Canadian University Sector:

A Strategic Insight on Finance and Leadership

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The University (Finance) Dilemma

Top financial officers of Canadian universities face missions that sometimes seem impossible. They are responsible for finding and using scarce financial resources to maintain and further lead and grow their institutions as centres of excellence for teaching, learning, research, scholarship, and creativity of all kinds.

In this brief, we give a strategic perspective on both the finance problem and the leadership challenge. We also suggest directions for a solution. Universities are full of experienced experts in diverse fields, many of whom have strong executive skills. Strategic specialists from outside the university can help these talented people to achieve their academic goals by either a better use of current resources, financial or otherwise, or discovery of new resources. The key to success is to have principal decision-makers in different units of the university buy into the strategic transformation as an essential enterprise that serves their own interests. The outside strategic specialists serve only to assist the discovery and guide the way forward to success. The overarching result should be a standardized protocol and tool kit for strategic planning and implementation in the university.

The Many Challenges of Universities

Let's remind ourselves about the strategic challenges of university finance and leadership and anticipate some directions for remedy and relief.

Budget Overruns: Financial complexity produced by multiple funding sources, such as federal and provincial governments, tuition fees, endowments and research grants, often result in budget imbalances and overruns throughout academic units of the university.

Misaligned Missions: As universities are largely financed by public funds, their missions become confused when they contemplate revenue-generating activities. Opinions vary widely about whether it is appropriate for a public institution to recover its costs through revenue initiatives. The right balance requires a compromise based on coherent principles.

Unclear Costs: The intrinsic conflict of revenue generation and balancing budgets produces a cloudy picture of the true costs of operations at the unit level. Unclear and/or confused costing leads to poor resource allocation and a pervasive sense of fiscal unfairness.

Navigating Blindly: While statistics are abundant throughout universities, pertinent real-time information for monitoring the progress of important strategic initiatives is often lacking. University accounting and operational information systems are incapable of answering many key strategic questions. What is the true annual operating cost of a new capital investment over its lifetime? How much of the operating cost of the new investment is funded by the host department versus general university funds? Are new investments – programs, facilities, etc. - justified by market trends for academic products and services?

Volatile Enrolment: Uneven enrolments in academic units throw off both budgets and workloads. At the unit level, developing and monitoring enrolment targets is usually a foreign concept. Because university funding is derived from public sources, academic units often take a passive and reactive approach to student recruitment targets. The balanced budget focus of a typical unit leads to the assumption that funding will always be there since the amounts are based on historical enrolments within each faculty. What happens when enrolments in previous years decrease? If capital investments are made based on the assumption that enrolments, and hence budgets, will continue unchanged, how can the operating costs of capital assets be supported when enrolments decrease?

Need for Internal "Transfer Pricing": Currently, many units, large and small, provide facilities or services to internal users (and sometimes external users) for "free". There are no established operating models, even something as simple as an internal price list, that can be applied when delivering services or renting out facilities. The result is a distorted cost structure throughout the university.

Finding Operating Funds for Capital Investments: Many sources of university funds, such as the federal agencies in the Tri-Council or the Canadian Foundation for Innovation, provide funds for capital expenditures for the purchase of research equipment or construction of new facilities. These same agencies provide little or no funds at all for normal operating costs. This situation strains the university's cash flow position when it is recognized that annual operating costs can exceed 30% of the initial capital cost. From a strategic perspective, every new academic venture, whether funded by an agency, benefactor, or industrial partner, should seek a complete and balanced portfolio of funds to cover all costs. A university that is flooded by ample capital funds can be made poor by the operating costs of maintaining the capital assets that these funds buy.

Need for Organized Strategic Reporting: While it is common practice in industry for business units to provide regular status updates on the progress of strategic and operational initiatives, universities have a difficult time enforcing such a discipline. This practice poses threats of missed objectives and budget overruns, which are usually discovered too late. It is not helpful to have, say, quarterly budget updates that are (1) not very detailed or well thought out and (2) unrelated to overall strategic objectives, both short and long-term.

Student Full-Time Equivalencies as a Common Currency: Sources show that approximately 60 to 70% of revenues per student in Canadian universities are provided by public funding[1]. This funding is anywhere from $8,000 to $22,000 for every 30 credits delivered, a measure that defines one FTE[2]. Faculty and departmental budgets, however, are preset and do not clearly account for FTEs as a revenue stream. Rather, they are based on an overall historical FTE count and an operating-only budget, with the expectation to end each year with a zero deficit. Furthermore, there are no incentives for the various units to introduce either cost-cutting or growth initiatives or both - the annual budget is "standardized" and is generally increased by a small annual increment, irrespective of performance. One simple option is introducing a rolling budget. This would allow the various divisions to increase appropriate budget accounts based on performance. For example, an increase in student registrations, which is essentially a good thing for the university, should equate to an increase in student administrators.

Strategic Options with Tremendous Potential

Universities face a unique challenge when it comes to aligning strategic objectives. Unlike corporations, the objectives at the unit level (i.e. faculty or department) are often detached from those at the administration level. In a corporation, there is a common ground in the name of profitability at both the corporate level and business unit level, as illustrated in Figure 1.

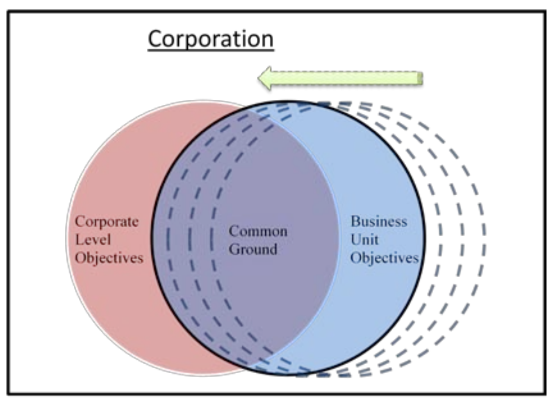

Figure 1 - Alignment between Corporate Level and Business Units in a Corporation

In a university, the common ground is essentially non-existing as illustrated in Figure 2.

[1] Source: DRSI, MELS
[2] Ibid

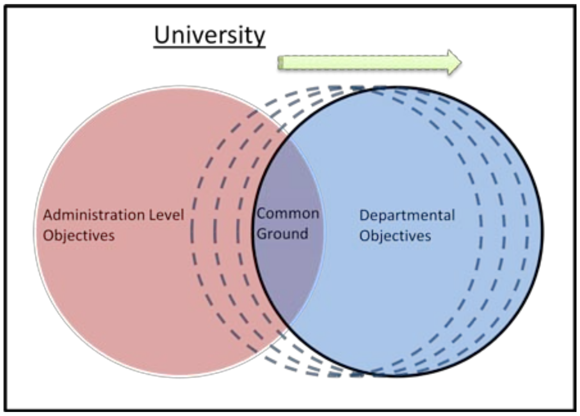

Figure 2 - Alignment between Administration and Departments in a university environment.

The administrative level objectives take cost-recoveries and additional funding into account while the individual departmental objectives focus on course delivery and research with little consideration on costs and the return on investments. Identifying a common ground that is mutually endorsed by administration and individual units will be the key in aligning strategic objectives at all levels.

A full strategic review would have many facets. It might begin with pilot implementations in one or a few selected academic units where efficiencies and improvements are clearly needed. The model could then be adapted and exported to other units, in each case with buy-in and involvement of key unit personnel.

The following are a few strategic methodologies that would feature in unit reviews.

Define the Organizational Structure: A key starting point is to define the right place and structure for the unit in the overall organization of the university. Is it correctly placed and sized? Can the faculty model be challenged? Are there any other services to amalgamate?

Standardized Approach to Strategic Planning: A strategic review should not involve the application of a cookie-cutter formula. Every academic unit is unique and needs customized attention. Yet, some key strategy principles and concepts should be uniformly applied in the whole exercise. The methodology is just as important as the strategic imperatives developed.

Use of Activity-based Costing: Academics might groan when a financial administrator suggests the use of better cost accounting but a sound costing model (such as ABC) is essential to efficient and rationale resource allocation. Properly used, an ABC framework will not only provide a clear and accurate picture of the financial health at a granular level; it will also arm the university leadership with information that can justify decisions made – especially decisions requiring substantial change management.

Balanced Scorecard: The balanced score card is a common-sense performance management tool that has been successfully applied by managers to track the execution of activities under their control and to monitor the consequences arising from these actions. The methodology is a way to measure and adapt strategically. As a non-profit entity, a university is prime for adopting a Balanced Scorecard framework because of the well-rounded and multi-faceted objectives that the scorecard is designed to monitor and achieve.

The Way Forward

The social and economic value created by universities is undeniably important for healthy social and economic development. That value contribution is threatened when the university is not able to use its financial resources efficiently and effectively in delivering its activities. Symptoms of below-par performance are plentiful but identifying the root causes of the problems and resolving them is not easy. A strategy is a plan of action designed to achieve a vision. We respectfully suggest that a strategic review of university finance is one key to improving the overall health of universities and allowing them, and society in general, to realize their full potential and vision. □

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