Management Changes: Impact on Ratings for Higher Education and Not-for-Profit Institutions

Recent unexpected departures of high-profile university presidents and other senior management officials of higher education and not-for-profit institutions have led market participants to inquire: What impact do these changes in management have on credit ratings? The answer is in part dependent on the reason for the changes.

Moderate turnover of senior management is typically a healthy credit sign for any organization. The importation of new personnel assures that different talents and alternative perspectives will reduce the possibility that inward looking management will fail to respond to changes in the institution’s environment and competitive position. While a single individual, especially a president, often plays a key role in setting or executing the strategic, financial, and capital plans for an institution, we expect there to be sufficient institutionalized policies and procedures to enable the effective functioning of the organization during periods of transition. Indeed, we view a mix of veteran and newer senior staff members to be a positive credit factor, as institutional history and memory is retained, but new thinking is also incorporated.

Further, the replacement of individuals who are not effective in their current role is usually a credit positive. Finally, adjustments to organizational structures, which can result in some turnover, may also be a credit positive if they better position an organization to respond to changes in the industry or competitive challenges. For example, as universities become increasingly financial complex, we have seen instances where the chief business officer function has been replaced by a structure incorporating a treasury officer, who may be responsible for both investment and debt management, and a chief administrative officer responsible for other more traditional business functions, such as budgeting, financial reporting, human resources, etc.

The wholesale turnover of a management team within a short period can affect both the ability to follow through on long-term strategic objectives and impact important ongoing initiatives, especially in the areas of fundraising and recruitment. While such change typically does not cause a near term rating downgrade, over time it could hurt credit quality if the institution is unable to achieve strategic goals.

Nonetheless, we recognize there may be times when such changes are warranted, or even necessary. For example, an institution whose market reputation and financial condition has declined sharply may benefit from the installation of a fresh team. In these cases, the decision to make management changes often reflects the correction of past board decisions to allow a stagnant management team to remain in place too long, ultimately damaging the organization’s credit quality. Significant management changes could, over time, ultimately lead to credit improvement if they resulted in enhanced strategic decision-making and implementation.
Frequent turnover of senior management in a single position, both at the presidential level or below, is often an indicator of systemic management weakness and may well result in credit pressure if it disrupts the institution’s ongoing operations. For example, we have seen instances where the Vice President for Enrollment Management or equivalent position has changed each year for a multi-year period, sometimes during the peak admissions cycle. This has then interrupted the institution’s ability to achieve enrollment and/or financial aid targets for several years in a row. Similarly, recurrent changes in the Vice President for External Relations/Development position during a campaign period have been known to affect progress toward campaign targets.

Changes at the presidential level due to scandal, disagreements with the Board, or votes of no-confidence by the faculty have typically not affected credit quality. However, it is possible that credit quality could decline if the change signaled fundamental governance or management issues at the institution, resulted in loss of donor support, or affected the ability to recruit or retain students. Again, in some cases, Board action to make changes at the presidential level could be viewed as a credit positive. An example of this could include replacement of a “visionary” President who has over-extended the institution, resulting in market challenges and financial stress.

There are good governance best practices that institutions can implement to ensure a more seamless transition in case of change. One key practice is the encouragement of a moderate amount of turnover at both the board and management levels, which is typically beneficial for an organization. This turnover can be most effective if it occurs in the context of a succession plan for key executive posts. Another best practice, highlighted by recent hurricanes, is to establish procedures for leadership in the case of an emergency where key personnel become unavailable. Under best practices, these policies are embodied in a document that is updated and reviewed by the board on a regular basis. Such procedures can help to defuse any concerns regarding an unexpected change in management.

During periods of change, it is often helpful for Moody’s to have direct communication with the Board to discuss transition issues and strategies. We examine each case of turnover on a case by case basis. It would be highly unusual for management change, in and of itself, to result in an immediate rating action. Rather, if these changes had a longer term impact, positive or negative, on the ability to attract students or philanthropic support, or resulted in change in fiscal condition, the rating could be affected over time.
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