

Financial Self-Sufficiency and the Public University

BY JOHN T. CASTEEN III

TAKEAWAYS

- 1 With the states providing less money per student, some public institutions have moved toward more reliance on other sources of funds, such as higher tuition and increased philanthropic support.
- 2 Greater institutional self-sufficiency requires a long-term vision, a well-planned fund-raising strategy, constant communication with key constituencies, and a willingness to be open and accountable.
- 3 If public universities are to survive and thrive, they will have to plan rigorously, carefully manage their resources, imaginatively raise new funds, focus on core academic goals, and constantly work in the public's interest. Boards have a role in supporting and encouraging these activities.

THE REDUCTIONS IN STATE TAX SUPPORT FOR public universities that began around 1990 and continue today are progressively redefining relations between government and public higher education. The reasons for the drop in appropriations per student vary from state to state and include aging electorates, voter fervor for tax cuts, and mandated restrictions on public spending. Such trends, along with competing claims for tax support, have largely fragmented what was once a public consensus that education was the states' first obligation.

In response, some public universities have moved away from dependence on tax support and toward reliance on other sources of funds. And flagship institutions in states like Louisiana, Ohio, Oregon, and Wisconsin are increasingly pushing to shed many of the burdens of state regulation in hopes of operating more autonomously—including being allowed to set their own tuition.

Higher tuition charges have in fact become the most common source of new revenues for public institutions. They are also the source most likely to elicit political hostility. Americans generally expect public colleges and universities to be inexpensive, and voters and elected officials have famously short memories about the rationales for tuition increases.

In a handful of instances, public institutions have focused instead on intensifying their fund-raising efforts, starting up major capital campaigns that have yielded philanthropic dollars to support core academic activities. Raising philanthropic funds is not for every public university, but in the right places at the right times, it can work.

This article will describe how the University of Virginia was able to raise such funds and the lessons it learned that might be of interest to other public institutions. The article is based on my experience as U.Va.'s president from 1990–2010, a period that saw dramatic declines in state support for all of Virginia's public colleges and universities. Over the course of those 20 years, tax dollars for the University of

Virginia's academic programs fell from 28 percent of expenditures to 6 or 7 percent.

Yet the past two decades have also brought dramatic improvements in the operating environment for public higher education in the state. For U.Va., the results have included increased stature among American and international universities, steady growth in student diversity, a measurable improvement in the quality of the student body and faculty, and success in major new initiatives undertaken without state support. The university's total budget has grown from \$746 million to \$2.4 billion, with direct academic expenditures holding constant.

How did it happen? As state appropriations collapsed, two occurrences made the difference between failure and eventual success for universities. One was a change in law: In 2005–06, Virginia's General Assembly enacted what appears to be the nation's first semi-autonomous-universities statute, which resulted in less-intrusive state regulation in exchange for greater university accountability in meeting the state's needs. Among other things, that allowed U.Va. to raise its tuition for both in-state and out-of-state students.

The other was the development within the university of strategies for managerial, financial, and programmatic self-sufficiency, including efforts to raise private funds to replace lost state tax appropriations. In the process, the university created a major endowment and built or rebuilt some 142 buildings, with only about 15 percent of the money coming from the state.

Needed: A Reliable Source of Support

Before I discuss further what happened in Virginia, I should provide some context as to the university's position in the early 1990s. U.Va. had never been wealthy; state appropriations had always been modest compared to those for similar institutions in neighboring states. To compete, it had to wring every penny out of each dollar.

Moreover, the system by which financial decisions were—and are—made at U.Va. reflected that. Faculty leaders serving in prior times as fiscal officers invented the machinery of frugal management. This system had long been charged with first putting dollars into the academic enterprise. With little involvement from the governing board in the internal politics of allocations, non-academic units came last and led uncommonly frugal lives.

In addition, although U.Va. lacked the support machinery and personnel for a major campaign, it had conducted modest campaigns several times before. It knew its likely major donors and their interests. So even without considering the prospect that the state would stand down from its historic level of support, the university's leaders entered the 1990s confident that they could raise and manage resources from private supporters.

When I became president in 1990, U.Va.'s endowment was estimated to be \$70 million. Annual and capital giving together amounted to about \$30 million in a typical year.

Together, private sources contributed about 3 percent of the expenditure budget.

Virginia was optimistic about its public universities in those days, but that optimism was short lived. In one memorable conversation, the then-governor predicted that increased state appropriations would amply cover the cost of increased enrollment and that state leaders wanted more than one world-class university. Yet in private conversations and in public addresses, including one delivered at my inauguration in October 1990, the governor criticized faculty members for being engaged in research and urged them to concentrate on teaching, public service, and advising—which he characterized as the university's mission. Not long after that, the state's revenue collections fell behind the state's revenue estimates. The state delayed acting until fall 1991, when the first deep cuts in allotments to state agencies were made.

In fact, by 1991 the state had abandoned the appendix to its budget manual that had previously determined the cost of education at the several public universities, allocated state funds, and identified state shortfalls. The consequence was chaos: No annual operating plan based on anticipated state appropriations could succeed. The state had become the least reliable source of support for its public universities.

Fortunately, U.Va.'s internal mechanisms for managing resources dampened down much of the effect of the first reductions. Faculty members and financial officers had disagreed with the state's revenue projections and foreseen a state-tax-collection shortfall as early as spring 1990. We had already begun making customary adjustments to deal with what we could predict, merging units whose functions were duplicative, holding open vacancies for as long as possible, moving essential academic functions from state tax funds to other sources of support.

State officials, meantime, denied that the state had a financial problem, then described it as temporary and soon-to-be-corrected, then made a series of mid-cycle reductions in allotments to most agencies and institutions, then ordered salary reductions, and then tried unsuccessfully to levy a charge that amounted to an illness tax on people using the university's hospital. Ultimately, in a measure that spoke eloquently to the cultural differences between universities and agencies of state government, they ordered that we return to grantors—not only government grantors like the National Institutes of Health, but also foundations, corporations, and private individuals—sums equal to salary reductions ordered for university employees regardless of funding sources. By and large, we gained relief from the most ill-considered of these strategies, although we were compelled to return grant dollars and then try to explain what was happening in Virginia.

Undertaking the First Major Capital Campaign

Early in the crisis of 1991–93, we began seeking advice on the major elements of what would become a survival plan.

We heard a good bit of cautionary and negative counsel. One fund-raising consultant told us that we could not hope to raise significant sums from donors—our donor base wasn't wealthy enough, our development infrastructure was weak, we lacked the necessary staff. An authority on institutional finance warned us that no public university would remain among the top 25 research universities in 10 years. Several people encouraged us to develop retrenchment plans to scale the university down to the level of a comprehensive institution and to prepare faculty members and alumni to settle for less of everything.

Through the winter and spring of 1992, we assessed options and disclosed what we were learning to trustees, faculty members, administrators, students, parents, and state officials. In early summer 1992, we invited alumni and anyone else with an interest to convene for a daylong discussion of the issues. By that fall, it had become clear that the state's financial crisis was not short-term and that the university's problems would not go away. Rather than retrench and scale back, we decided that if we and other public higher-education institutions were to advance and fulfill our great public promise, we would have to seek additional private support. We began planning for a major capital campaign.

We had to learn how to organize and execute this first major campaign as it went along. We knew a fair number of generous people, but we lacked a truly comprehensive list of prospects. Consequently, we modified our goals and deadlines repeatedly prior to the official end of the campaign on December 31, 2000.

We also had to devise a process for long-range planning. We enlisted volunteers—including faculty members, alumni, staff members, students, parents, and even a man in Australia who sent comments in response to drafts he found on the Web—to draft, critique, and revise plans. We retained a consultant to advise a new chief development officer as he assembled a staff, devised a campaign budget, and planned a kick-off event for October 1995.

Relatively few critics but many skeptics watched our initial effort. Labor leaders, for example, argued that university employees would be safer trusting the state than the university. With solid board support, we listened carefully, disagreed when necessary, and moved ahead.

And we succeeded—largely because of a broad-based consensus among alumni, faculty members, and other stakeholders that we would have to become self-sufficient in order to survive and grow. That meant that deans, development officers, and I had to plan aggressively and stay almost constantly on the road to keep our issues in front of our various constituencies. We had to demonstrate continuously that we could succeed. The measures of success were as simple as ranking in the top 25 in *U.S. News & World Report* and as complex as faculty elections to national academies.

With each successive state reduction, we became more committed to our goal. Our list of about 2,000 prospects grew to some 70,000 names. And many donors made mul-

multiple gifts, paid pledges early, made additional pledges, and brought other prospects to us.

This first campaign generated some \$1.43 billion by the end of 2000. It moved the university to a predictable philanthropic cash flow in the range of \$200 million.

Embarking on a Second Major Campaign

The first campaign also prepared the way for a second major campaign, launched in 2006 with a goal of \$3 billion, of which more than \$2.3 billion has been already raised. For this second large campaign, which continues today, U.Va. had to learn to manage far larger assets than it had in the past. Historically, the finance committee of the board had selected endowment managers and determined investment criteria. As the endowments grew, lay or volunteer oversight of investment managers was no longer sufficient. In 1998, imitating Duke University's endowment-management model, the board established the University of Virginia Investment Management Company (UVIMCO) to manage both endowments and operating reserves.

The second major campaign also has goals that were beyond U.Va.'s reach in 1995. The university now raises more money and makes more effective use of the proceeds. With new authority to issue institutional bonds for construction and significant reserves, our building costs are lower now than under the old state system. So instead of concentrating almost exclusively on construction dollars—which, in our experience have been the easy, first dollars to raise—deans and others who are working toward strategic goals can seek money for programmatic endowments, including core funding for faculty salaries. Increasingly, annual gifts go toward identified priority programs rather than simply into discretionary funds.

The university has 25 foundations that support and advise its various schools—for example, the School of Architecture Foundation or the Law School Foundation. Half were created since 1990, and the others go back to the late 1960s. Foundation board members participate in planning, actively raise money, and make their own gifts. Yet while they focus their support on their specific schools, all funds spent for university purposes flow through the university's books—a form of financial control that is unique among Virginia's public universities.

The benefit of this complex model has been that it has tended toward transparency in its operations and fostered collaboration. After surpassing its goals in the 1995–2000 campaign, for example, the foundation that supported our business school began supplying names to other foundations that needed strong backers.

The university's Council on Foundations, comprised of the volunteer chairs of all the related foundations, works alongside deans and faculty committees to vet plans for use of private resources. They discuss issues on a level playing field with the university's politically appointed board.

The most promising recent development has been a commitment from the chair of the university's governing board (called "rector" and "visitors" at U.Va.) that the board itself will try to raise about \$1 billion from new donors. U.Va.'s fund-raising efforts have benefited in the past from support from various board members, as donors, lead volunteers, and sometimes solicitors. The current chair's commitment is a big step toward what boards of public universities like U.Va. must do to sustain excellence in an environment of declining state support.

Lessons for the Future

Looking back from the perspective of 2011, the success of our funding strategy and the restructuring legislation of 2005–06 suggest that the core principles defined in 1990–92 deserve careful attention. U.Va.'s history of managerial and financial transparency, for example, explains why state officials could give up intrusive controls that were not working and trust the university to be accountable. We have learned several lessons:

Greater autonomy requires greater accountability.

Virginia's government has a long history of demanding transparent disclosure. The university's books and practices have always been open to the state's auditors; there is no constitutional status to shield anything. As accountability laws have evolved to reflect the new responsibilities of individual school-related foundations, the state's auditors have even broader authority, with the university's support, to examine the foundations' books and practices. So far, they are examining only a handful each year, but their right to examine anything is fundamental to this new variety of accountability.

Planning efforts, and reporting on all those efforts, are important. We have engaged a calculated mix of professional planners and constituents to protect the public's right to know and communicate what the university intends to do in the public interest. As we developed a culture of planning in the early 1990s, we saw successes and failures. Failures were especially instructive: Inevitably, they turned out to have been in some sense brokered or political. In our experience, planning succeeds when capable people participate and refuse to let politics intrude.

Institutional credibility depends on the board's willingness to keep "noses in, fingers out." That rule more often than not challenges the fundamentally political alliances that lead governors to appoint members. It's important to ensure that the people who are genuinely accountable can do their jobs. Our experience with any number of new functions—the operation of UVIMCO, creation of an operating board for the university's hospital, and commitments made in connection with fund raising itself—has reinforced the principle that properly defined and assigned duties with accountability work best at public universities like U.Va. A public university cannot be both self-sufficient and secretive.

Supporting entities, including institutionally related foundations, must adhere to public expectations of

accountability. To succeed in its current condition, the university engages large numbers of volunteers who may also be donors, gift solicitors, planning participants, and so on. The university is inside the foundations, and the foundations are inside the university. The university's governing board and the president each name one member to serve on each foundation's board. The Council of Foundations has one seat at the governing board's table, without a vote. The university presence, the state auditors' presence, face-to-face contacts with the president and the governing board, and frequent reminders that transparency and accountability go hand in hand seem to be the keys to success.

The 2005–06 restructuring of the relationship with the state has cut costs significantly, compensating for part of what the state has taken away during the last 20 years. But in ways originally proposed by university officials, the legislation also demands constant attention to the public mission and commitment to the public good. U.Va. now provides public-health services and economic-development programs in areas where the state does not. The state has not appropriated funds to pay for these new functions and services. They are the university's to fund because they are part of the price of being a semi-autonomous public university.

Within obvious limits, U.Va. reached financial self-sufficiency about three years ago. The timing was fortuitous—at just about the same time, Virginia and the nation fell into what some people call "the Great Recession." No Virginia university wants to give up the state's remaining contribution. In U.Va.'s case, some \$2 billion in additional endowment would be necessary to replace what remains. In addition, state bonding has come to replace the state's former capital budget, which disappeared early in the 1990s. The sums available for construction and renovation do not always equal those available from donors, but state bonds demonstrate that the state remains committed, whatever its fiscal limitations.

Today philanthropy of all kinds provides approximately 10 percent of U.Va.'s budget. UVIMCO now manages more than \$4.5 billion. The university's endowment consistently ranks among the five largest endowments of public institutions and among the 30 largest of all colleges and universities in the nation.

Officials of the government of Singapore visited U.Va. before the passage of the 2005 legislation. They came to ask questions about our version of what Singapore now calls its "semi-autonomous" public universities. Their chief point about accountability for public universities like U.Va. was that the topic is almost as old as higher-education institutions themselves. Our American distinction between private and public institutions makes little sense in nations where education is almost by definition public—where the notion that universities owe services to government, to the public good, is simply assumed as a condition of any financial support that the government provides and often as a condition of existence itself.

In the end, if public universities are to survive Virginia's 20-year financial crisis or California's self-imposed spending limits, something like the core understandings that I have described will have to become our common property. Constant, rigorous planning, brave and principled management of resources, determined transparency, imaginative and world-class fund raising, core academic integrity, and constant work in the public interest—these have to be the characteristics of tomorrow's public universities. ■

AUTHOR: John T. Casteen III is president emeritus of the University of Virginia.

E-MAIL: jtc@eservices.virginia.edu

T'SHIP LINKS: John Nelson and Kimberly Tuby, "Public University Trustees: New Expertise Needed as Funding Diversifies." July/August 2008

OTHER RESOURCES: "Especially for Foundations," *Best of Trusteeship* portfolio (AGB Press, 2011). David Leslie and Terrence J. MacTaggart, *The New Ethics of Trusteeship: How Public College and University Trustees Can Meet Higher Public Expectations* (AGB Press, 2008).

Appeared in the May/June 2011 issue of *Trusteeship* magazine.
Reproduced with permission of the Association of Governing Boards of Universities and Colleges.
Copyright 2011 © All rights reserved.