

# Balancing the B

► Higher education institutions the world over are facing an escalating fiscal crisis. In Europe, for instance, governments are buckling to cover the mounting costs of socially guaranteed higher education. Meanwhile, in the U.S., schools are facing mounting criticism over skyrocketing tuition fees while coping with dwindling government subsidies.

Business schools aren't immune to this global budget crunch. And, yet, even as their budgets tighten, b-schools face one of the most competitive markets for management education in years. The price to compete is substantial and includes the cost of new buildings, technology, curricula, and faculty. This spending spree has left many business school deans asking the same question: Where will we get the money?

James Johnson, management analyst in the Economic Model Office for Indiana University-Purdue University Indianapolis (IUPUI), notes that fiscal pressures on business schools are growing more intense. "Business schools don't get as much subsidy support as, say, a school of nursing," he says. "Yet business schools are also growing, going online, and expanding globally. That requires some dollars, so most business schools are bumping up against their capacity to fit these projects within their budgets."

Under these circumstances, an academic CFO's first impulse may be to slash student enrollment, downsize faculty, or even raise tuition. A close look at a budget's structure, objectives, and limitations may, however, help schools avoid these cutbacks of last resort. Innovative budgeting is more than balancing income with expenses, say experts. In many cases, it's not a matter of spending less in a budget—it's a matter of spending *differently*.

## Comprehensive Accounting

Even with the best of budgeting intentions, a business school is often burdened by "fund accounting," in which individual resources must be allocated directly to particular projects. A donor might require, for example, that her contribution be spent only on entrepreneurship or a new trading room. When a school must account for multiple funding sources, it often views them as separate entities. It then becomes easy to lose track of the whole picture, says Gary Matkin, dean of continuing education at the University of California Irvine (UCI) Extension and author of *Using Financial Information in Continuing Education*.



Business schools that take creative, comprehensive approaches to budget



# -School Budget

“Business schools get so many different kinds of funds—funds from the state, funds from donations, funds from tuition—we often lose track of the whole,” says Matkin. “Most institutional accounting systems try to account for those funds separately, which can make it difficult for a business school dean to put all that money together in a clearly drawn budget.”

Matkin recommends that schools set up what he calls “comprehensive budgets,” which outline all aspects of a school’s fiscal operations. A comprehensive budget shows all sources of income and denotes what sources fund what part of the operations, from one-time expenditures for special projects, to variable expenses such as scholarships and maintenance, to fixed expenses such as faculty salaries.

“A dean’s salary, for example, is a single amount, but it may be funded in part by state subsidies and in part by tuition,” Matkin explains. Different functions are performed with combinations of funds. Creating a comprehensive budget and reporting system puts it all together to show a school’s true financial situation.

Such holistic budgeting may not prevent the inevitable problems of restricted funding—a school may have a plethora of funds for entrepreneurship, while it struggles to find the money to hire a star to its faculty. But a comprehensive budget makes it clear where money is available and where fund-raising efforts may need to be redoubled.

## **Balancing Aspirations with Reality**

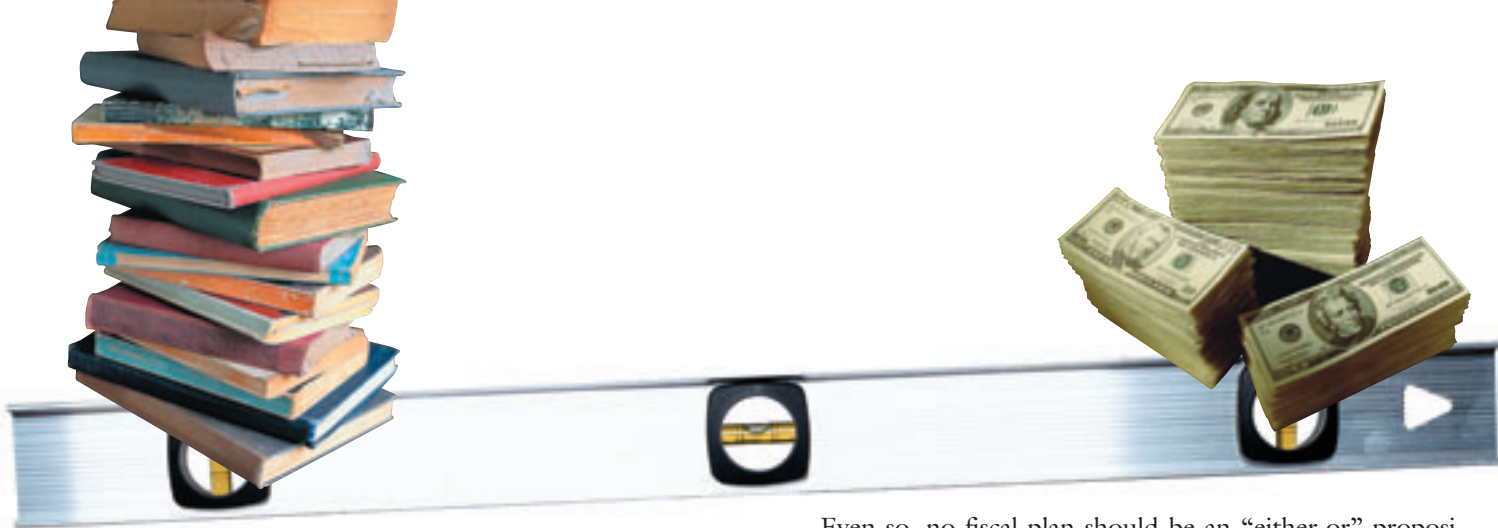
A central question revolves around how a school estimates its budget requirements for the coming one, two, even five years in a volatile market. Should an administration estimate according to its goals, which may be too optimistic? Or should it estimate conservatively, according to past failures, which may be too pessimistic? “If you’re aggressive and don’t make it, you have to spend your year cutting back,” says Lucie Lapovsky, president of Mercy College in Dobbs Ferry, New York, and a consultant in financing for higher education. “If you budget conservatively, you may miss important initiatives and sources of revenue.”

The more a school understands the true costs of its programs, from staples to salaries to scholarships, the better it can balance its aspirations with its capabilities. In the end, those numbers hold the answers to what a school can and cannot do. “Hammering out a viable



planning can make the scarcest resources fulfill even the loftiest missions.

by **Tricia Bisoux**



budget plan with aspirations, rather than numbers, is like pounding a nail with a marshmallow,” says Edward Whalen, retired vice chancellor of finance for the University of Houston and financial consultant for higher education. “Until the reality of limited resources is brought to bear on limitless aspirations, very little hammering is likely to take place.”

A school does not need to limit its number crunching to its own budgeting data. Lapovsky emphasizes that benchmarking against other institutions’ budget objectives is also an important step in effective budget planning, showing how a school is doing, both over time and relative to peers with similar goals. While some external information is inaccessible, most schools have access to an array of comparative data. Resources such as AACSB International’s Knowledge Services, for instance, offer data in areas ranging from budget-faculty ratios and average faculty salaries, to endowments and tuition, to sources and uses of operating funds by category. Such comparative information can highlight the strengths and weaknesses of a school’s existing budget; in addition, when used over time, benchmarking data also provide administrators a long-term idea of the effectiveness of specific budgeting decisions.

Even so, no fiscal plan should be an “either-or” proposition—that is, a school does not have to budget according to its aspirations *or* its budget constraints. Ideally, it should budget for both, with time being the only limiting factor. After all, an institution’s aspirations almost always should exceed its budget for it to remain competitive. Industry observers maintain that a school whose leadership keeps the status quo, just because budgets are tight, will soon be in decline.

“The aspirations of a school should never be in line with its budget. In fact, a dynamic institution’s aspirations will always exceed budget capacity,” Whalen emphasizes. “A school’s budget capacity simply sets a limit on how fast progress can be made toward those aspirations. It’s up to a business school dean to set priorities and decide what gets funded immediately and what must wait.”

In addition, a b-school budget often has to take into account investments that are difficult to justify in financial terms alone, say these experts. The calculation of return on investment on building reputation, for example, is more complicated for higher education than for business, because ROI isn’t always measured in dollars and cents. “If you’re trying to improve a school’s reputation, it means that the way some

## Decentralizing the Budget

A primary question in budgeting for higher education revolves around who really controls the bottom line. That is, should higher ed budgets be centralized or decentralized? In a centralized budget system, the larger university pays the bills, collects revenues, and apportions resources to individual schools and departments as needed. In a decentralized system, each school or department pays for its own expenses, while keeping most of the revenues it generates. A centralized budget ensures everyone gets an equal portion of revenues, while a decentralized budget does not. And under centralized budgeting, risks are minimized, but so is the potential for reward. Decentralization increases risk, but also the potential for growth.

Most academic disciplines benefit from a centralized budget system, but that may not be the case for all disciplines. Or so says Edward Whalen, retired vice chancellor of finance for the University of Houston. A consultant and the author of

*Responsibility Center Budgeting: An Approach to Decentralized Management for Institutions of Higher Education*, Whalen is positioned solidly in the camp for decentralization, especially where business schools are concerned.

In a centralized system, Whalen argues, the fortunes of everyone rise and fall with the economic tide. While this may defer risk, it dampens the entrepreneurial spirit of individual departments. Responsibility center management offers a profit incentive for growth.

Critics of RCM fear that such a capitalist structure will allow more fortunate departments to prosper while other, less profitable departments must fend for themselves. Whalen argues that while the inherent nature of a decentralized budget system motivates all departments to generate other sources of revenue, it also addresses financial imbalances among academic units. “A school operating under RCM does not get to keep all its funding. Some specified portion is taxed, if you will, by the central administration. Those funds are not used to support central administrative operations but are returned in different

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resources are allocated must be distorted,” says Matkin of UCI. “It takes someone with strength and determination to make those difficult resource allocation decisions.”

Successful budgets often create short-term plans that work to fulfill large objectives through incremental steps rather than large leaps of faith, agrees Thierry Grange, dean of the Grenoble Graduate School of Management in France. Such an approach allows a school to remain responsive to changing market conditions. And when plans fail, it allows them to reverse course altogether without catastrophic results.

“If you want to start a campus in Vladivostok, you must ask, how big a leap can you make? Perhaps you could go step by step, from close countries to far countries, taking two jumps instead of one,” Grange says. “In this way, you limit the risk and the strain on your budget.”

### **Planning an Exit Strategy**

Even under the best circumstances, there are areas of budgeting that must be based on assumptions and speculations: For example, how can you estimate the levels of demand for a new program? It’s that prediction that causes the most difficulty for higher education, says Johnson. It’s easy to dream big, he warns. It’s more difficult to plan for failure.

“Sometimes people’s expectations for success are much rosier than what a project can realistically deliver. Sometimes they just say, ‘Let’s go for it, hold our breath, and see what

happens.’ People are hesitant to put in place an exit strategy in the event the project doesn’t work,” Johnson says.

Exit strategies are crucial, not just for large-scale projects, but also for smaller objectives. After all, fiscal drains don’t always come in the form of multimillion-dollar new buildings, says Johnson. “Business schools often continue to add new programs without dismantling the old,” he argues. According to Johnson, it takes approximately five years for a school to phase out a program, but rather than phasing it out completely, many schools hedge their bets and keep the program on life support “just in case” more students are in the pipeline or a change occurs in the market.

When schools don’t create and follow exit strategies, says Johnson, it puts an unnecessary drain on resources and takes money away from new, more effective initiatives. “It creates an overload on everybody,” he says. “The school is under ever-increasing pressure to deliver more programs from the same resources.”

### **B-Schools as Entrepreneurs**

Unlike other disciplines, business schools are torn between two market realities: They must provide academic value to their campus communities *and* meet the demands of business for more immediate corporate training. In addition, they must compete with online for-profit providers, which are changing the marketplace. These new providers are offering

proportions to different schools in accordance with the institution’s overall objectives.”

Even centralized budgeting doesn’t prevent in-fighting over limited funding, Whalen continues. “Over a period of 40 years, I have observed that an ‘every unit for itself’ mentality exists under any budgeting arrangement,” he says. “Outstanding performance by a faculty member, department, school, or university is often watched with green eyes and met with muted applause by their respective peers.”

Nonetheless, he argues that RCM serves to reward those centers that compete constructively in an incentive-based environment and deters destructive competition among internal departments for limited funds. “When schools find that their revenues are connected to good teaching and student satisfaction, any neglected constituency receives the attention it deserves. Good teachers become appreciated not only for their contributions to the discipline, but also for their contributions to the financial well-being of the school,” says Whalen.

For many universities, especially public universities, adopt-

ing a budget based on RCM may be unrealistic or unwarranted given political realities. Even so, says Whalen, the income-generating capacity of many business schools sets them apart from other departments in a university.

Whalen raises a series of questions for b-school deans to consider. “What schools have faculty who are relatively well-paid among the disciplines? What schools have ample opportunities to generate consulting income? What schools have the biggest growth in enrollment and the best opportunities to offer income-earning professional conferences? Business schools,” Whalen says. “When all that income gets poured into a central pot, as usually happens in the so-called benign traditional budgeting systems, how much of that income percolates back to the business school?”

Not a great deal, he believes. Supporting the larger university may be one responsibility of the public business school, but even so, Whalen argues, today’s growing budget concerns should make even publicly funded b-schools ardent proponents of RCM.



**“The real threat for business schools is low-cost schools competing with full-service schools.”**

—Thierry Grange

lower-cost educational services, often in areas of the world that may be too cost-prohibitive for brick-and-mortar business schools. As a result, business schools are striving to compete with lower-cost rivals, via expanded e-learning programs and global partnerships.

“Five years ago, in all the deans and directors meetings, everyone thought that the main competition for business schools would come from consulting companies or corporate universities that would offer Web-based MBAs,” says Grange of Grenoble. “But it hasn’t happened that way. What has happened is comparable to what you see in the airline industry: Low-cost airlines are competing with full-service airlines. The real threat for business schools is low-cost schools competing with full-service schools.”

Still, say experts, it’s that free-market reality that constitutes business schools’ greatest advantage over other academic disciplines. Business schools have the ability to sell their instruction, information, and consulting to external markets. Rather than rely fully on state or university support, they have the unique opportunity to address budget shortfalls with entrepreneurial, potentially revenue-generating ventures.

This advantage is not lost on Grange, who is looking at Grenoble’s financial future with concern, given current demographic trends in France. The population of young people is decreasing, and with it, the school’s pool of applicants. Therefore, although Grenoble Graduate School of Management is one of only a few European institutions to charge private tuition, Grange believes that the school cannot rely on tuition income for its financial security. He sees another possibility for Grenoble—he hopes to build its revenues by selling more of its services to corporate customers.

“Currently, about 63 percent of our resources comes from students, 30 percent from companies, and 7 percent from supranational organizations such as the EU or World Bank,” Grange explains. “We would like to reverse those numbers by reducing student contributions to 35 percent and increasing corporate contributions for the rest.”

Such an entrepreneurial model for raising revenue, which sells services to corporations to subsidize individual tuitions, is one that business schools might more readily exploit, says Johnson of IUPUI. “Business schools are more sensitive to

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the market and can charge higher rates for their services than other academic disciplines,” he says. “They have the ability to generate revenues and surpluses.”

### **A Budget That Makes Sense**

In the end, budgets must do five things to be effective, Whalen asserts. They must be based on short-term and long-term plans; they must be flexible, able to increase or decrease in response to changing opportunities and priorities; they must be based on realistic estimates of available funds; they must be supervised throughout the year and adjusted in response to changing circumstances; and, finally, they must balance income and expenditure.

Johnson of IUPUI agrees that such a short-term and long-term approach to budgeting helps a business school weather nearly any storm. “There’s always the potential for crisis in higher education. In fact, it’s always in some sort of crisis,” says Johnson. “For business schools, most of these crises have been opportunities—corporate scandals and the call for transparency and ethics, for example. Crisis simply means that business schools have to be very nimble in adjusting their offerings, such as marrying full-time faculty with part-time faculty who are already working in the world.”

Furthermore, says Lapovsky of Mercy College, the best time to make budgets more efficient isn’t necessarily during an economic crisis. Administrators should view their budgets

critically even when revenues are flowing to prepare for less prosperous times. “In good times, schools often spend their increased revenues, rather than build these funds into their base,” Lapovsky notes. “These are the times, however, when they should look for special programs that can be discontinued or areas that could be outsourced, for example.”

Ultimately, balancing a school’s resources with its mission begins with looking outward to the market, not inward to internal demands. “In France,” says Grange of Grenoble, “we refer to the two e’s, *les etudiantes* and *l’entreprise*, and the two i’s, the internal and the individual.” When a business school’s budget is based on internal politics and individual objectives, it isn’t in line with what its students, donors, and corporate stakeholders value. As a result, its failure is all but assured, Grange argues. A school that bases its fiscal decisions on the needs of its students and community, however, will be much more likely to meet its objectives, avoiding catastrophe along the way.

There’s no question that business schools are under great pressure to expand their markets, upgrade their facilities, hire the best faculty, and add new programs to keep up with the pace of their peers. Still, it’s important to remember that the winners of this race won’t necessarily be those who spend the most. The business schools that eventually survive and thrive, even during times of economic uncertainty, will undoubtedly be those that spend *best*. 