

THE COST PROJECT

AGB An initiative on college costs.

What Boards Are Doing — and Not Doing — in Reviewing Institutional Costs

By Jane V. Wellman

College costs—how money is spent as opposed to where it comes from—have received relatively little attention compared with other aspects of higher education finance. Instead, most media and policy attention has been focused on rising tuitions, the intense competition for admission to selective institutions, the complex system of financial aid, and the eroding share of public revenues going to higher education. These concerns are leading to a renewed focus on institutional spending—and whether more can be done to manage costs without compromising quality or access.

Cost management does not necessarily mean cost or price control, though reducing the rate of growth in spending will help take pressure off needs for continuous increases in tuition or other revenues. It does, however, minimally mean

that decisions about spending are informed by data about how revenues are used in relation to the institution's mission. And it means that oversight of costs has been added to the public accountability agenda for governing boards.

Despite the prominent role of governing boards in financial oversight and strategic planning, little is known about (1) how most boards oversee college costs, (2) whether their role is as effective as it could be, and (3) how their effectiveness might be improved. To answer such questions, AGB conducted focus groups and interviews with board members and college presidents about the board's role in cost oversight, followed by a national survey of chief finance officers to learn more about the cost information they actually are presenting to board members and the

types of discussions they have with their boards about institutional costs.

The focus groups showed that the majority of board members and presidents are very concerned about long-term funding trends and believe that board-level review of spending will help strengthen public accountability for effective cost management. Most board members said they believed they were not effectively engaged in cost review, though they did pay a good deal of attention to different aspects of finance.

Along with presidents, they believe that proper board oversight of spending can help serve as a more robust basis for planning and strategic thinking about options and directions. At the same time, neither

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presidents nor trustees want to see boards engrossed in accounting details or invited to micromanage resources. And they worry that any expansion of cost review needs to take into account already-heavy agendas that put great time—and spending—pressure on staff and board members.

Co-sponsored with the National Association of College and University Business Officers, the Web-based survey asked CFOs

about the types of information they provide their boards in the following areas: (1) the depth, breadth, and extent of cost-related reporting, to see what kinds of information about costs are presented to boards; (2) the use of benchmarks and/or standard reporting formats in material presented to the board, to get a sense of how the issues are framed and whether costs are put into a context for the board; (3) the application of data to board decision making;

(4) CFOs' perceptions about the issues, the board's role, and obstacles to more effective board oversight of costs; and (5) advice about best practices.

Chief finance and business officers were surveyed, rather than board members themselves, because these officials are in the best position to be specific about the subtleties of these topics. CFOs also have access to information that has been presented to the board and its subcommittees across several years and thus are more familiar with the entire cost landscape than those who see only pieces of it.

A short overview of responses follows, with comments that were volunteered in open-ended areas of the survey shown in sidebars.

■ Almost all CFOs (95 percent) reported some type of cost data to boards.

■ The majority said they reported aggregate expenditures, not performance-related measures (such as costs per student or per degree, or cost data in comparison with other institutions). Even for such basic measures as cost of instruction per FTE student, less than one-third of private institutions, and just over one-third of public four-year institutions, reported these data to their boards.

■ Benchmarks and comparisons are common tools, but these are used primarily for faculty salary comparisons, tuition setting, and tuition discounting. Even in these key areas, CFOs reported they rarely shared cost comparisons over time or

About The Cost Project

This paper is the third in a series of reports and initiatives in AGB's Cost Project. Supported by a grant from the Robert W. Woodruff Foundation and a planning grant from the Lumina Foundation, the project is designed to build governing board capacity to monitor institutional costs effectively and strategically.

Costs and productivity are not new issues in higher education. AGB and its member governing boards have long recognized the importance of responsible stewardship of institutional resources as central to the work of effective boards. But the rapidly changing environment in higher education has brought a new urgency to the topic. Many institutions have been at the forefront of change, having reengineered core functions and decentralized responsibilities for resource management. The Cost Project intends to identify such successes and promote them broadly within the higher education community.

AGB is mindful that containing costs and sustaining quality require active partnerships among institutional leaders and others in the higher education and public-policy communities. A comprehensive effort needs to be built—to forge partnerships, to make the conversation more data-driven, to connect better with public audiences, and to find strategies to reach out to accreditation agencies and others concerned about ways to sustain quality and improve institutional effectiveness. While institutional chief executives must lead such efforts, boards should be actively engaged in these issues. Encouraging and enriching this process are goals of The Cost Project. As it continues this work, AGB will collaborate with other groups interested in contributing to the agenda.

Details about the project, additional readings, and updates on current research are available at www.agb.org/cost.

projected them forward to see future consequences of current trends.

■ The predominant use of cost data was limited to budget decisions and less often to address strategic issues. That is, trustees see expenditures for the previous period and requests for the ensuing period, but nothing that places expenditures in a larger context. Cost data rarely were used in program reviews or in board discussions about program expansions or eliminations.

■ Less than 25 percent of CFOs saw cost management as a high priority for their boards—though a majority said they believed it will become more important in the future.

■ Less than 25 percent of CFOs reported using a standard cost methodology (such as the NACUBO, Kansas, or Delaware Cost Project methodologies), which would allow

comparisons with other institutions.

■ Board review of cost-related information typically was split among committees and subcommittees by decision area, and such decisions often were made in isolation. That is, tuition levels were decided separately from faculty salaries, and capital outlays were decided separately from operations. And the finance committee generally reviewed financial data separately from budget and planning committees.

■ No major differences

were discovered in the patterns of reporting between public and private four-year colleges, though community college CFOs reported presenting more detailed information about instructional costs and other expenditures to their boards than the other sectors. There was more reporting about co-curricular expenditures among private four-year institutions than among public-sector institutions, perhaps reflecting the residential character of the former. Curiously,

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About the Survey

The survey was sponsored and conducted by AGB in collaboration with the National Association of College and University Business Officers (NACUBO). The survey population included 2,131 CFOs, drawn from member institutions of AGB and NACUBO, stratified into groups of public four-year, public two-year, and private two-year and private four-year institutions. The survey was administered online over four weeks from December 15, 2006, to January 15, 2007. The survey was preceded by a letter to AGB-member presidents, informing them of the survey and inviting questions about it.

Responses were received from 733

institutions—about 26 percent of the survey recipients (after correcting for duplicate responses and undeliverable e-mail). Response rates were highest (50 percent) among the “administrative units” (system offices), followed by 32 percent for private four-year institutions, 22 percent for public four-year institutions, and 18 percent for two-year institutions, both public and private. Responses from private two-year institutions were excluded from the subsequent analysis because of the small number in this category. The remaining groups are statistically valid for the sectors as a whole.

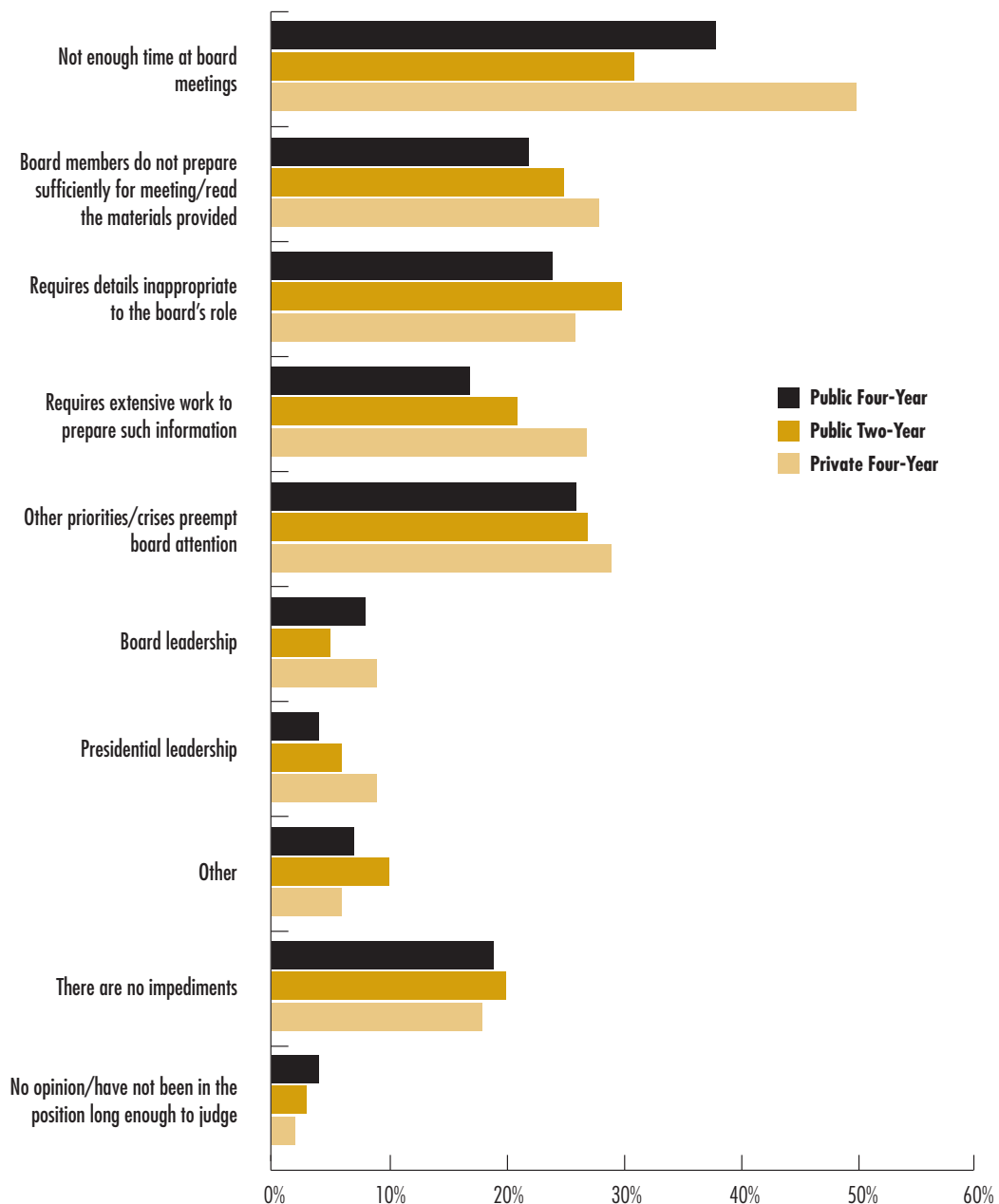
spending on athletics received the most attention in the public two-year sector—the group least likely to have significant activities in this area. Just over one-third of four-year institutions reported any type of cost information on athletics to

their boards. Even fewer reported on indirect administrative costs and how those compare with other spending priorities.

CFOs who reported to their boards on costs also seem to be relying primarily on annual and

historic data, with relatively sparse use of forecasting trends to see emergent patterns. And the trend data presented generally were aggregate spending figures—not contextualized information about performance patterns, such as

WHAT ARE THE IMPEDIMENTS, IF ANY, TO YOUR BOARD'S UNDERSTANDING OF COST ISSUES?



spending per student or trends in broad categories of spending such as student recruitment, fund-raising, athletics, or instruction.

CFOs also were asked to rate the levels of involvement of their boards in overseeing costs as well as the effectiveness of their institutions in managing costs. Just 15 percent said their boards had a “high” level of involvement in overseeing costs; 38 percent saw board involvement as “medium”; and 46 percent said it was “low.”

of public two-year college CFOs. These figures are in contrast with the roughly 20 percent from all sectors who said no impediments existed to board engagement in cost oversight and the approximately 10 percent of public and private CFOs who said lack of board leadership was the greatest barrier to broader board engagement. Because responsibility for setting board meeting agendas is shared by presidents and board leaders, this suggests that leadership may be more of an issue than is

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In contrast, fully 58 percent rated their institutions “high” in their effectiveness in managing costs; 38 said percent “medium”; and 5 percent said “low.” Almost all CFOs from institutions that rated their board’s involvement as “high” assigned a high rating to institutional effectiveness in managing costs.

CFOs also were asked to indicate what they perceived to be barriers to greater board engagement on costs. “Not enough time at meetings” was mentioned by 54 percent of private college CFOs as a barrier, in contrast with 44 percent for public four-year CFOs and 33 percent

commonly perceived. The lack of time at meetings also may reflect the relatively large size of private college boards and their less frequent meetings, compared with public institutions. (The chart on page 4 shows the various impediments to board engagement in cost oversight.)

Finally, respondents were asked to answer open-ended questions about strategies they successfully have used to control costs, offer suggestions about ways to improve board understanding of costs, and identify barriers they face in working with their boards on costs. These comments in accompanying sidebars

Comments From CFOs About Impediments to Better Board Understanding of Costs

- As new members come on the board, they’ll need to better understand the distinction between higher education budgeting and corporate budgeting.
- Cost data that we collect are not relevant to most policy issues. These are accounting data, not decision-making data.
- Inconsistent accounting presentation and reporting standards prevent a “clean” comparative data point for peer comparisons.
- Members of the board who have taken an interest in costs have preconceived notions about the data, perhaps because of their business backgrounds. As a result, their minds are not open to the data, and their approach to cost containment is simplistic.
- The issue of cost has become a political one.
- The most significant impediments are (1) that it is counterintuitive to board members that cost exceeds price, (2) faculty cannot easily be terminated, and (3) it is not unusual that staff employees outnumber faculty.
- We need to upgrade our administrative data system and hire an institutional effectiveness professional to provide consistent, accurate, and timely information to our board.

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offer advice about strategies to address these issues.

**PUTTING IT TOGETHER:
DIAGNOSING BOARD CAPACITY FOR
COST REVIEW AND STRATEGIES FOR
IMPROVEMENT**

Boards can and should play a stronger role in setting the agenda for oversight of institutional costs. Some already are doing this work, but in most cases board participation in cost oversight is narrow and technical, not strategic. Their involvement also may be poorly contextualized, either by

way of reference to other institutions or, more important, in relation to quality and value.

Board members say they don't get the “big picture” and look only at pieces, and the responses from CFOs suggest they are correct to feel this way. Too often, the perspective is cramped, inward-looking, and inadequate as a basis for planning or strategic thinking about options and directions. And the focus on annual budgets and incremental funding strategies keeps institutions from setting a strategic direction with cost

Comments From CFOs on Best Practices Leading to Cost Control

There were nearly 400 comments from CFOs regarding the best board and administration actions for controlling costs. In order of greatest frequency, these involved budget planning and management; salary, benefits, health care, and medical insurance; tuition, fees, and discounts; energy and utilities; and benchmarks, measures, and peers. Not surprisingly, these categories reveal some of the biggest cost drivers and best tools for addressing them. Here is a sample of the actions taken:

- Joined a consortium for health care.
- Ad Hoc Committee on Purchasing and Cost Containment combined purchasing power of universities in system. Saved over \$2.5 million in energy and utilities and \$2.2 million in IT over two years.
- Stopped building automatic cost inflation into every area of the budget.
- Reviewed vendor contracts—saved over \$200,000 annually.
- Started projecting budgets forward three years—helped to see patterns and trouble spots.
- Set outward limits on tuition; reframed expectations about future funding initiatives.
- Restructured debt portfolio—reducing annual interest by \$10 million per year.
- Committed to an energy conservation plan—reduced fuel consumption by 30 percent.
- Internal reporting mechanism presented fully burdened bottom-line financial information for each major academic division and program. Financially stressed programs are especially scrutinized relative to the mission of the institution.
- Updated strategic plan and linked it to rolling five-year financial budgeting model.
- Decided to manage down the tuition discount rate. We're higher than peers and the national average.

containment balanced against other institutional priorities.

In higher education, the tradition of focusing on revenues and growth is strong; countering such customs to bring attention to cost management will require discipline and an institutional commitment to a long-term agenda. The information presented in this analysis suggests that most institutions are still a long way from doing that, at least insofar as their boards are aware.

Of course, presidents and senior administrators of most institutions are doing a good deal more to review and control costs than what they report to their boards. It also may be the case that board involvement in cost oversight is not necessary for an institution to manage costs effectively. But boards can bring a badly needed perspective to this conversation if the information they are provided goes beyond accounting details to reveal a more comprehensive picture about spending patterns, quality, and value. In so doing, boards will be better institutional stewards and a bridge between internal and external accountability.

The board's role should be as a monitor of spending in the context of value and future capacity—not as a micromanager of fiscal decision making or mere reviewer of accounting information. For institutions that are not doing so already, organizing information in a language and format appropriate for board engagement will require deeper work to analyze patterns of

Advice from CFOs About Board Engagement in Costs

- Transparency is always best.
- Setting up the context is critical, with senior colleagues and the board.
- Identifying the key trade-offs and being open about the information are crucial to gaining confidence, respect, and support from colleagues in particular.
- Be patient and take the time to explain costs and how they relate to performance.
- Identify and measure cost drivers.
- Develop benchmark data using a close set of peers.
- Educate board on “business model”—student/faculty ratio, full-time/adjunct faculty, cost per discipline, tuition discounting, cost per recruitment.
- Spend time with key board members to enlist their assistance in explaining the complexity of the university cost structure to fellow board members. Don't make excuses for rising costs, but do take time to explain cost drivers that are unique to higher education.
- Link year-to-year budgets with factors and goals of the strategic plan. Make sure all strategic plan objectives have action plans that detail costs.
- Find ways to look out five years—look at relation of price/discounting/revenue/quality/market.
- The CFO plays a key role in working with the president and board chair on cost issues, determining what the board needs to know, and helping board members understand the work to be done.
- Involve board members prior to decision-making time to get their input, feedback, and support before making proposals requiring their action.
- If management is effective and can demonstrate that costs are being controlled, the board is less likely to get involved in details.

resource use and to relate them to performance and future goals. This is an appropriate extension of the board's responsibilities and does not need to add to its workload, though it must be recognized that conversations on the topic could go in unexpected directions. Nevertheless, such discussions are healthy and necessary for all institutions.

Although most board members appear eager to do more to review spending, they recognize that it is important that they do this in close partnership with presidents so that they do not get ahead of the rest of the institution or end up on a different page entirely. If cost measurement and management become the dominant domain of the board or detached from organizational conversations about quality and resources, this will harm rather than help the institution.

The president and CFO, as the primary educators of trustees in these matters, can ensure that board education, meeting agendas, and materials for board meetings appropriately focus attention where it is needed. The information they provide can engage trustees in timely and important decisions on costs.

Some institutions have taken board involvement in cost management and cost control seriously, and their example can help set a direction for others to follow. Combining the advice from board members and CFOs, the path ahead includes the following elements:

I. Attention to ongoing board

education and the development of information for new members to inform them about how the "business model" of the institution compares with that of other institutions.

2. A fresh approach to fiscal decision making within the board and its committees to better integrate decisions about tuition and aid, capital and operating budgets, and

strategic academic planning and long-term fiscal planning.

3. A much sharper focus on spending, beginning by organizing expenditure information into a useful framework that shows patterns, provides benchmarks, and focuses on the future. ■

Acknowledgments

AGB would like to thank the following individuals for advising The Cost Project:

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The Cost Project is an AGB initiative designed to build governing board
capacity to monitor institutional costs effectively and strategically.

The Cost Project is supported by a grant from the
Robert W. Woodruff Foundation.

Design and production by V Studio.