

CANADA'S UNIVERSITIES: COST PRESSURES, BUSINESS MODELS AND FINANCIAL SUSTAINABILITY

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Good morning. It's a pleasure to be in Saint John and to have the opportunity to meet CAUBO members from across the country and reconnect with colleagues.

Today I'd like to share a few of the key findings from the study that was commissioned by CAUBO to examine the financial sustainability of the current business model in Canadian universities. The paper is available on the CAUBO website.



CAUBO commissioned the study against a backdrop of what has been referred to as the 'Perfect Storm'. You are no doubt familiar with each of the components (**briefly review**). These components are not new, but the combination over the past few years has shaken confidence in the financial stability of universities and led to questions about the sustainability of the current business model.

With the 'Perfect Storm' as a backdrop this paper is intended to stimulate discussion about financial challenges and the sustainability of the business model. It focuses on facts and analysis to help improve our understanding about key cost drivers and cost pressures. The **paper does not provide a prescription**. Instead the emphasis is on examining some of the key factors that lead to questions about the sustainability of the business model in the first place.

The basic premise of the paper is that only when armed with a clear, realistic sense of mission, a full understanding of costs and cost drivers and a commitment to managing costs will the university community be in a position to tell its story in a compelling fashion.

Table of Contents

Introduction

Purpose and Overview

Part I: Setting the Context

- Business Models and Universities
- University Costs: Theories and Explanations

Part II: Cost Pressures and Cost Drivers

- Income Overview
- Expense by type and function
- Compensation – cost pressure
- Administrative “bloat”?
- Research
- Faculty Workloads
- Deferred Maintenance

Part III: Discussion / Considerations

- Internationalization
- Learning technologies

Appendices : Select info by province, inflation in academe, data issues, review of international salary comparisons

The Table of Contents provides an overview of the various topics that are examined in the paper. Given the limited time rest assured that I am not going to speak to them all. But I will touch on a number of the topics because they may help improve our understanding how we have ended up today with the ‘Perfect Storm’ ... and perhaps what to do about it.

The paper provides a ‘national’ overview and acknowledges, upfront, that there is considerable diversity in the funding circumstances by province and by institution within a given province. Accordingly various observations and national data trends may not apply to all universities.

Conference presentation

- 'The business model'
- Cost pressure theories
- Overview of revenue and expense trends
- Administrative 'bloat'
- Compensation pressures
- 'Research will be the death of universities'

- Considerations
- Concluding remarks

Over the next forty minutes or so, I will provide a brief overview of the report that starts with 'the business model', touches on some of the cost theories that have been used to help explain cost pressures in higher education, provides a snapshot of key income and expense trends, sheds some light on the topic of "Administrative bloat" and then focuses on two key expenditure factors that are major contributors to the imbalance between costs and revenue – increases in compensation and the costs of research. I'll finish with a brief set of considerations and concluding remarks. So let's turn to 'the business model'.

- *The lack of precision in the use of the term “business model” is resulting in gross generalizations, sloppy thinking, and unrealistic expectations about the nature and future of the business model of higher education. This allows others – others outside of higher education – to drive the conversation, with little rigor and even less familiarity with the history and nature of higher education let alone its future.*

- Eric Denna, “The Business Model of Higher Education”, Viewpoints, EDUCAUSE Review March/April 2014 (Denna is CIO, Utah System of Higher Education)

This quote zeros in on the key problem associated with the term ‘business model’ in the higher education setting.

The lack of precision in the use of the term “business model” is resulting in gross generalizations, sloppy thinking, and unrealistic expectations about the nature and future of the business model of higher education.

Over the years I have heard Board members, politicians, journalists and government officials speak about the need to ‘change’ the business model – yet it is clear there is limited understanding of the term and how it applies in Canadian higher education.

What is the Business Model?

- The 'business'? 'Education – teaching and learning
- With the 'degree granting' authority as the 'glue' that binds institutional activities.
- Teaching, Research, Service
- Since the late 1990s universities have been asked and/or have taken on responsibilities for other 'products' – the [Innovation Agenda](#)...and
- Social and economic catalyst for the city/region, province – requiring an expansion of existing activities & new activities
- **Expanded Mandates**

The paper explores the topic in some detail and suggests there are, in fact, a number of business models operating in a university – i.e. ancillaries, research, business schools. However for the institution as a whole the key product is 'Education' – defined as teaching and learning or knowledge transmission and knowledge discovery – with degree granting authority as the 'glue' that binds the main activities together – teaching, research and service – and produces graduates and research. **But since** the late 1990s or so, institutions have taken on added responsibilities – to realize the Innovation Agenda and become much more central to the social and economic well-being of the city, region, province, and country. That 'expanded mandate' – where institutions are expected to be 'everything to everyone' and be the social and economic catalyst – carries with it added costs.... and high expectations. And so we turn to the **financial** aspects of the Business Model.

What is the Business Model?

- The financial aspects of the model are characterized by a **reliance on public finance...**
 - operating in a **regulated environment...**
 - with cost pressures associated with an increasingly **complex organization...**
 - dependent on **highly qualified personnel** in a **labour intensive industry...**
 - an **integral part of the broader 'knowledge economy'.**

The financial aspects of the main 'business model' – the delivery of 'education' – has several key elements – each with cost implications:

Reliance on public finance – means that government priorities - political and otherwise – influence the institutional agenda and the universities are very reliant on government funding which is very much related to the state of the economy. Moreover, with the federal government and provincial government involved, leads to continuing squabbles over who pays for research and the costs of the Innovation Agenda.

Regulated environment – government controls (directly or indirectly) 90%+ of revenue (tuition and grants), program approvals, and heavily influences student assistance, the level and composition of enrolment, the composition of Governing Boards, and sets compliance requirements. Additionally, in professional schools there is a layer of external 'regulation' affecting program structure (and costs).

Universities are Complex organizations – 'multi-mission' "multiversity" – the size of small to medium sized towns, heavily unionized, with local, regional, national and international partnerships.

Highly qualified personnel – labour intensive industry – relatively expensive, and labour intensity is seen as key to quality and student engagement, and the labour component is critical to knowledge discovery.

Part of the knowledge economy – part of larger 'market' that values 'knowledge' personnel

Using data from the census and Labour Force Survey – Statistics Canada noted that much of the wage growth has occurred at the top end of the earnings distribution and "the majority of these high earners were highly educated."

And the latter two points have a direct bearing on compensation in academe....one of the key cost pressures.... And a matter we will return to in a few minutes.

So, if we have a sense of the business model and some of the inherent cost pressures how does that relate to cost theories.

University Costs: Theories and Explanations

- Baumol's 'cost disease' – highly skilled, labour intensive industry with little room for productivity improvement yet must provide competitive compensation.

Two theories have dominated the literature on costs in higher education; – the Baumol Effect (or 'cost disease') and Bowen's Law

Baumol, an economist, argued that even in sectors where it was difficult to improve productivity (a string quartet) you have to pay wages that are competitive with other sectors where increased productivity finances the wage increases or the highly skilled labour will leave (over time). The emphasis here is on 'highly skilled labour' in labour intensive industries where replacing the labour with technology is difficult. In academe student engagement and learning is linked to student/faculty interaction. While you can increase the student/faculty ratio that may not lead to greater productivity if, in fact, you are interested in a productivity measure that includes a quality dimension.

(The original study was conducted for the [performing arts](#) sector. Baumol and Bowen pointed out that the same number of musicians is needed to play a [Beethoven string quartet](#) today as was needed in the 19th century; that is, the productivity of [classical music](#) performance has not increased. On the other hand, real wages of musicians (as well as in all other professions) have increased greatly since the 19th century.)

University Costs: Theories and Explanations

– Bowen’s Law—costs are simply a function of revenue

- “The dominant goals of the institutions are educational excellence, prestige, and influence.
- In quest of excellence, prestige, and influence, there is virtually no limit to the amount of money an institution could spend for seemingly fruitful educational needs.
- Each institution raises all the money it can.
- Each institution spends all it raises.

The cumulative effect of the preceding four laws is toward ever increasing expenditure.”

Howard Bowen, also an economist, focused on universities and he argued that universities’ costs are simply a function of revenue – given the goals of institutions. Universities will spend whatever they have in pursuit of higher quality, excellence, prestige etc. – and they want more!

“*Costs of Higher Education* is best known for Bowen's Revenue Theory of Costs, sometimes called Bowen's Law:

...at any given time, the unit cost of education is determined by the amount of revenues currently available for education relative to enrollment. The statement is more than a [tautology](#), as it expresses the fundamental fact that unit cost [i.e., the cost of education] is determined by hard dollars of revenue and only indirectly and distantly by considerations of need, technology, efficiency, and market wages and prices. (p. 19) Bowen's book provided plentiful evidence that higher education institutions of similar size, situation and repute had radically different costs per student, and spent each dollar differently from one another. Their different costs were a function of their different histories in raising money.)”

University Costs: Theories and Explanations

Other theories/explanations include

- Competitive forces – the quest for the best (students, faculty) drives costs.
 - Lack of competitive forces – monopoly means limited need to be efficient.
 - Weak management – limited cost control, poor management practices.
 - Government regulation – cost of compliance as a key cost driver.
- The emergence of the Canadian “multiversity” reflects expanded mandates, size, and complexity – a ‘perfect storm’ for cost escalation

While Baumol and Bowen’s theories dominate the literature, there are other explanations;

Competition for students has led to increased student assistance, student services, facilities and new programs. Competition for faculty drives up salaries and may have significant research start-up costs.

Antithesis of the competitive market view is that universities have sufficient control over degree granting that they can pass on cost increases to students and/or taxpayers even if service levels and/or quality remain constant or decline

The ‘weak management theory’ suggests that weak management – aimed at the President but by association extending to other parts of the organization (academic and services) – contributes to cost inflation because costs are not managed properly. One could argue that tends to be more institutional specific than endemic to the sector, but nevertheless it is a view championed by some.

Then there is the issue of government regulation. Many segments of Canadian society (public and private) have had to cope with the regulatory cost driver. Specific regulatory aspects associated with sponsored research and the degree of regulation/intervention regarding program development, program approval, labour force planning, and tuition fees may, in fact , make it more taxing for the higher education sector

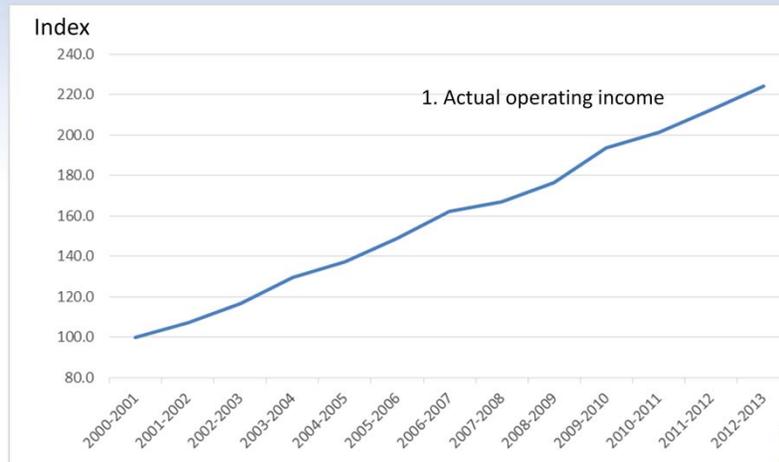
Another explanation is that as the university has become the ‘multiversity’ –expanding mandates trying to be everything to everybody has led to the pursuit of new initiatives and revenue diversification sources – satellite campuses, continuing education, international recruitment/campuses, research parks, that have all contributed to cost escalation –

Combined, the preceding cost theories and explanations probably help explain the major causes of the imbalance between cost pressures and income **although its important to note that the ‘theories’ originate in the U.S. where the ‘costs of research’ are handled quite differently than in Canada – a matter we will return to.**

So the business model and cost theories certainly point to cost factors – such as a dependency on highly qualified personnel, and there is certainly a belief that competition for students and faculty drives up costs, as does the increase in regulation. And Bowen’s Law speaks to the pursuit of excellence, prestige and influence – which all cost money.

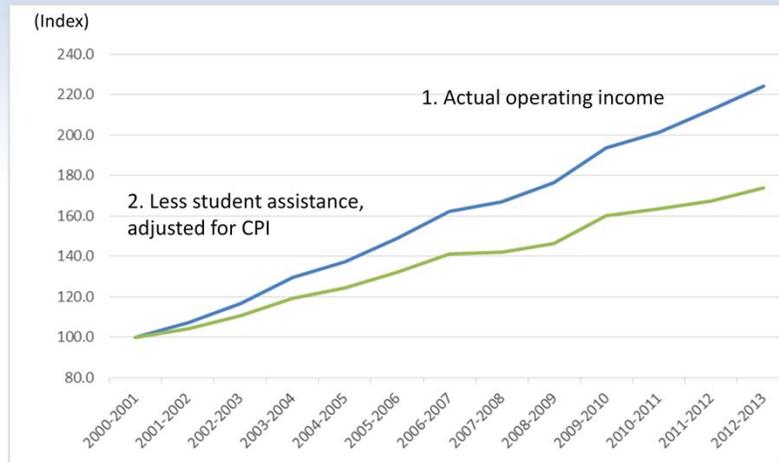
So let’s look at the money in Canadian universities.

Operating Income



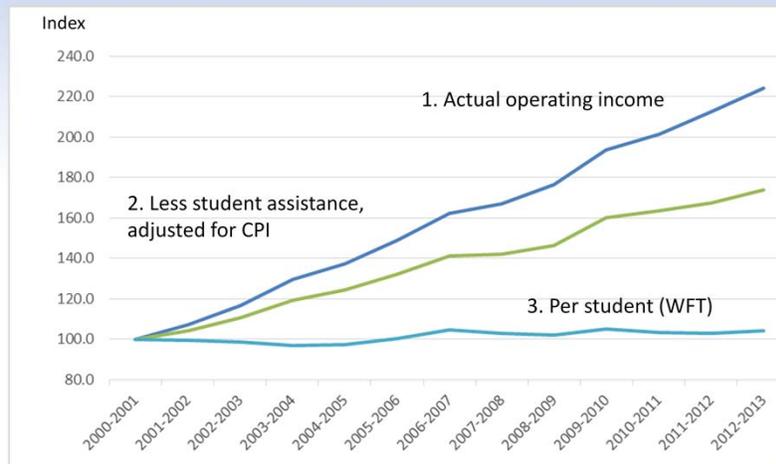
Since 2000 Operating Income has more than doubled to about \$20 Billion and Total income more than doubled as well to over \$33 Billion. And there have been tremendous benefits associated with that significant increase in sector funding: considerably more students, more graduates, greater access, better participation rates, more research, technology transfer, and greater attention to partnerships – local, regional, national and international. There is much to celebrate!

...adjusted for Student Assistance and CPI



After adjusting for financial assistance funded from operating revenues, and adjusting for CPI the increase is about 75% and...

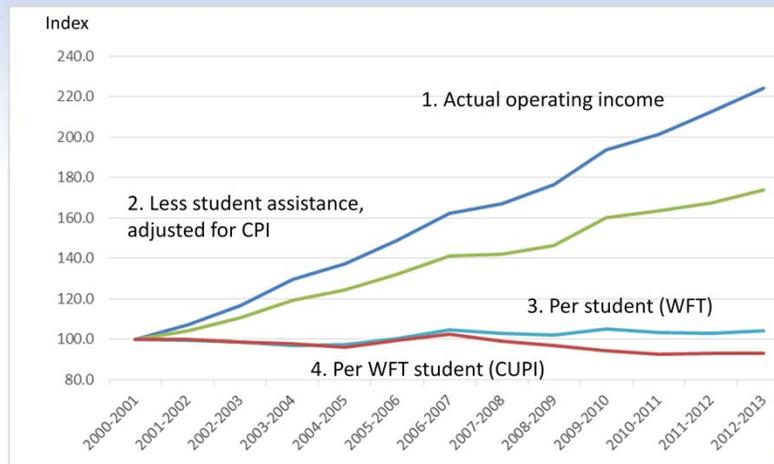
...and increased enrolment



When you consider the increase in the number of students during the period, revenue per Weighted FT student has increased, more or less, in concert with general inflation from 2000 to 2012 and ended up 4% higher in real terms. That figure, of course, is somewhat misleading because it implies that all of the income is available to support core operations – when, in fact, some of it is earmarked for special purposes. Nevertheless, the picture since the new millennium suggests that, in general, operating funding per student – at least to 2012-13 – kept pace with CPI inflation.

The ‘weighted Full Time’ measure is a very simple system undergraduates weighted at 1, Masters 3 and PhD 6.

..and a more relevant inflation index



If we go one step further and use a sector-specific price index, the Canadian Universities Price Index (CUPI), revenue per Weighted full-time student has actually declined by about 7% and this decrease was recorded almost entirely in the **second half of the period under review**. At the same time, the increase in Research Funding slowed considerably in the second half of the period.

One might speculate that during the rapid growth period from 2000 to about 2007 or so institutions were able to manage the internal subsidies associated with expanded mandates and new venture but as revenue growth slowed structural deficiencies emerged in the latter part of the period.

And the constraint continues. But the income side is only part of the story. What can we learn about cost pressures from the expenditure information?

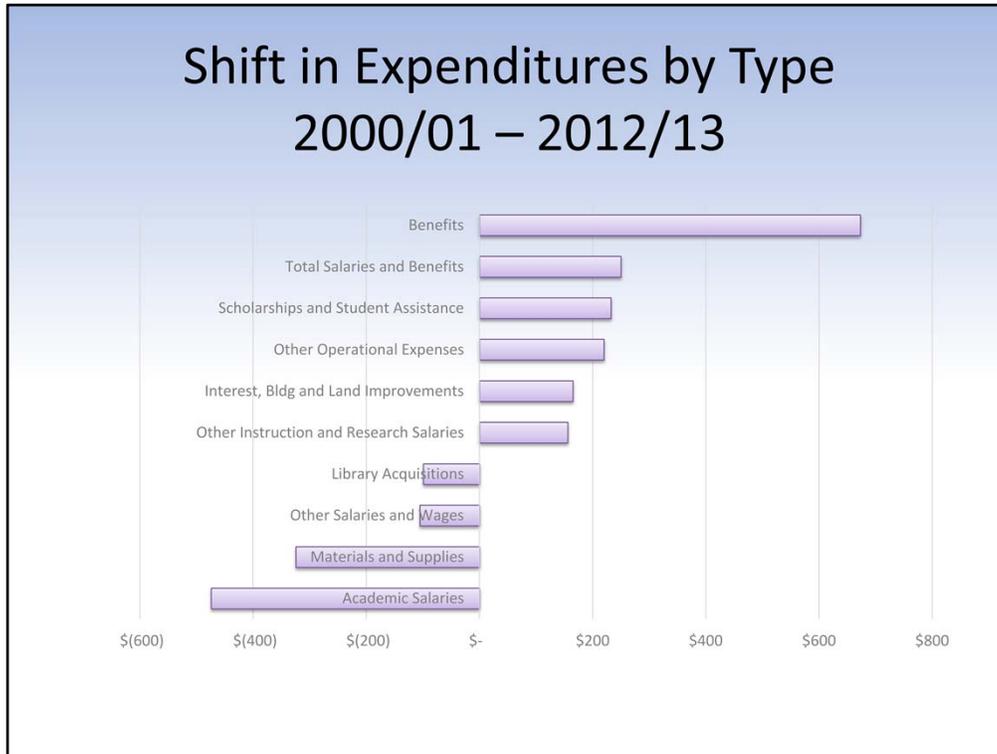
(Extra detail just for reference)

CUPI (the Canadian University Price Index) is a construct similar to the Higher Education Price Index in the United States. CUPI has been estimated, based on wages and benefits from four relevant categories of Statistics Canada price index, weighted at 75% to reflect the proportion of existing spending. The CPI, weighted at 25% for the rest. Details are in the paper.

Revenues from the Province (grants and tuition) are not sufficient to finance the cost associated with increased activity levels **and inflation specific to the sector** that is greater than the CPI.

(In addition, the graph above does not distinguish between earmarked grants, regulated tuition fees and "matching fund" type of expenditures and do not take into account changing enrolments (in particular in STEM programs where full costs are not fully recognized nor funded)

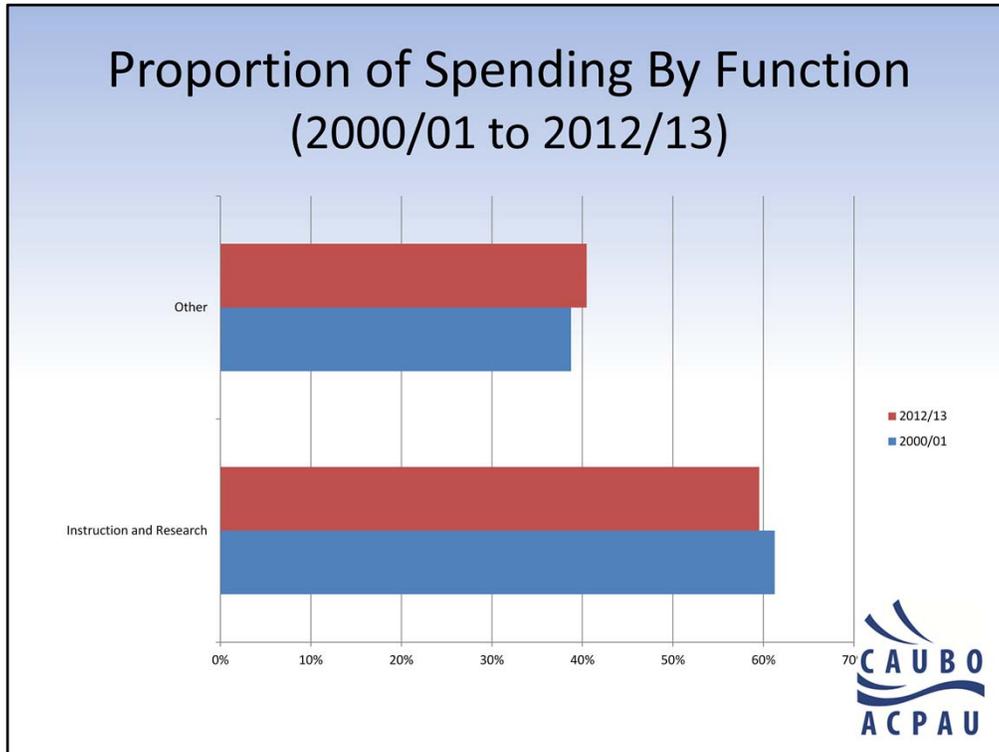
Shift in Expenditures by Type 2000/01 – 2012/13



This graph shows the 'shift' in expenditures by type over time. In 2000/01 expenditure on benefits represented about 10% of total operating expenditures. By 2012/13 that number had increased to 13.4% representing a 'shift' in the proportion. That 'shift' cost close to \$700 million – a major part of it in the form of pension contributions. In Ontario, for example, pension contributions were about 20% of total benefit costs at the start of the period and represented about 50% of benefit contributions by the end of the period.

Each of the expenditure items has a story – or at least an interpretation. The increase in Scholarships and Student Assistance is a function of at least two key factors – regulatory requirements in some provinces and increased competition for students. The increase in Interest, Bldg and Land Improvements points to, among other things, shortfalls in fund-raising or changes in government commitments – the end result, however, is increased 'cost' being borne by the operating budget.

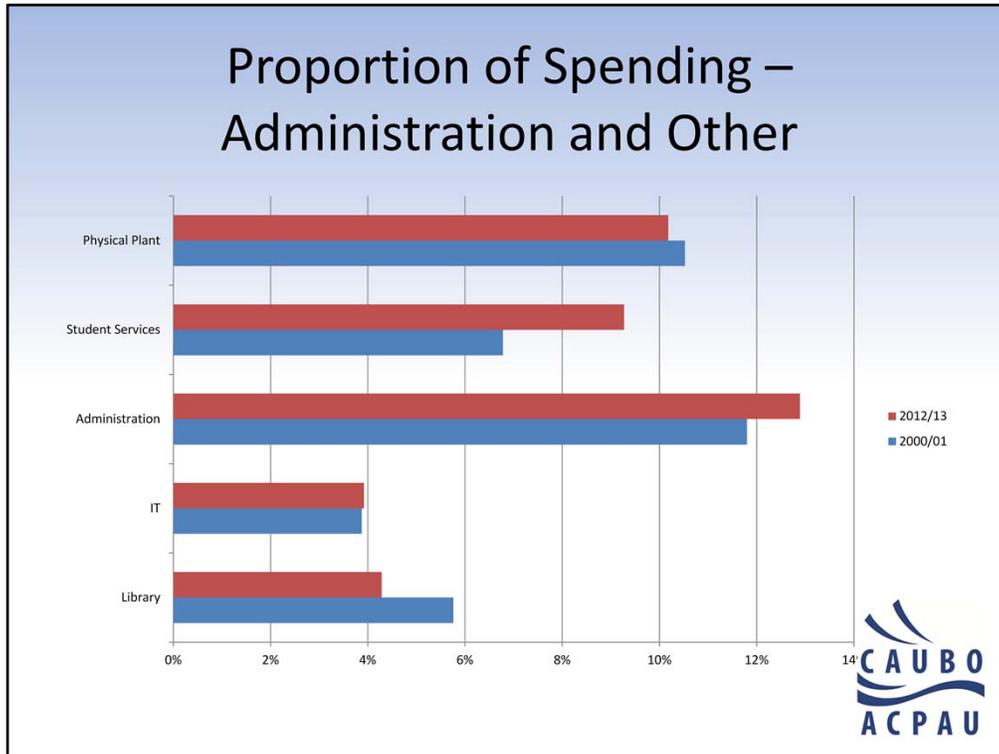
Academic salary expenditures (full-time and part-time ranked faculty) have actually decreased as proportion of expenditure, representing a 'shift' in expenditure of well over \$400 million. That in turn helps explain some part of the increase in student to faculty ratios that have occurred over the period and it also helps explain the increase in 'Other Instruction and Research Salaries' – reflecting the hire of non-ranked instructors, clinical assistants, post-docs, as well as teaching assistants, the latter which is in turn associated with the increase in enrolment at the undergraduate and graduate levels.



If we look at the distribution of expenditures by function

The proportion of the budget devoted to Instruction and Research has decreased nationally by 1.7% over the period. Only one province increased its proportion: Manitoba, all other provinces either registered a decrease over the period or maintained their relative spending level.

So in fact, spending on the non-academic or **administrative** side of the house has increased as a proportion of total operating spending, but is it Administrative Bloat?



If we examine the shift in proportion over time, it is clear that the fastest growing area was Student Services, followed by 'Administration'. IT essentially held its own over the period while the proportion of expenditures on Physical Plant and the Library declined with Libraries experiencing a larger decrease – an example where technology and co-operation among institutions has actually reduced 'costs' but maintained or enhanced quality.

Further examination of the increases in Administration indicates that most, but not all, of the increase in administration is, in fact, related to academic support services and external relations.

Administrative “bloat”?

The increase in the support services (or administration broadly defined) – is focused in three main areas

- **academic support, external relations, and student services**
- General **increase in regulations** – external and internal
- Increased emphasis on **accountability**
- Pursuit of **new revenue and new initiatives**
- And the **growing complexity** of the institution - a function of increased size, expanded mandates and the cumulative impact of the other factors

So is it Administrative Bloat? Student Services and Administration are the two ‘functional’ areas that have experienced significant growth since the turn of the millennium. Within the ‘Administration’ two specific areas have experienced greater growth – academic support services and advancement/external relations. But there has been growth in ‘administration’ generally as well – Internal Audits, research accounting, human resources/collective bargaining to mention few. Academic support services cover a range of services from Teaching Centres to Offices of Research services and VP Academic offices’ that often include offices and personnel dedicated to internationalization and quality assurance and other ad hoc special projects such as credit transfer, on-line learning etc. At the same time the External Relations portfolios in many institutions have grown driven by fund-raising and PR activities. Keep in mind that the observation about external relations – and specifically fund-raising - is based on changes in ‘gross expenditures’ over time. If we factor in increased revenue from donations, the equation may change somewhat. Donations were about \$850 million in 2000-01 and about \$1.250 billion in 2012-13 – including capital and endowment.

In Student services, the increase has been driven by a variety of factors such as - increased enrolment, increased student diversity and associated requirements, the effects of large class sizes and higher student to full-time faculty ratios, and the use of more adjunct/sessional appointments, and ‘helicopter parents’ and legal/moral issues....

And, in a way, may also be related to faculty spending less time on academic administration and less time on student engagement, or at least undergraduate student engagement – a matter we will return to in the Research section.

Interesting point to note, however, is that some part of the increase in student services may not be quite the ‘cost pressure’ it appears. Over the period ancillary fees more than tripled – and buried inside the ancillary fees is – in many institutions – provision to fund some part of the student services.

Most of the non student services growth is linked to the increase in size and complexity of the organization in an era of increasing government intervention/regulation, increased interest in accountability, and competition among universities.

But some of the growth is related to internal factors – the need for more internal regulation, the expansion of unionization/collective bargaining and attempts at revenue diversification and partnership building that often carry administrative overhead. **And the increase in some services happens to be in areas that are more visible to faculty – and heavy on ‘process’ and ‘regulation’ (unionization, collective bargaining, research accounting etc.) although the biggest ‘gripe’ seems to be with the number and level of salary paid to senior academic administrators.**

Each of the items could be the topic of a separate report but the point is there are some reasonable explanations for at least some of the increases in the non-academic area. However, explaining the rationale behind the increases should not be interpreted as justification.

Universities have been quick to pursue new initiatives/ventures without necessarily doing the due diligence and examining costs and benefits in detail. And they have been quick to plan new capital facilities without necessarily having a feasible financial plan.

And the management of people – the university’s key resource – has been less than stellar leading to greater unionization and all the tension and complexity that it entails. Further, although not expressly identified in the CAUBO data, universities are spending tens of \$millions (and perhaps more) each year on severance payment arrangements.

The preceding suggests there may be some truth to the weak management argument...



WE HAVE BRIEFLY DISCUSSED THE INCOME CONSTRAINTS AS WELL AS THE GENERAL TRENDS IN UNIVERSITY SPENDING. THE NEXT COUPLE OF SLIDES WILL FOCUS ON 2 OF THE MAIN factors that are seen as affecting FINANCIAL SUSTAINABILITY: SALARIES AND RESEARCH

Salaries – cost pressure

- Late 1990s through to about 2007 the increase in faculty salary levels reflected a premium attributed to ‘knowledge workers’ and a tight labour market for faculty. (Baumol effect)
- From 2008 onwards Faculty salary increases appear to have outpaced ‘knowledge workers’ in the general economy
- On average, faculty are in the top 5% of wage earners in the country; some full professors, and senior administrators, are near or over the threshold of the top 1% of wage earners*.
- Canadian faculty salary levels vs. U.S. salaries

*Statistics Canada, National Household Survey (2011) the *threshold* level (2010 reported incomes) for the top 10% was \$80,400, the top 5% \$102,300 and the top 1% \$191,100.

The ‘knowledge worker’ labour market is competitive – and highly educated workers in all parts of the economy have done very well since 2000. In the 2006 census the income of faculty with PhDs mapped closely with individuals with doctorates in other parts of the labour force. The 2011 household survey suggests faculty made some relative gains in the following five years – largely because the financial downturn in the interim resulted in less than a robust market outside academe. The Household survey data also suggests that on average faculty are in the top 5% of wage earners in the country and there are a number of professors and senior administrators with salaries that would put them in the top 1% of wage earners. (Point to the top 10% threshold \$80,000).

The tight labour market refers to the fact that just as universities needed more faculty to cope with the “double cohort” in Ontario, enrolment growth in general, and the Innovation Agenda, the supply of PhD graduates dropped – because intakes had been reduced during the austerity period in the 1994-1999 period. Students were not encouraged to pursue a PhD. The Law of supply and demand prevailed. Starting salaries were ‘bid up’ – and that had a ratchet effect for salaries in general.

On average Cdn faculty salaries compare well with U.S. **public** Doctoral universities – although the average salary for Associate Professors is somewhat higher in Canada – likely due to differences in the virtually automatic nature of the Progress-Thru-the-Ranks component in Canada. Note the reference to public universities. If one looks at private institutions that Canadian salaries are somewhat lower at the Full and Assistant Professor ranks.

Salaries – cost pressure

- Number of Canadian full-time faculty has not kept pace with the increase in enrolment, resulting in higher student to faculty ratios and pressure for more faculty.
- The 'salary base' and financial capacity to hire has also been affected by less turnover at the high end – abolition of mandatory retirement
- Staff salary levels have been affected by the general increase in the market for 'knowledge workers' and the increase in the number of professional staff in Academic Support, Student Services and External Relations and Administration.
- Over the past few years there has been a general slowdown in the rate of salary increase as the market for faculty weakened and governments introduced a variety of measures to slow the rate of increase.

What we also know from the data is that the number of faculty has not kept pace with enrolments – hence the increase in student to faculty ratios, greater reliance on part-time/adjunct faculty, and continued pressure for more full-time faculty.

And with the abolition of mandatory retirement there is a growing number of 65+ faculty who are staying on – contributing to **the financial pressure by not** releasing PTR 'savings and driving up the salary base by still garnering salary increases....

In 2012–2013, close to 10% of full-time university faculty in Ontario were over the age of 65.

Turning to the staff side of the house... again the 'knowledge worker' economy helps explain part of the rationale for the general increase in salary levels but it is also the case that where universities have added 'staff' – academic support, student services, external relations and some areas within administration (i.e. internal audit, research accounting, human resources) the staff tend to be professionals – thus resulting in a growing salary base that influenced by the changed composition of staff as well as the level of annual increase.

There has been a general slowdown in the rate of salary increases over the past few years – as the market for faculty weakened and government measures of one sort or another were introduced. However the salary increases exceed available revenue increases and thus result in continuing cost pressure. That reality has been accompanied by another major area of cost pressure – Research...

Research – cost pressures

- Innovation Agenda has benefitted Canadian universities - better research facilities and more faculty to expand research activity and benefit the learning environment - (CFI), (CRCs), the Knowledge Infrastructure Program (KIP), Tri-council investments and Federal Indirect Cost of Research (FICR)... but
- Increasingly evident that funding levels and funding mechanisms to support research are not covering the full indirect and direct costs of research at the institutional level

An interesting point to note is that the 'cost theories' reviewed earlier, have their origin in the United States where the costs of research are handled much differently than in Canada. Cost pressures in research are not a major burden in the U.S. because, for the most part, sponsored research includes provision for full indirect costs + direct costs including faculty time.

The Expanded Mandates include considerably greater research activity - a key financial challenge. The Innovation Agenda has benefitted Canadian universities in many ways.... But it is increasingly evident that the funding levels and funding mechanisms to support research are not covering the full indirect and direct costs.

Research – cost pressures

- *'Research Will be the Death of Universities'* - institutions are subsidizing the research enterprise.
- Fundamental financial challenge is the unfunded direct costs of faculty time.
- The *shift* in time (time=\$) towards research has not been fully recognized in the funding equation.

CAUBO's own report on the Indirect Costs of Research suggests "unless major steps are taken to address the variety of funding issues associated with indirect costs - Research Will be the Death of Universities. Part of the challenge rests with the private and public funders of research in Canada. The University community has work to do raising awareness of the indirect costs of research, accounting for the indirect costs of research, and addressing the exemptions and practices regarding the charging of indirect costs.

But the indirect costs are just one part of what I think is the 'fundamental' challenge – the direct costs of faculty time that are not adequately recognized in the funding equation. Some faculty are paid from research funds but the vast majority are funded from operating funds. The implications are far-reaching... and fundamental since the revenue portion of the operating business model is heavily oriented to teaching students not research.

Faculty Workloads

- Shift in faculty workloads largely associated with increased graduate enrolment and research
 - Workloads shifted from teaching to research and service fuelled by the [Innovation Agenda](#)
 - On average full-time faculty teach fewer undergraduate courses and spend more time on
 - graduate student courses and supervision
 - research activities
 - community service activities
 - technology transfer
 - partnership building
 - fundraising
 - profile building in the discipline

The 'workload' associated with 'research' has increased in concert with the competition for external funding, graduate supervision and the necessity of securing support, and increased emphasis on the dissemination of results and technology transfer.

This has a major impact on operating resources. A major part of the cost of the Innovation Agenda was simply absorbed by the institutions – faculty time. With no additional operating resources for research the 'cost' was simply reflected in large class sizes, increased student/faculty ratio, and greater reliance on part-time / teaching only faculty.

Faculty members took on the Innovation Agenda challenge – it is, after all, a major part of what they do. But the full implications are only now being felt across many institutions.

In a nutshell...

The revenue part of the 'business model' did not recognize

- the expanded mandates taken on by institutions
- cost implications of the 'shift' in faculty workloads,
- nor the importance of accounting for sector specific inflation.

In a nutshell, the revenue part of the 'business model' did not recognize the expanded mandates – particularly the Innovation Agenda – the associated cost implications of the shift in faculty workloads and the substantial indirect and direct costs of research and community service, nor the importance of accounting for sector specific inflation.

In a nutshell...

On the expense side...

Institutions spent on expansion, prestige, profile
(Bowen's Law)

Competition for students / faculty

Overextended – capital financing

Chased new ventures – revenue generation

Added complexity

When coupled with major increases in enrolment and changes in the composition of the enrolment, universities experienced tremendous growth and change on a number of fronts. Research parks, satellite campuses, overseas ventures, and major capital investments became the norm. Growth became the mantra and, coupled with increased government regulation, and heightened labour relations activity, bred a new level of organizational complexity.

During a period of funding expansion universities were able to mask the structural realities but since the financial crisis of 2008-09 financial strains have emerged.. Leading to the 'Perfect Storm'.

Considerations

- A major part of the financial challenge is directly related to government funding constraint, demographics, and pension deficits.
- But it is also evident that part of the challenge is related to internal practices, policies and decisions.

Over the past forty minutes we have covered a lot of ground. From the review we can take away a few key observations in helping to think about the current financial challenge.

Let me be clear.... Part of the financial challenge is directly related to government funding constraint and the related funding mechanisms and policies. Some part is also related to basic demographics and a slow-down or reduction in domestic demand. And the need to deal with pension deficits has placed a major expense burden on budgets. That is all true.

But... it is also evident that part of the financial challenge is related to internal practices, policies and decisions. Clearly work will be required to address the external factors that are directly affecting institutional revenues but there needs to be a better understanding and recognition of cost pressures internally, and a willingness to ask some fundamental questions about university mandates, institutional aspirations, and institutional policies.

Considerations

Throughout the paper a number of issues emerge that deserve consideration

- At the national level
 - counting students
 - development of a higher education price index
- At the provincial level
 - Discussion and better understanding of the higher education component of the Canada Social Transfer
 - Better recognition of the actual 'costs' of new/expanded initiatives – both start-up and on-going

And that leads to a brief summary of some of the issues that emerge in the paper
At the national level

- counting students (and faculty) – the absence of an agreed to standard methodology for counting students across the country affects our ability to adequately, or accurately, capture the shifts in program 'mix' and level of study that have major bearing on costs. Instead, we fall back on a single imprecise FTE calculation.
 - development of a higher education price index
 - We are doing ourselves a disservice by relating inflationary costs to CPI. With 75% of our expenditures devoted to salaries and benefits, our spending pattern is considerably different than the 'basket of goods' reflected in the CPI.
- At the provincial level
 - We need discussion and better understanding of the higher education component of the Canada Social Transfer
 - And the various federal and provincial contributions to PSE and research
 - Better recognition of the actual 'costs' of new/expanded initiatives – both start-up and on-going

Considerations

- At the institutional level
 - Revisiting the emphasis placed on research in some institutions
 - Managing retirement and an aging workforce
 - Revisiting faculty Progress-Through-the-Ranks (PTR)
 - Revisiting staff compensation – and the role of local markets

At the institutional level there are host of issues that emerge when looking at the data. As noted earlier research and compensation are 'big ticket items' – some institutions may need to revisit the emphasis they have placed on research and re-orient their research efforts (more collaborative efforts, emphasis on networks – implications for IT, travel etc). And it may carry over to hiring decisions and, again, the emphasis placed on teaching and research.

The abolition of mandatory retirement has created a financial challenge – and it needs to be managed. It has been exacerbated by the financial downturn in 2008-09 – individuals 'saw' a major loss of future income (money purchase plans) and put off retirement plans.

The data on US salaries and the major difference in Associate Prof salary levels begs further investigation – does it have something to do with our PTR provisions? And should there be changes? (See FBS paper on salary policy increments...)

And staff compensation – do staff salary increases have to be more or less similar to faculty increases? Are they?

Considerations

- At the institutional level
 - More attention to costs – research, new and expanded initiatives
 - Continual emphasis on ‘what are you trying to do?’, ‘what resources are required?’ (costs/policies/) and ‘how would we know this is making a difference in the learning environment? (indicators)
 - Less complexity is better – KISS principle (Or ensure that decision-makers know the costs and consequences of new / expanded initiatives)

As institutions strive to diversify their revenue are we paying enough attention to the difference between gross revenue and net revenue?

Someone needs to be constantly asking the fundamental questions about mission and mandate.

Less complexity is better and the KISS principle should be invoked whenever possible.

Concluding Comments

- No easy answers to addressing the financial challenge
- A multi-faceted approach is required
- discussion and partnerships with various external stakeholders and members of the university community
- strategies that include both revenue enhancement and expenditure constraint measures.
- Begins with the need for a more in-depth understanding of fundamental cost drivers in the institution.

As noted at the start, the basic premise of the paper is that only when armed with a clear, realistic sense of mission, a full understanding of costs and cost drivers and a commitment to managing costs will the university community be in a position to tell its story in a compelling fashion. While it is clear a major part of the current financial challenges are related to external challenges, it is also clear universities need to do more to get their own houses in order. To steal a line from Pogo – ‘we have seen the enemy and it is us’....

There are no easy answers to solving the current financial challenges faced by Canadian universities. Some institutions will have some very difficult choices and decisions to make over the next few years. But a better understanding of the key components of the business model and the key expenditure drivers may help inform those decisions.

Many topics touched on in the paper deserve more attention and, no doubt, there are topics that deserve less. And it may be the case that some important financial topics have been missed altogether. Nevertheless, to the extent the discussion paper sheds some light on key topics and helps inform and spark discussion about the financial future of Canadian higher education, it will have met its objectives.

Thank you.



Questions ?

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