The Basics of Institutional Finance
Strategic finance is aligning resources with the institution's mission and strategic plan.
Managing the New Normal

Mission

Market

Margin

Used by permission rpkGROUP
Mission, Market and Margin

Living at the Intersection of Mission, Market and Margin:

Three Questions

What are we good at? (Mission)

What do people want? (Market)

How do we bring these together in a way that is true to our mission and generates resources? (Margin)
How should we respond to the external and internal environment?

1. Know where your economic engines are
2. Focus on mission/market/margin opportunities
3. Have the courage to reallocate
Cost Effective: Cost Reductions + Productivity

Cost reductions =

Permanent structural reductions in spending

From paying $1 for X
To paying $0.75 for X

Productivity improvements =

Increase in output (learning, research, jobs), without changing admissions or spending

From paying $1 for X
To paying $1 for X + 2
Cost Reductions

Dollars Saved

Health Benefits Cost Shift

Fixed Operational Settings (Temp and Lighting)

Cogeneration Plant

Privatized Housing

Savings vs. Time

Dorm Landline Elimination

Summer/Winter Facilities Shutdowns

Wellness Programs

Time to Achieve
New Tools for New Times
1. Deciding What’s Important

- Key Performance Indicators
  - *Measures institutional performance in key areas*

- **How do you know if you have the right ones?**
  - Focus on important issues
  - Impact decision making
  - Understandable
  - Come from available data
  - Must have trend, benchmark, and target
  - Few in number

- Peer Groups

- Importance of Telling the Story
Graduation Rates Lag Behind COPLAC Peers

- Shepherd 4 YR: 20%
- Shepherd 6 YR: 43%
- COPLAC 4 YR: 35%
- COPLAC 6 YR: 54%
- Target 4 YR: 30%
- Target 6 YR: 50%
Cost Per FTE

- FY 2006: $12,429
- FY 2007: $12,527
- FY 2008: $13,755
- FY 2009: $14,526
- FY 2010: $15,549

Target < COPLAC Avg.
2. Return on Investment

- An understanding of net revenue is an essential component of determining return on investment

- Represents a key cultural shift in the move from “spending” to “investing”

- Calculating net revenue requires:
  - Right General Ledger Structure
  - Cost Center Based Budgeting
## Net Revenue – Sample Analysis

### Net Revenue Modeling - By Division

<table>
<thead>
<tr>
<th></th>
<th>PT</th>
<th>Undergraduate</th>
<th>Accelerated</th>
<th>Graduate</th>
<th>Institutes</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tuition Discounting</strong></td>
<td></td>
<td>5,656,577</td>
<td>0</td>
<td>876,158</td>
<td>0</td>
<td>6,572,761</td>
</tr>
<tr>
<td><strong>Discounted Revenue</strong></td>
<td></td>
<td>10,029,909</td>
<td>3,999,994</td>
<td>9,390,479</td>
<td>464,207</td>
<td>26,326,009</td>
</tr>
<tr>
<td><strong>Total Discount %</strong></td>
<td></td>
<td>36.06%</td>
<td>1.61%</td>
<td>8.53%</td>
<td>0.00%</td>
<td>19.98%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>PT</th>
<th>Undergraduate</th>
<th>Accelerated</th>
<th>Graduate</th>
<th>Institutes</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Discounted Revenue</strong></td>
<td></td>
<td>10,029,909</td>
<td>3,999,994</td>
<td>9,390,479</td>
<td>464,207</td>
<td>26,326,009</td>
</tr>
<tr>
<td><strong>Direct Costs</strong></td>
<td></td>
<td>8,284,316</td>
<td>1,554,435</td>
<td>2,874,851</td>
<td>347,933</td>
<td>14,339,204</td>
</tr>
<tr>
<td><strong>Net Revenue</strong></td>
<td></td>
<td>1,745,593</td>
<td>2,445,559</td>
<td>6,515,628</td>
<td>116,274</td>
<td>11,986,805</td>
</tr>
<tr>
<td><strong>Net Revenue %</strong></td>
<td></td>
<td>17%</td>
<td>61%</td>
<td>69%</td>
<td>25%</td>
<td>46%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>PT</th>
<th>Undergraduate</th>
<th>Accelerated</th>
<th>Graduate</th>
<th>Institutes</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Discounted Revenue</strong></td>
<td></td>
<td>10,029,909</td>
<td>3,999,994</td>
<td>9,390,479</td>
<td>464,207</td>
<td>26,326,009</td>
</tr>
<tr>
<td><strong>Total Direct and Allocated Cost</strong></td>
<td></td>
<td>9,954,583</td>
<td>3,149,668</td>
<td>7,858,580</td>
<td>347,933</td>
<td>23,677,592</td>
</tr>
<tr>
<td><strong>Net Revenue</strong></td>
<td></td>
<td>75,326</td>
<td>850,326</td>
<td>1,531,899</td>
<td>116,274</td>
<td>2,648,417</td>
</tr>
<tr>
<td><strong>Net Revenue % - FY 2010</strong></td>
<td></td>
<td>0.8%</td>
<td>21.3%</td>
<td>16.3%</td>
<td></td>
<td>10.1%</td>
</tr>
<tr>
<td><strong>Net Revenue % - FY 2009</strong></td>
<td></td>
<td>2.1%</td>
<td>28.8%</td>
<td>25.0%</td>
<td></td>
<td>16.5%</td>
</tr>
<tr>
<td><strong>Net Revenue % - FY 2008</strong></td>
<td></td>
<td>5.5%</td>
<td>20.0%</td>
<td>25.0%</td>
<td></td>
<td>16.0%</td>
</tr>
</tbody>
</table>
Net Revenue – Sample Analysis

Net Revenue Modeling - By Division

<table>
<thead>
<tr>
<th>Undergraduate</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>15,686,486</td>
</tr>
<tr>
<td>Tuition Discounting</td>
<td>5,656,577</td>
</tr>
<tr>
<td>Discounted Revenue</td>
<td>10,029,909</td>
</tr>
<tr>
<td>Total Discount %</td>
<td>36.06%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Undergraduate</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Discounted Revenue</td>
<td>10,029,909</td>
</tr>
<tr>
<td>Direct Costs</td>
<td>8,284,316</td>
</tr>
<tr>
<td>Net Revenue</td>
<td>1,745,593</td>
</tr>
<tr>
<td>Net Revenue %</td>
<td>17%</td>
</tr>
</tbody>
</table>

Undergraduate

| Discounted Revenue | 10,029,909 |
| Total Direct and Allocated Cost | 9,954,583 |
| Net Revenue | 75,326 |
| Net Revenue % - FY 2010 | 0.8% |
| Net Revenue % - FY 2009 | 2.1% |
| Net Revenue % - FY 2008 | 5.5% |

The undergraduate program appears profitable when measuring gross revenue but is barely breaking even when measuring net revenue.
Net Revenue – Pitfalls to Avoid

- Remember that you are creating a model, and that no model is perfect
- Failed attempts at calculating net revenue typically result from over complication of allocation formulas – keep it simple
Getting to Net Revenue: Cross Subsidies

- Almost all institutions have subsidized academic programs
- Cross subsidies are not bad, however institutions need to be more transparent about where they occur
- When determining the appropriateness of a subsidy, institutions should consider:
  - Program’s relation to mission
  - How long the subsidy should occur
  - Amount of the subsidy
3. The “Cost Pers”

- Cost per
  - FTE
  - Degree
  - SCH
  - Course
Cost per Degree

- Typically “Cost Pers” have been enrollment driven – SCH and FTE
- Cost per Degree looks at the key output measure under the attainment agenda
The “Top Eight” List

- Total revenues by source per FTE
- Total cost per FTE
- Total education and related spending per FTE
- Total education and general spending per FTE
- Spending by expense category
- Cost per student completion
- Student and Subsidy Share of Education and Related Spending
- Costs associated with excess credits
## Benchmarking Information

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Composite Financial Index</strong></td>
<td>3.6</td>
<td>(6.1)</td>
<td>4.4</td>
<td>7.0</td>
<td>3.0+</td>
<td>F</td>
<td>Yes</td>
<td>4.9</td>
<td>(4.3)</td>
</tr>
<tr>
<td><strong>Sufficiency of Net Assets Ratio:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Primary Reserve</td>
<td>50%</td>
<td>50%</td>
<td>84%</td>
<td>101%</td>
<td>40%+</td>
<td>N</td>
<td>Yes</td>
<td>76%</td>
<td>60%</td>
</tr>
<tr>
<td><strong>Debt Management and Physical:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Plant Ratios:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Viability</td>
<td>1.6</td>
<td>1.4</td>
<td>2.4</td>
<td>2.5</td>
<td>1.25+</td>
<td>F</td>
<td>Yes</td>
<td>0.7</td>
<td>0.4</td>
</tr>
<tr>
<td>Leverage</td>
<td>6.1</td>
<td>5.1</td>
<td>6.2</td>
<td>5.8</td>
<td>2.0+</td>
<td>F</td>
<td>Yes</td>
<td>1.4</td>
<td>0.9</td>
</tr>
<tr>
<td>Debt Burden</td>
<td>7.1%</td>
<td>7.3%</td>
<td>5.5%</td>
<td>5.0%</td>
<td>7%</td>
<td>F</td>
<td>Yes</td>
<td>10.1%</td>
<td>9.0%</td>
</tr>
<tr>
<td>Age of Facilities (years)</td>
<td>16.6</td>
<td>15.7</td>
<td>15.7</td>
<td>15.3</td>
<td>U</td>
<td></td>
<td></td>
<td>10.0</td>
<td>10.8</td>
</tr>
<tr>
<td><strong>Operating Measures Ratios:</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Income</td>
<td>2%</td>
<td>-55%</td>
<td>3%</td>
<td>23%</td>
<td>3%+</td>
<td>F</td>
<td>No</td>
<td>10%</td>
<td>-31%</td>
</tr>
<tr>
<td>Return on Net Assets</td>
<td>7%</td>
<td>-14%</td>
<td>-1%</td>
<td>12%</td>
<td>4%+</td>
<td>F</td>
<td>Yes</td>
<td>7%</td>
<td>13%</td>
</tr>
</tbody>
</table>

* Notes:
  1. Maryland Private Colleges include Goucher College, Loyola College, Maryland Institute College of Art, and Stevenson University.

Legend:
- F= Favorable
- N= Neutral
- U= Unfavorable
4. Understanding the Academic Portfolio

- Which programs house most of the institution’s students?

- How well am I responding to market demand?
  - Current academic portfolio
  - Untapped opportunities

- What is my student yield, particularly within high demand programs?
Undergraduate Students by Major - Fall 2011

Students in these 15 majors represent 44.9% of all undergraduate students.
1. Question - Are departmental costs higher or lower than the benchmark group?

Metric - Cost per unit - Student Credit Hour and Full-time equivalent

2. Question – Is the department more or less efficient?

Metric - Throughput – Student credit hours generated by each faculty member
Sample Metric - Direct Instructional Expenditure per FTE Student

Less efficient than market standard

More efficient than market standard

Source: Delaware Instructional Cost Study
Cost Effectiveness

- Once they determine the relative cost effectiveness, institutions can identify departments for additional focus and drill down to determine why cost structures vary.

- Key areas of focus for the drill down include:
  - Labor Costs as a % of Total Department Costs
  - Mix of Full-time and Part-time faculty
  - Mix of faculty rank
  - Average SCH taught by FTE faculty (throughput)
  - Average class size
Sample Metric - Student Credit Hours per FTE Faculty

More efficient than market standard

Less efficient than market standard

Source: Delaware Instructional Cost Study
Using Scorecards in Academic Portfolio Analysis

- A review of an academic program involves multiple variables, both qualitative and quantitative
- Variables generally would address mission, enrollment, finance and other outcomes assessments
Using Scorecards in Academic Portfolio Analysis

- Scorecard variables could include data such as:
  - Relation to mission
  - Market Demand
  - Student Yield
  - Retention and Graduation Rates
  - SCH Generation
  - Efficiency
  - Net Revenue
# Sample Academic Program Review Scorecard

## Program Options

- **Grow**: Maintain/Manage Cost
- **Maintain/Manage Cost**: Grow
- **Sunset**: Redesign
- **Redesign**: Sunset

## Scorecard

<table>
<thead>
<tr>
<th>Program</th>
<th>Mission</th>
<th># Prospects</th>
<th>Yield</th>
<th>Credit Hours</th>
<th>Student Cr Hr/FTE Faculty</th>
<th>Direct and Indirect AllocatedCost Model</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Yes</td>
<td>&gt; 5,000</td>
<td>&gt;33%</td>
<td>&gt; 1,000</td>
<td>Above Benchmark</td>
<td>Positive</td>
</tr>
<tr>
<td>B</td>
<td>Yes</td>
<td>&lt; 1,000</td>
<td>&lt; 33%</td>
<td>&gt; 500</td>
<td>At Benchmark</td>
<td>Positive</td>
</tr>
<tr>
<td>C</td>
<td>Yes</td>
<td>&gt; 1,000</td>
<td>&lt; 33%</td>
<td>&gt; 500</td>
<td>Below Benchmark</td>
<td>Negative</td>
</tr>
<tr>
<td>D</td>
<td>No</td>
<td>&lt; 1,000</td>
<td>&lt; 33%</td>
<td>&lt; 500</td>
<td>Below Benchmark</td>
<td>Negative</td>
</tr>
</tbody>
</table>

Used by permission rpkGROUP
5. Business Plan Pro Formas

- A more detailed analysis of proposed or existing academic and administrative programs can be provided through the use of pro formas
- Pro Formas project revenue and expense activity in order to determine start-up costs and return on investment
- Pro Formas also serve as an important accountability tool
Business Plan - Advantages

- *Sets the bar*
- *Creates Milestones – Go/No Go*
- *Resources identified up front*
- *Builds accountability*
A Strategic Finance Agenda

- Assess Data
- Develop Metrics
- Create Reinvestment/Innovation Pools
- Reduce Admin and Operating Costs
- Drive Revenue
- Streamline Academic Program
- Document and Communicate
Transitioning to Strategic Finance

Four Key Questions

– Where are we now?
  ▪ Reality Check

– Where are we going?
  ▪ Strategic Plan

– What will it take to get there?
  ▪ Resource alignment

– How will we know when we’ve arrived?
  ▪ Continuous monitoring of new metrics
To continue the conversation

Rick Staisloff
Principal
rpkGROUP
rstaisloff@rpkgroup.com
(410) 591-9018