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MOVING TO A RESPONSIBILITY- CENTERED BUDGET MODEL

PRINCIPLES OF
RESPONSIBILITY-CENTER
MANAGEMENT

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LEARNING OUTCOME

After participating...

...you will be able to assess if your institution is prepared to move to a responsibility-center budget model.

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SESSION AGENDA

- Responsibility-Center Management 101
- Assessing if RCM is a good fit for your institution
- Assessing if your institution is ready to begin developing an RCM model

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POLL

What is the dominant characteristic of your current approach to budgeting?

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RESPONSIBILITY-CENTER MANAGEMENT 101

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■ TERMINOLOGY

- Responsibility-center management
- Responsibility-center budgeting
- Activity-based budgeting
- Revenue responsibility budgeting
- Cost center budgeting
- Profit center budgeting
- Incentive budgeting

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DEFINITION

RESPONSIBILITY-CENTER BUDGETING

- Classifies individuals programs and units as either revenue or cost centers (or blended units)
- Revenue centers control the revenues they generate and are responsible for financing both their direct and indirect costs and are subject to taxes
- Cost centers are funded from central revenues and the taxes assessed on revenue centers

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CAVEAT

- No pure RCM models
 - Numerous hybrid models based primarily on RCM principles
- RCM-based hybrids are often used in combination with other models such as formula, performance-based, incremental, etc.
- Despite this reality, my discussion assumes RCM applies to all resource decisions

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WHY PURSUE RCM?

- RCM focuses attention on revenue
 - In particular, RCM establishes appropriate incentives for engaging in activities that lead to increased revenue
- RCM supports and facilitates responsible pursuit of entrepreneurial activities
- And it facilitates cost-benefit analyses and trade-off studies

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WHY PURSUE RCM?

- RCM encourages delivery of effective, competitive administrative services
- RCM focuses appropriate attention on cost control, price restraint, and educational outcomes
- Finally, RCM emphasizes revenue optimization as opposed to counterproductive internal competition

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■ PRINCIPLES

- Mechanisms for increasing available resources are preferable to those focused on merely dividing existing resources
- Outcomes measures are preferable to input controls
- Outcomes-based academic performance criteria are essential to the achievement of academic excellence

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■ PRINCIPLES

- Best decisions occur when decision maker is close to and has access to relevant information
- Level of decentralization must be proportional to organizational size/complexity
- Responsibility and authority should be aligned

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PRINCIPLES

- Accountability—rewards and sanctions—are required to achieve excellence
- All units throughout the institution must rely on common information systems providing timely and accurate data
- Transparency with clarity is critical

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PRINCIPLES

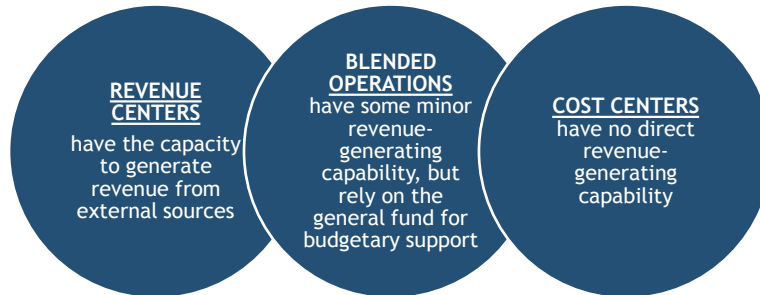
- Central administration must retain sufficient control to ensure achievement of institutional goals
- Stable financial environments facilitate good planning
 - Good planning contributes to stable financial environments

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RCM STRUCTURE

ACTIVITIES WITHIN THE INSTITUTION ARE
DIVIDED INTO THREE MAJOR CATEGORIES



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REVENUE TREATMENT

- Revenue ownership
 - Revenue centers own the revenues they generate
 - General revenues—unrestricted appropriations, investment income, unrestricted gifts and endowment income—are owned by central administration
 - Revenues generated by blended units are subject to varying treatment

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EXPENSE TREATMENT

- Revenue centers are responsible for covering all expenses
 - Direct
 - Indirect
- Revenue centers purchase services from cost centers, helping to underwrite the cost centers' operations

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EXPENSE TREATMENT

- A major charge incurred by revenue centers (and some blended units) is a tax on their unrestricted revenues, which must be paid to central administration
 - Some cost centers may generate small amounts of revenue that would be outside the scope of RCM

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EXPENSE TREATMENT

- Cost centers are financed in the same manner as they would be in any other resource allocation model
 - With the exception of some blended units, their entire budget represents a subsidy from central administration

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TAXES AND SUBVENTION

- As mentioned earlier, revenue centers pay taxes on unrestricted revenues
 - Taxes are used, along with general revenues, to achieve institutional objectives
 - Subsidize cost centers
 - Redistribute wealth through subvention
 - Fund institutional priorities in accordance with established plans

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**HOW DOES
RCM
BUDGETING
OPERATE?**

1. Charge all units to prepare and submit operational plans in support of the institution's strategic plan, infrastructural plans, and unit priorities
2. Based on approved operational plans, project the full budget for future year(s)
3. Estimate preliminary budgets for cost centers based on anticipated resources and required quality /volume of services

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**HOW DOES
RCM
BUDGETING
OPERATE?**

4. Project allocation of indirect costs to revenue centers based on preliminary budgets and historical usage data
5. Project tuition revenues and financial aid
6. Set tax rate in support of plans (influenced by degree of restriction on appropriations and other sources)...

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**HOW DOES
RCM
BUDGETING
OPERATE?**

7. Project utilization of central resources, including RCM taxes
 - Amount needed to fund cost centers
 - Amount available for subvention
 - Amount intended to support achievement of institutional priorities
8. Charge all centers to develop balanced budgets
 - Spending from unit reserves may be approved...

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**HOW DOES
RCM
BUDGETING
OPERATE?**

9. Conduct a structured review / feedback process of preliminary results, including deviations from guidelines
10. Rebalance the whole by vetting / refining revenue and cost centers' proposed budgets

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QUESTIONS

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ASSESSING IF RCM IS A GOOD FIT FOR YOUR INSTITUTION

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**What or who is the driving force related to the interest in RCM?
(Select all that apply.)**

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■ ORGANIZATIONAL MANAGEMENT PHILOSOPHY

- Basic principles of RCM require a decentralized management approach
- If the institution is wedded to a highly centralized management structure, RCM likely will not succeed
- Decentralized responsibility and authority must be aligned under RCM
 - Central oversight will still be required, but RCM operates with much more delegated authority than other models

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ANALYTICAL CAPABILITY

- RCM requires a significant overhead investment
 - Initially to develop the model and determine its specific characteristics
 - Thereafter to manage it and respond to changed circumstances
- If the institution isn't willing or able to make the required investment, RCM will not be successful

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SIZE MATTERS

- RCM operates best when implemented at the school / college level within a university
 - Most community colleges operate in a relatively centralized manner
 - If a community college wants to pursue RCM, it probably would have to be done at the division level

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■ SIZE MATTERS

- Three revenue centers is the minimum number to make it meaningful, and four or more is much better—though some smaller universities are attempting RCM
- If an institution has fewer than three revenue centers—that is, schools or colleges—it might consider implementing at the department level—though with some risk...

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■ SIZE MATTERS

- This is challenging because it's hard enough to find deans with the requisite skills
 - It might be impossible to find a sufficient number of department heads with the knowledge, skills, and entrepreneurial interest

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■ ASSESSING THE CURRENT CLIMATE

- Is there capacity to grow enrollment?
- Do you have flexibility with respect to tuition pricing?
 - Is there justification for differential tuition?
- How strong are your deans—especially in terms of financial capability?
- Do the schools and colleges have in-house finance professionals?...

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■ ASSESSING THE CURRENT CLIMATE

- How strong is the senior leadership?
- How would you characterize the level of trust between the administration and the faculty?
- How transparent is the current approach to resource allocation?
- Is your administration prepared to involve faculty and others in the development of the RCM model?...

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■ ASSESSING THE CURRENT CLIMATE

- What's the relative strength of the staff in the budget office?
 - Do they have the expertise to support the analysis required to design and implement the RCM model?
 - If not, are you prepared to invest funds to obtain consulting assistance?
- Are you prepared to visit other institutions to gain from their experience?

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■ ASSESSING THE CURRENT CLIMATE

- If you're at a public institution, how much of the operating appropriation is restricted to specific purposes?
 - Is any portion of the operating appropriation driven by enrollment within specific schools or colleges?

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IN SUMMARY

GOOD FIT

- Large, decentralized campus structure
- Differentiated tuition
- Budget-savvy deans and administration
- High level of trust and transparency across campus

QUESTIONABLE FIT

- Small, centrally-managed institution or community college
- Limited staff to execute change
- Highly restricted operating appropriations
- Lack of expansion capability

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QUESTIONS

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ASSESSING IF YOUR INSTITUTION IS READY TO BEGIN DEVELOPING AN RCM MODEL

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POLL

**Indicate the level of commitment
to RCM at your institution.**

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KEY READINESS QUESTIONS

- Is the senior leadership committed to RCM?
- Is there a credible individual with sufficient visibility to serve as champion for the effort?
- How likely is it that you can attract high-quality individuals to serve on a broadly representative task force reflective of the campus' diversity?

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KEY READINESS QUESTIONS

- Will you be able to identify co-champions from within the task force?
- What other major initiatives are currently underway?
- What's the recent track record with respect to major campus initiatives requiring broad-based buy-in?

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KEY READINESS QUESTIONS

- How will the informal leaders respond to a new resource allocation model?
- Does the culture support a transparent approach to developing an RCM model?
- Do you have the capacity to establish appropriate communication protocols to keep the campus informed of the effort?

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RESOURCE

Responsibility Center Budgeting by Edward L. Whalen

This book is an in-depth description of Indiana University's development of RCM. It covers the key approaches and includes an appendix covering their complex approach to allocating overhead using a simultaneous equation.

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RESOURCE

Responsibility Center Management by John R. Curry, Andrew L. Laws, and Jon C. Strauss and

This 2013 NACUBO book details the key elements of RCM and reviews the experience of nine large public and private institutions. It's particularly helpful because it discusses the benefits and challenges related to RCM.

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QUESTIONS

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EVALUATION

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Your comments will help us continually improve the
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