided by the price that the customer or sponsor is willing to pay.

3.4.6 Data analysis

Issues which need to be addressed from the analysis of the cost data collected are:

- How much are the variable costs?
- What are the indirect costs for which this project will be held responsible, specifically, or as a percentage?
- How much of a contribution to those indirect costs is the funder prepared to pay?
- If this activity needs to cover total costs and possibly make a profit, what is the price and/or volume of activity needed to do so?
- What is the sensitivity to changes in cost levels?

3.5 Competition

HEIs face competition from many sources, including other HEIs (domestic and overseas), FE colleges and commercial organisations, and the nature of this competition is becoming increasingly complex and in many areas more intense. Pricing decisions must take account of this competition.

How should HEIs manage pricing decisions in a competitive market? The first step is to understand the nature of the market in which one exists for a particular service or product. Once this has been achieved HEIs should then think about who the competitors are in the market and their characteristics. Armed with this information an HEI can consider the strength of its own market position compared to competitors, how it may best insulate itself from competitive threats, how it might influence competitors' behaviour and whether the competitive intensity is such that the market remains attractive in the long term. There are three aspects to this:

- understanding the market;
- analysing competitors;
- assessing market position.

3.5.1 Understanding the market

In different markets there will be different structures including the following examples:

- **Monopoly** – where one HEI or organisation effectively controls the market and therefore usually the price. This may mean the market is difficult to enter or conversely may actually mean there is scope for competition. An HE example here might be an HEI which has a patented research application.
- **Oligopoly** – where a small number of HEIs control the market. Often this situation is characterised by stable prices and again may offer opportunities for new entrants with alternative pricing strategies. An example here might be the provision of degrees in veterinary medicine where there are only six UK providers.
- **Openly competitive** – the most common scenario where many HEIs operate and is likely to be very competitive but also open to variations in pricing strategies. An example here might be the provision of degrees in English or History where there are many providers.

3.5.2 Analysing competitors

Taking competition for students (for example, overseas, postgraduate) as an example, an HEI should want to be able to answer the following questions about its competitors:

- Which HEIs are we competing against?
- How do we compare in terms of student numbers?
- What programmes do our competitors offer and how do they differ from ours?
- What are their admissions criteria?
- What is their financial position?
- What are their strengths and weaknesses (for example, external quality assessments)?
- What are their prices/pricing strategies?
- Is this a key strategic market for them (for example, what proportion of total student cohort or income)?

3.5.3 Assessing market position

Once analysis of competing HEIs has been undertaken, an HEI should undertake a full and frank evaluation of how it ranks in comparison to them. This is partially and necessarily a subjective exercise and should be closely linked to the HEI’s marketing strategy which should have identified its own strengths and weaknesses. A framework for analysing an HEI’s market position vis-a-vis its competitors is set out below:

- **Market leaders** – these are the acknowledged dominant HEIs in a particular programme or market segment. Leadership could reflect size of market share or perceived quality.
- **Challengers** – these are ‘second place’ HEIs, often characterised by an aspiration to become market leaders. These HEIs may well have ambitious plans for expansion.
- **Mainstream** – often the majority of HEIs in a particular market will occupy this position. Characteristics can include difficulties in maintaining market share and perceived significant barriers to growth (for example, if an HEI appears in the lower quartile of a national ranking).

- **Niche players** – HEIs which may serve a particular niche or specialist market that are not well served by other HEIs (for example, third age programmes or specialist postgraduate qualifications).

Case study: The recruitment of overseas veterinary medicine undergraduates

The University of Oak has a prestigious veterinary school and about 20% of its annual student intake is from overseas. The University is aware that this represents the largest number of overseas intake in all the UK veterinary schools and that the fees charged by the other veterinary schools are all broadly similar. The income from these students is important and it is perceived to help subsidise the costs of educating UK undergraduates. The University believes it is clearly important that the Oak veterinary school maintains its dominant market position and indeed has requested a report on the feasibility of increasing the share of the overseas student market. The University's finance department has calculated that to increase to 30% the total annual intake of these students would generate additional income to offset a reduction in fees of up to 15%. Any increase in fees below this would, therefore, result in additional net income.

However, the Dean and his colleagues at Oak veterinary school are unsure about how they should approach this matter. They believe that there is the possibility of growth in the overseas student market for UK veterinary schools but realise that any increase in market share may be at the expense of the other veterinary schools. They are concerned about how the other schools might react.

This is a complex scenario and requires analysis of a number of factors in order that an informed decision can be made. One of those factors is a detailed understanding of the other UK veterinary schools' position, and using this knowledge to assess whether a reduction in fees (price cut) would lead to a change in their behaviour and a consequent counter move to protect their own position. In the longer term it may well be that Oak veterinary school's best option is to seek competitive advantage and focus more closely on meeting the specific needs (academic and non-academic) of overseas students to such an extent that the school may well look to increase its fees. That is to say that additional income would be generated not from increasing market share but ensuring that the value perceived by the potential student is such that he or she will be prepared to pay a premium to attend the school.

3.5.4 Data collection

In many situations HEIs may be faced with a large number of potential competitors, and gathering information on each would be unfeasible. In these cases a judgement needs to be made as to whether some broad assumptions can be made about competitors based on evidence collected from a sample. As in all cases of data collection, knowledge from the HEI's own staff should not be overlooked and should be welcomed as a potentially rich source of information.

Competitor data collection

Key issue	Possible sources of information
Who are the key and current competitors?	UCAS; Advertising by other HEIs; Surveys of potential, current and previous students and customers; HESA statistics.
What prices are charged by competitors?	Targeted research; Advertising and publications produced by other HEIs.
How important is the market to competitors?	Targeted research; Analysis of financial statements, student numbers, strategic plans (if available); Intelligence from new staff.
What are the competitors' strengths and weaknesses?	Any externally published qualitative assessments (for example, league tables); Surveys of potential, current and previous students and customers; Intelligence from new staff.

3.5.5 Data analysis

Information on competitors can be useful for a number of purposes. However, in relation to pricing it should be used to help develop an informed judgement of the following:

- How might competing HEIs react to potential pricing moves and what action by them may result?
- What aims (for example, market share, financial return) can the HEI reasonably set itself given the competitive environment in which it operates?
- How can the HEI best insulate itself from actual or potential competitive threats?
- Is it viable for the HEI to continue to operate in this market in the long-term?

3.6 Other factors

Beyond the specific factors described above there are likely to be a number of other factors which may impinge on pricing decisions in HEIs. These may include legal, political, ethical and other considerations. Such factors may be relevant to many different types of organisation, both public and private sector, but they are especially relevant to HEIs because HEIs receive large amounts of public funding and have a strong degree of public accountability for their activities and their use of public funds.

We outline below some examples of the key issues involved.

3.6.1 Avoidance of unfair competition

HEIs need to avoid any charges of unfair competition. Firstly, HEIs need to avoid any accusations of forming cartels with one another and running the risk of breaching competition legislation.

Secondly, in making unilateral pricing decisions, HEIs need to take care to ensure that they do not put themselves in a situation where they may be accused, by other organisations, of unfair competition through the use of a public subsidy. This situation can exist where HEIs provide goods and services to customers at a price below total cost with a subsidy being provided through public funds. The financial memorandum of HEIs requires them to base prices for goods and services on the full costs of provision unless there are good reasons for doing otherwise. Failure to do this may have legal and political implications. HEIs that decide to price goods and services below total costs must have a robust and defensible case. Failure to do this could result in some form of investigation being conducted resulting in embarrassment to the HEI concerned.

Case study

Lakeland College, which is situated in an area of outstanding natural beauty, offers holiday packages in the summer months involving accommodation and catering. Since it already employs cleaning and catering staff in the summer months it decides to price the holiday packages at below total cost. This substantially undercuts the rates charged by local hotels and guest houses.

The local chamber of commerce representing hoteliers complains to its MP about this practice since it claims the college is using public funds to subsidise its activities and thereby undercut local traders. The MP raises the matter in the House of Commons and the college is subsequently the subject of numerous investigations and critical press comment. Relations with local traders are also damaged.

3.6.2 Minimisation of risks to public funds

Vice-chancellors and principals of HEIs are ultimately accountable to Parliament for the financial health of their HEI and for their use of public funds. Failure to do this can result in all sorts of public and parliamentary concerns and, in extreme cases, in investigations by the National Audit Office and the Public Accounts Committee. In making pricing decisions HEIs need to ensure that not only are they not planning to use public funds to subsidise the delivery of the goods and services involved, but also that there is minimum risk to public funds should some problem arise in relation to the activities involved. Before embarking on a particular venture, HEIs need to have conducted a thorough risk analysis of the venture and have identified means of minimising the risks involved and of dealing with unforeseen events should they occur. This would include the identification of a source of non-funding body funds to meet any financial problems that arose.

3.6.3 Fair access to goods and services

The pricing of particular goods and services may have implications for the degree of access for different individuals or organisations to the goods and services involved. A price which is too high may inhibit access for certain individuals and organisations, and examples are described below:

- access to the good or service by particular groups of individuals may be inhibited (for example, the unwaged);
- access to the good or service by particular types of organisation may be inhibited (for example, charities);
- access to the good or service by particular overseas countries may be inhibited (for example, developing countries).

These considerations may be of little relevance to a commercial organisation but they may be of relevance to an HEI which receives large amounts of public funds and has a high degree of public and political accountability. Any concerns in this area may lead to substantial public concern and bad publicity for the HEI involved.

Case study

The health studies school of Cedardale University runs a series of training programmes on mental health issues for local organisations. Such programmes are open to staff from any organisation with an interest in mental health issues. The School has agreed a price with the local mental health NHS trust for places on the training programme, and places on the programme are offered to other organisations at the same price. The price charged covers the full costs of the programme plus an acceptable profit element.

The places on the training programme are occupied entirely by staff from the mental health trust and from private sector providers of mental health services. No representatives from the voluntary sector have attended and a substantial number of complaints have been received from local mental health charities. The charities claim that the price charged for places on the training programme is prohibitive and that they do not have the resources available to finance such activities. They accuse the university of failing to take account of the needs of the local community and the voluntary organisation sector. They also point out that they have been active collaborators in University research projects at no cost to the University.

The pricing policy of the HEI may need to take account of the impact of its prices on access for different segments of the community. To ensure that a reasonable degree of access is provided across the customer base, it may be that some form of tiered pricing arrangements, with differential prices being charged for different groups or individuals, would be appropriate. However, such a differentiated pricing arrangement should avoid the use of any form of subsidy from public funds as described earlier.

The HEI will need to review its pricing policy; it may be that in some instances there is a strategy not to target particular groups or individuals. The HEI will need to consider the implications of this decision both in legal terms and public relations terms. Having considered these factors, reducing access to certain services may be a deliberate and valid part of the HEI's strategy.

3.6.4 Service delivery vehicle

In delivering goods and services to customers, HEIs may use a number of different delivery vehicles:

- direct delivery by the HEI itself;
- use of an HEI owned company;
- use of an HEI trust;
- partnership with other HEIs or other organisations.

These different delivery vehicles will have different commercial and taxation implications and so the pricing decision may be influenced by the type of delivery vehicle actually used.

3.6.5 Data collection and analysis

The factors discussed in this section are essentially 'soft' in nature and do not easily lend themselves to data collection and analysis techniques. However, some points of guidance for HEIs follow:

- The need for HEIs to have robust procedures for dealing with certain issues (for example, risk management, intellectual property rights. This will be discussed further in Module 6).
- The need for HEIs to ensure the availability of specialist advice (for example, legal advice) where required.
- The need for an HEI to demonstrate sensitivity in relation to its local community.
- The need for HEIs to demonstrate probity in the use of public funds.

Module 4 Developing pricing decisions

Aims

By the end of this module you should understand:

- the different pricing strategies that can be employed in a market;
- the range of common pricing tactics used to target particular customers.

Structure of this module

Module 2 explained the position of price in the overall marketing plan and Module 3 looked at some of the key information needed to make an effective pricing decision. This module aims to give the reader guidance on how the information and analysis should be integrated and used in developing a pricing decision.

The module looks at some general approaches to pricing in a market based on the relationship between price and value (to the customer). This provides a strategic framework for HEIs to plot the outcome of their analysis and broadly consider which pricing strategy will meet their particular objectives in a given market.

The module then considers more specific pricing tactics that can be employed to meet the needs of customers or segments of customers. Customers are not wholly homogenous and HEIs need to think of their pricing tactics in terms of the individual segments of a market within the context of their overall (strategic) approach. The marketing officer in an HEI should be able to assist in identifying the individual segments of the market.

4.1 Strategic pricing approaches

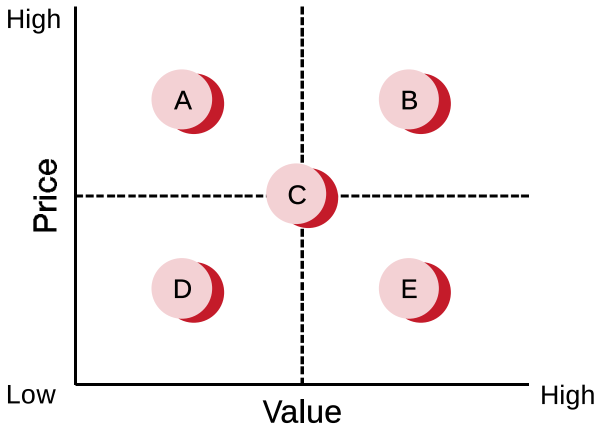
The first point to make is that pricing is not an end in itself but an ongoing process that needs to be continually revisited and reviewed. It is one of the dynamic components of the marketing mix, and as such will be closely affected by other elements such as promotion, distribution and the features of the market itself (see Module 2). Therefore, a pricing decision is part of a continuous loop.

Developing a pricing strategy should not be an overly complex or laborious task. Based on the knowledge acquired it should be possible to make an informed judgement on how a market will react to different prices. The selection of a correct pricing strategy for an HEI will require the integration of the analyses conducted in Module 3. There is not a ‘right’ strategy for every situation or market, and deciding the correct pricing strategy should be seen as a further step in a continual process rather than the finishing line. A pricing strategy will need to be constantly reviewed in line with the other elements of the marketing plan.

HEIs should be looking to develop p*rice-benefit* strategies that seek to balance the outcomes of the analyses in relation to customers, costs, competitors and corporate objectives. The diagram below provides a basic framework on which HEIs can plot their own pricing strategies for a particular market based on the knowledge they have now acquired. This approach is centred around the relationship between price and the value of the good or service as perceived by the customer. HEIs should be looking to develop pricing strategies for each of the main markets they serve.

If you are unsure about whether your HEI has sufficient knowledge to prepare a pricing strategy for a market, revisit the issues raised under **'data analysis'** headings in Module 3. If you are confident that the HEI can address most of these issues then you should be able to complete a price-value strategy.

Pricing strategies



The diagram illustrates the positioning of five different pricing strategies, A-E. In reality HEIs may want to be more precise about exactly where they wish to position their pricing strategy on the price-value matrix. However, as guidance the five different strategies illustrated above can be defined as follows:

4.1.1 Case A: High price/low value

A pricing scenario where customers are paying a high price for something that they do not perceive as having a particularly high value. This segment is only likely to appeal to a small number of buyers and is sometimes referred to as 'skimming' pricing – designed to capture high financial margins at the expense of high volume. Organisations who are in a monopoly can also operate with this pricing strategy.

4.1.2 Case B: High price/high value

Here the product or service is positioned at the 'top end' of the market. An example in HE would be a prestigious MBA course, the student may place a high value on the course in terms of an expected increase in earnings on graduation. The price of the MBA will reflect its perceived high value by the customer.

4.1.3 Case C: Mid-point

This can be described as an offer of reasonable value to the customer for a reasonable price. Although many HEIs may not wish to admit they occupy this position, the careful analysis already undertaken (see Module 3) may well lead them to adopt this realistic position. An example may include conference facilities of an HEI which, although are well equipped for most events, are also situated in an unattractive environment and as such will struggle to achieve the label of 'state of the art'.

4.1.4 Case D: Low price/low value

A situation of medium to low value to the customer is not necessarily synonymous with low quality, remembering that value is the economic (or exchange) value perceived by the customer as compared to similar offers. An agricultural college, for example, may find itself with a surplus of produce which it needs to sell quickly and therefore will adopt a low price strategy for a product which customers could easily obtain elsewhere.

4.1.5 Case E: Low price/high value

A scenario in which it appears an organisation is prepared to offer a price below the value perceived by customers. This is not necessarily marginal cost pricing because this is based on customer's value and not cost. This is sometimes known as 'penetration' pricing and is usually a strategy employed to quickly gain market share or volume. An example of this strategy occurred in the early 1990's when there was rapid student expansion. Since this time many HEIs have moved towards partnership and therefore may be less likely to take this competitive penetrative stance in the future.

It is important to remember that these strategies should be taken in context. We are defining prices in relation to their value. Although prices may be designated as low to medium in value, they are not necessarily cheap but are low relative to value. Perhaps the best way to illustrate this is by taking an example from the motor car industry. There are examples (mainly from Japanese manufacturers) of some cars which have penetrated the lower price end of the luxury car market and have been successful because customers perceive them offering exceptional value despite a price that many people would still find expensive.

4.2 Adopting a pricing strategy

Understanding the behaviour of customers and competitors is of critical importance, which is why an effective pricing strategy can only be prepared once the necessary preparation, research and analysis has been completed. For example, an HEI that wishes to move from quadrant D towards the position marked C will need to know how customers will react to an increase in price and what other compensating measures may need be needed (such as a refreshed or new branding, or the introduction of new facets or benefits). How will competitors handle an HEI entering into a new market at position E and undercutting their price?

Case study: Price strategy on entering a new market

Sycamore University College of Art and Design has a strong reputation for delivering high-quality undergraduate and postgraduate courses. Each year, the number of applications from students significantly outweighs the places available. It has recently decided to offer a new part-time distance learning postgraduate course in computer aided design aimed primarily at small businesses and the self-employed within the graphic design sector. A key feature of the new course is that the resources and tutorial support will be delivered via the Internet.

The College has decided that for the first three years intake will be limited to 50 students per year. Initial market research has shown that there is potentially strong demand for this programme. It is anticipated that applicants will come from two sources – those who would otherwise attend a similar course at a non Art and Design HEI and those who would have previously not considered the benefits of such a programme.

There are some set-up costs, most notably the recruitment of one new senior member of staff and two administrative staff, preparation of the materials and development of the web site.

As this is a new market, it is not perceived that any immediate competitive threat will emerge. It is intended that the programme will generate a financial surplus and will further strengthen the College's position as the UK's leading Art and Design HEI.

Sufficient market research has been undertaken to determine demand, and the programme fits in with the College's overall strategic direction and the competition seems at this stage to be limited. The College's analysis has also shown that the market has limited price sensitivity because the customers place a high value on the product's differentiating attributes.

The aim is to generate a surplus within two years (i.e. in the third year a surplus will be generated after set-up costs and annual running costs have been accounted for) and as such the pricing strategy has been set at the higher end of the market for postgraduate Art and Design courses.

Towards the end of the first three years the position would be thoroughly reviewed to determine options for increasing the numbers of students, any competition that may have emerged and the extent of further investment costs.

This case study can be regarded as an example of case B which involves a high price/high value strategy.

Case study: A reduction in price in an existing market

Elm University offers a range of degree programmes for professions allied to medicine (PAMS). It has an existing four year contract with its local health authority to deliver these programmes. This contract was difficult to negotiate because the health authority refused to accept some of the arguments on indirect costs put forward by the University when discussing the price.

The University felt that, strategically, it needed to have a presence in this growing market and is now looking to expand its provision for mainly financial reasons. It has calculated that it could take on an additional 25% of students on its programmes for only a small increase in costs and that this would make the PAMS degree programmes more cost-effective. It realises that the only way it can attract these students is by approaching one of the neighbouring health authorities.

Given that the customer appears to be price sensitive, the University recognises that it may have to offer a price incentive in order to win this business. Nevertheless it has decided that it must pursue this and is now preparing for an initial meeting it has secured with another health authority.

The obvious danger with a price cutting strategy is that competitors may also react aggressively and ultimately the accepted market price is lowered. In this case, it may in the medium-term result in a deterioration of the financial position of the HEI as the price for all its PAMS course is forced down – an example of the tail wagging the dog. A pricing strategy aimed at lowering price is probably the quickest way to achieve market growth but usually offers only short-term competitive advantage.

If we accept that the aim of pricing is to maximise the difference between the value created for the customer and the cost incurred by the HEI, it could be argued that in this case unless the University can secure additional market share while maintaining current levels of price in the medium and long-term, then it is not worth pursuing this objective. It still leaves the University with the problem of what to do with its current PAMS courses which are not considered to be cost-effective. There may be other measures which can generate additional income (for example, cross subsidies from another area of activity which generates a financial surplus – perhaps from part-time continuing professional development courses). Ultimately this is a strategic decision to balance finances, the future development of the market and the HEI's purpose and long-term goals.

4.3 Pricing tactics

So far we have looked at broad pricing strategies that HEIs may wish to adopt in relation to particular markets. However, within any market there is likely to be a range of different customers for whom different pricing tactics may have to be adopted. For example, not all customers may be aware of the alternative offers available from competitors, or others may not be bearing the full cost themselves and passing part of it onto a third party. Understanding these differences should be one of the outcomes of the analysis undertaken in Module 3. However, it should be recognised that in some markets (such as overseas students) the opportunity to segment customers may be limited, and it may be unfair to attempt to discriminate. In these cases a ‘one size fits all’ approach may by the only option.

For many markets served by HEIs (for example, research, conferences, courses for businesses, consultancy) it is possible to segment the customers and it should, wherever possible, be undertaken as part of the analysis that precedes any pricing decision.

In most markets an HEI will be faced with a number (sometimes a very significant number) of other HEIs competing for the same customers. Approaches will vary and it is important to stress again that there is no right or wrong way to reach an individual pricing decision. However, those HEIs which have a firm grasp of the environment in which they are operating will be at a considerable advantage. They will be able to set a pricing strategy which will determine how much flexibility exists for individual pricing decisions – in other words the pricing tactics that can be used to secure the objectives. All too often individual pricing decisions are taken in isolation and the (usually negative) consequences for the rest of the organisation emerge at a later date.

The following is a list of common pricing tactics that can be used, but should only be considered once the overall strategic pricing approach and marketing plan have been agreed.

- cost plus pricing;
- market-based pricing;
- competition-driven pricing;
- lump-sum pricing;
- piece-rate pricing;
- psychological pricing;
- block pricing;
- incidental charges;
- loss leaders;
- premium pricing;
- discounting.

4.3.1 Cost-plus pricing

This is probably the most common method. Calculations about cost-plus pricing differ but essentially it is the cost (however defined – see glossary at Appendix 1) of a good or service plus an element to contribute towards full costs and (or) surplus. Apart from the fact that it can be difficult to reach an agreement on what constitutes cost, this approach does not factor in customers and their characteristics. For example, irrespective of the costs associated with a particular service, what are customers prepared to pay and how will demand be affected by price?

4.3.2 Market-based pricing

This is the process where prices are set by looking at the market to be served without a strong relationship to the costs. Put simply, competitive pressures will force the price down and demand will force the price up. The market based price attempts to set the price somewhere (usually the average) between the two. However, without a fixed reference to costs there is clearly an element of risk, and the low-price culture of higher education means that to rely on just what 'the market will stand' is in most cases not advisable.

4.3.3 Competition-driven pricing

This technique is where pricing is effectively driven by what competitors charge and setting the price just over or under. It assumes that competitors are pricing accurately, and that they have done all the 'leg work' in determining a correct pricing strategy. So, on the one hand this tactic could involve less work for an HEI, and there is usually a guarantee that your price will be in the right 'ballpark'. However, it is not always easy to obtain competitors' prices (for example, a formal tender or sealed bid) and again it may be a risky strategy to follow in a low-price culture. It also assumes there are no loss leaders in the marketplace.

4.3.4 Lump-sum pricing

This is a situation where a variety of goods or services are packaged together and offered at one price. For example, a company wishes to purchase some consultancy advice from an expert at a University about the economic prospects of the South-East Asia region. The company wants the academic to address a meeting of its senior managers and facilitate a discussion afterwards. The HEI could develop a package which includes the member of staff's time and research, an appropriate venue (using the university's own conference facilities) and catering arrangements all for one price. The customer is not presented with an itemised quote, but instead an overall figure; this presents an opportunity to charge certain elements at a premium. This situation could also arise when the university is sub-contracting part of a piece of work so that the actual price agreed with the sub-contractor is not disclosed to the buyer, and if appropriate the HEI can artificially increase this cost and the final price.

4.3.5 Piece-rate pricing

Breaking a service down into, for example, daily rates is another form of pricing and is often used by HEIs when pricing their consultancy services. This has the advantage of transparency which the customer may prefer – he or she can see what they are getting for their money. In addition, charging for work on a piece-rate basis may in the end generate more income than a fixed lump-sum price. However, there is an element of risk since the customer can often 'turn off the tap' more easily under this type of arrangement and once the price or rate has been agreed there is little opportunity to move from it; this arrangement can limit the opportunities for an HEI to generate a surplus, since the work is delivered in 'pieces' and there is little opportunity to move from the agreed rate.

4.3.6 Psychological pricing

Customer responses to differences in price often depend on the absolute price being charged. For example, the opportunity to save £500 on a contract with a total price of £2,000 will usually be pursued by customers. However, the opportunity to save £500 on a £20,000 contract may not be pursued with the same vigour. Buyers tend to see price differences in proportionate (or percentage) terms rather than absolute terms, and there are likely to be psychological price thresholds to which the customers attach importance. For HEIs it may be worthwhile thinking about the effect of a series of small price increases rather than one large price increase, and conversely one large price reduction rather than a series of smaller reductions in price. There is also the well-known but apparently still valid notion of ‘odd-numbering’ prices – that is pricing goods or services just slightly below the nearest round number (£19.99 or £2,995). It relies on the theory that most people read from left to right so the first figure they see is the most significant. However, it must be true to say that the larger the item then the weaker this psychological effect. Additionally, increasing the price in order to create a perception of higher quality can be described as a form of psychological pricing (see 1.2.4 in Module 1).

4.3.7 Block pricing

This technique is sometimes used where the provider sets a single price to cover a variety of goods or services. For example, an HEI may decide to price all its academic staff at the same rate for consultancy services. Within this price there will be higher and lower cost staff but by charging just one ‘block’ price for all staff the HEI is assuming it will recover more income than it would through a range of different prices. Administration of this type of pricing arrangement is simpler, and customers may feel they are getting better value for money. However, this type of pricing is only really effective where fixed costs are higher than variable costs (for example, use of specialist equipment or premises).

4.3.8 Incidental charges

The introduction of incidental charges can sometimes generate income over and above the fixed price. For example, separating out staff travelling expenses or printing charges can be worthwhile if they are expressed as a percentage of the price (‘plus travelling and subsistence expenses not exceeding 10% of the total price’ or ‘design and printing costs estimated at 15% of the total price’). This can be risky if the customer is a sophisticated buyer and would seek to clarify these ‘grey’ additional costs.

4.3.9 Loss leaders

This is a common technique designed to attract customers in the hope that they will then continue to buy from you (at a higher price) in the future. Entering any market with a price that is not viable in the long term does present risk, and an HEI would need to feel very confident about future business to pursue this strategy. Under-pricing can also lead to similar moves by competitors.

4.3.10 Premium pricing

Setting the price above the competition is usually associated with concentrated marketing positioning the good or service as of higher quality and possibly of limited appeal. If used carefully then this pricing tactic can generate significant surpluses and at the same time make the customer feel that he or she is getting the best. However, it is a thin line between being desirable and over-priced.

4.3.11 Discounting

Much of the process of discounting is undertaken through negotiation (see Module 5). Discounting needs to be thought about very carefully and the reasons clearly understood. If discounting is a common feature at an HEI we would suggest that very clear guidelines on who can authorise a discount is prescribed (see Module 6). Above all, HEIs need to ask themselves: why are we discounting and what is wrong with our original price? The common forms of discounting are:

- **volume discounts** – a scale where the more the customer buys the greater the discount on price. For example, where an HEI offers a discount on the price it charges for the use of its halls of residence during the vacation depending on the length of the booking;
- **promotional discounts** – used where there is a need for an HEI to ‘push’ a particular good or service. For example, some HEIs may offer a discount on tuition fees charged to some of its students if they enrol by a certain date;
- **cash discounts** – frequently used by organisations in order to achieve early repayment;
- **discounts offered within a fixed price context** – for example, ‘our discounted price for this service is £ xxxx’; even though here the term discount is just used as a label and is designed as a psychological pricing tactic.

In the real world the dynamics of any pricing situation are often more complex than the theory outlined above. However, these examples serve to demonstrate that there is a significant range of imaginative pricing techniques and tactics that HEIs can use. The important point is that these must be set in the context of an overall pricing strategy within the overall marketing plan (that ultimately derives from the HEI’s corporate strategy).

Module 5 Operational pricing considerations

Aims

By the end of this module you should be able to understand:

- practical aspects of tendering and contracting;
- the importance of ensuring timely receipt of payment;
- the three key principles of negotiation;
- issues to consider in undertaking sharing arrangements;
- issues to consider in setting up or participating in incentive schemes;
- the fundamental principle of customer care.

Structure of this module

This module addresses the following practical aspects of pricing:

- content of tenders and the use of sealed bids; terms and conditions of contract; payment terms;
- negotiation;
- sharing arrangements;
- incentives for staff;
- customer care.

5.1 Tenders/sealed bids, contracts and payments

5.1.1 Tenders/sealed bids

Bidding by tender is becoming more commonplace as buyers of services seek to comply with government policy on accountability for public funds.

Under a tender scenario, the tenderer will issue an invitation to tender which lays down the requirements and objectives for the work. Tendering bodies will then reply in full to the questions asked, which range from the general (for example, 'Please outline the methodology you would use in addressing these objectives') to the specific (for example, 'Please attach a copy of your HEI's equal opportunities policy').

The tendering body will probably set criteria against which bids will be marked, and weight each criterion according to its perceived importance. Price, for example, may account for 0.3 of a score out of a total of 1, with other factors, such as the quality of the team and likelihood of delivery to timescale, making up the difference. Under a 'sealed' bid, the tenderer is bound to accept the lowest-priced bid which meets the technical criteria.

The key point to consider in writing a successful tender is to address the tenderer's requirements as explicitly and as fully as possible:

- Firstly, it can be a good idea to meet or telephone the potential client to ensure that you understand their requirements completely. Such meetings are often useful sources of additional material, for example, what the budget is, what the real agenda is, whether price is a more important factor to the client than quality, and who else is bidding.

- Secondly, if the tender documentation gives three issues which the project should address, it is often a good idea to use those issues as your structure. Most tenderers will be conducting a formal appraisal of tenders received, and they will appreciate anything which makes it easier to see whether or not you have addressed a particular point.
- Thirdly, make sure that you have complied with any ‘housekeeping’ points. If the tenderer asks for a particular number of copies of your tender, by a particular time, in a particular envelope, then you ignore these directions at your peril. Most conditions are imposed in order to ensure, and to demonstrate, that all tenderers have been treated fairly and equally.
- Finally, find out as much as you can about the competition. How many bids were sent out and to whom? What do you know about the staff involved in these bids? Never criticise your competitors explicitly in your written document or at any presentation, but if you know what their marketing stance is likely to be, and what their weaknesses are, you can point up the comparative strengths of your case without explicit and negative point-scoring.

5.1.2 Contracts

A contract is not a luxury, but a necessity. The consequences of not having a contract for income-generating work can be severe, including loss of income, loss of intellectual property rights (IPR) and liability under the law. The HEI should therefore develop short-form contracts and make them easily accessible to staff. Equally, care should be taken to ensure that staff involved, and the HEI itself, are fully covered by insurance for the work being undertaken. HEIs would be best advised to seek legal advice at the outset when dealing with contractual issues.

As a minimum, a contract will describe what is to be done, by whom, by when and detail the terms of payment. A further issue is stating the ownership of resulting IPR. The contract may refer to some of the terms in a previous proposal or tender.

In terms of research contracts, there will be explicit terms about what can be claimed for indirect costs, equipment and other matters. European Union contracts will also give prescriptive conditions. Compliance with these conditions is mandatory or the awarding body may ‘claw back’ grant paid.

The HEI may already have standard terms and conditions covering issues such as legal liability. These should have been reviewed by a solicitor when drafted, and occasionally thereafter in the light of emerging legislation and case law. The terms and conditions may not always be appropriate, therefore staff should ensure that they are familiar with the terms and conditions and understand when it is necessary to include them.

The tendering body may insist that the HEI complies with their terms and conditions as a part of the contract, or they may ask to negotiate on particular terms. Staff may be able to deal with particular issues without the assistance of a solicitor, for example, issuing payment terms. However, HEI guidance should offer staff a legal expert as a contact if more difficult issues arise.

Generally, HEIs should have published procedures on undertaking work within, and out of, normal staff contractual terms. For example, some HEIs allow staff to spend a certain number of days on personal consultancy per year. The procedures should also cover issues such as approvals and permissions required to undertake the work, protection of IPR and profit-sharing with staff. The staff member should be clear about the limits of their authority or they may risk dismissal. These procedures should follow from and complement the financial procedures that the HEI will have in place.

Staff contracts and/or appraisal documents should refer to the procedures and reflect any particular arrangements for profit-sharing, and any targets, income-related or otherwise, for which the staff member is responsible.

5.1.3 Payment

The timely receipt of funds is important for cash flow management in the HEI. Payment terms should be unambiguous and staff should keep uppermost in their minds what the ‘trigger’ event is for payment. If, for example, payment is dependent on the production of a summary report, then a summary report must be produced as soon as possible after the work is complete. If payment is to take place once the work has been completed to ‘satisfactory’ or ‘acceptable’ standards, staff should be sure they are clear what that means, and who decides when that standard has been achieved.

Part-payment throughout the life of a longer contract can help with the income stream of both parties. If a status report is required for a staged payment, then time to produce such reports should be built into the price.

Most organisations have targets for payment of debtors, for example, within 30 days. If payment becomes delayed, staff may need to involve the finance department in recovering the debt. Ultimately, specialist agents may be called in and court is the final resort. Alternatively, the HEI may decide to write off the debt. A written-off debt is a serious matter: the time and resources invested to date will have been wasted unless payment is received, and without the cash flow there may not be the money to employ staff to continue with that project or it may impact negatively on the progress of another project.

5.2 Negotiation

Negotiation is a topic in itself, but the three key points are:

- be prepared;
- aim high;
- look for a win-win.

5.2.1 Be prepared

Before entering a negotiation situation, HEIs should prepare thoroughly. In particular, before you enter the negotiation process, you should be able to answer as many of the following questions as possible.

- How much do I think is in the buyer’s budget?
- What is the buyer’s main preoccupation (which is often not price)?
- What added value am I bringing, which overrules price considerations (for example, quick delivery, sole provider of the service)?
- What concessions are we prepared to make, and what value do they have to the other party?

- What can we gain from offering concessions (for example, areas of the contract or work that we would like to see changed, flexibility over timescales, an agreement for follow-on work, joint publication of results (research contracts))?
- What will it cost me to deliver this piece of work, including a contribution to indirect costs and any surplus? How low can I afford to go? (This last point is often the first and only question staff ask, but, as the rest of this course has shown, it is not the primary question. Often, simply making a contribution to variable costs, or even a loss, is acceptable if the strategic circumstances dictate it.)
- What are the competitors' pricing strategies likely to be?
- How confident am I about my methodology and project plan? What contingency time do I need?
- What is the availability of my staff and their willingness to work additional hours?
- How important is this work to me and to my HEI?

5.2.2 Aim high

There are a number of factors or situations that sometimes occur in HEIs that you should ensure do not affect pricing negotiations and decisions.

- A pressing need to give under-utilised staff something to do. This is understandable and may, indeed, be the right thing to do, as the project will contribute to variable costs, and the HEI may have lost its last few proposals in tight negotiations through no fault of its own. However, it may also indicate a lack of 'pipeline' planning. Low pricing cannot be allowed to become the norm, or the low prices set for those particular circumstances will become what the market expects, with poor consequences for the HEI's financial health;
- The idea that under-pricing will bring increases in volume which more than make up for the lost income. Such a strategy works in markets with identical products and marketing profiles, like supermarkets, where price cuts do bring volume increases, but only in the short term. A more stable pricing strategy builds a premium image for the product and never sacrifices that quality for volume. Moreover, academic staff time is a finite, and somewhat inflexible, resource, and it is difficult to staff up and down for a short-term surge in activity. Therefore, such a model is not generally suitable for the academic field;
- A lack of confidence in one's product, and a lack of confidence in oneself, coupled with poor presentation skills, such that asking for what appears to be a large amount of money seems impossible. Assuming that you do have a good product, practice is part of the answer – making strong statements aloud about the quality of your project helps you repeat them in a real negotiation;
- A fear of what the competition will offer. Often this fear is inflated through a lack of knowledge of likely competitor behaviour and all the other issues rehearsed in the previous section. Preparation will reduce this fear.

5.2.3 Win-win

Negotiation is not war – both parties will have to work together after the event. Moreover, the project can be a very good sales tool for further work, but only if relations with the client are preserved, starting with the negotiation process. Both parties should leave the negotiation with at least some of the points which were important to them. Be realistic in your expectations and remember – competitive stances encourage competitive stances!

5.2.4 A final point

Never commit to anything if you are unsure. If this is the case always take time out, for example, you may suggest that you want to speak with a superior or a solicitor in order to gain some breathing space.

5.3 Sharing arrangements

Most HEIs have partnerships of some sort, ranging from the local further education college, to the catering company, to the overseas college with whom joint courses are delivered. Most HEIs will, therefore, already know that partnerships usually start optimistically.

In terms of sharing arrangements, the first question is what exactly is being shared, in terms of surplus, income, costs, responsibilities and intellectual property rights. For example, if surpluses are being shared, are there any management fees or other incidental expenses which the partner is top-slicing?

The following case study explores the issue of matching risks and responsibilities to reward:

Case study: Sharing risks

The University of Oakwood delivers a training course abroad in partnership with a local HEI, Beech College.

Oakwood provides the lecturer for the six-week course and provides the teaching materials.

Beech sources the students, hires the accommodation and does all administration – registration, graduation and fee-collection.

Oakwood's costs are:

Air fare =	£1,000
Hotel costs at (£50 x 6 weeks x 7 nights) =	£2,100
Teaching materials =	£500
Staff salary at (£25,000/52 x 6 weeks) =	£2,885
Total	**£6,485**

Beech's costs are:

Advertising =	£500
Administrative assistant at (£8,000/52 x 6 weeks) =	£925
Room hire =	£750
Total	**£2,175**
Grand total	**£8,660**

(continued)

Case study: Sharing risks (continued)

Therefore, costs are incurred in the ratio 75:25 Oakwood: Beech.

However, the following points also require consideration:

- Oakwood is undertaking this course primarily in order to encourage students to come to the UK for degree courses. So far, 10 students have done so, each funding their own fees.
- Oakwood appears to be paying the lion's share of the costs, but, relative to the local cost of living, Beech is, in fact, contributing a great deal more than Oakwood.
- Beech incurs advertising and other costs in advance and takes the risk these will not be recouped.
- Beech has the risk of any bad debts.
- Beech has promised to underwrite Oakwood's projected share of the profits, even if insufficient students are found to make the course profitable. This is a distinct possibility, as the course has never been run before.
- Beech is willing to do all this because the relationship with Oakwood is vitally important in terms of Beech's own image, as well as providing a source of hard currency.

The example shows that sharing arrangements can be far from straightforward. Sharing arrangements are part of the HEI's overall strategy and need to be assessed in that context. Equally, exploitation of one partner by another will not provide the foundation for a lasting partnership.

An HEI may consider undertaking a risk analysis of a shared arrangement, where probabilities are assigned to various risks and the risks are then allocated to the partners. The risks can sometimes be quantified in monetary terms.

5.4 Incentives for staff

Another form of sharing arrangement is that between an HEI and its staff. Usually, incentive payments are restricted to those responsible for bringing in the work, either by virtue of their reputation, or by direct marketing and selling. Such a payment is part reward and part recompense for sharing risks.

The potential effect of introducing incentive schemes should be studied. They may create an additional cost layer which cannot be passed onto the consumer, for no added benefit, or they may energise the entire HEI.

It is important to have clear terms for incentives. For example, where a member of staff receives a bonus out of income, rather than out of surplus, they will have no personal interest in ensuring that the project does make a surplus, rather than a deficit. The risk of deficit will be underwritten by the University, rather than shared with the staff member.

The underlying targets and incentive terms must not be too challenging, or they will de-motivate. There may, for example, be changes in the marketplace which are out of the control of the staff member. Conversely, targets which are too easy can lead to perceptions of inequity. As a related issue, incentives should not be paid as a function merely of rank, but to reward a real contribution.

Incentive schemes must be taken into account as part of the overall staff remuneration package. The targets should also be fed through into the appraisal process.

Individuals will require guidance on the tax implications of any incentive scheme. Some may wish to set up separate companies for their private consultancy income. Internal guidelines should make clear the distinction and different circumstances between private work and work conducted in the course of employment.

5.5 Customer care

Pricing is only one aspect of the art of selling, and not necessarily the most important. The heart of successful selling is customer care. As HEIs seek to raise more of their funding from non-government sources, and the environment becomes more competitive, it will become important to ensure that a customer-focused philosophy is entrenched in every aspect of HEI activity. Funding is not now, and probably never was, a natural right, but needs to be proactively sought and won against competition, time and again. Moreover, a satisfied customer is a repeat customer, and it is generally considered easier to retain existing customers than source new ones. This section draws together some previous themes and issues under the heading of customer care, in order to emphasise the importance of this issue.

5.5.1 Stage 1: Winning the work

This is the beginning of the relationship with the customer and it is therefore important to present a professional approach.

When writing a proposal to a body, for funding, or to sell a product, staff should spend some time researching the body. For example:

- What is the name of the correct person to contact?
- What projects has the body recently been involved in?
- How relevant is this proposal to this body? A wide-range ‘scattergun’ approach in proposals is often a poor use of time, compared to a more focussed approach.
- Does the body prefer proposals in a standard form, or addressing standard headings, and, if so, what are they?
- Does the proposal provide enough information for the body to judge its merits fairly? (This is particularly important when large sums are involved.)
- Are the projections of cost and timescale feasible?
- Does the proposal state the unique selling point explicitly?
- What are the risks to the HEI of undertaking this work, for example, damage to the HEI’s reputation through failure to deliver, failure of customer to pay? What are the risks to the HEIs’ reputation and financial health if this project is not won?

5.5.2 Stage 2: Conducting the work

During the lifetime of the study, the team should:

- provide status reports and other information to the customer as requested;
- communicate openly and honestly with the customer;
- allocate responsibilities clearly;
- minimise disruption to the customer from any unavoidable changeover in personnel;
- ensure the project manager has sufficient management information to keep tight control of the project;
- have scheduled internal review meetings and, if appropriate, meetings with the customer;
- only ask for additional money or time if absolutely necessary. The customer should not have to pay for delays caused simply by poor internal project management, and will dislike being held to ransom midway through a project.

5.5.3 Stage 3: Completing the work

Ensure that staff:

- complete the work to the quality standards, timescale and cost originally projected;
- provide all reports and documentation and publish the results, if required, within three to six months of completion of the work. Experience suggests that academics and academic partnerships sometimes fail to deliver in this area. Line managers should consider systems to put in place for handover of such responsibilities when staff leave, and for follow-up of staff who are behind schedule. If necessary, penalties might be imposed on staff;
- issue a prompt invoice for payment to the customer and follow-up the debt as required.

5.5.4 Stage 4: Quality assurance and sell-on

Ask the customer:

- if they were satisfied with the service and product provided;
- if you can use them as a reference site;
- if they would like to continue the project, or to progress another one with you.

If the answer to any of these question is no, find out why.

Module 6 Internal organisation of pricing decisions

Aims

By the end of this module you should be able to understand:

- the various activities which underpin pricing decisions in HEIs;
- how such activities might be organised and undertaken within HEIs;
- key controls and procedures to be put in place.

Structure of this module

This module is primarily concerned with how HEIs should put into practice the matters discussed in previous modules concerning the factors which influence pricing decisions.

In this module the following topics are addressed:

- An overview of the key activities which need to be undertaken in arriving at pricing decisions in HEIs.
- Consideration of the different ways in which these activities might be organised in HEIs.
- Identification of the key controls and procedures which should exist in all HEIs in relation to pricing decisions.

6.1 Pricing activities

The following are seen as the key activities which will underpin any pricing decision in an HEI. Not all of these activities will be conducted to the same extent in all HEIs or for all pricing decisions. However, we would expect to see some activity on each of these activities in most situations.

- **Market research** – the conduct of any form of market research to assess the likely demand for a particular good and service and the price that might be charged.
- **Financial analysis** – the identification of the costs of delivering a particular good or service, the income to be generated and the financial return to be derived.
- **Risk analysis** – the identification of the risks (financial and non-financial) associated with the proposed activity and the actions to be taken to deal with those risk factors.
- **Legal advice** – the provision of legal advice about any matters pertaining to the delivery of a particular good or service.
- **Approval** – the forum and approach for considering different pricing options and for approving the pricing decision.
- **Ex-post evaluation** – pricing decisions should be subject to some form of ex-post evaluation to judge the degree of success and the lessons that can be learned for the future. In practice the evaluation of pricing decisions will probably form part of a more comprehensive review of the whole activity.

6.2 Organisation of activities

Clearly HEIs show considerable variations:

- organisational size;
- diversity of activities;
- organisational structures;
- organisational cultures.

In the light of these variations it makes no sense to try to provide a blueprint, which would be applicable to all HEIs, for undertaking and organising the pricing activities. In reality different HEIs will have differing organisational arrangements and cultures and these will have differing degrees of centralisation and decentralisation incorporated into them. The organisation of pricing activities will reflect the existing arrangements and cultures within HEIs that can, largely, be organised according to the three different models below.

6.2.1 Largely centralised model

In this case the vast bulk of the analysis and authorisation of pricing decisions will be undertaken centrally within one or more of the central support departments of the HEI (for example: costing work would be undertaken in the finance department, market research by the marketing department with a final decision being made by a senior manager such as a pro vice-chancellor or assistant principal).

6.2.2 Largely de-centralised model

In this case the vast bulk of the analysis and authorisation of pricing decisions will be undertaken in a decentralised manner within an academic school or department. Central support departments of the HEI will provide advice and assistance as requested (for example, costing work and market research would be undertaken within the academic school or department with assistance being provided by central support departments as requested. The final pricing decision would be made by the head of school or department).

6.2.3 Mid-way arrangement

The reality is that most HEIs will probably have arrangements which fall somewhere in between the above two extremes.

Given that no blueprint can be given for organising pricing decisions in HEIs it follows that it is for each HEI to develop its own arrangements that best meet its own needs. However, it is important that a number of key controls and procedures are in place in all HEIs in relation to pricing decisions.

6.3 Key controls and procedures

Although it is not possible to set down a blueprint, applicable to all HEIs, for the organisation of pricing decisions, some key controls and procedures should exist in all HEIs. Within every HEI, the following should exist:

6.3.1 Pricing procedures manual

This is a manual which is widely circulated within the organisation and which specifies for pricing decisions:

- the various tasks to be undertaken and the individual responsibilities involved;
- the minimum standards to be applied in undertaking these tasks;
- the departments/individuals who should be consulted for advice in relation to different types of pricing decision;
- sources of internal (to the HEI) advice and information on pricing matters (for example, intranet sites);
- sources of external (to the HEI) specialist advice where required (for example, specialist legal advice or Internet sites in relation to matters of IPR and patents);
- the levels of authorisation needed for making pricing decisions.

6.3.2 Costing guidelines

A set of guidelines outlining the methods to be used for establishing the total costs of proposed activities. These should be developed and approved by the director of finance of the HEI.

6.3.3 Internal audit review

The internal audit plan of the HEI should incorporate a periodic review, on a sample basis, of how pricing decisions were made in the HEI, any weaknesses found and recommendations for improvement.

The production of these controls and procedures will not be enough to secure improved pricing practices in your HEI. These are the tools, but they will not be sufficient if they are not used. Change will not occur immediately; repeated dissemination of the importance of correct pricing and the benefits to be retrieved, along with training colleagues in pricing activities, will come some way toward the culture change many HEIs will need. Furthermore a number of senior ‘champions’ in an HEI will substantially help in turning people’s minds to the importance of correct pricing.

Appendix 1 Glossary

break-even: where the price set/income achieved has successfully covered costs and any more income would be surplus.

clawback: when the funding body has the right to take back funding due to poor quality or because the funds are unspent or were not spent on the objectives specified.

contribution: the arithmetical difference between price and variable costs incurred implying a contribution towards fixed costs and surpluses.

cost-plus pricing: this can be either based on marginal or full cost. In marginal cost-plus pricing, the cost-plus element can be set to contribute towards full costs and surplus to a greater or lesser degree, depending on the strategic aims and objectives of the HEI.

distribution: the various means of getting products and services from the supplier to the customer.

fixed costs: costs which do not alter with changes to the volume of activity.

marginal (or variable costs): the additional costs incurred as a consequence of increasing activity level.

marketing mix: the four components of a marketing strategy: product, price, distribution and promotion.

promotion: the various means of promoting sales of products and services.

transfer pricing: the price paid for one department to do work for another within the same organisation. This should be set in the interests of the overall organisation, not either department's perceived financial performance.

Transparency Review: the exercise undertaken in HEIs to identify the costs of teaching, research and other activities.

Appendix 2 Further reading

- Management Information for Decision Making: Costing Guidelines for Higher Education Institutions, UK HE funding bodies, 1997 (available from the HEFCE)
- Costing, Pricing and Valuing Research and Other Projects, CVCP, 1998
- Transparency Review of Research: Proposals for a new uniform approach to the costing of research and other activities in universities and colleges of higher education, JM Consulting, 1999
- Transparent approach to costing, Volume I: Overview and implementation pack and Volume II: Reference manual, JCPSG, 2000
- Costing and Pricing for Decision Makers in Higher Education, User Guide, JCPSG, 1999
- Value Pricing, T. Fletcher and N. Russell Jones, 1997
- The strategy and tactics of pricing, T. Nagle and R. Holden, 1995
- Marketing, G. Lancaster and P. Reynolds, Macmillan Press, 1998
- Quality in Public Services, L. Gaster, Open University Press, 1995

Appendix 3 Pricing checklists

Key questions	YES	NO
Module 1: Introduction		
Have you considered and listed the external and internal factors that may impact on your pricing decision?		
Module 2: Strategic pricing and marketing strategy		
Have you read the marketing strategy relevant to your pricing decision?		
Have you read the corporate strategy and business plan(s) relevant to your pricing decision?		
Have you spoken with your HEI’s marketing staff to see what further assistance/information they can provide?		
Module 3: Key pricing factors – corporate strategy		
Have you identified how your pricing decision fits with your HEI’s corporate strategy?		
Have you resolved any conflicts between the HEI’s corporate objectives and your (your department’s) financial objectives?		
Module 3: Key pricing factors – customers		
Have you identified your potential customers for your product?		
Have you segmented your customers in order to consider if different pricing strategies are relevant for different customer groups? Seek assistance from your HEI’s marketing staff if you are unsure.		
Have you collected and analysed any available data from the HEI’s market research staff on your customers?		
Have you used the above information to inform you of the value each customer group will attribute to purchasing your product?		
Have you used the above information to consider the pricing factors that affect each of your target groups?		

Key questions	YES	NO
Module 3: Key pricing factors – costs		
Have you calculated the direct and indirect costs of the product?		
Have you decided if you want to make surplus and at what percentage?		
Have you decided if it is appropriate to use marginal cost or total cost to set the price?		
Have you established the break-even position?		
Module 3: Key pricing factors – competition		
Do you understand the market for your product?		
Have you identified your competitors in the market?		
Have you assessed your market position through collection and analysis of data and information?		
Module 3: Key pricing factors – other factors		
Have you consulted your HEI's solicitor where you believe there may be a risk of an accusation of unfair competition?		
Have you carried out a risk analysis and identified means of minimising any risk to public funds?		
Have you considered if the price enables access to the product? If the price precludes participation from certain groups ensure this is in line with your HEI's corporate strategy.		
Have you identified the 'delivery vehicle' (for example: HEI, HEI trust, HEI owned company)?		
With the 'delivery vehicle' identified, are you clear about the financial implications of that vehicle? Consult your HEI's finance office if you are unsure.		
Module 4: Developing pricing decisions		
Are you clear about which pricing strategy you should adopt?		
Have you identified your pricing tactics?		

Key questions	YES	NO
Module 5: Operational pricing considerations		
If you are setting a price for a tender proposal are you familiar with the tendering process?		
Have you considered a contract for your product?		
Have you consulted your HEI’s solicitor on the content of the contract?		
Where relevant have you considered the ownership of any resulting intellectual property rights from the product?		
For research contracts are you familiar with any relevant prescriptive conditions or explicit terms?		
Have you read and abided by your HEI’s procedures and guidelines documents?		
Have you set out terms for payment?		
Module 6: Internal organisation of pricing decisions		
Are you familiar with all of your HEI’s pricing controls and procedures?		
Are you familiar with your HEI’s costing guidelines for pricing purposes?		
Have you followed these guidelines in setting a price?		