THE NINE SACRED COWS OF FINANCIAL MANAGEMENT:

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How To Get a Handle On Controlling Expenses and Increasing Income

For independent schools all sources of income and expense are like the various points on a waterbed. If you push down on one area, the other areas pop up. There are "trade offs" to budgeting decisions in the operations of independent schools. **How do independent schools analyze these tradeoffs and make appropriate financial management decisions that support the mission and vision of the School?**

The first, important exercise, that very few schools undertake, is to assess their "sacred cows". These are their treasured goals that are often in conflict with one another.

The "Sacred Cows" that we all aspire to achieve, preserve and enhance are as follows:

1. High Faculty and Staff Salaries (at least very competitive with the marketplace)
2. Strong Program, Curriculum, and Technology that is "State of the Art"
3. Low to Moderate Class Size
4. Appropriate Maintenance of the Physical Plant (to avoid deferred maintenance)
5. A Strong Financial Aid Program to Help Ensure Diversity
6. Management of Enrollment: Enhance Income (but Not Too Large)
7. Moderate Increases in Tuition and Fees
8. Enhanced Annual Giving, Endowment and other Gift Income
9. More Profit Centers (School Store, Dining Room, Summer Schools etc)

There is a simple, starting exercise to determine each trustee's position with regard to these issues and priorities. Ask every trustee to rank each of the nine "sacred cows" as to whether they want to see more of it (a PLUS); about the same level (a ZERO); or less emphasis given to that area (a MINUS). Then add it all up to see if there is a sense of direction and agreement.

The key to achieving the school's goals and yet balancing the budget and controlling expenses,

especially in a time of economic downturn, is to know how to balance the "Sacred Cows." Schools can do this in a way that the board, faculty and administration all support, by appropriately educating these constituencies to ensure that they understand the underlying tradeoffs. To learn HOW to assess and then balance the "sacred cows", read further.

The income sources among the "Sacred Cows" are:

1. TUITION AND FEES
   Do the Board and Head want to be able to increase this area to generate more income? Does the Board want to keep tuition increases moderate right now, or is it important to raise tuition more aggressively? What will your constituency support? What is the justification for a tuition increase beyond the standard 2-5%? If the percentage increase in tuition must, in fact, be higher, more key questions follow.

   Has the School a strong need, such as competitive teachers' salaries, that will clearly motivate the parent body to dig deep into their pockets to pay more for attracting and retaining strong teachers?

   Has the School thought of creatively "packaging" tuition and fees? Many years ago a consultant urged schools not to "nickel and dime" the parents to death by charging fees for books, labs, lunch, and athletics. The goal was to "lump" all these into one, flat tuition.

   Experience has taught us that the schools that took this advice put themselves at a competitive disadvantage vis-à-vis their peer schools. Interviews and research have shown that parents focus primarily upon the "tuition" figure and perceive a higher number at the school where the fees are lumped in with tuition.

   Pricing strategy in the independent school world follows pricing strategy in the business world where a $10.00 item is priced at $9.99. While infuriating on one level, because we know intellectually that $9.99 is $10.00, on the recognition and emotive level, the item STILL costs $9.00 to us. The same is true with "unbundled" tuition and fees.

   Parents widely understand enrollment fees, building fees, renewal and replacement fees to cover the children's "depreciation" of the building.

   Should the parents who are new, and did not contribute to the capital campaign that just built the new lower school and science wing, be able to use the facilities without a "construction" fee? This fee is the equivalent of the average gift all other parents made in the capital campaign. New parents will, after all, have more long-term use of that building than current parents.

Thus, the general concept is to set your goal, determine what the school needs and then move forward. If "tuition", as a "sacred cow", should not be raised above 2-3% in your school culture, and you have analyzed and maximized fee income as well, you then move forward to address the other "sacred cows" to determine in what other areas you can gain income or control expense. That leads us to: TOTAL SCHOOL ENROLLMENT.

2. TOTAL SCHOOL ENROLLMENT
   Enrollment management is one way to generate income. The more students, the more flexible income, as certain fixed expenses remain constant. There is still only one head, one business office, etc. However, for some parents a fixed enrollment is a "sacred cow"; the school already feels "full" to them, and there is a sense of worry about becoming too big, losing that sense of "community."

   Actually, there is very little proof that size leads to a loss of sense of "community" if the UNITS within the school are small enough. Independent schools with high schools having over 400 students do seem to lose "community." A high school enrollment of up to 400, however, does seem to work. A high school of 400, a middle school of 300 and a lower school of 500 are common numbers among independent schools. That is 1200 students, if the market warrants it and the space allows for it.

   However, if this "sacred cow", which is a valuable income source, is viewed as untouchable, then we move on to the next source of income: GIVING.

3. GIVING OF ALL KINDS
   Annual giving, planned giving, capital giving, endowment giving are goals of most schools. The important question: Is the School willing to "prime the pump" and spend more to make more? Does the School have the necessary skills in the development office to increase dramatically the level of giving?

   Giving also comes from special events, which parents and alumni, grandparents and past parents may not see as "fund raising" but simply as good fun that they would provide for the family anyway. Many schools have auctions, gift fairs, outdoor events, and celebrations of all kinds which are aimed more at "friend raising" than fund raising. Nevertheless, these events can often bring in significant dollars.

   Most schools would place "giving" high on their list as a desirable "sacred cow." The key is: How to do this? How much money does the "pump priming" take? Most experts believe that within five years of establishing a development office, the total money raised each year from all sources of giving and events should be five times the total cost of the development office (including staff salaries).

If you lack skilled development office personnel or the funds necessary to generate more giving, then move on to PROFIT CENTERS.

4. PROFIT CENTERS
   A "profit center" is any school activity that generates more income than it costs. Very few schools have studied seriously the idea of profit centers. Many schools need these.

   They include bus operations, for example, and few schools realize that yes, running a bus system can and should make money. Food service can also generate a profit where there is a required lunch program and fee. This also allows for better control over food quality, quantity and a range of diets than "canteens" and vending machines.

   One school of 1000 students nets over $350,000 a year from the school store. This store sells books and supplies. However, it also sells "GAP" and "LIMITED" and other name brand clothing that also carry the school logo. The school buys at wholesale and sells at retail, at least a thirty percent mark up. These schools also sell everything that could be attractive to grandparents, and spectators turning up at athletic events where a cart full of school store supplies is wheeled out to the games.

   Other profit centers include: rental of the facilities; night classes for adults; and summer school camps and programs. One school rents signs out to corporations for a three-year period. The signs are in the gym and along the football and soccer fields. They are of uniform quality, color and size, and bear only the companies' names, no slogans. The signs are tastefully done, build good will with local corporations, and the income generated is over $50,000 a year. To "sell" this idea to area businesses, the School quantifies the number of spectators that would see these signs in each setting each year.

   If there are no opportunities for viable profit centers, or those existing cannot generate sufficient margins, then consider CLASS SIZE.

5. CLASS SIZE
   We think of all class sizes as "sacred." Somehow if the average class size is 16, and the faculty student ratio is 1 to 7, that is "sacred." For another school, it may be a maximum class size of 20. The reality is that we have very little evidence of the "break points" in class size where one number above the break point provides less effective instruction. There is little difference between 16 students and 18 students or even between 20 students and 22 students, in both research-proven delivery and results.

In fact, a class of 25 homogeneously grouped eighth grade students in advanced algebra might receive better instruction than 17 students of mixed abilities. So, class size is relative. Its importance is more in parental perception.

Would a school be willing to increase average class size from 18 to 20 or from 17 to 19, to achieve an extra 5 base points to faculty salaries?

Class size is a unique "sacred cow". It is BOTH a source of income as it grows, AND a source of expense, if a school is trying to reduce it. If class size is a "sacred cow" that is too sensitive to adjust, then move on to EXPENSES.

The "Sacred Cows" of expenses are as follows.

6. SALARIES
   Are faculty and staff salaries competitive enough right now? Or do they need to be raised significantly? What is the school's philosophy of compensation? Few schools have a philosophy of compensation, and one SHOULD BE in place.

   For example, one boarding school with limited resources recruits aggressively to attract bright young graduates from Ivy League schools. These young teachers coach three sports, advise, do dorm duty and teach three classes.

   After three to four years in the north woods boarding school, they are worn out and have little or no social life. Most leave. However, this school utilizes its scarce salary resources to identify those 4-6 teachers each year that it dearly wants to keep. It retains them by bumping the base salary $6,000-$10,000, cutting back on one coaching responsibility, and giving them a modest leadership role to enhance their sense of self-esteem. The latter gives them the ability to translate that leadership role into another major job at another school in a few years. This strategy tends to keep these key teachers.

   Schools need a SALARY SYSTEM that maximizes the effectiveness of the salary pool. What does the school wish to stress in rewarding its faculty? Quality of teaching? Workload? Attitude? Mentoring fellow teachers? Going the extra mile? Professional growth? Demonstrating leadership? Relationships with students? Relationships with parents?

   Whatever the school wishes to reinforce in its teachers, it needs to devise a salary system and a philosophy behind that system that enables the school to spend those salary dollars wisely.

   If salaries are a key "sacred cow", then reduce or press down on other areas and press forward on this one. If salaries are high enough now, and if there is a clear philosophy of compensation delivery, then move on to another "sacred cow."

7. PLANT

   Most schools do not want to defer maintenance. However, it may be necessary and may be the better of two evils if the choice is EITHER to lose good faculty (or not attract them in the first place) or to tax the physical plant for a few years. Neither picture is healthy in the long run. However, when facing economic stress and tough choices, schools need to have these discussions at the FULL board level and NOT JUST at the finance committee level. Trade offs of "sacred cows", such as salaries and capital expenditures, are crucial to effective policy formulation and ultimately crucial to the realization of the mission of the school.

   If physical plant cannot be ignored, then analyze PROGRAM.

8. PROGRAM

   The questions are simply: Do we have enough? Is technology becoming TOO high a priority? Are there other things on which we should focus such as the International Baccalaureate degree, foreign languages, the Library, the Arts? Science?

   The board should review the degree of the "richness" of its program currently, and with the guidance and full input of the head of school, determine if program is an area of expense reduction, increase or maintenance at the current level. If program is "untouchable", then move on to FINANCIAL AID.

9. FINANCIAL AID

   Has the school committed adequately to this area? NAIS has recommended 10% of the budget be set aside for need-based financial aid to help ensure that independent schools are not enclaves of the wealthy but have an appropriate degree of social, economic and racial diversity. Yet very few schools are at the full 10% level or more.

   The question for any budgeting process is: what are the school's values on this topic versus its resources currently? Can it discount seats, or is the school full? Are faculty utilizing too much of the financial aid (or tuition remission) resources?

SUMMARY

A board of trustees functions effectively as a true, policy-making entity when, together with the head and management team, it takes on the challenges of weighing the school's "sacred cows". This is not a purely financial analysis of how to maximize income sources and control expenses. When trustees engage in an in-depth dialogue with one another, raising the various questions posed above, it is behaving as a group appropriately holding the mission of the school in "trust".

The NINE SACRED COWS are a friend to those schools who know how to use the formula wisely and to understand the assessments behind it. To those who ignore these basic issues and trade offs, an opportunity has been missed.

(The "sacred cows" concept was first introduced by John Shank, Professor at the Amos Tuck School of Business Administration at Dartmouth, and an advisor to John Littleford on his book, "Faculty Salary Systems in Independent Schools", and a friend.)

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