

# Slouching Toward PRIVATIZATION

No American college or university is an island. A shift toward strategic partnerships and alliances now appears inevitable.

BY ROBERT C. DICKESON AND DAVID J. FIGULI

## TAKEAWAYS

- 1** Tuition-dependent private institutions and taxpayer-dependent public institutions are seeking new revenue streams and ways to cut costs.
- 2** Tactical and strategic alliances have become essential and commonly accepted business practices.
- 3** Charged with institutional stewardship, boards will need to determine which financial strategies are appropriate in advancing the mission of the college or university.

THE PAST TWO DECADES HAVE SEEN A significant shift in the financial model of American higher education, laying groundwork for a transformation that could reshape our understanding of the academy. The shift—toward increasing degrees of privatization—is unmistakable and has affected every American college and university to varying extents.

Reasons for this surge toward privatization probably vary by institution, but certain patterns of institutional behavior can be attributed to one or more of the following forces:

- Except for a handful of elite institutions with sizable endowments, the traditional model of higher education finance no longer seems to be working well. The majority of independent colleges suffer from excessive tuition discounting brought about by the competition for a declining base of full-tuition-paying, academically capable students. These institutions are fighting the iron laws of

demographics—and losing. More and more public institutions are operating with fewer public dollars. The University of Colorado, for example, now receives less than 10 percent of its revenues from state funds. These fiscal realities are forcing governing boards to seek alternatives.

- All institutions are under increasing pressure to cut costs. Tuition increases have outpaced all relevant consumer price indices as well as families' ability to pay. Because the revenue side of the ledger is thus constrained, the expense side is in jeopardy. This has forced many campuses to cut or reprioritize academic programs

and services, shift from a full-time to a part-time faculty, and reduce the proportion of faculty eligible for tenure.

- Board members who come from the corporate sector transplant business ideas to their higher education responsibilities. Concepts such as outsourcing and tactical or strategic alliances are routine in the business world, and such concepts are being grafted onto the collegiate tree. There appears to be no insuperable ideological barrier to adapting market-savvy business practices.

- National bond-rating services, such as Moody's and Standard and Poor's, provide external reality checks on institutional finances. There is a direct relationship between an institution's rating and its degree of tuition discounting. Bond-rating advice on cash flow and warning signs on expenses have had a significant effect on the governing board's sense of institutional efficacy.

- Traditional notions of "public" and "private" have become blurred in many sectors of our nation's economy. Indeed, some private colleges and universities actually receive proportionately higher public support than some public institutions. Most colleges and universities, regardless of sector, are searching for new sources of revenue-generating activities, and entrepreneurial leaders are in higher demand than ever.

- Academic content no longer is the sole province of the academy. Thanks to extraordinary advances in technology, some of the very best content is free. When MIT places its curriculum online, available to the world, higher education institutions must justify their value in other terms.

- In the global economy, the United States must rely on its two greatest strengths: intellectual power and capital supremacy. The irresistible movement toward privatization is recognition among colleges and universities that fusing these strengths is essential.

**Five Variations.** Privatization can be defined as the transfer of responsibility or service delivery to another sector or entity. A snapshot taken today of higher education finance would find all institutions arrayed along what might be called a privatization continuum. Although each institution currently can find its unique position fixed within such a continuum, most have seen their position change over the past 20 years, and the future is likely to bring even greater privatization.

Our privatization continuum could be constructed with five major elements, each of which is discussed on the following pages.

1. *Operating as fully self-contained.* On this end of the continuum, an institution controls all of its operations, academic and non-academic. Fiercely independent, the institution does not rely on outside sources for its portfolio of academic content, its delivery, or its systems. Fifty years ago, all institutions more or less lived by this model

of vertical integration. Today, it is hard to imagine a single institution that embraces it.

2. *Outsourcing non-mission-critical functions.* All higher education institutions now outsource certain functions that traditionally were conducted in-house. The most commonly cited reasons for outsourcing include reducing costs, ensuring accountable results, upgrading program quality, increasing customer satisfaction, and gaining access to special expertise.

These non-mission-critical functions may include admissions management, bookstores, campus security, conference management, continuing education centers, counseling, testing and psychiatric services, custodial and housekeeping, day care, dining and food services, facilities management, human resources, payroll and benefits administration, legal services, motor pool operations, physical plant maintenance, printing and publishing services, remedial education, financial-aid administration, housing, computing, and health services.

The growth of the breadth and depth of outsourcing has been a quiet but demonstrable evolution across all types of institutions, and that growth is likely to continue.

3. *Tactical alliances.* Across the landscape of higher education institutions, we can point to a large and growing number of tactical alliances. Through state, regional, and associational relationships, institutions have aggregated for the purposes of joint purchasing, cost reductions, and achieving more efficient business operations.

In the independent sector, the Michigan Colleges Foundation serves as an example. Originally conceived as a fund-raising organization, the foundation now has developed collaborative projects among its 14 member institutions in faculty development, business process redesign, sharing instructional staff, teacher preparation, and joint degree offerings with the University of Michigan.

An example of public sector collaboration can be seen in the Oklahoma State Regents for Higher Education initiatives to secure cost savings through statewide economies of scale. Through leveraging of resources, advances have been made in providing member institutions with legal counsel, record keeping, technology, and student information. A new initiative is under way to provide "substitution in academic program delivery."

Nationally, the Coalition for College Cost Savings, a group of 12 member organizations that serves 335 private colleges, is collaborating on group purchasing, information sharing, and negotiations for goods and services that are unavailable to single institutions.

What distinguishes tactical alliances is that the institution maintains control of its mission and uses the alliance to help it manage resources more efficiently.

4. *Strategic alliances.* Broader in scope than tactical alliances, the growing and promising opportunity for

strategic alliances enables an institution to add value, secure needed capital, expand markets, leverage networks, and gain access to physical facilities.

Strategic alliances may take several forms: merger-like arrangements with other institutions, joint offerings with dissimilar but complementary institutions, association with other nonprofit entities, or association with for-profit entities.

A successful example is Regis University in Denver. In 2003, it formed a for-profit joint venture corporation with the Ana G. Mendez University System in Puerto Rico to manage a newly formed campus in Orlando, Fla. The venture combined the programmatic and distance-delivery expertise of Regis with the bilingual instruction and Hispanic-market brand identity of Ana G. Mendez to offer an array of degree programs taught in a bilingual format.

Another good model is the marketing and program-delivery affiliation that many institutions have formed with the University Alliance. This Florida-based for-profit company employs its marketing resources and capabilities as well as its expertise in online program development and delivery to bring specialized degree programs to the global learner marketplace.

Several other initiatives have been launched with the objective of sharing online program content and marketing capabilities to bridge the growing disparity of available capital between small colleges and universities and highly capitalized mega-universities. A successful example is the Online Consortium of Independent Colleges and Universities, a nonprofit alliance of 63 small-to-medium institutions. Schools in this alliance share content and a common online platform with the for-profit electronic learning providers E-college and Blackboard.

Increasingly, public and private colleges and universities are being approached by venture capitalists eager to apply financial and business management resources to a targeted educational enterprise. While some of these entreaties are nothing more than bald plays of “cash for accreditation,” many others propose a thoughtful marriage of capabilities to serve niche markets or address capital-intensive opportunities.

What distinguishes strategic alliances is that the institution establishes with a partner a shared commitment to the pursuit of its mission and uses the partner’s capabilities to strengthen the institution’s ability to accomplish that mission.

*5. Operating as fully privatized.* Perhaps no single recent phenomenon has altered the American higher education scene as has the growth and development of for-profit higher education companies. Sensing unmet market demand, an array of for-profit institutions and holding companies have developed multiple campuses, delivered course and degree programs in high-demand areas, achieved customer expectations—and earned a

profit. The eight largest publicly traded higher education companies employ nearly 60,000 full-time and part-time faculty members and serve more than a billion learners worldwide. Some are among the largest higher education institutions in the United States.

While traditional institutions decry what they call a lack of “quality” at for-profit colleges, the evidence is actually mixed. One for-profit, Acton School of Business, has been identified as having one of the most academically competitive M.B.A. programs in the country. With a commitment to market-driven excellence, these companies often outspend their nonprofit competitors in every strategic category, including program development, student service, instructional salaries, and most assuredly, student recruitment.

Successful for-profit institutions follow a simple but effective marketing strategy: Find out what people want and give it to them. Unhampered by such guild-centric practices that hold back traditional institutions, today’s for-profits may be shaping the way higher education takes place in the future.

The five-element continuum described here can’t capture all the real-world complexities and combined approaches of individual institutions. But every college and university in the United States has moved along the privatization continuum to some extent, some more rapidly than others. This is not to say that all institutions will eventually arrive at the same end point; it is to say that the tendency and the direction seem irreversible.

Perhaps the most important function of a governing board is to superintend the destiny of its institution. Given the admixture of forces confronting boards, it is no wonder that new financial models are needed. ■

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**T’SHIP LINKS:** “When Competition Turns to Collaboration,” by John R. Shaddock, May/June 2007. “In Troubled Waters, Steady as She Goes,” by Leo I. Higdon, March/April 2006. “The Temptations and Realities of Outsourcing,” by Richard D. Wertz, September/October 2005.

# Questions for Boards

The growth of the breadth and depth of outsourcing has been a quiet but demonstrable evolution across all types of institutions, and that growth is likely to continue.

- What are our institution's areas of strength?
- How do these areas of perceived strength compare in quality with those of our competitive peers or those that aspire to compete with our institution?
- What would it take to leverage our strengths into a competitive market position?
- What opportunities for new market-savvy initiatives currently exist in our institutional portfolio?
- What resources do we need that we now lack to avail ourselves of these opportunities?
- How could a strategic alliance or new capital partners and sponsors solve our resource needs?
- What changes do we need to make in our institutional culture to engage these partners and sponsors in a meaningful commitment?