

FIFTH EDITION

COLLEGE AND UNIVERSITY BUDGETING

A GUIDE FOR ACADEMICS AND
OTHER STAKEHOLDERS

LARRY GOLDSTEIN



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CHAPTER 13: RESPONDING TO EXTRAORDINARY CIRCUMSTANCES

The more things change, the more they appear to remain the same. Along with the shifting perspectives about the value of higher education addressed in earlier chapters, the industry continues to be plagued by financial challenges that, in some cases, result in major institutional disruption. The third edition of this book was published as institutions were experiencing cutbacks triggered by the dot-com bubble burst at the turn of the millennium. The fourth edition followed another extraordinary circumstance—the Great Recession that began with the collapse of the U.S. subprime mortgage market in 2008 and continues to have long-lasting effects even as this edition is being written.

More recently, there is turmoil growing out of the 2016 presidential election. Higher education has not been a primary target for the Trump Administration and its new policies, but that does not mean that institutions have escaped impacts from its actions. A few of the more significant changes affecting institutions include:

- ▶ Visa challenges facing foreign students and faculty due to the travel ban affecting selected countries
- ▶ A variety of implications from the 2017 Tax Cuts and Jobs Act, including the potential for selected independent institutions to pay taxes on some endowment earnings, anticipated reduced philanthropy due to the doubling of the standard deduction, and changes to the unrelated business income rules
- ▶ Cost increases resulting from tariffs imposed on foreign-sourced goods

Colleges and universities are being forced to adapt to new financial challenges and the operational impacts from these and other dramatic policy changes. For some institutions, this represents another chapter in the ever-evolving environment in which higher education must operate. For others, however, changes of this magnitude have serious implications for the ongoing viability or even survival of institutions. Recent evidence suggests

that the long-predicted closure and merger of institutions—especially smaller, poorly endowed independent institutions—finally has arrived.²¹⁵ Accurate data are hard to find, but there is evidence that the economic climate has led to more mergers and institutional closures than at any time since the Great Depression.

Long before the current distress, an institution would occasionally encounter unique problems that called for retrenchment. Such institutions typically would be guilty of a lack of emphasis on planning. As a result, a combination of factors would create a sustained period of financial distress with no clear solutions available. Or the institution might simply have failed to heed obvious warning signs. Sometimes, an unpredictable event prompted the retrenchment—such as a physical disaster that greatly exceeded the institution’s insurance protection or the sudden closing of a local manufacturing facility, which led to a dramatic enrollment reduction.

In recent years, however, even higher education institutions employing best practices in the area of planning have had to retrench and adapt to what now is described as a new normal. Normal now means operating with reduced resources, coupled with increased demands for services—all under never-ending scrutiny by regulators and funders.

The broad gamut of financial distress ranges from serious—institutions that find it difficult to honor their debt service obligations—to those “on the brink” and facing imminent closure absent dramatic infusions of resources. There was a time when this group was limited to those with an ongoing structural deficit. That has changed, and it’s fair to say that any institution with serious enrollment challenges that also is experiencing philanthropic shortfalls may be forced to consider merging or shuttering completely.

A structural deficit arises when annual operating expenses exceed annual operating revenues. An institution with substantial endowment resources can operate reasonably well in this condition by using nonoperating financial gains to offset operational deficits. The vast majority of institutions, however, will not survive for long if they continue to erode reserves by suffering ongoing operating deficits. Even modest enrollment shortfalls may be enough to drive such institutions out of the market.

WHAT EXACTLY IS RETRENCHMENT?

Retrenchment results from a financial crisis that, when serious enough, can threaten the institution's survival. It usually includes systematically (or, in some cases, haphazardly) eliminating major portions of an institution's programs and activities.

Because each financial crisis is unique, the elements of a retrenchment will vary from one institution to the next. Still, one action almost always accompanies retrenchment: personnel reductions. With such a large portion of institutional budgets committed to compensation, it is inconceivable that an institution can respond to a financial crisis without eliminating positions.

Though necessary for survival, personnel cutbacks have lasting negative effects on institutional culture. Any action that results in the elimination of someone's job has a devastating impact on a community—even when the position supported an activity that no longer added value for the college or university. When the cause is a financial crisis—especially one that should have been anticipated and avoided—the impact lasts for years.

Planning for circumstances that could result in retrenchment creates the opportunity to effect change that otherwise might be difficult to implement. As an example, the discussion of IBB in Chapter 9 includes a description of reallocation strategies. Some view reallocation as an exercise forced on an institution by external factors or organizations. In fact, it can better position an institution to respond to financial crises, possibly avoiding retrenchment in the process.

Reallocation allows an institution to systematically reduce the resources it devotes to some activities, thus freeing up resources that can be better deployed elsewhere. It is one mechanism for providing funds for initiatives that support new priorities. It has the added benefit of providing a cushion if an unexpected financial crisis arises. The institution may be able to avoid the more drastic responses that otherwise might be needed. In fact, if the reallocation enables the institution to weather the storm with only a minimal or zero loss of faculty and staff, short-term morale problems and a long-term negative cultural impact may be avoided.

PLANNING FOR RETRENCHMENT

Planning for retrenchment may be a misnomer. The more correct phrasing is planning to *avoid* retrenchment. In reality, prior to the Great Recession, few institutions had invested the effort in preparing for the possibility of significantly reduced resources. Admittedly, few could have anticipated the recession's magnitude. But even less pervasive cases of financial strife have caught institutions unprepared.

Just as institutions have developed disaster recovery and other emergency preparedness plans, they should develop plans to accommodate financial crises of varying proportions. In the wake of the 2008 recession, for example, several states imposed double-digit budget cuts on public colleges and universities. Some institutions could increase tuition rates to partially offset the reduction in public support, but others did not have this option because of state policies. The institutions best able to respond to the reduced resources were those with formalized contingency plans to deal with such a severe financial challenge.

It simply is not possible to plan effectively for every contingency—especially for something of cataclysmic proportions. Nevertheless, failing to prepare the institution in any way for financial difficulties increases the likelihood of having to operate in crisis mode—at least for the short term. A lack of preparation virtually guarantees that the time needed for considered judgment will not be available once the problem surfaces.

Generally, the less time an institution has to react to a fiscal emergency, the narrower the range of options available. Rather than carefully considering their options—which could include tapping into reserves or using a budget contingency, along with unallocated initiative funds—the institution typically responds by implementing travel bans, hiring freezes, and across-the-board budget cuts. None of these actions is strategic, and each demonstrates an unwillingness or inability to protect priority activities—assuming any have been identified.

Of course, the crisis may still necessitate actions affecting travel, discretionary spending, and the filling of vacant positions, but effective planning can have a mitigating effect. For instance, the planning process

should already have identified activities that will be exempt from expense controls and established the criteria for making decisions about other exceptions to necessary controls. Sponsored research programs; recently undertaken academic initiatives; patient care operations; and safety activities, for instance, might represent priority areas and, therefore, should not be subject to cutbacks.

To minimize the negative effects of financial stress, planning must focus on both midrange and long-range activities and consequences. In the short term, institutions may achieve small savings by selectively reducing nonpersonnel costs, such as travel, equipment, and supplies. But some short-term actions, such as reducing purchases of library materials, deferring maintenance and renovations, or deferring the purchase of essential replacement equipment, might cause severe long-term programmatic damage if they continue beyond one cycle. Although deferring a roof replacement may seem appealing in the moment, the decision may prove unwise if the roof leaks and damages expensive laboratory equipment integral to ongoing sponsored programs.

With compensation absorbing so much of their budgets, institutions cannot make large-scale reductions without eliminating faculty and staff positions—or at least resorting to furloughs. If effective planning minimizes the impact of the financial problem, normal attrition might generate enough savings to meet the reduction target. However, normal attrition may create different problems because the vacated positions may be critical to operational effectiveness. Even so, this still is preferable to layoffs or reductions in force because of how these actions affect the community.

In planning their responses to fiscal crises, institutions must remain sensitive to legal constraints and external factors. Collective bargaining agreements, for example, may limit the available options. State governments have become more involved in personnel matters in public higher education. This involvement may extend from direct participation in the negotiation of faculty contracts to controlling the number of faculty and staff positions. Under some budget formulas, adjustments to instructional methodologies or staffing patterns may affect state appropriations. For instance, increased reliance on distance education affects student-faculty ratios and increases the

need for academic support personnel, such as instructional technologists. Finally, special attention needs to be given to the resources associated with diversity programs, which sometimes represent state mandates.

A direct correlation exists between institutional size and the ability to reallocate resources and absorb deficits. Larger institutions tend to have more cushion than smaller ones simply because the magnitude of their operations creates opportunities for flexibility. The cushion may be spread throughout programs and support services spanning the full range of priorities. That's partly why large institutions frequently favor across-the-board cuts. The presumption is that serious, negative programmatic effects will be avoided because the impact on any single activity is nominal. Unfortunately, the reality may be quite different.

Some programs operate with little or no flexibility. Even a small cut in resources may cripple them. In other cases, even a larger cut may have no discernible impact. For this reason, the planning process must identify priorities—activities that will be protected—and either explicitly, or through omission, indicate the areas that will be sacrificed should cuts become necessary.

SPECIFIC STRATEGIES

The responses to financial hard times are as diverse as the universe of American higher education. Some cutback strategies, such as across-the-board cutting, are adopted solely because of their ease of implementation and the fact that everyone suffers together (albeit not fairly). Others reflect careful consideration of programmatic activities and prompt the institution to focus more on critical success factors.

When considering specific strategies, institutions should avoid arbitrarily cutting support areas. Understandably, an institution wants to preserve primary academic programs and activities as much as possible. On the other hand, effective delivery of primary programs requires adequate support. Even though it is much easier to eliminate staff support positions than faculty lines, this response may not be the most effective one to support the mission.

In the short term, for instance, it may be more appropriate to rely on savings generated through faculty vacancies than to eliminate support positions. Another alternative may be restructuring support operations to expand the range of units served by individual academic support personnel. Rather than each academic department having one support position, a single position might support all units housed within a given building. The most effective institutions balance the need to minimize the adverse impacts on primary programs against the need to ensure those programs operate effectively.

Seven Planning Principles

When planning how to address a financial crisis, employ these general principles suggested by Robert M. O'Neil* and revised in the wake of the Great Recession:

- 1. Involve everyone in planning—especially in times of financial distress.** Boards, management, faculty, staff, and students—as well as alumni and donors—have a major stake in what happens on campus. They not only deserve to participate in meaningful deliberations and decisions but also can provide valuable insights about how resource distributions affect programs and support services.
- 2. Provide participants with access to all available information.** The people responsible for planning should be sensitive to the implications of sharing information, especially when it pertains to personnel and programs. Establish confidentiality standards and emphasize the importance of adherence. Such standards facilitate access to the sensitive information needed to make informed judgments.
- 3. Ensure planning does not ignore the institution's culture.** During times of financial distress, the institution may have to consider actions that run counter to its values, traditions, or operating style. Such actions, if deemed essential, should be undertaken only after extensive communication with constituencies and with acknowledgment that they represent a shift in the institution's evolution.

*The principles discussed in this section originally appeared in Robert M. O'Neil's article, "A President's Perspective," on pages 17–20 in *Academe* 69 (January–February 1983).

Seven Planning Principles

- 4. Inform the governing board and—in a university system—central administrative staff of progress.** Educate the trustees or regents and central administration on how the financial crisis response is unfolding—the first step in building support for proposed actions. Similarly, communicate changes in programmatic directions to significant friends of the institution, including alumni, donors, and local supporters.
- 5. Recognize the impact of the media—especially social media.** Thanks to technology, constituents have nearly real-time access to information about most activities taking place on a campus—including responses to financial challenges. Members of the media are especially interested in higher education because of its community impact—and because of the controversy that frequently surrounds the range of campus activities.

Because information will likely be disseminated anyway, have a broad, consultative process when it comes to responding to financial challenges. Furthermore, proactively use various forms of technology and social media to distribute accurate information. This reduces the possibility of erroneous information being widely shared.

- 6. Never ignore the state legislature (if a public institution).** Legislators who remain informed about planned actions tend to be more sensitive to institutional interests when setting state-level policy. Even in an environment in which the institution is granted significant autonomy, it is in the institution's best interests to remain closely connected with state government during financially challenging times.
- 7. Avoid unintended consequences by projecting the long-term impact of retrenchment strategies before implementing them.** A simple but effective approach is to model the various strategies under multiple scenarios to determine the most likely outcomes. The administrative tools available make it possible—and easy—to predict the outcomes from various strategies with reasonable accuracy.

Seven Planning Principles

In addition to following these principles, institutions should seek out resources available from higher education associations. In times of significant financial distress, it's common for associations like NACUBO to offer toolkits, suggested strategies, and other resources to their members. In some cases, these resources are developed by the association staff and member volunteers while, in others, the resources come directly from member campuses and represent proven solution sets.

One final caution is in order. Too often, institutions immediately engage in cost shifting as a response to financial stress. Cost shifting refers to the practice of implementing a charge for goods or services that previously were funded centrally or as part of a service unit's budget. It may be appropriate to require units to begin paying for certain goods or services that they consume. In fact, this may be an effective mechanism for conserving scarce resources. A problem is created, however, when units that must now pay for these goods or services do not receive any additional resources.

If the decision is made to begin charging units, it's best to first distribute a portion of the existing budget to the units that will be required to pay for the goods or services. Savings can be generated by not distributing the entire budget. If a good or service has been provided at no charge to the user, it's highly likely there has been some waste related to the item. By distributing a portion of the existing budget—say 70 percent—and capturing the balance as savings, the institution will achieve the objective of reducing expenses but without adversely affecting units that rely on those goods or services.

Institutional retrenchment strategies fall into one of two groups. They are either short term—spanning one to three years—or long term—beyond three years.

SHORT-TERM STRATEGIES

In the short term, institutions can respond to financial difficulties either by reducing expenses or by increasing revenues. Boosting revenues significantly in the short term usually is quite difficult. It takes time to identify and pursue new revenue sources. A robust economy might make it possible to improve short-term investment returns through enhanced cash management, but

this scenario is unlikely with weak markets (and likely wouldn't produce material amounts of revenue anyway).

Because of the difficulty with identifying and quickly pursuing new revenue streams, attention usually focuses on reducing or deferring expenses. Unless institutions have been operating under severe conditions for an extended period, they usually can achieve modest savings by curtailing discretionary expenditures for supplies, travel, equipment, and minor maintenance.

Larger short-term savings can be achieved by carefully managing the number of faculty and staff. Faculty positions that become vacant may be left open, filled with lower-salaried faculty, or filled with temporary or part-time faculty. Similarly, leaving staff positions vacant or employing part-time or temporary personnel can result in savings. Fewer courses and larger sections can be scheduled while also offering fewer sections of some courses.

Without a plan focused on differential actions, short-term budget strategies invariably focus on across-the-board measures. Imposing the same burden on all units on short notice may seem more acceptable to the greatest number of people, but it fails to address the concern that priority areas could suffer serious damage.

Across-the-board actions result in high-priority activities being treated the same as those that may contribute little to no value to the institution. In addition, across-the-board philosophies carry the implicit assumption that all budgets are equally capable of responding to a modest cut. In fact, vast differences in budget adequacy may exist among programs. For some units or programs, an equal percentage cut may merely affect discretionary expenses, while for others, it could force the elimination of a staff position to meet the target.

Given the shortcomings of across-the-board cuts, it always should be preferable to apply cuts selectively rather than uniformly. Such cuts can be accomplished only with a clear understanding of priorities and the level of resources needed to maintain and deliver effective programs. Selective reductions, even in accordance with an established plan, will not be well received by all constituents—especially those experiencing the disproportionately higher cuts. Therefore, cutting budgets represents one of

the most difficult tests for a campus administration. If the planning process is to have any credibility, however, it must guide the decisions.

Short-term strategies can generate quick savings. If the institution has not invested the effort to develop a plan, these savings can buy the time needed to undertake a more considered approach to cutting expenses. On the other hand, the amount realized through short-term strategies tends to be small compared to the overall budget. Significant reductions take considerably more effort.

In addition, short-term strategies can inflict long-term damage on programs as well as facilities. For instance, when significant scheduled maintenance is deferred, it can have a serious impact on operations. There's an accepted maxim in facilities management that poorly maintained facilities are more expensive to operate. Additionally, when forced to apply the maintenance, it's almost a certainty that costs will have risen.

Similarly, when temporary or part-time employees fill vacancies resulting from the retirement or departure of experienced faculty, the institution's character can change dramatically. Programs requiring extensive involvement of senior faculty may wither, and part-time or temporary faculty may not be interested in (or capable of) student advising and counseling.

Finally, relying on attrition to achieve salary savings may mean the programs being de-emphasized may not be the ones that experience vacancies. If the vacancies occur in priority areas, the institution will need to fill the vacancies and diminish the potential savings.

LONG-TERM STRATEGIES

Every institution should have infrastructural plans (see Chapter 7) that provide the context for establishing program priorities in core programmatic and essential support areas. These plans should establish and reinforce the institution's priorities and identify decision-making criteria. Without the principles embodied in the plans, an institution will find it difficult to alter its allocation of resources in an intelligent manner.

Institutions faced with the prospect of implementing major budget reductions, or with the need to force significant reallocations, must review

their academic programs and support activities carefully. To achieve economies and maintain or strengthen the quality of the institution, program review must be an active process that, over time, examines all programs and activities—both primary and supporting.

Infrastructural plans provide the framework for examining the distribution of resources, while information garnered from program reviews describes how well the program array is executing the plans. A typical schedule results in a comprehensive review of each program on a five-year cycle. Programs should be reviewed with respect to their:

- ▶ Linkage to and support of the institution's mission
- ▶ Service load
- ▶ Uniqueness
- ▶ Enrollment demand (for academic programs)
- ▶ Service demand (for support activities)
- ▶ Overall effectiveness (for example, quality and productivity)
- ▶ Available resources and costs incurred

In the absence of planning, the need for significant resource reductions or forced reallocations requires aggressive program reviews. In general, passive program shrinkage or elimination—usually through faculty and staff attrition—is insufficient to meet reduction targets. This approach may offer the least contentious way to cope with program shrinkage from a political perspective, but it typically will not achieve the objective. Faculty and staff do not limit their resignations, transfers, and retirements to low-priority, mediocre-quality, or low-demand programs and support activities. Normal attrition generally will not free up sufficient resources quickly enough to avoid retrenchment.

Large budget adjustments require changes in staffing patterns. Thus, retrenchment ultimately must focus on personnel policies and procedures. One frequent response is to provide financial incentives for early retirement, voluntary separation, or unpaid leaves. As with most retrenchment strategies, the objective is to provide institutions with budget-reduction alternatives that help avoid forced terminations.

Ideally, the people opting to depart under such programs would be the least-needed or least-productive faculty and staff, but this rarely happens. In fact, the institution risks losing its most productive and valuable faculty and staff because of their marketability.

An additional concern is that the people remaining may not possess the requisite educational and research background to fulfill the commitments of those who have departed. Even faculty trained in the same discipline may not be adequately prepared to step in and teach another faculty member's courses—especially if they have not taught the content previously. A faculty member teaching in the accounting program may be well qualified to teach any accounting course, but there is no guarantee he or she has the ability to teach an auditing or tax course.

Moreover, unless used in conjunction with program review, these strategies do not identify the programs and support activities that are the preferred candidates for contraction or elimination. The only way to avoid significant problems with incentive programs is to design them carefully and establish criteria that minimize the risk of losing the most valuable faculty and staff. Even so, the institution must prepare for the possibility of losing them.

Long-term strategies for achieving salary savings fall into these categories:

Early retirement. Faculty and staff who meet specified age and service criteria are offered a lump-sum separation allowance for agreeing to retire or resign early. In addition to the lump-sum payment, the package typically includes benefits such as pension and health insurance.

Some public institutions are precluded from offering such programs unless they are consistent with programs available to all state employees. Still others must obtain special authorization to offer a program of any type. Another problem is the possibility that some excellent performers may choose to retire. To minimize this outcome, the program might set the severance compensation at the average salary for a particular age cohort. This criterion may discourage the best faculty from participating because they are more likely to earn well above the average salary.

Early retirement programs typically require significant front-end costs, such as a severance package and payouts in lieu of some benefits. It must be demonstrated that the program will ultimately save money and improve the overall financial picture. Nevertheless, an early retirement program may be a less expensive alternative than forced terminations that sometimes require one to two years of notice and frequently result in expensive legal challenges.

The current economic climate, the quality of life on campus, and the institution's general outlook play a significant role in a program's success. For instance, many programs offered in the wake of the Great Recession failed because of the depressed stock market at that time. Even with incentives, individual retirement portfolios had lost so much value that many feared they might not have sufficient retirement income. As a result, few were willing to participate in the programs.

Early retirement represents a big step, and employees appreciate having time to consider it carefully and consult with their advisors. Programs that require a commitment during a small window of opportunity may discourage participation. On occasion, institutions have offered programs in consecutive years with differing features and requirements. This technique usually is implemented when the financial condition continues to deteriorate or the retirement programs do not generate the level of participation needed to achieve reduction targets. Unfortunately, once this practice is utilized, it tends to encourage potential participants to wait for what they believe to be the best possible offer.

An additional concern with early retirement programs is that they may not work as effectively for staff as for faculty. By their nature and design, early retirement programs focused on faculty will be targeted to older faculty—typically those with the highest salary levels. To the extent that the programs are attractive, the faculty who depart will usually be replaced by more junior, lower-paid faculty. Even considering the extra costs incurred for the incentives, the institution will realize net savings fairly quickly. With staff, however, it has proven difficult in some cases to attract lower-cost talent. If the longer-serving senior staff take advantage of the program, it is

possible that the individuals' salaries will not have kept up with compensation increases over time. When that's the case, the institution may find that it is not possible to attract affordable individuals to the positions. If this happens, the desired savings may not materialize.

Partial buyout. This approach enables faculty and staff to choose part-time appointments for a number of years up to an established maximum. During this period, they receive a prorated salary with full benefits. Participants commonly receive a full year of retirement credit for each year in the program.

Partial buyouts tend to appeal to senior faculty and staff because their salaries are larger and they are closer to retirement. For this reason, the program can generate substantial savings with relatively low participation.

Alternative approaches. Individual campuses have employed short furloughs, forcing staff to take unpaid time off. Others have implemented modest across-the-board pay reductions or introduced midcareer changes—a euphemism for retraining, a term sometimes found objectionable by faculty. With the latter arrangement, faculty or staff in programs targeted for reduction or elimination have the opportunity to transfer to other departments or positions to continue employment. In general, these strategies are difficult to implement unless existing policies already allow them. Otherwise, the opposition from faculty and staff can be overwhelming.

Another option involves liberalization of the existing guidelines used to determine retirement benefits. For instance, rather than develop a specific early retirement program, an institution can elect to provide full benefits at a lower retirement age or with fewer years of service. In a traditional early retirement program with unique features, individual negotiations may take place. With liberalized guidelines, everyone qualifying under the formula receives the amount of compensation and benefits available to anyone with the same combination of age and service.

Surviving Personnel Reductions

Personnel actions are a delicate subject in the best of times. When implemented as part of retrenchment, they take on an entirely different character. The following recommendations may prove useful if you become forced to take personnel actions to generate savings.

Analyze the possible strategies. If offering an early retirement program, for example, ensure the savings would outweigh the implementation costs by a margin sufficient to justify the effort and attendant disruption.

Avoid targeting specific individuals. Rather than focusing exclusively on faculty and staff assigned to a program deemed less essential, address the program itself. Singling out individuals may lead them to believe they were the victims of inappropriate discrimination.

Discrimination in and of itself is not illegal. It happens routinely and appropriately. For instance, assigning a larger reduction target to a low-demand program is a form of discrimination. On the other hand, discrimination against individuals based on age, gender, ethnicity, race, etc. clearly is illegal. Follow due process with any personnel reduction programs driven by retrenchment to ensure that employees do not feel they were coerced into making a decision and that those who choose to participate are not stigmatized.

Focus on more than the finances. Savings should not be the sole consideration when implementing new personnel policies. Consider also the impact on programmatic goals and objectives.

Take care to avoid actions that faculty may perceive as a threat to tenure, academic freedom, or academic due process. Both faculty and staff will find personnel reduction programs easier to accept if the risks associated with career transitions are minimal.

When developing personnel reduction initiatives, consult the constituent group members expected to participate in them. In addition, position and publicize the opportunities as providing benefits both for the individuals and the institution.

TERMINATION OF FACULTY

Sometimes, the magnitude of the reductions needed within a short time period makes termination unavoidable. The termination of faculty is particularly difficult because most institutions maintain a strong commitment to tenure. In addition, many American colleges and universities have policies that align with principles and guidelines established by the American Association of University Professors (AAUP).

These principles and guidelines cover academic freedom, tenure, financial exigency, and discontinuation of a program for reasons other than financial exigency. The AAUP guidelines, for example, oppose the dismissal of faculty or the termination of appointments before the end of specified terms, except when financial exigency occurs.

The guidelines are designed to prevent administrators from using financial exigency as a justification for capricious actions. They define financial exigency as, “A severe financial crisis that fundamentally compromises the academic integrity of the institution as a whole and that cannot be alleviated by less drastic means [than the termination of tenured faculty].” While helpful, this definition can be difficult to apply due to differing interpretations of what constitutes a severe financial crisis as well as disagreements about the availability and impact of less drastic means. Moreover, the AAUP’s history of investigating campus actions and, in extreme cases, censuring institutions clearly indicate that there frequently is a strong difference of opinion about the appropriateness of institutional activities when responding to financial crises. It is, therefore, necessary to interpret the guidelines and adapt them to specific institutional settings whenever they are employed.

Views differ on whether enrollment fluctuations can be the impetus for exigency determinations. Some individuals argue that fluctuations are cyclical and should not serve as a basis for program discontinuation. Others contend that enrollment fluctuations constitute an appropriate aspect of educational policy and, therefore, should be considered.

Clearly, the quality of academic programs influences resource decisions. A program of mediocre quality with low enrollment, for example, might drain resources from higher-quality, more competitive programs. It might

be necessary to respond to sagging institutional enrollments by shifting resources to make selected programs more attractive to potential students. Such action, though damaging to some programs, may be the only way to protect the financial viability of the institution as a whole.

The major issue in significant retrenchment efforts is how to handle personnel in all categories: tenured, nontenured, and staff. The AAUP guidelines address the elimination of entire academic programs. Absent financial exigency, the guidelines do not permit the termination of particular tenured faculty because of mere reduction in scope or reorganization of academic units. In a small institution with instruction as its primary mission, for example, enrollments might not justify a five-person, fully tenured philosophy department. If the institution wishes to reduce its commitment to philosophy, while also adhering to institutional policies compliant with AAUP guidelines, the only alternative may be to disband the entire program. Moreover, the institution would have to justify the elimination of the philosophy program on academic considerations other than enrollment.

This example helps explain why some institutions have modified the AAUP guidelines or abandoned them completely in favor of other approaches. Those institutions have more flexibility when dealing with low-demand or low-quality programs because they would have the option to reduce the number of faculty based on enrollment.

Rather than terminating tenured faculty members, an institution might allow the size of the program faculty and staff to shrink through natural attrition. This takes time though. Alternatively, faculty members can be reassigned or retrained to assume other duties or teach in related disciplines. When taking any such actions, institutions must be careful to honor commitments made to students currently enrolled in these programs.

It's noteworthy that in nearly all recent cases, accreditation actions taken by the regional accrediting agencies have included financial challenges as a factor. Financial challenges can include the inadequacy of resources as well as the lack of appropriate policies and procedures related to financial resources. Whether warning, probation, or loss of accreditation actions, finances play a disproportionate role to other factors that influence the

accrediting bodies' actions. Given that regional accreditation is required for participation in federal financial aid programs, institutions placed on probation or warning due to financial issues would clearly be in financial exigency—whether declared by the institution or not.

Other institutions may not be in such peril but still face serious financial distress due to dramatic decreases in revenue from declining enrollment, tumultuous financial markets, reduced state appropriations, or other situations. If these colleges and universities have adopted the AAUP guidelines as written, they may struggle with how the guidelines apply as they respond to financial difficulties.

Any institution facing serious financial hardship must assess whether financial exigency—as defined in its own policies (whether adopted from AAUP guidelines or developed on their own)—actually exists. Because the phrase carries special meaning in the higher education community, great care must be exercised before it is invoked. In the past, some institutions have used the phrase prior to initiating actions that resulted in the termination of faculty because their policies required it.

Other institutions, recognizing that the phrase can trigger other serious consequences, have attempted to address financial crises without referring specifically to financial exigency. In doing so, they hoped to avoid problems with bond-rating agencies, bondholders, other creditors, and accreditation agencies. Unfortunately, failure to invoke the phrase does not guarantee that drastic measures can be avoided.

FOCUSING ON THE LONG TERM

STRATEGIC RESOURCE ALLOCATION (SRA)

Within the most effectively managed institutions, planning is a continuous activity because of the complexity of the academic enterprise and the need to act intentionally rather than haphazardly. The best planning processes are those that involve administrators, faculty, appropriate stakeholder groups, and—depending on culture—students. Even when things are going well, it usually is desirable to have some periodic process for evaluating the

various activities that are consuming resources (i.e., people, money, space, technology, and equipment).

One option for responding to the need for structural change is periodic SRA, or prioritization, as described by Bob Dickeson.* At its core, SRA is undertaken to facilitate an orderly and systematic redistribution of resources away from underperforming academic programs and support functions toward those existing activities that will contribute to enhanced institutional effectiveness and long-term success.

Directed by senior leadership but relying on a broadly participative effort carried out by faculty, staff, and midlevel managers, a systematic process is undertaken to assess all activities that consume resources and compare them to other similar activities. Academic programs are evaluated by a task force comprised of faculty and academic department heads utilizing institutionally specific criteria to evaluate each program against all other academic programs. A parallel task force consisting of staff, midlevel managers, and faculty use different institution-specific criteria to evaluate all support functions within the institution. These assessments result in all programs and functions being classified into quintiles (i.e., five equal categories), with the goal of equal distribution based on the value of financial investments in the programs and functions. The recommended categories are:

- I. Enhance through additional resourcing** – Programs and functions whose contributions to institutional success would be enhanced with increased investment to the extent funds are available for reallocation
- II. Maintain with no change in resourcing** – Programs and functions that currently operate successfully and consume the appropriate amount of resources relative to the total amount of available resources
- III. Modify through reduced resourcing** – Programs and functions that will curtail some operations or reduce their quality due to a reduction of resources available to the programs and functions going forward

*The strategic resource allocation discussion is influenced significantly by the book: *Prioritizing Academic Programs and Services* by Robert C. Dickeson (San Francisco, CA: Jossey-Bass, 2010).

- IV. Transform** – Programs and functions deemed essential to the institution’s character or operations but that are underperforming in comparison with programs and functions in categories I through III. Such programs and functions must be reengineered or reenvisioned due to their inability to perform at levels that meet current needs. Programs and functions in this category may receive additional resourcing or may be transformed in such a way that previous resource levels can be reduced.
- V. Phase out or merge** – Programs and functions no longer deemed essential to the institution’s character or operations that underperform compared to programs and functions in categories I through III. Programs and functions in this category will be subjected to an additional thorough examination to determine whether and how best to carry out the recommendation for a phaseout or merger.

It should be noted that, except in very rare situations, it is inconceivable that 20 percent of an institution’s investments could be curtailed without adversely affecting the institution’s operations and its ability to carry out its mission. In particular, care must be taken that disproportionately large cuts in support areas do not prevent the institution from adequately delivering the academic programs that will remain following implementation of recommendations coming out of the process.

The use of quintiles, as described above, is recommended because of the difficulty to carry out the classification without forced distribution. Realistically, except in dire situations, the maximum amount that can be reduced in a reasonable time period is in the range of 10 to 12 percent. It should be noted that the savings using this approach will not be available immediately. Instead, given the obligations to students currently registered in programs slated for phaseout—as well as contractual and other obligations to current staff and faculty—it may take up to four years to fully realize the savings from SRA.

Once completed, the classification of programs is reviewed by senior leadership. In addition to the work of the task forces, they will receive

the benefit of input from individuals and stakeholder groups throughout the institution who will want the opportunity to weigh in on the recommendations. Ultimately, senior leadership will make the decisions about which recommendations to accept and implement—and in what sequence. The end product of the effort (i.e., management’s intentions) should be communicated to the board. In most instances, the board will be required to formally endorse or approve the plan. Implementation begins following board action.

Although significant coverage is given to SRA—the author’s preferred approach, there are other models that can help establish the prioritization of activities with resulting resource redistribution. Some campuses have employed the Balanced Scorecard approach. In carrying out the process, institutions view activities from four perspectives and develop key performance indicators, targets, and actions relative to each one of them. The perspectives include financial, customer (or stakeholder), internal business process, and learning and growth.²¹⁶

Another approach, the Resource Allocation Map,²¹⁷ relies on four dimensions to help align organizational resources with strategic priorities. The dimensions are the mission/strategic plan, financial performance, internal competencies, and market trends. While both SRA and the Balanced Scorecard are holistic systems that can be used to evaluate and prioritize all operations, the Resource Allocation Map is focused primarily on academic programs and activities.

Another option for tackling in-depth academic program analysis is available from Gray Associates, Inc. In addition to examining the current complement of programs, it has the expertise (and robust database) to assist institutions with the identification of potential new programs that would lead to improved financial performance. Its integrated program analysis tool examines four dimensions referred to as MAMM:

- ▶ Mission
- ▶ Academic standards
- ▶ Markets for programs
- ▶ Money

The resulting information is used to provide a program scorecard incorporating numerous data points for each program offered by a college or university.

Gray has a proven track record of helping institutions examine their programs in a detailed manner that allows them to identify those that have stopped contributing to institutional success. Acting on this information, institutions can free up resources to pursue new programming that will better serve the institution's current students and attract new ones.

PROGRAM REVIEW

In the absence of a comprehensive approach, such as the one suggested by Dickeson, there is a need for some type of in-depth program review. A typical process would usually include the following elements:

- ▶ Confirmation of the continuing relevance of the mission statement
- ▶ Review and modification (if necessary) of campus-wide or system-wide policies, procedures, and statements of priorities
- ▶ Examination and updating (if necessary) of personnel policies
- ▶ Establishment of guiding principles specifically applicable to program review
- ▶ Establishment of policies and procedures, including criteria, for the review of existing and proposed programs and activities

Fiscal conditions ultimately are the force behind retrenchment and any significant exceptional reallocation effort. Nevertheless, finances often are overshadowed by genuine concern for personnel policies and procedures—especially those related to faculty and staff welfare and legal rights—and the potential impact from program reviews.

PROGRAM REDUCTION

Program reduction has obvious political costs and a devastating impact on morale. These costs must be compared with the net savings and other benefits, such as the ability to respond to enrollment pressures and hire quality faculty. Institutions sensitive to the well-being of those affected

by program elimination will incur costs for early retirement, buyouts, outplacement services, or retraining.

If faculty and staff must be terminated, the institution will be responsible for severance payments. Invariably, some faculty and staff will contest their dismissals through the courts, so legal defense represents another cost to factor into the equation. The net savings from program reduction will be a function of the specific strategies employed. To the extent that the institution elects to assign faculty and staff to positions elsewhere within the institution, savings may be reduced as compared with outright or phased terminations.

Program reduction or elimination may be a consequence of enrollment decline. These decisions will result in a loss of tuition and fee revenue and, for public institutions, possibly reduced operating appropriations. Public institutions may not be authorized to reinvest savings gained through retrenchment in other programs and activities. Instead, these institutions must return savings to the state. Finally, programs that enjoy significant external financial support may require considerable institutional support to continue. Reducing or eliminating such programs may not generate any net savings.

Other effects of retrenchment and reallocation may be more subtle and difficult to quantify. Faculty teaching in a department being downsized may find they no longer have the job satisfaction they desire. They may elect to seek employment elsewhere, potentially impairing the ability to sustain the program at the expected levels. For example, if an institution reduces the scope of a program from the doctoral to the master's level, faculty whose primary interest is doctoral training and research may not be satisfied teaching at the undergraduate and master's levels.

Taking actions that affect programs that enjoy significant support from donors may result in reduced support. Thus, it may be desirable to include external support as a criterion to consider during program reviews. This is a risky action to take because it can lead to individuals who are not part of the institution having significant influence over operational matters. The question must be asked whether the external financial support is sufficiently large to allow this to happen.

Similar to the situation involving donors, certain programs may have strong political connections. If a prominent political figure serves on a program advisory board, or the program participates in projects with important community organizations, the intangible costs of contracting or eliminating the program may outweigh the financial benefits. In terms of diminished public support, the institution as a whole bears the cost of reducing or eliminating such a program.

Retrenchment may disrupt shared governance, unless faculty are meaningfully involved in establishing the policies that guide the retrenchment steps. Even when review criteria and related policies and procedures have been established, governance groups may struggle to specify the programs or activities to reduce or eliminate. Morale problems will assuredly arise as specific plans become known, and until they are announced, the rumor mill will be fully consumed with guessing what might happen.

Faculty who have served the institution for a long time may suddenly feel unwanted. If faculty terminations are decided on the basis of seniority, as is frequently the case, conflict may develop between junior and senior faculty. Retrenchment also may lead faculty and staff to pursue collective bargaining as a way to gain greater influence over the process. Adverse publicity about program reductions may exacerbate declining enrollment. Finally, situations leading to retrenchment may highlight the deficiencies within the current administration. Although the steps taken may be positive in the long run, the short-term effects can create havoc.

The economics of retrenchment require long-term plans for all programs and activities, with responsible parties held accountable for meeting plan objectives. In the academic arena, enrollments may have to be restricted to maintain the desired level of service with the available resources. Enrollment can be controlled for high-demand programs by establishing special admission requirements or implementing variable-rate tuition pricing. Long-range enrollment targets can be established for all academic programs so that planners can better gauge resource needs. Programs that fail to achieve the targets will experience consequences, which might include financial

penalties (for example, reduced resources in future periods) or personnel actions (for example, demotions or dismissal).

The development of long-term enrollment targets also supports the establishment of projected staffing patterns. Institutions can project the impact of enrollment levels on decisions about the promotion, tenure, turnover, and hiring of new faculty with the objective of making future decisions in a proactive way.

Plans for program reduction also should anticipate changes in programs and activities. If an academic program is to be phased out, for example, arrangements must be made to accommodate its current students. Tenured faculty in the program being eliminated may need to be placed elsewhere within the institution. The elimination of a degree program may affect other programs that depend on it for courses or for students. Finally, the impact of retrenchment on diversity objectives must be considered both in terms of staffing and enrollment.

KEY POINTS

- ▶ Retrenchment is more than belt-tightening—it is a dramatic contraction of activities and operations, usually resulting in the elimination of positions.
- ▶ In extreme situations, retrenchment will be accompanied by a declaration of financial exigency—a statement to the internal and external communities that the institution’s long-term viability will be in question if extreme actions are not taken. Beyond just eliminating positions, exigency typically entails the elimination of entire programs with the eliminated costs used to help close the budget gap.
- ▶ Financial exigency is likely to result in action by an institution’s regional accreditor. Failure to respond appropriately could cause the institution to lose accreditation and, as a result, cease participation in federal financial aid programs.
- ▶ Strategic resource allocation (or similar comprehensive evaluation processes) can help prevent retrenchment or, at the least, deal with it effectively. Such processes evaluate all activities in a manner that supports the establishment of priorities and directs resources toward those priorities. Ultimately, the goal is to redirect resources away from underperforming programs and activities toward those that contribute more to institutional success.

