

# Responsibility Center Management and the COVID-19 Pandemic

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## Premise

The COVID-19 pandemic has caused an uproar in higher education and uncertainty abounds. Many colleges and universities are projecting enrollment declines and budget shortfalls, and some are even faced with closure. The days of looking to the past to guide decision-making appear unhelpful due to the unprecedented nature of this crisis. However, what remains constant across the higher education enterprise is the need for institutional leaders to make resource-allocation decisions for current and future planning despite the current context. For this reason, flexibility with regard to planning and budgeting is necessary. Centralized budget approaches have received mounds of criticism from scholars and practitioners for being inflexible and unresponsive to change. Although decentralized budget approaches, such as responsibility center management (RCM), have also received criticism, RCM has been viewed by practitioners as more flexible than the centralized approach. Can RCM help some institutions survive this crisis? Yes, but it depends.

## What Is RCM?

Responsibility center management—also known as responsibility center budgeting, revenue center budgeting, incentive-based budgeting, and value-center management—is a decentralized budget model and system used by many elite private nonprofit and large public research universities in the United States and Canada. Under RCM, financial authority is devolved from a central group of university leaders (known as central administration) to responsibility center leaders, such as academic and auxiliary units. Responsibility centers differ across institutions that employ RCM, but a common theme is that resource allocation is guided by a series of revenue-attribution, cost-allocation, and taxation formulae. Together, the devolution of budget authority and resource-allocation formulae allow central administration and responsibility center leaders to fund the university's operations.

RCM grants ownership of revenues and costs to responsibility centers; responsibility center leaders (e.g., deans and auxiliary-unit directors) are accountable for generating enough revenue to cover the direct and indirect expenses of their units' operations. Other campus units (i.e., noninstructional or revenue-generating units), as well as the university's overhead costs, are funded by central administration using subvention funds collected from taxing the revenues of the responsibility centers. Collectively, this system of allocation formulae allows university leaders to fund the university's mission and strategic objectives. In addition to ensuring the university's operations are funded, the resource-allocation formulae incentivize behaviors that: (1) promote revenue growth, (2) encourage academic excellence, (3) create accountability and transparency in the budget process, and (4) enable flexibility.

## Incentivizing Revenue Growth

Incentivizing revenue growth has been a primary impetus for implementing RCM at colleges and universities. While various research articles suggest that RCM can increase net tuition revenue and the number of credit hours taught, there are mixed reviews on the types of colleges, schools, and departments that realize revenue growth. In other words, not every unit experiences enrollment and net tuition increases. However, the ability to generate other types of revenue enhancements—grants, contracts, and donations—may contribute to positive feelings about RCM and its success.

## Academic Excellence

The ability of academic units to generate and carry forward surpluses that function as reserves is a hallmark difference between institutions that practice RCM and those that use a centrally controlled budget model. When academic leaders carry balances forward, those balances can be used for the future expansion and development of higher-quality academic programs (e.g., to fund research projects, recruit top faculty, invest in state-of-the-art equipment, and provide a better experience for students).

## Accountability and Transparency

Many RCM experts believe that coupling academic and financial decision-making indirectly reinforces accountability because there is an inherent incentive to monitor costs and avoid overspending. This notion has implications for bridging the gap between academic programming and fiscal responsibility because it empowers deans and other responsibility center leaders to make prudent financial and academic program decisions. Additionally, the RCM budget model is inherently more transparent because administrative and academic leaders must communicate with central administration to negotiate funding, subvention, and reserve balances.

## Flexibility

RCM provides flexibility to those charged with academic leadership. Specifically, under RCM, deans and department chairs can make decisions on whether to staff an academic program with a tenure/tenure-track faculty or adjunct, whether to scale up or reduce the number of course sections based on enrollment and demand, and whether to cease or phase out an academic program all together. The flexibility to enhance programs may also contribute to the increased graduation rates that some researchers have observed among universities that practice RCM.

## What Does This Mean in the COVID-19 Context?

Applied to the COVID-19 pandemic, many of the RCM-incentivized behaviors described above can help universities weather the current pandemic. However, it also depends on each university's context and circumstances.

## Exercising Flexibility for Projected Enrollment Declines

Enrollment (and tuition revenue by extension) is expected to decline as a result of the pandemic.

RCM can provide flexibility to university administrators and mitigate the need for harsh across-the-board changes that typically occur in centralized budget approaches. Although it is context specific, this may mean that the university adjusts its allocation formulae (e.g., revenue attribution, cost allocation, and tax assessment) to temporarily bring more funds back to central administration in order to provide more subvention funds to colleges and schools that will experience shortfalls in enrollment (and revenue by extension).

Additionally, this can mean that deans, department chairs, and faculty critically assess their programs and offerings based on student demand. This approach could guide decision-making regarding which programs or courses to modify, merge, enhance, or phase out if necessary. Moreover, RCM can incent the university to evaluate space utilization, specifically seeking opportunities to minimize space and costs—for campuses that will allow students to return to face-to-face instruction or a hybrid approach. On-campus activities, of course, would need to fold in physical and social distancing requirements to enhance safety.

## Practicing Academic and Financial Accountability

Again, as a result of projected enrollment decreases (and tuition revenue by extension), the need for universities to be academically and financially accountable is paramount. RCM provides accountability by granting ownership of revenues and expenses to the responsibility centers. This creates an added layer of accountability for deans and faculty to take part in the future of the university.

On the academic side, this may require academic unit leaders and faculty to critically examine their offerings and adjust in relationship to projected enrollment changes. Additionally, conversations across academic units might help leaders identify and minimize duplicative offerings.

On the financial side, the implications are at least twofold. First, it may require deans and department chairs to remove budget items that do not support the core mission of the university nor the mission of their respective academic units—for example, items that are “nice to have” versus “needs.” Secondly, this may mean that academic unit leaders use previous carryover funds conservatively, as the duration of the pandemic remains uncertain. Striking a balance between academic and financial accountability is critical, not only to fund core operations, but also to inspire coordination among units and promote student success.

### INSTITUTIONS QUICKLY PIVOTED AND CHANGED EDUCATIONAL DELIVERY

Empirical research is needed to evaluate whether the entrepreneurial spirit caused by RCM can result in giant steps forward.

There is hope that the experience of RCM leaders can bring about change that advances student and university success.

## Inspiring Innovation to Impact Enrollment

In addition to adjusting funding formulae and accountability measures noted above, RCM may inspire innovation among university leaders and faculty. This may have an impact on enrollment. For example, as a result of the pandemic, colleges and universities were forced to transition their offerings to online platforms. While this may have driven up costs for many universities to provide instruction, it, too, may have inspired creative ways for faculty to develop and deliver pedagogy. Scholars have suggested that RCM incents academic units to critically assess their offerings against other campus units and other institutions to help drive enrollment. The pandemic has created an opportunity for such an evaluation across universities—not only in what they offer, but also through what modes. It, too, may make a difference in how institutions fare with regard to enrollment.

## Understanding Context Is Key

Finally, RCM's ability to help universities overcome the pandemic depends on each university's specific context and circumstances. Moreover, it applies differently for institutions that practiced RCM prior to the COVID-19 crisis compared to institutions that may be considering RCM in response to the crisis. With regard to the former, RCM has mostly been implemented by private elite universities and large public research universities due to their scale and complexity. This means that most "RCM universities" are relatively well resourced and selective. As such, their enrollment may remain relatively unchanged in fall 2020 compared to less selective universities. Moreover, universities that used RCM prior to the pandemic may currently possess sufficient reserves to account for the budgetary shortfalls it may cause. Together, these implications suggest that the previous use of RCM may contribute to how well, if at all, the "RCM universities" overcome the pandemic, although empirical research is required to address this inquiry.

This is a different context for universities that may view RCM as the solution to surviving the pandemic and economic crisis it has caused. A number of large research universities implemented RCM shortly after the Great Recession in 2008 as a means to overcome the financial challenges caused by the economic downturn. The COVID-19 crisis is very different, especially with regard to enrollment projections. Enrollment continued to increase across many universities despite the economic downturn in 2008.

For universities considering RCM in response to the current pandemic, several notes of caution are warranted. First, RCM is not a panacea. It requires a considerable investment of time, typically years, and significant financial resources. RCM varies across universities that use it, and thus far, empirical research on it remains relatively limited. Therefore, the principles presented in this white paper should be used to inspire further thinking, strategic planning, and ingenuity. These principles should not be used to drive universities into implementing RCM. The decision to implement RCM should be well studied in the context of each university's circumstances while also considering the pandemic environment and its potential effects.

## Key Takeaways

### A RESPONSIVE MODEL

- RCM mitigates the need for across-the-board cuts.
- RCM leaders are creative and entrepreneurial.
- RCM units adjust to situational changes.

### A STAKE IN THE FUTURE ENHANCES ACCOUNTABILITY

- Responsibility centers own revenues and expenses.
- Deans and faculty are incented to be a part of success.
- Academic offerings are evaluated to align with enrollment.
- Extraneous budget items are scrutinized.
- Fund balances can be used to affect change.

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