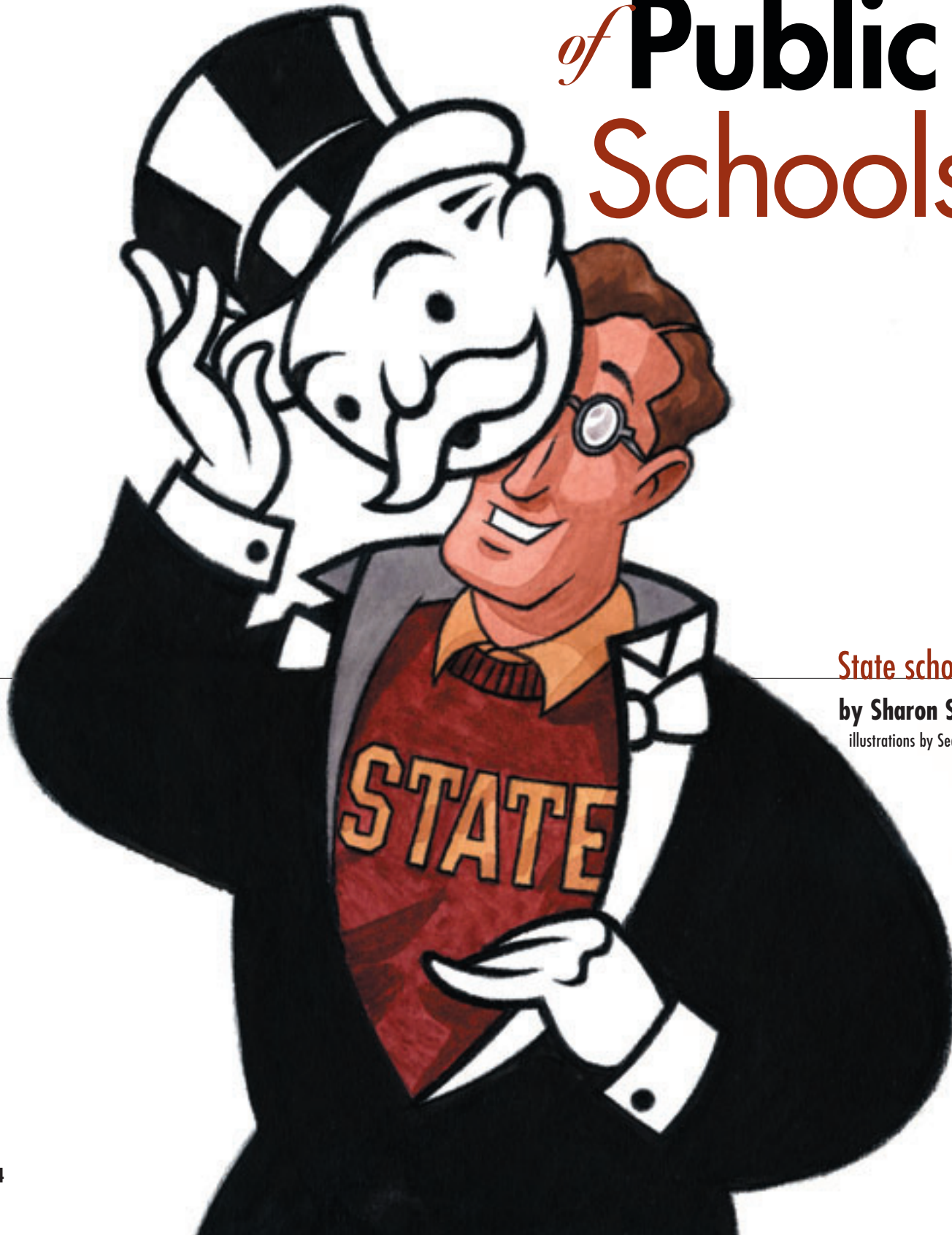


The *Private* Face
of Public
Schools



State schools stay

by Sharon Shinn

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In the competitive world of elite business schools, money is everything. With sufficient funds, a school can attract world-class faculty, invest in state-of-the-art facilities, enroll the best students, and score high in the rankings. But that upward climb requires adequate funding, which usually translates into a healthy endowment and high tuition fees.

Private schools generally have both. Public schools? Not so much.

Yet a handful of public business schools are positioning themselves to be among the best worldwide by transforming themselves so that they operate much like private schools. They're raising fees, courting alumni, taking control of their budgets, and throwing their mortarboards into the ring. They're here to compete at the highest levels, and if that means acting like private institutions, so be it.

"We haven't explicitly set out to say we want to be 'more private,'" says Robert J. Dolan, dean of the Stephen M. Ross School of Business at the University of Michigan in Ann Arbor. "But we do want to be the best business school of our type. That means being able to attract the top talent and compete with all universities, including private ones. Just defining our competitive set as other public institutions isn't the right way to think about it. Our aspirations are much higher."

Howard Frank, dean of the Robert H. Smith School of Business at the University of Maryland in College Park, puts it even more bluntly. "If you look at the top ten schools, seven or eight of them are private," he says. "They're not in the top echelon because they're private, but because they have more money."

The urge to pursue private money really began as states started cutting funds for education. "Many state schools now identify themselves, not as state-

competitive with the top elites by raising enough money to act like private schools themselves.

supported, but as state-assisted," says Hasan Pirkul, dean of the School of Management at the University of Texas at Dallas. "Depending on what school you're looking at, support from the state could be as low as 15 to 20 percent of the university's total budget. That makes it absolutely necessary to provide alternative funding sources."

The percentage is even lower at the Smith School, where the annual budget is between \$55 million and \$58 million. "We get roughly \$4 million from the state," says Frank. "The rest is made up from tuition and revenues for services and programs. A private school gets no state support, so the difference between the Smith School and a \$50 million private school is basically nothing."

Frank and other deans emphasize that the move toward privatization brings with it a whole new attitude. "We're running an educational business," says Joseph A. Alutto, dean of the Max M. Fisher College of Business at The Ohio State University in Columbus. "We happen to be located in a public institution, but we need to think carefully about the quality of the product we have and whether that product is providing value to those people who purchase it." In other words, they need to operate like privately run businesses.

Balancing the Budget

Like private business owners, these deans become wholly responsible for the budgets governing their enterprises. This is a major difference between a typical state school and a public school with private leanings. Currently, many state schools use an “expenditure authorization system,” says Alutto, in which a dean is given a set amount of money to spend regardless of how much his school is generating. Resources are allocated depending on where the money is most needed; business units that aren’t generating enough money to survive are funded by the units that are generating a surplus.

The new model, which he calls “responsibility-based budgeting,” requires every college to be responsible for all revenues generated and all expenditures made. Some units still might lose money, Alutto notes, but a “tax” system in place gives the university some flexibility in diverting funds to less successful units. “The school still has to manage within its budget plus whatever the school gives it through the taxation system—or its budget and whatever the school takes away through taxation,” says Alutto. “But then what the tax rate should be becomes a public discussion rather than a hidden distribution of slush funds.”

Responsibility-based budgeting has the immediate impact of making school administrators consider how to bring in more money. The three most obvious sources are increased tuition, stepped-up private giving, and an expanded executive education program.

Tuition is often the first component to be addressed. State schools looking to privatize first raise their tuition—or at least their graduate school tuition—to something close to market rates. For instance, the Darden Graduate School of Business Administration at the University of Virginia in Charlottesville benchmarks its graduate tuition against schools like Harvard and Wharton. While a portion of tuition goes back to the central university, the school retains control of the rest. “Of course, we are often in dialogue with the university about what our resource priorities are and why they should be like that,” says Robert S. Harris, dean of Darden.

Another critical step is to emphasize increased donations from alumni and other potential donors. Says Dolan of Michigan, “We hope a number of alumni will say, ‘Now is my chance to perpetuate the school’s goals. The school’s on the right track, but it needs my financial support.’”

Last year, for example, alumnus Stephen Ross donated \$100 million to the University of Michigan, a donation that is expected to have a big impact. “We’ll spend about \$75 million on our facilities, which really need to be upgraded if we’re going to be competitive with our peer institutions.



We’ll also put \$25 million in our endowment,” says Dolan.

The third leg on the fund-raising tripod is executive education, where schools typically can charge a premium price that is not set by the university administration. Not only will executive education bring in additional funds, Pirkul says, but it can improve the school as a whole. It encourages faculty to maintain close ties with the business world; it also creates a whole body of alumni who are already in management positions and able to offer financial support to the school very quickly.

Once a school becomes responsible for its own budget, says Alutto, it never stops looking for other areas to expand—especially at relatively low costs. For instance, research centers can bring in money both from the private sector and from federal funding. One-year master of science programs offer a chance to generate revenue while not requiring the high infrastructure expenditures necessary to support an MBA program. As the school’s mindset reflects private-school values, Alutto says, other areas of revenue growth may be discovered.

Good to Great

Most deans see the trend toward privatization as overwhelmingly favorable. For one thing, higher tuitions force schools to provide even better programs.

“As you increase the costs of attending your program, students want to know they’re getting value for it,” Alutto says. “They become far more responsive and involved in the development of high-quality programming. You can no longer hide a professor who’s not teaching well when you’re charging students at the high end of the cost continuum, so there’s a lot more accountability.”

Privatization also encourages colleges within a university to work across boundaries. Because schools are being encouraged to generate revenue, says Alutto, “units that otherwise might not have been working with the Fisher College are suddenly very anxious to work with us. We’ve especially reached out to the school of engineering, because we think the com-

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bination of engineering and business will provide real additional value to students and faculty."

Another advantage to becoming more like a private school, suggests Harris of the Darden School, is that it allows the school to develop stronger ties with alumni. When alumni know that their investments—not the state legislature's budget—are shaping the future of the school, they tend to develop a "shared sense of destiny." He says, "I think the alumni of most private institutions have a different link with their schools than alumni of most public schools. They see that their investment is what's going to make the school go forward."

This is particularly true because, in general, privately raised funds face fewer restrictions than state funds. For instance, Pirkul notes, state funds are rarely earmarked to fund overseas travel for faculty, but private donations may be used to send professors to international conferences—which will improve both the faculty and the school.

Private funds can also be used specifically as donors request. "It's very clear that people want to see where their gift is being used and how it advances the agenda they're interested in," says Dolan. "One thing that helps us in our fund raising is that a gift to the business school really does get used for the business school."

Not So Fast

Still, operating a public business school as if it were private does have a few drawbacks. Frank points out that the school can suffer if enrollments go down and the school fails to meet its projected budget. Meanwhile, the business school isn't really in line for extra money if the university has any to hand out. For instance, when the University of Maryland had \$10 million to distribute to offset state budget cuts, the Smith School's take was only \$75,000.

Another downside is that there can be some tensions between the central administration and the more independent school. "As we initially started expanding, the university had no way of coming to grips with the kind of creature we were building," Frank says. "We still give the university controller more problems than any other three schools combined as he tries to figure out what we're doing."

Privatized business schools also sometimes have to worry about jealousies from other schools on campus. "Business schools are already thought to be the wealthiest places on campus, even though often they're not," says Frank. "As you go out and generate your own revenues, the campus tensions actually get worse. For instance, we have a terrific building, and some people are jealous of it. But I paid for it with our hard-earned funds! That gets lost in translation."

One School's Private Journey

How does a school move from public to private status? Through small, incremental changes, says Howard Frank of the University of Maryland. Upon arriving at the Smith School of Business in 1997, his first task was to raise the price of the MBA program to market rates, essentially by quadrupling the cost of the program over a number of years. Concurrently, the number of students was also quadrupled.

"Within a few years, we were generating 16 times the revenue we were generating the day I arrived," he says. "Did we wake up one morning and decide we were going to do that? No, it was a series of steps."

During this time, the school also opened satellite campuses and evening and weekend programs. Meanwhile, the executive education program was refined until it went from generating about \$500,000 annually to bringing in more than \$6 million. The school also launched an EMBA program in the U.S. and an executive education program in China.

Then Frank addressed various research centers on campus, slimming down existing ones and opening several new ones. In the process, he began an aggressive pursuit of research grants and contracts; today, the school brings in about \$5 million in such funds. "Along the way, we changed the culture so there were some inherent rewards for going after these grants," he says.

At the same time, he worked to expand the school. He added about 50 faculty members and almost 100,000 square feet to the facilities. The school now can boast laboratories for financial markets, supply chain management, behavior research, and electronics. "In the last few years, we have received the equivalent of \$10 million in gifts of software, hardware, and services to build these labs," he says. "Seven years ago, we had basically nothing."

And of course, there's the fund raising, though Frank considers that a somewhat modest proportion of the school's entire revenue chain. Still, charitable gifts have brought the endowment from \$6 million to \$35 million, and individual donors continue to give money on a regular basis. "Out of our budget, gifting will generate something like \$3 million a year," Frank says. "We're launching a campaign to triple that."

Ultimately, it all comes down to funding—to hire the top faculty, upgrade the facilities, and craft an image. Says Frank, "A *Financial Times* reporter recently asked what my top three priorities were, and I said, 'Money, money, and more money. And if I had a fourth priority, it would be money.'" With more funds, he says, he can build faculty, strengthen the school's reputation—and continue his quest to make the school competitive with the best.

The Touchy Topic of Tuition

Raising tuition is one of the time-honored sources of new revenue. But how much should it be raised—and should such increases affect all students? At many state schools, undergraduate tuition is set by the universities, which also determine how many undergraduates should be admitted to the business school.

The restrictions are chafing to some deans, including Joseph Alutto of The Ohio State University. "Since I arrived here, I've said that one of the best things I could do, even at the undergraduate level, is to triple the cost of tuition. It always gets a gasp. But as long as tuition is low, students will accept poor performance on the part of staff and faculty. Once they're paying market rates, they will demand—and they will get—high-quality performance at all levels."

Yet providing affordable education is part of the compact the public school makes with the state, and most schools are still bound by that contract. So, for now, undergraduates at the University of Maryland's Smith School of Business pay \$6,700 a year. At the University of Michigan, an in-state BBA student pays \$9,000. Says Michigan's Robert Dolan, "Where we show we're public is more in our undergraduate programs than our graduate programs."

Even so, as graduate tuitions trend higher, do deans worry that public schools might leave the neediest students behind? Most don't. "We now offer more scholarships than ever before, both at the graduate and undergraduate level," says Alutto. "Most of us in the public sector understand that we have a public policy imperative that insures that we still provide opportunities. The way we do that simply changes. We've gone from an endowment of \$10 million to a permanent endowment of about \$120 million. A good portion of that is designed to provide scholarships and fellowships for students."

At the University of Texas at Dallas, Hasan Pirkul agrees—

to a point. "In most excellent schools, there are scholarship funds available, and I think universities are very responsive to students in need," he says. However, he notes, as education gets more privatized, it becomes less affordable. "The people who get squeezed are not the poor, because there are funding sources that target them specifically. And obviously the well-to-do have the means to send their kids to college. I do think privatization hurts the middle class."

While higher tuition at the MBA level doesn't worry Robert Harris of the University of Virginia, he does think price hikes might affect undergraduates from less wealthy backgrounds. "Even though we're a public school, our out-of-state tuition is higher than that of other public schools," he says.

Therefore, the University of Virginia has launched a program called "Access UVa," which commits funds to financial aid. He

adds, "If you're going to raise tuition, then you have to figure out how to provide the education for a certain group of people.

Many of us believe that's better done through selective scholarships than through an across-the-board discount."

He has no qualms about raising tuition for grad students, even given the argument that "the taxpayers of the state have an obligation to finance the children of the taxpayers." He says, "We could argue all day whether or not that's relevant at the undergraduate level, but at the MBA level, the average age of students is 27 or 28. Their parents aren't paying for their educations; they are. And MBAs make good salaries when they graduate. Arguments for large state subsidies for graduate business students aren't the same as they would be for an undergraduate English major. You can take this public policy argument off the table when you talk about an MBA."

While it takes many components to make a public school resemble a private one, it seems clear that a key component is market-based tuition. That signals to everyone—students and stakeholders alike—that the public school is on a par with private institutions and certainly knows what its education is worth.



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than through an across-the-board discount." —Robert Harris, University of Virginia

Dolan, on the other hand, has not experienced conflict with the central university. "We haven't said anything like, 'We don't want this many in-state undergraduates,'" he says. "I also think we've convinced people that the BBA program benefits from a strong MBA program. We've been able to communicate to the university that we have a strategy in which all the parts are working together."

That's small comfort to another group of state schools who find the real disadvantage to privatization is that they're not able to do it. "Private funds go disproportionately to universities already known for excellence," notes Pirkul of the University of Texas at Dallas. Private funds also are donated by successful alumni, he says, and schools whose students come from a lower socioeconomic background might have few alumni in a position to give a great deal of money.

Another type of school that would find it hard to privatize would be a school with a unionized faculty, says Frank. "If a finance professor and a French literature professor make the same amount, you can't expect that business school to prosper in the upper echelons," he says.

This means that state schools that aren't able to make the leap to greater independence will find it harder than ever to compete with the best schools. "Schools that don't have an alumni base with enough success or a long enough heritage to help them out will be struggling to provide a quality education," says Harris of Darden. "So will schools where political reasons keep them from raising more private funds. I do worry about that gap."

Pirkul believes that what ultimately will separate public and private schools—or elite public schools and public schools with fewer resources—is the ability to do research. As financial support decreases, the resource gap between schools will relegate small, regional schools to being teaching institutions in the shadow of larger national research universities. "In the long run," says Pirkul, "that does have an effect on the quality of the education students will receive."

Making the Leap

Despite such concerns, these deans believe it's inevitable that more state schools will begin to pursue a private funding model. "Considering the way states are funded and society's appetite for tax cuts, I'm not sure any major change will take place in the funding of higher education," Pirkul says. "If you don't tax people to support higher education, they are going to have to pay for it."

For business schools that do want to move from a more public to a more private model, these deans recommend five essential steps.

Develop a strategy. Start with a carefully thought-out financial model. Harris suggests, "Sit down and ask, 'What kind of endowment do I need, what kind of tuition do I have to charge, how much money do I have to raise each year, how much money in scholarships do I need to offer to get students at this higher rate?'"

Alutto of the Fisher School points out that schools have to understand which programs make money, which ones don't, and which ones they're going to keep even if they're not profitable. "If you haven't defined your core values, then you can get in big trouble," he warns.

Work collaboratively. To succeed at the new model, you'll need "the support of the political apparatus that surrounds the public university," says Harris. He adds, "If it comes down to a fight, I don't think it works. There has to be a shared understanding of why it makes sense for the public and for the school. The change requires support from alumni, political forces, and university administrators. You've got to build some coalitions."

Build a strong management team. Frank structured his team slowly during his first few years as dean. "Once the team is in place, you'll have a very collegial set of department chairs," he says. If this group is full of entrepreneurially-minded people, so much the better. "My role has gone from being the one who creates new programs and ideas to being the one who makes sure there's enough energy behind the great ideas coming from many different places," he says.

Keep control of the money. Not only should the business school keep most of the funds it raises for itself, but the dean should be the one who decides what to do with it, Frank believes. "The finance department doesn't own the money it uses. That's owned by the dean's office," says Frank. "That's tremendously important when it comes to optimizing resources. While I don't do it frequently, I can move money in and out of a department."

Remember your roots. Even though the Darden School has gone toward a model of more private funding, Harris is quick to point out that the school has not split off from the university. "We're still proud to be part of the University of Virginia," he says. "We still partner with other schools around the university. Our students are still University of Virginia graduates, and I still report to the president."

As competition increases for the best teachers and the best students, business schools worldwide must refine their programs, define their niches, and align their priorities. Those who want to compete at the highest levels will be looking for ways to fund their ascension—and most will be taking the private route up an increasingly elite mountain. 