Perspectives in higher education
2013
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Introduction

The education industry has faced many challenges over the years. And while the challenges have varied year by year, one common theme has emerged — the higher education environment is getting more and more complex. From liquidity and financing considerations caused by the recent economic downturn, to safety concerns brought to light by tragic incidents on campuses, to governance demands placed on the board of trustees, institutions are being pushed to keep up with the dynamic pace of change. Dealing with these challenges, as well as many others, has required the attention and involvement of a variety of constituents throughout an institution.

In our current edition of “Perspectives in higher education,” we have again highlighted several of the pressing challenges and related opportunities facing colleges and universities. From a financial perspective, institutions continue to evaluate the effects of federal budget cuts, as well as their overall cost structure and potential efficiencies that could result for shared services. From an operational perspective, institutions are evaluating their overall delivery model, their emergency management programs, and their approach to information technology. These topics, as well as such broad issues as athletics and the overall regulatory environment, are highlighted in this document.

Change within the higher education industry will not slow in the future. Those institutions that respond appropriately to the current challenges will be in a position of strength, while those that maintain the status quo may struggle to achieve their goals. Embracing change will be imperative, and will require focused efforts by many within an institution. Establishing a culture where change is encouraged by senior management and the governing board, with input and transparent and productive debate within the campus community, will be a critical component in ensuring institutional short- and longer-term strategic success.

Institutions should remember that the higher education industry in the United States is resilient and continues to be the finest in the world. Foreign countries often try to replicate the American educational system, and international students continue to flock to the United States to gain their higher education experiences. Approaching the current challenges and demands in a proactive and positive manner will ensure that the United States higher education industry continues to lead the world and fulfills its societal responsibilities and obligations as it has done for generations.

As a leader in providing audit, tax, and advisory services to the higher education and not-for-profit industry, PwC has been honored to work with many of the nation’s premier educational institutions in addressing their most pressing challenges. These opportunities provide us with a unique, national view into industry issues. Our industry professionals in accounting and auditing, regulatory compliance, risk management, exempt tax, and advisory services deliver to our clients a clear understanding of critical issues and guidance from experienced teams in the field. While this document is not meant to be comprehensive, it draws upon our understanding of the diverse nature of higher education institutions that have complex educational, research, and clinical activities and can serve as a broad platform for discussing these topical issues.

We hope you find this document useful, and I invite you to contact me at (646) 471-4253 with questions or comments.

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Governance practices

Background

Over the past year, boards of higher education institutions have found themselves front and center in the news. Whether it is a “philosophical difference of opinion” resulting in the firing and re-hiring of a University President or a prominent University’s board being challenged with mishandling a very public crisis, there is no question that governance practices in higher education have never been more important than they are today.

Additionally, in today’s corporate environment, boards are being held increasingly more accountable and are expected to be involved in more issues than ever before. In PwC’s 2012 Annual Corporate Directors Survey, 860 public company directors responded. Some of the highlights of that survey were:

- “…a marked increase in the hours directors dedicate to board work. More than half of directors say the amount of time they spent rose last year,
- over half of directors (52%) believe that some form of annual education should be required,
- …three-quarters want to dedicate more time to overseeing strategy,
- …directors are taking specific actions overseeing compliance programs designed to reduce fraud,
- …73% of boards have no clear allocation of specific responsibilities for overseeing major risks among the board and its committees, and
- …directors are uncomfortable with the challenge of effectively overseeing IT strategy and risk.”

Clearly, governing boards across all industry sectors are being required to be more involved in various aspects of the organizations they serve. More specifically, within the higher education industry, trustees are looking for ways to become more informed about the various risks of their particular organizations. They are also becoming more focused and aware of their individual responsibilities as they relate to risks across the institution.

Although the survey noted above was of corporate directors, many, if not all, of these same issues may be applicable for higher education boards. Recent highly publicized perceived failures have boards and trustees on high alert and asking themselves, “Could this happen to me and to the institution I serve?” As a result, institutions have heightened their awareness of the adequacy of the design and effectiveness of their governance structures, policies, and practices.

Impact on educational institutions

Currently, many institutions, including the board and audit committees, have focused on assessing the effectiveness of governance policies and practices. Several of the areas of current focus have included:

- Board structure – Institutions are trying to find the appropriate balance between having enough members to elicit challenging views and expertise on specific strategies, but not so many members that a consensus becomes difficult or impossible to achieve.

- Code of conduct – Integral to the code of conduct is the portrayal of the appropriate tone at the top. Boards are revisiting their codes of conduct and making sure they include clearly defined ramifications for breaches.

- Coordination across committees – A topic of focus has been appropriate information sharing among the various Board committees. This can be accomplished through cross-committee membership. Also formal

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1 Insights from the Boardroom 2012, PwC’s Annual Corporate Directors Survey
reporting lines are being clarified to ensure major issues get discussed at full board meetings. Coordination becomes more challenging in the academic medical center (AMC) environment, where there is a plethora of additional considerations from a governance perspective. Most AMCs have separate standalone governance structures for the clinical and teaching arms of the organizations because the risks and complexities are very different. The challenges in the AMC environment will continue to escalate as these institutions deal with the future impact of healthcare reform. In any environment, the ultimate goal is to ensure the entire universe of risks is being monitored, and that clear reporting lines exist from a governance perspective across the multiple boards or committees within a complex university academic medical center.

- Conflict of interest – Typically, conflict of interest policies have existed for board members, faculty researchers, and senior university officials. Many institutions are also considering conflict of interest throughout the entire administrative structure of the university, or for individuals in “sensitive” positions (e.g., procurement, investments, and facilities).

- Board education – The myriad issues facing higher education institutions currently require boards to be engaged in countless aspects of the organization. Only through proper orientation and annual training can board members feel secure they have the requisite knowledge to ask the right questions of management and other external advisors.

More specifically, audit committees’ areas of focus continue to include:

- Committee membership and meetings – The changing environment and role of the audit committee has necessitated more frequent meetings. Typically, audit committees at larger institutions meet between three and five times per year for approximately two hours at each meeting.

- Charter – The charter must clearly articulate the audit committee’s responsibility with respect to the relationship with the external and internal auditors, review of the IRS Form 990, responsibility for whistleblower hotlines, code of conduct and conflict of interest practices, legal contingencies, and other general risk and compliance issues.

- Self-assessments – Self-assessments should be performed annually and can be performed by comparing performance against the charter or against leading practices. The most effective assessment would incorporate both.

For other specific considerations related to emerging best practices for audit committees, see our publication, “Keeping Current Emerging Issues and Leading Practices for Today’s Audit Committees of Colleges, Universities and other Not-for-Profit Institutions.”

Our perspective

The list of risks and concerns that higher education institutions are facing is going to continue to increase and evolve. In response, institutions need to ensure the members of their boards have enough time and expertise to dedicate to the organization. More frequent and lengthier meetings are likely to continue. Board education is critical to ensuring members have the appropriate knowledge and institutional information to appropriately challenge and support management to get to the right answer, and to understand the universe of risks at a particular institution and how those risks play into the overall strategy of the organization. Several of the topics that will require the attention of institutional governing boards will continue to include the following:
Crisis management

External threats played out in mainstream media, such as Hurricane Sandy, unfortunate university scandals, the shootings at Sandy Hook Elementary, and other random acts of violence, will, unfortunately, require institutions to ensure they have appropriate plans to react swiftly and appropriately to maintain the health and safety of the student body and to communicate to the campus at large.

Financial transparency

Boards want to be sure they understand the financial health of their respective organizations. In particular the audit committee charged with oversight of the external audit relationship and review and approval of the audited financial statements needs to have a clear understanding of the financial information included. Also, many boards are asking for more transparency in the financial information they are provided. Internal management financial reports are being refined to display the key indicators that not only management and the board find relevant, but also rating agencies and other interested constituents. These financial reports include actual current-year information as well as future, longer-term projections including cash flows, key balance sheet ratios, future capital plans, and other key financial forecasts.

Information technology

Students are demanding the most up-to-date information technology capabilities, driving many institutions to undertake major financial system upgrades or implementations. At the same time, institutions are scrambling to keep their systems and data safe, develop strategies for distance learning, establish massive online open courses (MOOCs), and contemplate cloud computing. It’s no wonder boards are feeling ill equipped to deal with the onslaught of risks tied to IT. To deal with the unique nature of IT strategies and risks, institutional boards may find it necessary to establish separate committees or subcommittees.

Enterprise risk management

Enterprise Risk Management (ERM) continues to gain momentum in the higher education industry. As crises described above are played out in the media, those institutions with ERM initiatives well under way feel better prepared to deal with the issues, or at least have a better understanding of where gaps in effective risk management may exist.

Formal ERM programs are still considered a best practice, and many institutions are actively working to develop formal programs. However, many institutions are still debating how best to incorporate the ERM program into the decentralized structure of their organizations. As the strategic challenges of educational institutions intensify, the societal expectations become greater, and the resultant board fiduciary responsibilities continue to increase, ERM programs will be a hot topic of discussion between institutional leadership and their boards.

The next 18 to 36 months will be challenging in higher education as the complexity of issues facing the industry escalates. As institutions are faced with major strategic decisions in the areas of distance learning, global presence and expansion opportunities, healthcare reform, tuition affordability, student loan funding, research funding, deferred maintenance, and outdated information technology, just to name a few, coupled with continued pressure on the bottom line, governing board responsibilities, and their importance, will continue to be critically important.
The higher education delivery and business model

Background

Higher education is a popular topic in mainstream media today. Every aspect of the traditional model is being challenged — affordability, cost structure, delivery models, efficient processes, and the level of financial support provided by federal and state governments. The higher education system as a whole should acknowledge these challenges and take each aspect of the traditional model and assess its strengths, shortfalls, and potential improvements. A transformation in the delivery model and its current business practices will be critical to ensure the long-term success of higher education institutions.

The current challenges in higher education include the volatile economy, funding cuts, increasing public and political scrutiny, technological changes, and growing competition for students. In order to address these challenges, institutions are reviewing the current methods for delivering an education, the impact of the global economy and the competition for students, as well as the business model, including the faculty employment structure and shared services. Institutions recognize that change in each of these areas will not happen in the short-term; it will take a longer-term vision, with each area prioritized according to the institution’s needs.

Impact on educational institutions

Summarized below are three of the more significant areas currently under debate in this area, and several of the more pertinent questions institutions are asking themselves as they discuss each area.

Delivery model

Each week, articles appear in higher education journals and national newspapers highlighting the new trends in delivering an education to students. As a country, the United States is comfortable with the current face-to-face delivery model, including its tradition, the way students interact, and faculty familiarity with teaching under this method. But a shift from that “comfortable” model is on the minds of provosts and academic leaders. A new model of massive open online courses (MOOCs) is in the news daily, with strong interest from top-tier schools. Several institutions have already invested millions of dollars in the concept, course content, faculty involvement, and the financial success of these courses. Students are also interested — they are signing up, finishing courses, and determining how to apply the completion certificate to their degree.

But there are many questions being asked about MOOCs, including: Are they real? Can they make a profit? Do they destroy the real-time interaction between faculty/students therefore limiting the real learning experience? Is there a proper blended model between the two methods such as an online course with occasional class instruction? Does a blended model contribute to a faster degree at a more affordable price?

Additionally, a key point of discussion is whether faculty will align themselves behind new delivery models. Faculty understand education, delivering curriculum to students, and the motivation for students to learn, but may debate online courses, their delivery effectiveness, and the value of an online degree. Changes to the delivery model should involve academic leadership and faculty. Without faculty support, changes may be short-lived, with few campus-based institutions adopting the new model, and could derail the institution’s long-term vision.
**Global economy**

Globalization is here to stay and higher education is in a unique position to define its strategy for the future. Institutions are exploring their international plans to determine how best to meet the goals of their students and faculty. International expansion can include opening branch campuses, joint venture arrangements, collaborations with other institutions or foreign governments, study abroad programs, and specialized learning programs. In addition to exploring options for an international strategy, each campus must continue to recognize the intense competition among institutions to attract and retain quality students from around the globe.

Investing globally will be a question debated by boards and institutional leadership over the next few years. Globalization of higher education will continue to grow and be critical to the success of US-based institutions. The debate for new campuses in other countries will be lingering and the data does not support quick success. Difficult questions about the staffing of foreign campuses, measuring of return on investment, and determining the best timeline for go, no-go decisions are continued to be asked by institutional leadership.

**Business model**

Campus leaders are asking whether the current way of doing business is sustainable, and are thinking long term — 10 to 15 years into the future. Such business models as those in the for-profit higher education sector are leading to healthy competition for traditional institutions. From a cost-savings and efficiency perspective, several institutions are adopting shared back-office functions across multiple departments, schools, and colleges, as the old silo approach to the traditional organizational model can create duplication, inefficiencies, and inconsistencies in process. Faculty tenure, one of the most controversial topics in higher education, is also being reviewed and alternatives created, including action plans to move into a more accountable structure for instruction, research, and other activities of faculty.

Is an institution ready for a new business model? Senior leadership is exploring that question and the potential for revenue enhancements. Additionally, for the academic mission, faculty salaries drive expenses, thus the relationship between productivity and contract types (tenure versus one- to three-year arrangements) are being considered. On the administrative side of the structure, consideration is being given to what areas can be consolidated or shared to minimize duplication. In looking at a new business model, upfront investments to fund changes must be factored in to the overall cost/benefit analysis. New business models for sharing services should be aligned with academic priorities and support structure for students, research, and other activities.

There are no turn-key solutions to the new business model on campus. Finance officers, provosts, and other campus leaders must look beyond their own offices to see what can transform a process, function, or revenue line. What risk and investment will the institution be willing to absorb to create a long-term solution to the financial security of the organization? This question and others are currently being critically debated within the industry and within educational institutions.

**Our perspective**

The current forces pushing higher education to explore new models are unavoidable. Proactive efforts, leadership commitment at all levels, and resources dedicated to finding solutions will be critical to any potential new institutional model. When debating the options, institutions should consider the following:

- Embrace change. As senior leaders strategically plan for the next 10 to 15 years, higher education institutions must incorporate a change management strategy for their campus. Leaders must think about change in every activity — in academic planning, budgeting process, athletics, online learning, and globalization. Change will lead to success — or to failure if not introduced timely. Change can’t be an after-thought, but rather must be part of the proactive plan.
- Make use of new technology advances. Information technology must be strategically prioritized to advance the educational mission, especially in the online academic arena, taking the organization global, while implementing efficiencies in administrative and academic processes and procedures.

- Differentiate the institution from its competition locally, regionally, nationally, and globally. Each institution cannot be all things to all students. The market analysis for the next delivery model on campus must be planned with the competition in mind. Think about partnerships — they will be critical in the future. Higher education institutions should consider partnering with other local, regional, or national institutions on new business models to keep the cost of higher education down. Globally, consider service models that can be outsourced to serve back offices abroad. As long as institutions are unique in their competitive strategy, all other services should be on the table for discussion in partnering and lowering the cost of education.

- Include the faculty and other academic staff in all strategic discussions. The move to new delivery models, global expansion, and business models will not succeed if planned in a vacuum. Faculty and others on campus will contribute to a new vision, change, and partnerships when their input is valued.

Higher education will be challenged in the next 10 to 15 years to think of new ways to execute their missions. Priorities will have to be set, monitored, and adjusted. The delivery model will change; MOOCs are already creating one version of the next-generation education process. All institutions will not be able to move to a global strategy; that will take a distinctive vision regarding location, services, and delivery value to students. Many institutions are already looking at new business models, and it will take time to implement and see the advantages of new processes. Change management, information technology, competition strategy, partnerships, and including the academic community in change is critical to any success. There are many moving parts in this dialogue, however one of the most important current actions is to initiate discussions surrounding strategic priorities.
Regulatory compliance

Background
The regulatory spotlight is on educational institutions to be proactive in meeting current and future compliance and regulatory standards. “Accountability” and “transparency” continue to be key words. Congressional focus on colleges and universities, both not-for-profit and for-profit, have highlighted that institutions need to look for ways to improve operations and maintain compliance while minimizing costs.

In addition, educational institutions continue to be viewed as “publically accountable” organizations by external constituents. Several current examples of continued regulatory attention and focus in this area include the following:

- **Municipal bond regulation** - Higher education institutions continue to monitor the comprehensive SEC report issued last summer recommending that the municipal bond market be placed under direct SEC regulation, including the authority to regulate the timing and content of issuers’ market disclosures. The report was prepared under the direction of Commissioner Elisse Walter, a vocal advocate for making significant regulatory changes in this market. The extent to which the report’s recommendations move forward is uncertain in light of major changes in SEC leadership. Ms. Walter’s term officially ended last year; however, she may continue to serve through the end of 2013. She also stepped into the role of chairman for several months between the departure of Mary Schapiro in December 2012 and the appointment of Mary Jo White in March 2013. It is unclear at this point whether the new SEC chairman will champion any of the recommendations in the SEC report, as her background does not include significant involvement with the municipal bond market. If Ms. Walter stays on and Ms. White decides to defer municipal matters to her, the prospect of municipal regulation would likely continue to move forward, at least through the remainder of Ms. Walter’s term.

- **Public accountability** - The FASB continues to explore how “public accountability” should manifest itself in financial reporting differences between “nonpublic” and “public” entities. During the past year, the FASB held extensive discussions with its Not-for-Profit Advisory Committee (NAC) on this topic. While virtually all not-for-profit entities are considered “publicly accountable” for regulatory purposes, the regulatory notion could be considered too broad to be useful for accounting standard-setting purposes (i.e. certain accounting standards required of public companies may not be as useful to the users NFP entity financial statements). On the other hand, the current dividing line (issuers of publically traded debt) is generally viewed as too limiting. Instead, it may be more useful to focus on factors such as number and types of users of a not-for-profit’s financial statements and the extent to which they have direct access to management to obtain information beyond that contained in the financial statements. As the user base broadens, the ability to have direct access to management is likely to lessen, which may in turn indicate that more robust information is needed in the financial statements. Although currently in the early stages, a formal standard is expected over the next year to address the issue of what entities should be considered “nonpublic” (by default, all others would be “public”). Regardless of where the final line is drawn, the FASB recognizes that even “public” not-for-profits might benefit from accommodations related to disclosures as well as transition guidance and effective dates, due to their unique characteristics.

Impact on educational institutions
Many institutions are challenged to respond to the increasing regulatory requirements, as well as the continuing political and public focus. Adherence to these requirements and responding to regulatory scrutiny has been difficult for many educational institutions and has strained internal resources. Colleges and universities are determining the need to implement new policies and procedures and modifying existing financial and information systems to accommodate new data collection.
Financial accounting requirements

The significant volume of standard-setting activity is continuing. It is affecting, and will continue to affect, not-for-profit and governmental institutions in the near future and beyond.

FASB - The FASB continues to work with the International Accounting Standards Board (IASB) to collaborate on eliminating major differences in US GAAP and International Financial Reporting Standards (IFRS). This includes continuing its progress on the major convergence projects. A final standard on revenue recognition is expected in summer 2013, and it is possible that a final standard on financial instruments will be issued by the end of the year. The boards have also completed their redeliberations on leases, and the focus has now shifted to the forthcoming re-exposure draft where there is sure to be feedback on the proposed “dividing line” for determining the expense recognition pattern.

Not-for-Profit Advisory Committee - The FASB’s Not-for-Profit Advisory Committee (NAC) continues to play a crucial role in working with the FASB to address the standard-setting needs of not-for-profit entities. In addition to providing real-time feedback on how the board’s decisions in the convergence projects would affect not-for-profit organizations, the NAC is advising FASB on the not-for-profit financial reporting project the NAC requested that it undertake in late 2011. This project seeks to improve the FAS 117 financial reporting model established back in 1994, and is taking a fresh look at matters such as net asset classification, presentation of a defined performance indicator, and improving the balance sheet requirements and notes to better reflect financial liquidity or other measures of financial health. The NAC has also provided input to the FASB on two not-for-profit projects that made their way through the Emerging Issues Task Force (EITF) this year. One other development of note is the release of the AICPA’s new audit and accounting guide for not-for-profit organizations, a complete overhaul of the 1996 guide. Although it is not authoritative, it was prepared by a panel of recognized industry experts and provides clarification to not-for-profit sections of the FASB accounting codification.

GASB - Entities that apply standards issued by the Governmental Accounting Standards Board (GASB) are also facing significant standard-setting changes. GASB’s comprehensive re-examination of its existing GAAP in two important areas has been completed, with the issuance of new standards on post-employment benefits and the financial reporting entity. The pension standard, which is a total revamp of the pension reporting model governments have applied for years, have significant implications for every organization that applies GASB standards. The reporting entity standard’s clarifications, which become effective in the coming year, may have significant implications for educational organizations in how they present legally separate corporate-type component units — in particular, in their ability to “blend” (i.e., consolidate) legally separate corporate-type component units. In addition to those two major standards, GASB has moved into new territory by adding two new financial statement elements — deferred inflows and deferred outflows of resources — to the elements governmental entities have historically used. The addition of those elements means that the equity section of GASB institutions’ balance sheets will now report “net position” instead of “net assets.” In addition, it triggered a comprehensive re-look at all asset and liability captions, with the result that some balance sheet items will hereafter be reported as revenue or expense, while others will be treated as deferred inflows or deferred outflows.

Educational institutions are proactively analyzing the impact that could result from standard-setting activity. As the details of what are likely to be the final rules are becoming clearer and the expected effective dates and transition provisions are becoming known, organizations are starting to plan for implementation of the forthcoming FASB convergence standards, including changes to financial reporting systems and internal controls. Institutions are analyzing how the proposed revenue recognition standard could affect the accounting treatment for sponsored research and how the proposed leasing standard could impact their future budget and the debt presented on their balance sheet. Governmental institutions are evaluating the potential implications of GASB’s reporting entity standard and, where indicated, having discussions with disclosure counsel on how the changes might bear on the financial statements they provide to investors in municipal bonds through EMMA and the continuing disclosure covenants entered into when the bonds were issued.
**IRS items**

- **College and University Study on UBTI:** In April, 2013, the IRS released its long-awaited final report summarizing its findings in its Colleges and Universities Compliance Project. Based on responses to a 2008 questionnaire that the IRS sent to 400 randomly selected colleges and universities, the IRS conducted examinations of 34 colleges and universities focusing on unrelated business taxable income (UBTI) and compensation issues. The examinations resulted in disallowance of losses and adjustments to UBTI on the returns of a significant number of the institutions examined. Many of the adjustments were connected to campus activities such as fitness centers and sports camps, advertising, facility rentals, arenas, and golf courses. The most common reason for disallowance of losses was that the claimed losses were associated with activities for which the institution lacked a profit motive, as evidenced by years of sustained losses.

  The examinations also focused on practices and procedures used to determine compensation for the highest paid individuals of the colleges and universities, primarily with respect to the rebuttable presumption standard under IRC Section 4958 (if institutions follow certain steps the burden is shifted from the organization to the IRS to prove that compensation is unreasonable). The IRS found that although most of the colleges and universities examined attempted to meet the rebuttable presumption standard, approximately 20% of schools failed to use appropriate comparability data in determining reasonable compensation.

  The IRS has indicated that as a result of its findings, it plans to look at UBTI reporting more broadly, especially at recurring losses and the allocation of expenses, and to ensure, through education and examinations, that tax-exempt organizations are aware of the importance of using appropriate comparability data when setting compensation.

- **Affordable Care Act:** Employer Provisions: Employers of all types are gearing up for compliance with ACA provisions related to employer responsibility for healthcare coverage. These requirements phase in over the next couple of years. Because of their employee mixes, colleges and universities may be at particular risk with respect to determination of healthcare coverage requirements for part-time and adjunct staff. They may also have exposure to the high-cost plan excise tax (i.e. Cadillac plan tax). Some ACA milestones to be aware of in 2013 include:
  - Inclusion of healthcare benefit value on W-2s
  - Distribution of Summaries of Benefits and Coverage
  - Payment of Patient Centered Outcomes Research Institute (PCORI) fee
  - Notice to employees of health insurance exchanges by October 1, to precede exchange open enrollments starting in October
  - Tracking hours of variable-hour employees, such as adjunct faculty and part-time workers, in connection with employer shared-responsibility provisions taking effect in 2014

  Implementation of the above will require institutions to spend additional time and resources in implementing and administering the requirements.

- **International:** The IRS continues to scrutinize tax-exempt organizations, including private colleges and universities, that report ownership of foreign bank accounts to determine whether these institutions comply with substantiation and filing requirements and how they ensure that foreign activities and grant-making further their exempt purposes. At the same time, the IRS continues to offer penalty relief for organizations that failed to properly report foreign financial interests in prior years. Under the Offshore Voluntary Compliance Program, organizations that voluntarily file delinquent foreign activity reporting forms, such as Form TD F 90-22.1, *Report of Foreign Bank and Financial Accounts (FBAR)*; Form 5471, *Information Return of US Persons With Respect To Certain Foreign Corporations*; or Form 3520, *Annual
Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts, may avoid penalties if they have no unpaid tax liability associated with the unreported foreign interests and have not previously been contacted by the IRS. In addition, global operations continue to be an area of interest for the IRS. Increasingly, institutions continue to “go global” to enhance their brand. The IRS has expressed concern where US charitable assets are being used for non-charitable activities. The IRS has included a focus on international operations as part of its annual Work Plan for the last several years. (It is also important to note that international operations often create tax considerations for both the institution and the individuals that they send abroad.)

- **Tax-Exempt Bonds**: The IRS has signaled its continuing focus on tax-exempt bond compliance by indicating that market-segment examinations of qualified section 501(c)(3) bonds and post-issuance compliance will be conducted in 2013. Consistent with the trend toward increased bond-related reporting requirements, Form 990, Schedule K, Supplemental Information on Tax-Exempt Bonds, is again expanded for tax year 2012 (fiscal year 2013) to contain additional questions concerning compliance with private business use and arbitrage restrictions.

- **Governance**: Continuing its focus on the connection between organizational governance practices and tax compliance, the IRS has completed an analysis of 1,300 governance practices check sheets obtained from tax-exempt organizations that were under IRS audit. According to the IRS, the results of the analysis suggest that certain factors may be positively associated with tax compliance, including: having a written mission statement, using comparability data in making compensation decisions, using controls to ensure proper use of charitable assets, and providing the Form 990 for review by the governing board prior to filing. This year, the IRS is initiating exams of a statistical sample of 501(c)(3) and 501 (c)(4) organizations to obtain additional information on their governance practices.

- **IRC Section 501(r)**: Section 501(r), which was enacted in 2010, contains requirements that not-for-profit hospitals, including academic medical centers, must satisfy to maintain tax-exempt status under Section 501(c)(3). In the last year, the IRS has issued two sets of proposed regulations addressing a range of issues under Code Section 501(r).

  In June 2012, the IRS issued proposed regulations that describe anticipated guidance on requirements for financial assistance and emergency medical care policies, limitations on charges, and restrictions on billings and collections practices. In April 2013, the IRS issued proposed rules regarding the consequences for failing to comply with Internal Revenue Code Section 501(r). The proposed rules also provide details regarding the community health needs assessment (CHNA) requirements and related excise tax and reporting obligations. Importantly, the proposed regulations indicate hospital organizations will be given opportunities to correct unintended violations and that the revocation of exempt status is expected to be limited to egregious cases. The proposed regulations are not binding, but hospitals may rely on guidance contained in the proposed regulations until temporary or final regulations are issued.

**OMB reform of federal polices relating to single audits and cost principles**

The White House has recognized the need to ensure a proper balance between meeting regulatory objectives while minimizing the burden on institutions. To that end, President Obama, through an Executive Order, mandated that federal agencies take steps to modify or repeal specific rules that are ineffective and excessively burdensome.

In keeping with the President’s executive order, the Office of Management and Budget (OMB) issued in late February 2012 an Advance Notice of Proposed Guidance (ANPG) for public comment. This document sets forth specific areas related to the single audit, the cost principles, and administrative circulars where updates and changes could be made to improve efficiency and minimize the burden of regulatory rules and monitoring.
OMB received numerous comments on the ANPG and, on February 1, 2013, issued a more detailed exposure draft of proposed reforms to the single audit, the cost principles, and administrative circulars. Proposed reforms include:

- Raise the single audit threshold to $750,000 from $500,000
- Combine the current A-133 audit circular, cost principles circulars for different types of entities, and the current administrative circulars into one document
- Remove effort-reporting examples and encourage institutions to consider alternative methods of accountability in combination with existing salary distribution systems
- Include an option to extend current indirect cost rates up to four years to ease the burden associated with preparing a full indirect cost rate proposal each year
- Focus A-133 compliance audit procedures on the elimination of fraud, waste and abuse, as well as the reduction of federal improper payments
- Reduce the minimum compliance audit coverage from 50% to 40% of programs expenditures for low-risk entities and increase the individual Type A program audit threshold from $300,000 to $500,000
- Eliminate the current A-21 requirement to follow cost accounting standards and prepare a Disclosure Statement (DS2) for most entities expending federal awards
- Report award results in relation to award goals set by the awarding federal agency and cost effectiveness achieved
- Implement several other changes designed to streamline the current rules

Educational institutions are reviewing the proposed changes and the effect they may have on their current policies and procedures.

**DATA Act**

On April 25, 2012, the House passed the Digital Accountability and Transparency (DATA) Act that would require federal agencies to consistently report spending information on a new, searchable Web database. The proposed act would create a new Federal Accountability and Spending Transparency Commission (FAST) to succeed the Recovery Act Board, which will have responsibilities to: 1) oversee federal reporting by grantees and contractors, 2) maintain a new public website populated with spending information, and 3) require use of electronic tags on each piece of federal funding information (i.e., XBRL).

The Senate passed its version of the DATA Act in September 2012, which is substantially different from the House version. The Senate version would require the federal agencies to populate the public database rather than award recipients. The public database would not be a newly created database, rather an existing website — USAspending.gov — would be used. Unlike the House version, the FAST Commission would be scaled down to an advisory board to Congress. The IRS, OMB, and GSA would be tasked with determining the electronic tag structure for federal funding information.

The House and Senate version of the DATA Act have not been reconciled yet. However, in May 2013 the House Oversight and Government Reform Committee approved a revised House version of the DATA Act. The revisions include authorization of a three-year pilot study, use of USAspending.gov rather than create a new website to make data publically available, and keeping the Recovery Act Board in place to oversee reporting rather than creating the FAST commission.
Institutions currently contemplating changes to their chart of accounts and IT system architecture are encouraged to ensure the resulting chart of accounts and IT architecture will accommodate an XBLR reporting request.

For-profit education

For-profit educational institutions provide access to higher education programs for a large segment of the population and are an important component of the Obama administration’s goal of increasing the number of college graduates by 2020. The cost of the programs offered by the for-profit sector compared with the not-for-profit sector and the resulting level of student loan debt incurred by students is a focus of several regulators.

This sector of education continues to be under the microscope as Congress investigates perceived abuses of Department of Education regulations and the level of oversight provided by the Department of Education and accrediting agencies. Incentive compensation paid to recruiters, questionable recruiting techniques and the rate of program completion are examples of areas Congress is investigating. Accrediting agency and Department of Education oversight is being called into question, as well as management practices.

The “Gainful Employment” rule is considered a first step toward reducing the perceived abuse and improving oversight of this sector. Although certain significant components of the rule were overturned in a court ruling last year, the court clearly indicated the Department of Education has the statutory authority to issue regulation similar to Gainful Employment as long as it is based upon more factual studies and analysis. The Gainful Employment disclosure requirements survived the court ruling.

Our perspective

The attention to educational institutions from Congress, the President, and other regulatory bodies is not slowing down. While some legislation is in progress to streamline compliance requirements and reduce the financial burden, other legislation in progress, as described previously in this paper, will result in more compliance requirements and added cost of implementation. Therefore, when the opportunity arises, institutions need to tell regulatory bodies what they think of proposed changes and the impact the changes will have on the continuing viability of educational research and other programs. In the meanwhile, institutions will need to continue to enhance internal controls over compliance.

In connection with the development of an organizational framework for institutional compliance, educational institutions should continue to develop other proactive responses to myriad regulatory initiatives. Institutions should consider the following to enhance overall compliance and reduce the financial, operational, and reputational risks associated with noncompliance:

- Stay abreast of new regulatory developments and ensure their voice and points of view are heard through industry associations and political influences
- Continue to educate trustees, faculty, and staff of the ever-changing regulatory environment to ensure there is the appropriate level of focus on compliance with not only external rules and regulations, but also internal policies and procedures
- Determine who is responsible throughout the organization for compliance with rules and regulations and whether actions are needed to improve or maintain compliance
- Assess key exposures and implications to the institution from an operational, financial reporting, and legal/compliance perspective, and respond to these exposures through risk management programs, involvement of appropriate parties with the identification and monitoring of risks (including senior management, internal auditors, and other key departmental administrators), and establish ongoing programs to mitigate potential noncompliance
• Identify best practices for appropriate compliance metrics and other means to track and report the processes and procedures associated with regulatory compliance

• Consider conducting “mock audits” of UBTI activities and compensation processes to evaluate compliance with IRS rules

• Establish processes for compliance with ACA requirements and project financial impact of employer tax changes

While educational institutions are not SEC registrants, many are considered “public interest entities” due to their issuance of tax-exempt municipal bonds and other factors. As a result, institutions must be cognizant of the level of reporting, controls, and compliance responsibilities associated with this designation.
Federal budget and the effect on higher education

Background

The Budget Control Act of 2011 created a fiscal cliff across the federal agencies in a targeted attempt to reduce the deficit by $2.8 trillion over 10 years. This included the creation of budget caps and a “super committee” tasked to find $1.2 trillion of savings. Unfortunately, Congress failed to agree on the savings, resulting in sequestration, the automatic across-the-board cuts to defense and non-defense discretionary spending, as well as Medicare. Whereas there was a FY13 Continuing Resolution (H.J. Res 117) that funded the government until March 2013, as of July 2013 an additional Continuing Resolution is not anticipated.

Higher education will feel the biggest impact of sequestration within research funding, with the federal research and development budget dropping by 8.2%. This included over $2 billion in cuts to National Institute of Health (NIH) and National Science Foundation (NSF), and consistent cuts across the other funding agencies. Sequestration also affected financial aid with the same 8.2% cuts across Federal Work Study, the Supplemental Educational Opportunity Grant, and college access programs (the law specifically exempted the Pell Grant Program). The financial aid cuts will have a trickle-down effect across organizations, with Title I grants losing $725 million, and Title III and V grants both dropping by 5%.

Not only do universities face direct grant and aid funding cuts, but, according to the federal Consumer Financial Protection Bureau and US Secretary of Education, there are over 850,000 private student loans worth more than $8.1 billion that have gone into default. Private loans offer lower rates than their federal counterparts (which are scheduled to double in July 2013), but are much more difficult to refinance and do not offer the flexibility of federal loans. Congress is exploring options, including preventing the interest rate from doubling and finding other methods for creating student-loan affordability.

Recently, the White House released its FY14 budget request, which included a 9.2% increase in nondefense research and development spending to $69.7 billion. These figures include a repeal of sequestration dollars and do not take into consideration the caps related to the Budget Control Act.

Impact on educational institutions

Most higher education institutions are currently challenged to determine the short- and long-term impact of sequestration on the organizational budget and cash flow, especially as it compares with the investments required in the operational research and education missions. Beyond the direct federal funding risk through sequestration, revenues from state sources are decreasing, with no sign of recovery. As a result, all missions of the university are under increased scrutiny to identify efficiencies and innovative ways of doing business, including diversifying the research portfolio, seeking operational improvements, and assessing the programmatic portfolio. Several of the areas of current attention include the following:
Research operations – Universities are reviewing their research facilities to drive a master plan that allocates appropriate space based upon financial metrics (such as direct or indirect cost per net square feet) within research. Universities are also pursuing research optimization and cost-reduction initiatives to lessen the subsidy on research operations, including shutting duplicative core facilities, reviewing institutionally funded research initiatives, and implementing research productivity metrics.

Diversification of funding – Increased collaboration with other universities allows an institution to create the strongest research team and to leverage research skills, environment, patient population for clinical studies, etc. In addition, public-private partnerships continue to be a source of revenue opportunities between the university, state, and industry. Some organizations are creating key research centers that bring together multidisciplinary researchers marketed as a single operation to external parties. An example of this is the formation of drug or device development centers within health and life sciences.

Diversification (and Research Commercialization discussed immediately below) introduces new compliance considerations. For example, research with nongovernment sources may create income tax implications (federal and state), depending on the type of research conducted and who benefits from the research. In addition, research with nongovernment sources can also result in private use when research is conducted in tax-exempt bond-financed space. (Tax-exempt bond-financed facilities are subject to limitations on the level of use by certain outside organizations.) Tax obligations should be taken into account when contract pricing is considered. Similarly, the location of commercial activities, including private research, should be planned and monitored.

Diversification may also mean “going global.” Many organizations seek to enhance their brand by continuing to initiate programs in all parts of the world. Global compliance considerations should be considered — both corporate and individual. Although an institution may be tax-exempt in the United States, this does not result in tax-exempt status abroad.

Research commercialization – Commercialization of research has become a more pointed focus across patent and start-up licensing and new-venture creation. At the same time, many organizations are reviewing their patent portfolios and divesting those patents that are costly to maintain but are not being actively managed.

Shared service centers – Higher education continues to see growth in the development of shared services to drive administrative efficiencies. These are being seen at the campus level, school level, university level, or by function, including research administration. The development of a shared service operation allows a university to provide a higher level of service, often with fewer resources.

Programmatic review – Many institutions are performing reviews of their current academic programs in an attempt to increase academic efficiency. Research universities have started consolidating their basic science departments, while many others are identifying centers of excellence around which to focus their academic mission. Other organizations are exploring more drastic changes, including dropping entire summer sessions.

Student aid – Fewer student aid dollars will affect the institution’s ability to recruit students and provide the support to maintain targeted four- or five-year graduation rates. Universities are forced to be more proactive in sponsoring various flexible payment plans, including using third-party vendors to leverage flex payment software that complies with Family Educational Rights and Privacy Act (FERPA) regulations. In addition, high-tuition programs and/or universities are completing intensive financial aid counseling throughout the student lifecycle, from application to exit interviews.

Executive compensation – The dialogue on the affordability of education often shines a spotlight on executive compensation. This area continues to be an area of interest for faculty and students, donors, the media, unions, and federal and state government officials. Establishing reasonable compensation, as well as careful documentation and reporting of compensation, continues to be an important area of focus. More on executive compensation can be found in the IRS Items section on page 10 of this paper.
Our perspective

As institutions continue to deal with leaner budgets, they will need to put financial and operating models in place to manage their short- and long-term strategic missions. Universities should complete detailed, mission-based profit and loss statements/financial models to identify their financial positions across research, academic, clinical, and outreach missions, as well as within administration. A detailed, mission-based model provides management with a financial tool to drive decisions at the mission, school, department, and even division level. Detailed financial models also provide a mechanism for departments to become actively involved in planning on an ongoing basis.

As part of the mission-based profit and loss statement or as an independent initiative, non-salary research expenditures will receive higher scrutiny. Historically, research expenditures have been excluded or limited in consideration of increasing purchasing power due to the direct, external funding of equipment or supplies from sponsors. Universities’ procurement offices will begin working more closely with the research operation to explore strategic sourcing initiatives, often leveraging institutional, regional, conference-based, or national group purchasing organizations.

Managing through the current financial environment is not solely about expense restriction. Higher education institutions will continue to innovate and collaborate across and beyond the industry to drive revenue, although these initiatives are not without their challenges. Discussions with university leaders indicated ongoing regulatory concerns, competition, and lack of proven results and technology as threats that deter university collaboration. Universities should consider bypassing their current fears about increased competition from outside collaboration, and focus attention on monetizing assets through further development of public-private partnerships, peer collaborations, and brand globalization. There are many successful examples of partnerships across these three areas, and the demand continues to grow as global entities seek to leverage US higher education success and industry continues to offload internal research and development to other collaboration partners.

Institutions should keep in mind the compliance considerations that result from diversification of revenue sources. These compliance considerations, both domestic and international, can be managed, but should be anticipated as diversification of funding and commercialization occurs.
A recurring focus on the cost of higher education

**Background**

The cost of attaining a college degree has increased significantly in the last decade, contributing to continued scrutiny of the industry from college-bound students and their families, lawmakers, rating agencies, and other constituent groups. Given the current economic environment and ongoing uncertainty in the job market for college graduates, many are left to contemplate how they are going to be able to afford tuition and related education expenses. Between 2000–2001 and 2010–2011, prices for undergraduate tuition and room and board at public institutions rose 42%, and, specifically, prices at private not-for-profit institutions rose 31%, after adjustment for inflation.² The cost of a college education is not only currently outpacing the rate of inflation, but student loan debt has surpassed credit card debt.

Criticism of the cost of higher education is commonplace. Purdue University’s new president Mitch Daniels recently cited such criticisms in an open letter to the Purdue community. The points he mentioned included:

> “College costs too much and delivers too little. Students are leaving, when they graduate at all, with loads of debt but without evidence that they grew much in either knowledge or critical thinking. Administrative costs, splurging on “resort” amenities, and an obsession with expensive capital projects have run up the cost to students without enhancing the value of the education they receive.”

The rising price tag of higher education has caused institutions to respond to questions about the benefits of a college degree. Messaging about career advancement opportunities, lifetime earnings, and increased chances for employment has grown stronger as colleges and universities counter the arguments that the cost outweighs the benefits of attaining a degree. Published statistics support the fact that unemployment rates are lower for those with a college education. Institutions are using these facts, as well as successes of their own graduates, to support the long-term value of obtaining a diploma.

**Impact on educational institutions**

Although the rate of tuition increases has lessened in the past few years, the challenge of tuition affordability continues to raise myriad questions for colleges and universities to answer. Institutions are being asked to provide more and more to their students with fewer resources. As a result, institutions are closely scrutinizing how tuition dollars are being put to use and are looking for efficiencies in their delivery model and related support. This examination began in 2008, when colleges and universities appropriately responded to investment declines and the overall economic recession by reducing expenses, reviewing cost structures, and revisiting long-term budgeting considerations. Senior management and their boards are now asking whether enough has been done to control expenses and to make their institution as efficient as possible.

As institutions have evaluated their most significant expenses, payroll and related employee benefits are being closely reviewed. In certain instances, these evaluations have resulted in employee reductions, freezing of defined-benefit pension plans, and requiring employees to pay greater portions of healthcare premiums. In other instances, institutions continue to dialogue with their employees about the changes that need to be made, but are challenged by historic union contracts, concern from faculty, and cultural aspects of their organization. On top of employee salaries and benefits, the overall organizational structure and number of administrators are being reviewed. To reverse the trend of growth in administrative ranks, leadership at institutions are requiring reviews of

administrative roles and responsibilities to root out duplication and assess whether there are opportunities to consolidate positions. Moreover, institutions are continually re-evaluating certain benefits given to both faculty and administrators, including housing allowances, below-rate mortgages on primary residences, tuition discounts for family members, and sabbatical leaves, to determine what cost savings could be gained by reducing these types of benefits.

Institutions are also assessing their current and future capital costs, including deferred maintenance priorities, deliberating the merits of building new versus renovating existing space, and leasing compared with buying. Space studies, including those associated with research facilities, are being conducted on many campuses as institutions struggle with how to prioritize and fund capital requirements. Additionally, more and more capital campaign goals are including targeted amounts for capital renewal and replacement.

As institutions strategize to determine their current and future capital needs, distance learning initiatives are also becoming a more integral part of the debate. Discussion of future capital plans is including consideration of whether lecture halls will be replaced by massive open online courses or other distance learning programs.

Along with capital and distance learning strategies, institutions are closely evaluating information technology budgets and long-range plans. The complexity of the decentralized nature of information technology in the higher education industry and the number of outdated information systems are requiring significant capital spends. Institutions are implementing or upgrading large enterprise systems or considering cloud computing as a way to reduce costs. Additionally, keeping pace with ever-evolving mobile device and other technology is stretching financial resources as institutions face ongoing challenges to keep up with student and faculty technology expectations.

In addition, auxiliary enterprises present financial opportunities. Analysis of financial margins associated with dining, parking, bookstores, athletics, and other enterprises are facilitating discussions about outsourcing and shared service centers. Such discussion topics as consolidation of dining facilities, the number of varsity and club sports, and amenities provided to students are being assessed to determine where economic efficiencies can be obtained.

Finally, institutions are undertaking thorough reviews of both course offerings and major areas of studies by evaluating the level of interest based on enrollment data. Private industry is often required to adapt to changing environments based on customer demands; this adaptation is becoming more prevalent in higher education as institutions look to cut costs by discontinuing unpopular courses or majors, or explore differential tuition pricing for “in-demand” programs or majors.

**Our perspective**

The spotlight on tuition and the overall affordability of higher education is still bright. Boards and senior management will continue to define and prioritize what is of necessity to attract students to their campuses and imperative to the student’s learning experience. Making hard decisions on future plans to make tuition more affordable is going to require consensus across multiple constituents who may have very different opinions on what the priorities of the institution should be. As boards and senior management continue to discuss the financial future of their institution, hard questions should be asked on what more can be done to both enhance the efficiency of the educational delivery model and related support needed, and challenge the related current cost structure of the institution. These questions may include such items as the following:

- Have long-term projections of the cost of employee benefits been performed including pension, post-retirement medical plans, and other benefit programs? Have potential benefit plan changes been assessed to determine cost savings? What messaging has been communicated to the employee base about benefits and the impact they are having on the financial health of the institution?
Has a top-to-bottom review of departmental and school administrative ranks been performed to determine if redundancies exist with roles and responsibilities, and whether communication and process improvement efficiencies can be realized?

Has a detailed analysis been performed of the profits and losses by major program, department, or auxiliary service that is provided to students to assess profitability? Does the detailed assessment include a full allocation of indirect costs, and financial aid, to allow for a complete picture of the results at a component level?

Have recent studies been conducted on the capital needs of the institution? What are the funding sources for these needs and is ongoing depreciation being funded? Are alternatives being reviewed when new construction is considered?

How are information technology costs being handled? Should the board consider establishing a subcommittee to oversee information technology goals and initiatives? Do long-term information technology budgets include significant information technology projects and mobile device initiatives, as well as consider the use of the cloud and distance learning programs? Is there proper cross-dialogue between board information technology and finance committees?

Have shared service models been explored across various departments, units, or functions to determine where efficiencies could be achieved? Could constituents be better served in a decentralized environment by exploring shared services across the institution?

To gain the necessary agreement from trustees, management, faculty, and others, strategy sessions on the long-term financial challenges of an institution must continually take place. These sessions should include discussions of such items as the organization’s reliance on the endowment and the related impact of market fluctuations, the future cost of employee benefits, projected capital and deferred maintenance costs, among other key financial considerations. These types of costs should be “scenario analyzed” against flat to small tuition increases to provide constituents with an idea of the financial challenges that will occur when tuition and other revenue growth does not keep up with expenditures growth.

Although there may be differing opinions on what the priorities need to be at an institution, few would argue that the cost of higher education cannot continue to grow at the same pace as it did in the past. Regardless of where an institution stands in its post-recession strategy, it is crucial that institutions create careful and deliberate budgets that are aligned to their strategies in order to be best positioned for future success. Included in these budgets should be clear, measurable goals of how efficiencies in the delivery process could impact the financial success of the institution. It will be an ongoing institutional priority for senior management to strategize with their governing boards and assess their current practices to respond to financial challenges facing their institutions currently, and how to best position their institution over the next decade.
Student loan bubble — fact or fiction?

Background

Many industry sectors have seen their fair share of economic “industry bubbles” — such as the recent dot-com bubble and the real estate bubble. Many ask whether the higher education industry sector is now experiencing its own economic “bubble.” Critics of higher education wonder why, in the last 25 years, the cost of education has risen more than four times the rate of inflation and twice the rate of medical care. There are significant pressures on the growing cost of education and how students of all economic classes will pay for it. Colleges and universities, especially private colleges, feel significant pressure to control tuition increases as students and parents continue to feel the financial pressures of a slower-than-expected economic recovery.

Financing education through student loans has soared to more than $1 trillion, with the borrowing rate twice that of 10 years ago. But after graduation, many students are jobless, which means student loan defaults and bank write-offs are up significantly. For example, during the year ended June 30, 2011, students defaulted on $964 million of Perkins loans — a 20% increase from five years earlier. Furthermore, the ability for students and parents to take out a private loan or to refinance their homes to pay for education is now difficult or impossible.

Private colleges and universities with significant endowments are offering more of their own endowment resources in order to attract and retain a diverse student body. Tuition-dependent private colleges are negatively impacted by the decline in college-aged student demographics as well as students who are able to pay full-price tuition. Public colleges and universities have seen significant cuts in their state appropriations for higher education. Where in the 1980s and 1990s, public universities were funded, on average, by the state for more than three-quarters of their cost of education, states are now funding only approximately half of that cost.

In addition, for-profit colleges are teaching about 10% of students, but are receiving 25% of the federal aid. Senator Tom Harkin (D-Iowa) has been vocal about his concerns on for-profit institutions and their growing share of federal student aid. His reviews have shown that some of these institutions are spending financial aid dollars on aggressive and sometimes fraudulent recruiting, resulting in students taking on too much debt, dropping out, and/or not graduating from the private colleges or universities, and often defaulting on their loans.

Each of these challenges, among others, has resulted in a boiling cauldron of challenges and risks for educational institutions.

Impact on educational institutions

Several arguments exist that would indicate a student loan bubble exists, including: total outstanding student loans are at an all time high of $1 trillion; Perkins loan write-offs are almost $1 billion a year; banks wrote off $3 billion in student loan debt in the first two months of 2013; student loan delinquencies as a percentage are greater than credit card delinquencies for the first time in 2013.

On the other hand, student loans, when compared with the recent mortgage bubble, are miniscule. And unlike the subprime mortgage market, there are very few student loans being traded on the open market. Much of the debt is issued by the federal government directly rather than through banks.

Additionally, as a sector, higher education is not overleveraged. There is strong demand for higher education, and recent unemployment data continues to show the value of achieving bachelor and advance degrees on an
individual’s employment status. True, students have more debt, but the most significant student debt increases are shown to be greater at the graduate level and at non-traditional colleges.

Nevertheless, student funding of higher education and the role and responsibilities of the federal government, the student, and the educational institutions is, and will be, the subject of ongoing policy debate — and will present certain financial, compliance, and reputational risks for educational initiatives. We have summarized several of the more critical potential policy changes and risks below:

**Potentially greater level of federal government oversight**

In his State of the Union address in both 2012 and 2013, President Obama highlighted the affordability of higher education as a priority for his administration, and outlined initiatives to achieve this goal. First, the President has proposed creating a “College Scorecard” that consumers can use to compare colleges and universities with each other. The scorecard will include items such as the estimated cost of attendance, graduation rates, job placements, and potential earnings opportunities.\(^3\) Second, the President is proposing creating monetary incentives in the form of grants for states that work with higher education institutions on ideas to reform current policies and procedures to help make education more affordable, as well as to increase graduation rates at their institutions. Finally, federal aid for colleges and universities that do not succeed at keeping costs down will be shifted away from them and to those that are successful in doing so.\(^4\)

As states continue to decrease their funding for higher education, institutions rely more and more on the federal government to assist in funding the cost of education through Perkins loans, Federal Family loans, and other Title IV funding. To create controls around eligibility, Senator Harkin has called for basic minimum institutional performance requirements to be met in order to qualify to receive federal aid. These recommendations started with for-profit colleges and universities, but have ultimately turned into suggestions for any institution that receives federal aid. Suggestions include requiring thresholds for retention, graduation rates, and loan repayment percentages.

**Perkins loan dilemma**

Under the Perkins Loan Program, students are granted loans. When the loans are repaid, the institution makes a new loan to another current student. If a student defaults on the Perkins loan, current students have fewer loans for which they can be eligible. A Perkins loan is not as advantageous for a student, as the interest rates are higher and loan deferments during times of financial hardship or unemployment are not as easily obtained as in the Stafford or Federal Family Education Loan (FFEL) programs.

President Obama has indicated that he would like to expand the Perkins Loan Program. Under his proposal, the Perkins Loan Program would increase by almost eight times the current levels and the Education Department would service the loans instead of the educational institutions.

Federal laws mandate that colleges and universities follow certain procedures to collect Perkins loan balances from their students, and if none of those collection efforts result in payment, pursue legal action against students with unpaid Perkins loans. With almost $1 billion in defaults in 2011, many universities, who are following the requirements of the law, have begun to sue former students over nonpayment.

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\(^3\) Source: Whitehouse.gov, Improving Transparency and Accountability

\(^4\) Source: Whitehouse.gov, Keeping Costs Down
Federal financial aid changes

Financial aid packages are one of many factors that attract and retain top students. There are several potential changes to the financial aid program being considered by the federal government through program changes, tax legislation, and compliance programs for 2013. They include:

- Increase the Subsidized Stafford loan interest rate from 3.4% to 6.8%.
- Eliminate The American Opportunity Tax Credit, which provides a $2,500 federal income tax credit for paying certain college expenses.
- Require greater transparency on college costs. Starting in 2013–2014 school year, a “Financial Aid Shopping Sheet” will be provided by some colleges that provides a comparable list of costs, aid, and outcomes.

These potential changes could bring significant impacts. A student may not able to attend the college of their choice, or attend college at all. The loan burden on students could become greater. Enrollment could decline at tuition-dependent private colleges that tend to give financial aid packages with a greater percentage of loans and whose “Financial Aid Shopping Sheet” may not be as strong as an institution with greater endowment that is giving more aid in the form of grants.

Enrollment demographic changes

Community colleges and public universities have seen significant increases in applications and enrolled students. Lower-cost-structured online universities, such as University of Phoenix, are increasing the number of traditional-aged college students through their less expensive online offerings. These demographic changes have resulted in certain private colleges with smaller endowments experiencing declines in the number of enrolled students for the first time since the late 1980s. As the number of traditional college-aged students declines over the next decade, enrollment numbers will potentially become even lower for all institutions.

These enrollment changes will significantly impact higher education over the next ten years. Rating agencies, as a result of these enrollment changes have posed a Negative outlook on the majority of the education sector. They have sited that partnerships, mergers, and economies of scale are needed in higher education.

Cost of diversity

Institutions are searching for the freshman class that is well rounded through different races, cultures, socio-economic backgrounds, and life experiences. Diversity is critical in developing a successful and well-rounded graduating class. Diversity comes at a potentially higher financial aid cost, which gives more highly endowed institutions an advantage. However, endowment spending and federal programs cannot always cover the financial aid needs of a diverse, need-blind class of students.

Diversity comes at a cost to those students who are considered “diverse.” The term “diverse students” often means students without the financial resources to pay for a college education. Those students are taking on more loans than ever and may not be prepared to pay off those loans after they graduate.

Fiduciary responsibility of the board

The challenges above have placed increased responsibility and focus by institutional boards on tuition affordability and financial aid funding strategies. Several of the many questions boards are currently asking include the following:

What is the board’s responsibility in overseeing the institutions financial aid strategy and compliance with offering student financial aid? Are boards aware of the institutions overall financial aid strategy? The board needs to better
understand the institution’s mission and approach to attracting and retaining students. For instance, the decision to be need-blind results in a significant impact to the college’s tuition discount and overall operating budget. Can the college continue to afford this need-blind policy, and is this policy achieving the overall strategy desired?

Related to compliance: Are boards aware of proposed changes in financial aid and their impact to the college’s strategy? Are boards aware of the significant compliance requirements that financial aid departments and business offices deal with on a daily basis? Are Title IV guidelines being met so that in instances of student defaults on federal money, the institution has completed all of the proper procedures to be made whole? Is management oversight of these programs at an appropriate level to reduce the strategic and reputational risk of the institution?

**Our perspective**

The “bubble” impacts more than student loans. In January, Moody’s Investors Service put a negative outlook on the entire education sector. This included major research universities. The bubble impacts institutions, their students, and their boards at all colleges and universities in the United States. The associated financial risk, political risk, reputational risk, and compliance risk can be significant for institutions.

In addition to the questions above, institutions should have well-thought-out strategic financial aid plans that consider all of the risks with offering federal, state, and institutional aid. These financial aid plans must correlate directly with the institution’s overall strategy. Colleges and universities must look at the changes impacting higher education — such as online and distance learning, offering year-round programming, and changes to the faculty models — and determine how those will positively or negatively impact their institution by implementing or not implementing such strategies.

Colleges and universities must also stay focused on compliance and continue to ask themselves: “Are compliance and oversight programs in place that will allow the institution to monitor and communicate changes to regulations impacting higher education?” Also, programs should exist to ensure that appropriate communication of impact, outcomes, and results of new regulations to the institution’s management, and board, as appropriate.

Boards, and more specifically, audit committees, have a fiduciary responsibility to ensure that the handling of student financial aid within the institution is performed under the appropriate federal Title IV compliance rules and regulations. Audit committees should have an understanding of financial aid programs and potentially extend their oversight of review of controls beyond the review of the OMB circular A-133 reporting requirements. Inquiries must be made in the types of aid institutions offer, default rates, participation rates, tuition discount rates, and compliance requirements.

The increasing level of student borrowing is the largest in history and will continue to impact an institution’s ability to attract and retain qualified students and ensure adequate fiduciary responsibility over the monitoring of federal and non-federal student loans compliance and collectability.
**Shared service centers — a new model?**

**Background**

The organizational structure of educational institutions has not changed dramatically in recent years. It traditionally includes a governing board, executive leadership, academic units, and administrative functions to support the delivery of education, research activities, and clinical services. Academic units are typically structured to include faculty and administrative generalists who perform a variety of activities related to procurement, payroll, human resources, and research. Operational functions (e.g., facilities, student affairs, information technology) also include employees who perform similar administrative tasks. Personnel who perform these general administrative tasks across academic and administrative units across campus are often generalists that do not acquire expertise in any one area. Inefficient? Duplicative? Costly? Many would say yes to all three.

Recent federal and state budget cuts, legislation impacting revenue sources, and other pressures to become more efficient have required institutions to reduce costs. The annual practice of budget cuts across campus often more adversely impacts administration due to greater difficulties in reducing the number of academic courses, faculty, athletic programs, and student services. Across-the-board budget reductions may be successful in the short-term; however, future upside may be limited if deeper cuts are made to the same areas in subsequent years. Many believe this practice is not sustainable and a new business model may be required to create efficiencies in areas outside the core mission of the organization — mainly back-office services.

Additionally, compliance challenges, internal controls deficiencies, and audit findings often support the need to look at the current organizational structure and consider a new way of doing business. Updated policies and regulatory changes are often not communicated timely to the staff at many institutions. These employees are constantly challenged to balance their daily workloads while trying to understand changes affecting their roles. Implementing effective internal controls and standard policies and procedures will require leadership to reassess its operating structure and create efficiencies in administrative areas across the institution.

A shared services model, a prevalent concept in the commercial sector, has surfaced as a potential solution for the education industry. Departments, schools or units share certain administrative functions to minimize redundancy by implementing a shared service solution across academic and administrative units. Shared services allow staff to become experts in their specific function. As a result, the new policies and procedures for institutions will increase productivity of transactional work and decrease process inefficiencies that are inherent in any institution. Several institutions are underway in transitioning to a shared service center concept. Others are beginning to evaluate the concept, or are currently in the implementation stages.

**Impact on educational institutions**

As mentioned above, economic pressures and ongoing challenges to reduce administrative costs are sparking a broader and more proactive discussion on the consideration of shared services among academic and administrative units on campus. The most common functions currently discussed are:

- **Finance** – The transactional process of accounting, monitoring accounts, and financial reporting
- **Procurement** – Negotiating purchasing contracts and procuring goods and services on campus
- **Human resources** – The activities surrounding hiring, evaluating, terminating personnel, on-boarding, payroll, and corrective actions
• Research administration – The functions that faculty need in order to process grants and contracts, including sponsor requirements, budgeting, timely submission, award set-up, expense monitoring, billing, and reporting

• Invoicing – In academic medical centers, the critical process of ensuring appropriate, accurate, and auditable bills are generated specifically for clinical and research activities at the department or clinic level

• Communications – Universities, particularly those with integrated academic medical centers, have central communication groups. However, departments often have separate staff for purposes (e.g., advertising clinical services, announcing the recruitment of a well known physician, or other impactful events) that do not work in coordination with the central group or are not working to maximize communication effectiveness.

Information technology shared service center models have been adopted by some organizations. However, buying restrictions (e.g., which computer to purchase) and pressures to respond quickly to address faculty information technology needs have been the greatest obstacles to initiate change in this area.

A frequent question is “what are the key benefits to the organization when a shared service model is implemented?” The most common answers to this question are:

• Process quality and standardization – Achieves better quality through common and consistent processes within an organization

• Transactional based – Creates subject matter experts (SMEs) in a specific function

• Customer service focus – Promotes customer-focused approach and enables high-quality services

• Improved efficiency – Reduces the number of touch-points and reviews in the process

• Enhanced control environment – Allows greater leverage and support for employees to scrutinize costs, transactions, practices, and more uniform policies and procedures

• Business focused – Frees-up resources to concentrate on a specific business task by eliminating the “all things to all people” model of current workload distribution

• Flexibility and scalability – Provides a flexible and scalable model according to business needs

• Cost savings – Provides opportunities to reduce costs, depending on the design and specific function of the service center

The implementation of any new customer service delivery model, like shared services, is a significant undertaking. It involves senior leadership (vision and support), central office staff (to work on new processes), school/department administration (to lead the change process for deans and chairs), and the transactional staff (to perform additional tasks included in the effort). Task forces are often required to review current processes and determine the activities that can be shared and those that should remain in the designated unit for control, accountability, and oversight.

The implementation of a shared service center also raises the following challenges:

• Funding – Institutional leadership should be involved in funding decisions to ensure these are equitable and reflected in the budget process. Considerations include the flow of funds as staff move from their unit to the shared service center and the allocation of funds to the service center that were previously provided to the unit.
- Space – As every academic leader knows, space is at a premium on any campus. Finding separate and unique space for a new service center is a challenge and usually involves a determination of the proximity of the new service center to its customers (e.g., can the center operate remotely off campus?).

- Change management and communication – This challenge must be understood by the organization and a plan must be in place to effectively manage and be transparent to all the constituencies involved in the project. One critical question in the change process is “who will champion/lead this effort?” This question must be answered before the process begins and must have both an academic and an administrative sponsor/leader. An effective change management strategy can be the critical success factor of this new model.

Institutions have learned that the impact of shared services will vary according to what functions will be shared. For the project to be successful, the main goals and the challenges of each of the various faculty and staff members need to be addressed. One important point that the institution needs to consider is who will lead and be passionate about the outcome of a successful shared service model. What institutions have been learning in the current environment is that administrative leads can help accomplish this goal; however, only executive and academic leadership can champion and drive its success.

**Our perspective**

The current forces challenging educational institutions are unavoidable. Federal funding of administration cost supporting institutional research is often exceeded by the actual costs incurred by the institution. The response of academic and administrative leaders to this financial challenge and others is critical. Budget cuts and realignment of funding to support mission-critical activities, will always be a high priority on campuses. Boards and presidents/chancellors must be actively engaged in potential new models for managing their business of educating students, conducting research, treating patients, and supporting the local community. The new model of shared services may become a more effective way to help support the academic, administrative, and financial needs of the institution.

In considering a new business model and exploiting the specific strengths of their institutions, leadership must:

- Understand that the current decentralized structure to deliver business and administrative services across campus is costly, outdated, and inefficient. By moving to a shared service model, all aspects of process flow, accountability, and document approval will be scrutinized and new methodologies to create efficiencies and improve transactional flow should be implemented.

- Consider the most important aspects of customer service: 1) timeliness of response to customer needs, 2) the availability of data and reporting for management of units, and 3) the elimination of non-value-added steps in all processes.

- Emphasize that the core mission of the academic and administrative units are not lost in this shared service model, in fact, they should be highlighted. Back-office operations are moved so leadership can invest time and energy concentrating on the mission-critical needs of the organization. Deans/chairs/administrators can use their time more productively by strategizing key hires, expanding services, and growing revenue.

- Recognize that information technology today creates an easier path to these types of services being shared among units. Paper is obsolete, technology creates instant response, and space between people is no longer a hindrance to productivity. Information technology is a tool and leadership must use every tool it can to create efficient processes.

Educational institutions must challenge the short-term solution of yearly budgeting (to create savings) and create long-term strategically aligned goals. Will shared service centers create instant savings and efficiencies? It is highly unlikely. Will they create a new way of thinking, a new idea, or a new realization of progress in today’s academic
business model? Absolutely. Shared service models will challenge every constituency in the organization and force the academic community to think differently about business and support for faculty, customers, and stakeholders.

Change is a challenge for large organizations and academic institutions, especially in the short term. In the long term, changes to new business models, like shared service centers, may become more of an established norm.
Harnessing the power of information technology

Background

Educational institutions face demands for innovative technologies from a diverse set of constituents — students, parents, faculty, researchers, donors, patients, board members, legislators, and the public at large. The intensity of these demands fluctuates over time in response to changes in constituent perceptions and interests, adoption of new technologies, competition, and shifts in the institution’s priorities.

Impact on educational institutions

Effectively responding to these demands is particularly complex in most institutions due to the diverse and distributed nature of technology resources in these institutions. In a traditional corporate environment, those providing technology services typically report in a single chain of command to a chief information officer (CIO). In an educational institution setting, many, if not most, of those providing technology services do not report to the CIO, but instead report to myriad functional units (e.g., student, financial, human resources, facilities), academic units (e.g., deans, department heads), and faculty (e.g., researchers).

In some cases, this reporting structure correlates with the mission associated with the technology services — instruction, research, patient care in the case of academic medical centers, service, and administration. For example, support for technology used for a specific research project is often grant funded, so the associated technology resources report to the faculty member(s) conducting the research. In other cases, functional units, such as those providing student or administrative services, maintain a group of associated technology resources. This reporting structure may or may not provide the most effective approach to technology service delivery, either from the constituents’ perspective or from the university’s as a whole. Providing an effective response to changing demands is complicated when resources are managed in such a distributed and in some cases historically haphazard manner and when, as frequently is the case, the complete population of technology service providers is unknown.

Management reporting structures aside, constituents outside the institution expect the university will respond to them as one organization. Students and parents expect that university representatives, no matter which area of the institution they represent — registrar, financial aid, bursar, or counselor — will know of their interactions with representatives for other areas. They expect that the information the university representative references will be accurate and up-to-date. Similarly, board members, legislators, and the public at large expect that information reported to them represents that of the university as a whole. They expect that university information is based on shared data definitions and structures adopted enterprise-wide.

Likewise, when university leaders meet to make decisions and compare performance against goals, many anticipate focusing on developing strategy and making fact-based decisions based on data drawn from a “single source of truth” rather than dedicating scarce time and effort to reconciling differences among reporting systems.

In short, the expectation is that the university will “speak with one voice” and that information will be available from an integrated set of information systems drawing on a “single source of truth.” The challenge is to advance the institution’s mission(s) and achieve these objectives in the highly distributed structure typical of a leading university.
Within this environment, university leaders are faced with the challenges and opportunities associated with a set of “pressure points” in higher education technology. These include, but are not limited to, increasing student demands, cloud computing, security and compliance, and technology funding issues.

**Student demands**

The traditional freshman class of 2013 was born in the mid-90s. These millennials are multi-taskers of the Internet generation. They tend to have high technological competence of others and of themselves. An online experience is not novel to them; it is fundamental and expected, and they are ever in search of a better one. They “bring their own device(s)” and expect they can access content from all of them at any time and from any place.

Their online experience interacting with candidate institutions impacts their college selection decision. Virtual tours create an initial impression. Social media exchanges further mold their perceptions of the institution. Ubiquitous, personalized, and easy access; and “one-time entry” of application, financial aid, and registration data (or lack thereof) can impact their leanings and ultimately their college selection decision.

Once on campus, their technology experiences can impact their perception of the institution, their academic success, and, in many cases, their ability to find employment and career success. Some of these technology experiences include:

- University-sponsored campus portals
- Course/learning management systems
- E-books
- Online learning support, such as course websites and online syllabi, support for collaboration with peers, instructors, and advisors; technology-based library and research services; and game-based learning and simulation facilities
- E-portfolio support

In parallel, close interaction with the student provides the university with opportunities to more effectively monitor and guide academic progress and intervene as necessary to provide struggling students with the support they may need.

**Cloud computing**

The student of 2013 is an unabashed consumer of technology services from the "cloud". And as the array of services available on the cloud proliferates, the power to select services will shift increasingly to the consumer. Consumerization of technology services creates both challenges and opportunities for universities.

Consumerization increases the velocity of change and opens a greater variety of options. New apps and new devices become available at an ever-increasing rate. As providers of access to the cloud, universities face the challenge of balancing the need to support innovation with the capability to research issues and implement policies addressing compatibility, licensing, security, compliance, and privacy.

At the same time, cloud computing provides new alternatives to the institution just as it does to the student. These include services provided over the public Internet, through a more closely controlled intranet and through various combinations of these options. Similarly, an institution may choose (and a number of institutions in fact have) to acquire services at or across the various layers of technology that comprise an automated system. Examples include, but are not limited to, infrastructure-as-a-service, network-as-a-service, software-as-a-service, storage-as-a-service, and desktop-as-a-service. The business models associated with these services are evolving and include subscription-based and pay-by-use models.
**Security and compliance**

In this innovative and rapidly evolving environment, security and compliance present universities with acute challenges, particularly as the consumerization shifts the balance and constrains the service provider’s — in this case, the university’s — ability to influence which and how technology services are used.

The data troves of colleges and universities have traditionally been the target of the inquisitive, some of whom are malevolent. These range from the state-supported cyber-terrorist bent on acquiring research secrets to the hacker in search of personal financial information to the mischievous computer science major challenging his ability to simply “break in.” Access through the Internet, particularly in the relatively open environment of a college campus, increases the institution’s exposure to security breaches and violations of provisions of federal and state legislation such as the Federal Education Rights and Privacy Act (FERPA), the Graham-Leach-Bliley Act (GLB), and the Health Insurance Portability and Accountability Act (HIPPA).

**Technology funding**

Addressing these challenges effectively requires a structured but dynamic approach to acquisition, application, and measurement of the performance of technology resources (including funding) enterprise-wide. Since technology services in universities is typically funded from numerous sources and through numerous organizational sub-units, understanding the magnitude of technology funding enterprise-wide is often challenging.

In addition, universities are and have been under pressure to provide more services with fewer resources. The affordability of higher education is a topic of national discourse. Returns on endowments have been limited. The threat of sequestration and other federal funding constraints reduce funding for research and healthcare reimbursements, a key source for academic medical centers. State legislatures are transferring the burden of funding higher education from the taxpayer to students and parents. In the face of the cut-backs, the cost of supporting instruction, research, healthcare, service and administration, and the technologies that support them, continue to increase.

As universities address these funding constraints, institutions have focused funding cuts on central services in an effort to protect the academic and research core. In the face of increased demand for services, distributed functional and academic units have increasing elected to direct funding to support unit-sponsored technology initiatives and operations. Central technology organizations have responded with student fee and charge-back initiatives for selected services as additional sources of funding.

**Our perspective**

Universities will continue to face increasing challenges with respect to the provision of technology services in support of instruction, research, patient care (for academic medical centers), service, and administration. To effectively address these challenges, institutions should review and confirm that the structures and processes they have in place support an effective enterprise-wide approach to technology. This approach should address more than the structures and services provided by the central technology organization(s). It should encompass those units and individuals scattered throughout the institution that provide technology support on a full- or part-time basis.

**Key elements of this approach should include:**

1. **Understand the full scope of technology support throughout the university.** Achieving this objective will likely include an assessment of the sources of technology support in academic and operational units as well as those within the central technology organization(s). This assessment would inventory and evaluate the nature/type of technology service, source location within the university, funding source, qualifications of the service provider, and reporting relationship of the service provider to the host organization and to the institutional technology support organization(s). The result of this assessment should inform institutional leadership regarding the university’s level of technology funding and serve as a baseline for evaluating the effectiveness of technology spending in support of institutional missions.
(2) **Refine (or if need be, establish) technology governance and leadership structure to reflect technology’s strategic role.** Technology is a strategic asset of the university and should be managed as such. Technology governance should reflect this. Leadership of the technology function should reside with a chief information officer (CIO) to whom technology service providers should report either directly or indirectly. The CIO should develop, disseminate, and measure compliance against technology standards for all reports, and should have meaningful influence over the outcome of the report’s performance evaluation.

(3) **Update the university’s strategic technology plan.** Update the plan to closely align technology support with university mission. The plan should address all elements of technology support — instruction, research, healthcare (if appropriate), service and administrative — and reflect the results of analysis of user expectations and sourcing options, including the cloud. Financing, including student service fees, should be considered. Security and compliance should be considered as projects are identified and prioritized, and supporting plans developed.

(4) **Incorporate “big data” and analytics in technology planning for competitive advantage.** As the strategic technology plan is developed, the university should consider the vast amount of data contained in its repositories and how that data can provide the institution and its constituents a competitive advantage. For example, institutions are tapping into this data to improve student success, identify revenue opportunities and, in the case of academic medical centers, improve patient outcomes.
**Athletics - governance and compliance considerations**

**Background**

Collegiate athletics has become a big business. According to a Forbes report issued March 17, 2013, beginning with the 2011–12 academic year through 2024–25 season, the NCAA will average approximately $775 million annually in rights fees from CBS and Turner Sports (an increase of 58% in the annual average payout from the previous deal). Approximately 96% is distributed to Division I membership, either directly to member institutions or by way of a school’s respective conference. In addition to the proceeds received from the NCAA, several institutions have very large athletics budgets, driven largely by football and basketball programs. According to a USA Today Sports’ College Athletics Finances report, in 2011 seven institutions had over $100 million in athletic department expenses and an additional 23 had expenses greater than $75 million.

Despite the revenue growth in athletics, less than 10% of athletics departments at NCAA Division I public schools generated enough revenue on their own to cover their expenses in 2012. In a USA Today report issued May 10, 2013, just 23 of 228 athletics departments at NCAA Division I public schools generated enough revenue on their own to cover their expenses. To balance the budget in athletics, institutions received subsidies in the form of student fees and school or state support, with subsidies for all of Division I athletics rising by nearly $200 million compared with what they were 2011.

With the aforementioned size of the collegiate athletics market, institutions are faced with a variety of challenges ranging from compliance-related demands to questions about university subsidies and overall athletics expenses. Additionally, institutions with large athletics programs are often defending how athletics complements the overall higher education experience, when many see it as contradicting the academic mission. Institutions are continually challenged with determining the most appropriate reporting structures among athletics departments, academic administration, and the governing board.

**Impact on educational institutions**

To respond to recent highly publicized incidents within athletics programs, as well as a negative public perception of college athletics as strictly a business, many institutions are taking a fresh look at all aspects of their sports programs. From increasingly complex NCAA compliance requirements, to growing athletics department expenses, to the need for more oversight over athletics, institutions are taking a fresh look at athletics, including their overall control and compliance structure, the cost structure including the subsidies paid, and the reporting structure between athletics and key constituents at their institution.

From a compliance standpoint, the NCAA rulebook has been expanding rapidly in recent years as the NCAA membership and its governing body try to keep up with an ever-changing landscape in college athletics. As such, institutions are ensuring they are cognizant of the changes and updates to the rulebook and have adequate compliance programs in place. To be proactive in preventing compliance issues from occurring, institutions have been asking sharper questions surrounding their athletics compliance program, such as:

- Are processes in place to investigate potential sports compliance-related violations?
- When was the last time the institution performed a sports compliance risk assessment outside of any NCAA or conference requirements?
• How well do individuals understand their responsibilities as they relate to compliance-related matters?

• How frequently do individuals at the institution receive periodic sports compliance-related training?

• What policies, procedures, and internal controls are in place to prevent violations of internal policies and external rules and regulations?

Responses to these questions have served as a starting point for institutions to identify and respond to risks related to their compliance program. Perceived weaknesses in the program are being addressed through strengthened athletics compliance offices, risk management programs, and internal audit reviews.

The increasing cost of athletic programs continues to be an area of focus. Such expenses as coaches' salaries, athletic scholarships, travel, and insurance continue to increase at a time when institutions are looking for ways to control overall expenses. Hard choices are being made regarding non-revenue generating sports, including assessing which programs to cut back or eliminate altogether. Additionally, to provide a more accurate picture of the financial results of athletics, institutions are enhancing their budgeting and reporting by factoring in allocations of depreciation, interest, and other indirect costs. Along with operating expenses of athletics programs, significant capital costs have been incurred by many institutions. From football and basketball stadiums, to practice facilities for other sports teams, the capital outlays to keep up with competing institutions have been significant. To ensure funding is in place to pay for these capital projects, institutions are ensuring the donations are secured before starting construction, or that other funding sources are available.

The governance and reporting structure between the athletics department and university administrators has historically varied by institution. In many cases, the athletics director reports to the president. In other cases, the reporting is to the executive vice president or another senior member of management. One common medium of communication at Division I institutions is the faculty athletics representative (FAR), who serves as the primary liaison between the faculty and the athletics department. In addition to providing the faculty perspective on the athletics program, the FAR is a part of larger group across all Division I schools which provide a network to solicit or provide feedback on issues.

As institutions look to enhance their governance and reporting structure, the roles and level of involvement by such individuals as the vice president for student affairs, chief financial officer, legal counsel, internal audit, and others are all being considered. Institutions are recognizing that the monitoring of such areas as the academic progress of student athletes, coaches' contracts, recruiting practices, alumni involvement through booster and other clubs, and other athletics-related activities is requiring a multitude of individuals and departments. In addition, institutions are strengthening the reporting provided to the board of trustees by determining which committee (such as the audit committee) should oversee athletics, the frequency of reporting throughout the year, and what types of information should be provided to the committee.

Our perspective

With the continued growth of college athletics, the level of both risk and reward is increasing at institutions. Proper attention and oversight over a variety of aspects of athletics will continue to be necessary to strengthen accountability and to promote transparency.

To respond to the ever-increasing compliance requirements, ongoing education and training is needed for those not only in the athletics department, but others who may indirectly support or supervise aspects of an institution's sports programs. Along with education, the policies and procedures within the athletics department should be formalized to ensure consistency in execution. Assessments of compliance-related activities should be ongoing by both those within athletics and outside the department, such as internal audit and risk management representatives.
As institutions strive to achieve the most effective reporting structure, clear lines between the athletics department, senior management, and the board of trustees should be established. As part of this reporting, enhanced transparency and education on the compliance and financial aspects of the athletics should be communicated so key constituents are familiar with NCAA requirements and operational aspects of the department. As part of this increased information sharing, such items as recruiting practices, compliance-related activities, the overall revenue generated and cost structure, as well as institutional subsidies should be considered. As institutions strengthen reporting to the board of trustees, a clear understanding of which committee is responsible for oversight and exactly what their role is, should be clearly established. Included in their role should be an education on the risks within athletics and the processes in place to mitigate these risks.

From a messaging perspective, institutions should continually promote the advantages of collegiate athletics programs, and how athletics complements the overall educational experience on campus. These advantages should highlight how sports aids in the development of students, including teaching teamwork, discipline, and striving for high performance. Institutions should also stress how important athletics is to building institutional loyalty and intergenerational school spirit among current students and alumni.

It is clear that maintaining the status quo in an institution’s approach to college athletics is insufficient in today’s environment. Institutions must deal with the current challenges head on, or risk the chance of issues similar to those that have occurred on other university campuses. Support of any initiatives to strengthen the accountability and transparency of athletics must come from the highest levels of administration and the board of trustees at the institution.
Business continuity and emergency preparedness

Background

When super-storm Sandy hit the United States’ eastern seaboard in October 2012, it was a stark reminder of how easily the interconnected world can become disconnected, leaving institutions literally in the dark. What became readily apparent was that a good emergency response plan will prepare an institution to get through the initial impacts of a major event, but in order to effectively address large-scale disasters and their extended aftermath, an institution requires a comprehensive business continuity management program. A well-designed program will prepare an institution to get through the crisis and on to the restoration of operations.

Business continuity management is much more than emergency response management. During Hurricane Sandy and other recent catastrophes, established and tested emergency response and crisis management plans helped universities and other organizations through the first 48 hours, providing command and control structures that addressed the immediate needs of safeguarding employees, students, property, and critical data — essentially, carrying everything to a metaphorical high ground as the floodwaters rose. For many, that was not enough. In the days that followed the event, many found that inadequate planning or failure of testing had left gaps in their preparedness for a fractured operating landscape, leading to a slowed recovery process.

Another current topic that has been receiving greater focus and attention in business continuity and emergency preparedness discussions has been institutional compliance with the Clery Act. Beginning in 2008, as a result of the Clery Act, colleges and universities receiving federal financial aid have been required to report campus crime statistics in a public format accessible by potential students and their parents. This reporting has resulted in an increased awareness of and attention on campus safety programs. Emergency response plans and exercises are being added for student safety on and off campus, and for staff in campus offices. With the increased focus on collecting and reporting crime and safety statistics as well as emergency response preparedness, many colleges and universities have taken compliance with the Clery Act a step further, and have started assessing campus safety in a more holistic way. This has included developing a more robust business continuity program, and training in this area as an integral part of the institution’s overall business continuity and emergency preparedness plan.

Recent natural and manmade incidents on campuses have required institutions to take a fresh look at how prepared they are for emergencies and the related aftermath. Institutions are finding that, although the best-laid plans may be in place, gaps in actual preparedness and execution could be problematic. To respond to these potential gaps, institutions are continuing to develop robust emergency response structures that include vulnerability assessments, communication protocols, and post-crisis debrief sessions.

Impact on educational institutions

While institutions have developed emergency response plans, many have, over the past months, determined them to be, impractical in execution, or never practiced, lending a false sense of readiness to the institution. More often than not, individuals identified in a response plan are unaware of the role they play in emergency mitigation, and lack formalized training in how to respond to incidents. Additionally, campus and municipal law enforcement agencies are not always effectively integrated in their approach, communication, or efforts, often delaying the response efforts. Campus safety and Clery Act reporting has evolved to a point where it is no longer acceptable to simply comply with the reporting requirements to avoid financial sanctions. Institutions must now create, communicate, and exercise specific emergency response plans that address scenarios likely to occur on their campuses, or face the financial impact of Department of Education sanctions, reputational damage, or a potential lawsuits brought against the institution from parents and other constituents.
To respond to the need for effective business continuity and emergency management, institutions are planning more than ever for potential incidents. These current planning efforts include:

- Establishing governance and program management structures to align crisis and business continuity management objectives and defining authorities, roles, and responsibilities
- Identifying and prioritizing critical functions, based on risk assessments and impact analyses
- Setting recovery time objectives for the safety and well being of the institution, including restarting of the institution’s various systems, based on overall organizational needs and evaluating how long critical functions can remain offline
- Establishing workarounds to return critical functions to operation when deprived of their usual support structures
- Defining the parameters of the institution’s duty of care during a crisis and to what extent it extends beyond employees and students to include contractors, guests, families, and the community

In addition to effective planning, more and more institutions are beginning to examine the financial and reputational impact of a major event occurring on campus far beyond the traditional dormitory fire or after-hours safety escort. Institutions are now focused on a wider array of scenarios — from an active shooter to pandemic influenza to weather, and are creating Campus Emergency Response Teams (CERTs) to respond to this new host of threats. Success of these CERTs has been through the establishment of an interdisciplinary approach to training and preparedness, with representation from critical functions of the college or university participating. In this way, institutions are better prepared for a potential disruption to day-to-day operations, are able to carry on with critical functions and processes, and are able to resume operations in a timely fashion after a disruption, with minimal impact to student and staff safety, reputation, or financial health of the institution.

Our perspective

The new normal has increased the threat of business interruptions and impacts to institutions. For the business continuity planning process to succeed, universities must have energetic buy-in and support at the senior management and board level. Sufficient funding must be in place to support a continuity plan scaled to train, drill, exercise, and audit the viability of plans against varying crisis impact scenarios. This planning must follow a consistent process in order to promote smooth synchronisation in the event of a crisis. To ensure such a process, a strong program management function is central to the business continuity management planning effort, organizing and providing a structure for the effort and helping to manage tasks, activities, and dependencies across all functional areas.

The cornerstone needed for effective business continuity plan development will continue to be a business impact analysis and risk analysis that leads to creating impact scenarios. The business impact analysis functions to assess, value, and prioritize business functions and processes. It scopes out the potential impact of disruptions, identifies all legal and regulatory requirements, and determines the maximum tolerable period of disruption for each critical function and the maximum acceptable data loss. A risk analysis identifies risks (fire, flood, sabotage, epidemic, technical failure, etc.) that could impact key functions, quantifies the probability of those risks actualizing and their likely resultant damages, assesses the vulnerability of specific university assets to those risks, and evaluates the controls that are or could be put in place to reduce the impact of risk events.

Specifically, with respect to the Clery Act, institutions have historically focused on complying with the specific requirements in the Clery Act. However, to truly enact a campus safety and emergency response plan, institutions must now examine the effectiveness of plans currently in place with a critical eye and must exercise them. For example, most institutions maintain an emergency contact roster as part of a missing persons scenario; however, audits reveal that many of these emergency contacts are parents or relatives who are frequently hours away, and who have no real knowledge of the day-to-day routine of the student presumed missing. While this meets the specific requirement of the Clery Act, the intent is to be able to determine the whereabouts of students on campus. A closer examination by institutions in this area and other emergency preparedness areas will produce an agile emergency response plan that will enable a college or university to respond and recover from an incident with minimal loss, as well as to ensure compliance to the Clery Act.
As institutions of higher education are continually changing, business continuity and emergency preparedness must be an ever-evolving process. Changes such as new branch campuses, overseas operations, and increases in the student body all require ongoing updates to institutional preparedness and the related aftermath. As institutions are challenged with keeping up with these changes, they must always keep in mind that the cost of prevention is far less than the cost of response and consequential damages of an incident.
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