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Alternative revenues:

Can institutions of higher education balance mission and financial goals?

EY

By Kasia Lundy and Haven Ladd
Parthenon-EY Education practice

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Introduction

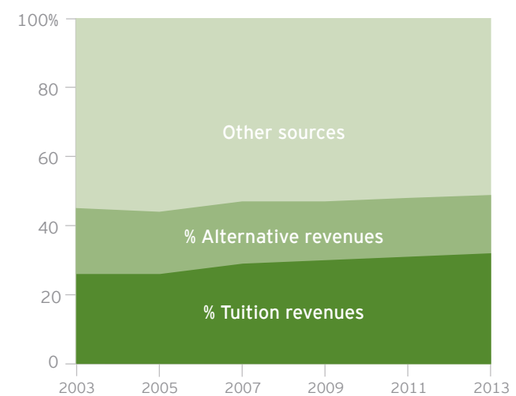
Alternative revenues that do not derive from degree program tuition, research or endowment returns are not a new concept. Higher education leaders have been interested in diversifying revenues for a long time. However, different segments of post-secondary institutions have approached this concept with varying levels of openness and enthusiasm. Liberal arts institutions, for instance, though more dependent on tuition revenue than larger universities are, have shown themselves to be more cautious about pursuing alternative sources of revenue than the broader set of private institutions. Some of this wariness stems from concerns that a focus on revenue growth creates a commercial mindset that may be at odds with the academic mission of the institution and may have an adverse effect on its brand and reputation.

Is there a path that institutions can pursue to grow alternative revenues without putting their reputations at risk? How can they productively engage key constituents in developing revenue growth strategies? How important is it to separate alternative revenue management from the rest of the institution? This brief offers some of our perspectives on these topics.

Tuition has been one of the most stable sources of revenue for institutions

When enrollment growth was steady, interest in growing other revenues was lower. In the post-recession landscape since 2009, however, much has changed. Enrollments have flattened or declined at many institutions and are projected to remain relatively flat over the next five years.[1] Increased public and policymaker attention to college affordability has led to increases in financial aid and has resulted in increasingly steeper tuition discounts. In fact, some institutions rely so heavily on discounting that when they raise tuition, they put their tuition revenues at risk.[2] Despite the flattening trend in overall net tuition revenue, tuition is still one of the most stable sources of revenue for institutions, as depicted in Figure 1. Dependence on tuition as a percentage of revenue has trended upward since 2003. Alternative revenues on the other hand have remained flat as a percentage of revenues.[3]

Figure 1: Traditional and alternative sources of revenue at higher education institutions (2003–2013)



Smaller institutions tend to be more tuition-dependent

As shown in Figure 2 (page 3), institutions benefit from multiple sources of revenue: tuition, gifts and grants (private gifts, public and private research grants), investment returns on their endowments, and income from sources such as Auxiliary, Independent, Educational Activities, and Other.[4] The smaller the institution, the more tuition-dependent it tends to be. While under a third of the revenue is tuition-generated for all four-year institutions in the U.S., this share jumps to 40% for smaller institutions (e.g., institutions classified as under 5,000 students and baccalaureate[5] institutions, which also tend to be small). Elite liberal arts institutions,[6] a small subset of private four-year baccalaureate entities, represent an interesting sub-segment, with somewhat different characteristics. Their recognizable and admired brand names have translated into larger endowments and lower dependence on tuition. They have also shown less interest in diversifying revenues the way other private institutions have. Only about 10% of their revenues come from alternative sources, compared with almost 20% at other small institutions or the broader universe of private institutions and universities.

Some institutions are bucking this trend

The broader higher education trends described earlier – intensified competition for students and constraints on increasing tuition revenue combined with high fixed costs of maintaining campus infrastructure – are affecting most institutions, including the elites, leading some to break away from the pack. Institutions such as Bryn Mawr, Dartmouth, Middlebury, Oberlin and Smith – to name a few – are

1 Parthenon-EY, *proprietary enrollment forecasting model.*

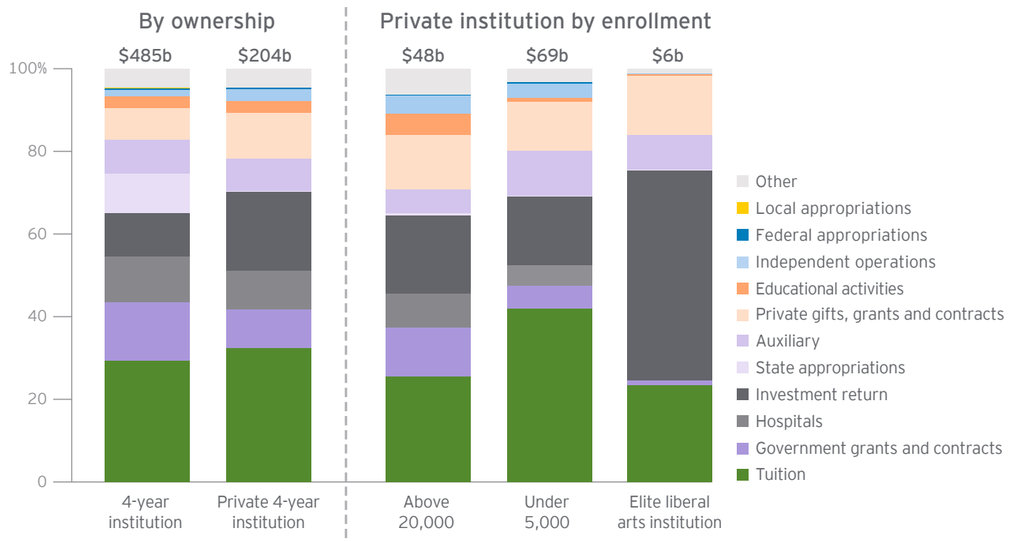
2 Moody's Investor Service Announcement, *"Annual tuition survey forecasts weakest college and university revenue growth in a decade,"* Nov. 17, 2014.

3 The Integrated Postsecondary Education Data System (IPEDS): *Data pull of higher education revenues*, 2003–2013. For the purposes of this analysis, alternative revenues are defined as the sum of Auxiliary, Independent, Educational Activities, and Other revenues (as classified in IPEDS).

pursuing revenue-generating opportunities outside the traditional full-time degree programs. These opportunities vary widely in terms of focus, but many have one theme in common – better utilization of campus space, especially in summer months:[7]

- Bryn Mawr College rents out its classrooms after academic hours to local organizations.
- Dartmouth College hosts undergraduate bridge programs in partnership with the Tuck School of Business and runs summer athletic day camps for youths.
- Middlebury College offers language program sessions throughout the year, including summer.
- Smith College offers subject-specific summer programs for women as part of a pre-college program.
- Many institutions rent out space in the summer to third-party providers such as iD Tech, which offers a variety of camps targeting kids and teens ages 6–18. Many of these camps are in STEM-related areas such as programming, game design and robotics.

Figure 2: Revenue breakdown by type of institution



	4-year institution	Private 4-year institution	Above 20,000	Under 5,000	Elite liberal arts institution
% Alternative	17%	18%	22%	19%	10%
Avg. enrollment	4,327	2,460	30,644	1,331	2,004

Five practical perspectives

Through direct work in this area, interviews with a range of institutions, and extensive secondary research, we offer the following practical perspectives for consideration by higher education leadership:

- Clearly **defining goals** for alternative revenue generation is a necessary first step
- Programs that **leverage the institution's core assets** tend to generate the most operating surplus
- There is no silver bullet; a **portfolio approach** is needed
- **Early wins** are critical in building ongoing engagement and support
- Revenue-generating ideas typically require **separate management** to be successful.

4 *Auxiliary revenue* includes revenue from enterprises that exist to furnish a service to students, faculty or staff (examples include residence halls, food services, student health services, intercollegiate athletics, college unions, college stores and movie theaters). *Independent revenue* includes all operating revenues associated with operations independent of the primary missions of the institution (generally, only revenue associated with major federally funded R&D centers). *Educational activities revenue* includes revenue from the sales of goods and services that are incidental to the conducting of instruction, research or public service (examples include film rentals, sales of scientific and literary publications, testing services, university presses, dairy products, machine shop products, data processing services, cosmetology services, and sales of handcrafts prepared in classes).

5 IPEDS: *The Carnegie classification of higher education institutions describes these as colleges that primarily award bachelor's degrees, and award fewer than 50 master's degrees and 20 doctoral degrees each year.*

6 All statistics for elite liberal arts institutions refer to the top 24 private liberal arts institutions, according to the *2015 U.S. News & World Report* rankings.

7 Secondary research (*institutional websites; press*)

Clearly **defining goals** for alternative revenue generation is a necessary first step

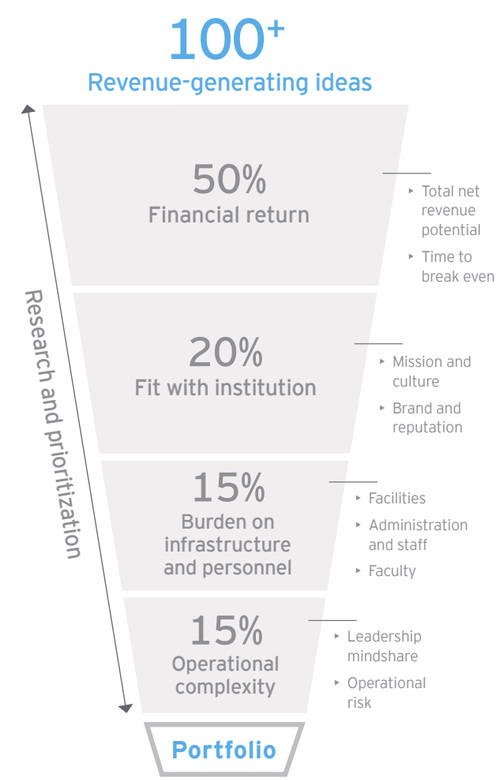
Is there internal agreement on the target annual net revenue from alternative sources and on the time frame to achieve this target? A goal of $20 million in additional net revenue over 5 years will yield a very different list of recommended programs than a goal of $5 million over 10 years. The $20 million goal will likely require a more aggressive portfolio and bigger, riskier bets.

Are there non-financial factors that should be considered? Certainly. Non-financial criteria – such as fit with the institution's mission and culture, potential impact on brand and reputation, potential burden on existing infrastructure and personnel, and operational complexity – will affect the ultimate prioritization of ideas. For example, certain types of student fees may run counter to an institution's equity policies – the blowback from putting in place these fees may outweigh any future financial returns.

> **Institutions should adopt a customer-centric approach when considering potential revenue-generating ideas.**

To maximize return on their most valuable assets (people and knowledge), institutions should start by identifying their core strengths, but they should resist letting those attributes be the sole driver. Doing so may pose the risk of developing a program for which there isn't a market. Instead, institutions can utilize a customer-centric approach to ensure that there is adequate demand for additional programming, which in turn will drive financial returns. The target customer segment doesn't need to be the largest segment. It just needs to be large enough to support a financially viable program. It is also important that the target customer is both willing and able to pay for the offering. Programs in which there is interest but low ability to pay may well be de-prioritized as part of the initial assessment. Figure 3 shows a hypothetical idea assessment framework, with illustrative weights assigned to key criteria. Rating each idea on these criteria requires a certain amount of analytical due diligence and qualitative deliberation.

Figure 3: Illustrative criteria and weights



The good news is that there is no shortage of alternative revenue ideas within institutions. This is not surprising as institutions have plenty of smart people with good ideas. Figure 4 shows one way to organize these concepts and illustrates just how diverse the ideas can be. What institutions do need is a process for evaluating and prioritizing these ideas, and a mechanism for engaging key constituents, both in idea generation and in winnowing. An outside facilitator can also help institutions move outside their comfort zones and give more serious consideration to bolder, sometimes more controversial ideas.

Figure 4: Revenue-generating idea examples

	Potential customers			
Revenue types	**Current students**	**Broader community**	**New populations**	**Sample revenue-generating ideas**
Post-secondary course offering (credit-bearing)	•			12-month vs. 9-month academic year
	•			Summer sessions for popular courses and major prerequisites
	•			Summer sessions for independent study
	•	•	•	Extension school programs: degrees and certificates
			•	High school students: dual enrollment programs (online/blended)
			•	High school students: pre-college (AP courses online)
			•	College grads: post-baccalaureate programs
Enrichment programs (not credit-bearing)	•	•		Academic travel programs
		•		Online enrichment classes
		•	•	Mid-career professionals: advancement programs
			•	Middle/high school: youth academic programs and summer camps
			•	College grads: undergraduate bridge programs
Facility utilization		•	•	Event hosting and partnerships with local hotels and conference organizations
		•	•	College-affiliated retirement communities
			•	Classroom, dorm and athletic facility rentals
			•	Off-peak parking space rentals
Products and services	•	•	•	Dining options on campus: fine dining, coffee shops
	•			Schedule-related fees: e.g., course drop, late registration
	•			Convenience services: e.g., laundry, textbook rental
	•			Retailer partnerships: e.g., Amazon, Barnes & Noble
		•		Parent orientation packages
		•	•	Memberships & subscriptions: e.g., athletic events, library database

Programs that **leverage the institution's core assets** tend to generate the most operating surplus

Institutional resources are constrained – there is only so much time people have in the day and only so much space on campus. And while space is less utilized in the summer months than during the academic year, demands on space can add up quickly. It behooves institutions to be analytically rigorous about space utilization – upon closer examination

> Institutions have important "assets" or resources at their disposal: people, knowledge and space.

of existing programs, they may discover significant variance in program net revenue or operating surplus, on a per-student, per-bed, per-square-foot or per-week basis (whichever metric the college chooses to adopt for comparability purposes). All other things equal (e.g., fit with the college's mission and culture), some programs may need to be "swapped out" with programs that bring in more net revenue per selected metric.

In our work, we have found that programs that leverage the institution's core assets (people and knowledge) generate more operating surplus than programs that solely leverage secondary assets such as space. Take, for example, summer programs that are operated and delivered by third-party providers on campuses – these tend to generate less net revenue on a per-seat basis than pre-college programs operated and taught by the institution, or post-baccalaureate programs that leverage specific academic strengths of the institution. Leveraging the institution's academic assets allows it to charge higher rates and retain all the revenue, which it can, in turn, reinvest to support its teaching, learning and research missions. Renting out space to third-party providers allows the institution to access only part of the program revenue.

Programs that leverage core assets

- **Middlebury Language Schools:** Middlebury is renowned for its language programs. What started as a modest program 100 years ago now counts 11 language programs that enroll 1,500 students each summer in courses that range from 2 weeks to 8 weeks. Longer courses range from $5k to $7k in tuition.
- **Bryn Mawr post-baccalaureate pre-med program:** Enrolls students in a year-long non-residential program. Students have a 98% school acceptance rate. Tuition is $26k; students receive access to loans but no other financial aid.
- **Pre-college programs such as Smith Summer Science and Engineering Program:** Four-week residential program for exceptional young women in grades 9–12 that reaches 100 girls each summer. Tuition is $5.5k.

Programs that primarily leverage space

- **iD Tech camps:** Summer day camps and overnight camps for kids 6–12 and teens 13-18. Computer camps and STEM camps. Also offers Alexa Café, an all-girls program for ages 10–15. Fees are $800–$900 per week. About 15% of the revenue per student comes back to the host campus.
- **Dartmouth summer athletic camps:** Run by Dartmouth assistant coaches. Fees of $200–$1,000 per student depending on sport. Dartmouth keeps a portion of the revenue.

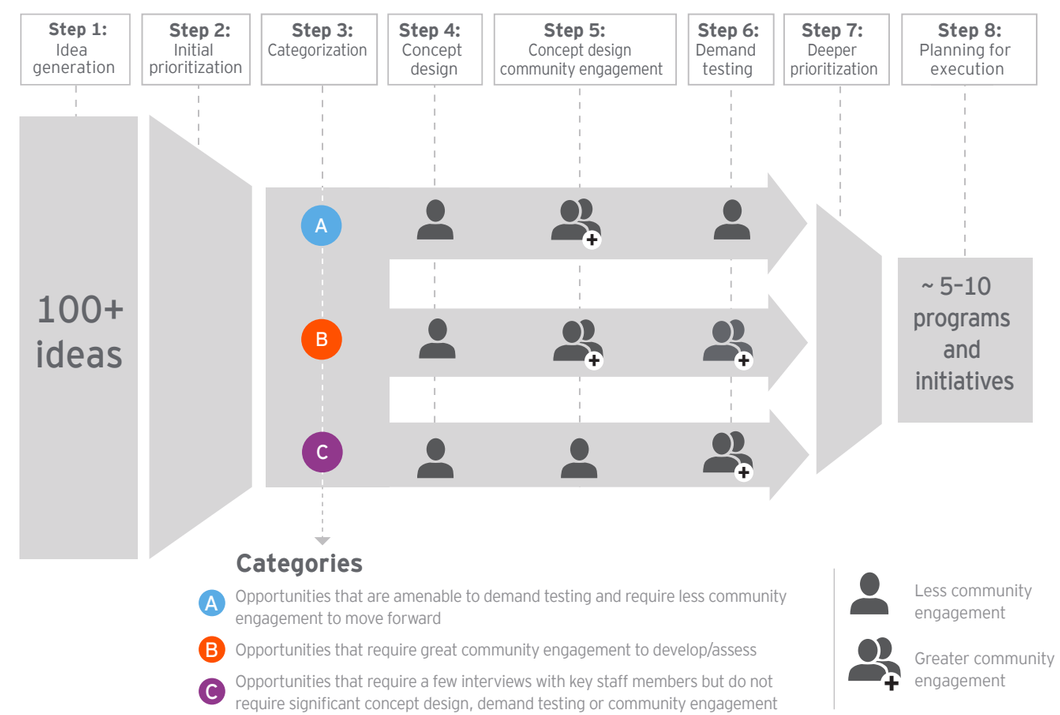
All things equal, it would seem that institutions should try to develop and operate their own programs, especially those that take advantage of the inherent academic strengths. However, there is a strong rationale for including third-party-operated programs in the revenue-generating portfolio, as described in the next point.

There is no silver bullet; a **portfolio approach** is needed

The quest for alternative revenues shows time and again that there is no single program or initiative that can help an institution meet all its financial goals. A portfolio approach is needed – a mix of larger and smaller programs, conservative and riskier initiatives, and new ideas as well as improvements to existing revenue-generating concepts. Figure 5 illustrates the journey to develop this portfolio.

Tolerance for risk drives the boldness of the overall portfolio. Institutions can hedge their bets by investing in a range of revenue-generating initiatives, from scaling up existing and proven concepts to investing in concepts that are new to the institution, and therefore represent a higher risk, both operationally and from a market positioning standpoint. One example of a bolder investment is the acquisition of the Monterey Institute of International Studies by Middlebury College (see Figure 6).

Figure 5: A portfolio of ideas is the most likely endpoint



Another example of a riskier venture that is arguably very different operationally than the core business of teaching and learning is the development of affiliated retirement communities, such as Kendal at Oberlin College (see Figure 6). This type of risk can be mitigated through partnership with a private developer and operator who typically provides the capital, develops and markets the community, and bears the risk. There are many other examples of college-affiliated retirement communities in the U.S., including the University of Alabama, University of Arizona, University of Central Arkansas, Cornell University, Dartmouth College, Denison University, Davidson College, Duke University, Indiana University, Ithaca College, University of Florida, Lasell College, University of Michigan, University of North Carolina, University of Notre Dame, Ohio Wesleyan University, Penn State and Purdue University.[8]

Figure 6: Examples of higher-risk investments

Middlebury Institute of International Studies at Monterey

When: Middlebury formally acquired the Institute in 2010, following a five-year affiliation with the school.

What: This program allows students and qualified alumni to earn both a bachelor's degree at Middlebury and a master's degree at the Institute in five years in five program areas. The Institute also offers certificates and short enrichment programs in policy, diplomacy and language.

Kendal at Oberlin: Retirement Community

What: A retirement community developed and operated by a third party – also affiliated with the University of Akron, Case Western Reserve University, Cleveland State University, Lorain County Community College, Bowling Green State University and Ohio State University.

Size: More than 300 residents; can audit Oberlin classes for free.

Fees: Entrance fees range from $90k to over $450k. Monthly fees range from $2k to $3k.

Early wins are critical in building ongoing engagement and support

Leadership's interest in diversifying revenues and growing alternative revenue is often perceived as overly "commercial" by stakeholders on campus. As such, it is sometimes received with skepticism and misgiving. Engaging key stakeholders (faculty, administrative leadership, board members, students and even alumni) in a well-designed process to identify and assess revenue-generating opportunities (e.g., through task forces, advisory groups and focus groups) can go a long way to addressing these concerns head-on and making these core groups feel like they are part of the solution. Appropriate engagement of key groups is an early win in and of itself.

This is also why a portfolio approach that allows for a sequenced rollout of revenue-generating initiatives is critical. Every portfolio will have one or two "big ideas" that will likely bring in the majority of additional revenue, while also having half a dozen or more "small" ideas. These play a different role in the portfolio but are also very important. They are typically extensions of existing concepts or new concepts that are less operationally complex and therefore easier to implement. Extensions of existing programs provide incremental surpluses since operations are already ongoing. They are easier to execute because they build on existing infrastructure; thus, they can generate net revenue sooner. Relatively small investments in these types of ideas will allow institutions to achieve early success. Once the revenue starts flowing in, it can be reinvested in core assets of the institution (people and knowledge). These early, tangible benefits are important for continued buy-in, support and momentum.

> "Appropriate engagement of key groups is an early win in and of itself."

8 "Best Guide Retirement Communities," *Best Guide Retirement Communities website,* http://www.bestguide-retirementcommunities.com/Collegelinkedretirementcommunities.html, Copyright © 2006-2015

"The Business of Campus Retirement Communities," *University Business website*, http://www.universitybusiness.com/article/business-campus-retirement-communities, December 2014

"Why boomers are retiring to college," *PBS NEWSHOUR website*, http://www.pbs.org/newshour/updates/why-boomers-are-retiring-to-college/ PBS.org, April 29, 2014

"Should you Retire to College?" *nextavenue website,* http://www.nextavenue.org/should-you-retire-college, February 4, 2014

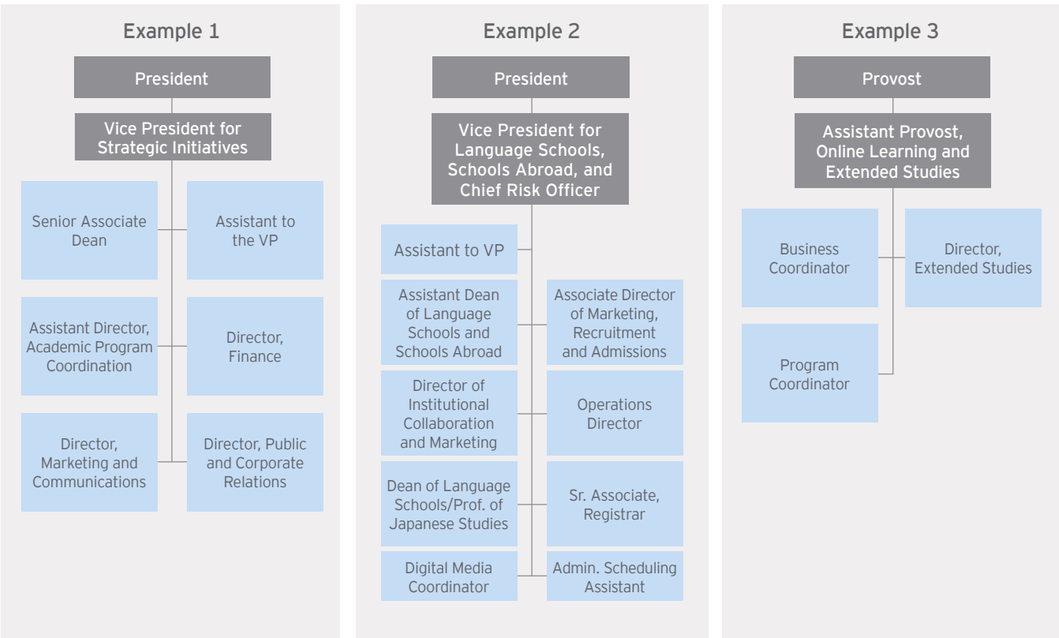
Revenue-generating ideas typically require **separate management** to be successful

Every institution has a slightly different context, so there is no "one size fits all" organizational recipe for how to manage revenue-generating programs. In our work, we have observed that institutions that are serious about growing the revenue potential of programs outside the core (degree program) tend to create separate structures outside of traditional academic lanes. This provides a higher level of autonomy as well as accountability for the team pursuing alternative revenues. In Example 1 of Figure 7, the new unit reports directly to the president and is responsible for myriad revenue-generating initiatives. In Example 2, one of the big ideas has become so big that it requires its own management; this unit also reports directly to the president. In Example 3, the additional structure has been created within the provost's office but still has separate oversight.

Perhaps even more important to ultimate success than reporting lines is the institution's willingness and ability to dedicate a team to these efforts. If the revenue-generating effort is undertaken as a marginal activity "on the corner of people's desks" and as part of a much broader set of responsibilities, it is almost surely doomed to fail. Success requires a laser-like focus on the goals and activities to achieve these goals, which in turn requires dedicated resources. The dedicated team needs to make revenue growth a priority while working collaboratively with the rest of the institution.

With the right leadership in place, this team has the potential to put healthy pressure on the rest of the institution to evolve its business model. It will innovate, take ideas to market, refine programs, set metrics and track outcomes, and decide where to accelerate projects vs. where to pull back. All with the goal of creating a sustainable stream of revenues for the institution, which will contribute to its core operations while preserving its reputation.

Figure 7: Potential reporting structures



Conclusion

Higher education institutions have built their reputations over decades, sometimes centuries. Many of them have strong brand names that have kept enrollments steady, even during the recent period of flat enrollment and financial pressures. They are in a position to leverage these strong and lasting brands to diversify their revenue streams. This can help reduce reliance on tuition revenue, and if done thoughtfully – through a process that allows for intentional engagement of key stakeholders and incorporates a rigorous approach to analyzing markets, customers, institutional strengths and capacity constraints – the institution will be able to keep its reputation intact and potentially enhance its reach and impact. It may also allow the school to improve its financial situation and ongoing sustainability of operations.

Diversification of revenues is both necessary and attainable, and Parthenon-EY can assist institutions in establishing a structured approach to achieve this goal.

Authors

Kasia Lundy
Managing Director
+1 617 478 6328
Kasia.Lundy@parthenon.ey.com

Haven Ladd
Managing Director
+1 617 478 7055
Haven.Ladd@parthenon.ey.com

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