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Aligning Budget Models with Strategic Priorities

Increasing the Size, Stability, and Focus of Central Strategic Investment Funds

PART

6



- 1 The price tags of urgent strategic priorities are growing, as colleges and universities strive to differentiate and meet new student expectations in the post-pandemic “next normal.” Because it’s becoming harder to increase tuition revenue in a flat enrollment environment, and more expensive to borrow with interest rates set to rise, many institutions are holding budget model workshops, looking for redesign opportunities that generate funds for strategic investment from within

- 2 Three kinds of budget model design decisions merit strategy team attention, because of their potential to increase the size, stability, and focus of strategic investment funds:
 1. **Migrating to a higher strategic tax rate:** For most institutions using hybrid or Responsibility Centered Management (RCM) budget models, a “tax” of between 3-5% on funds allocated to units is a reasonable target. If your institution is not at that rate already, the strategy team and Chief Business Officer (CBO) should develop a migration path that secures academic unit buy-in, through phased increases until the target rate is reached, and creation of earmarked funding pools for faculty priorities closely aligned with institutional strategic goals

 2. **Growing fungible investment funds:** Most institutions are aware of concepts like budget surplus gainsharing, vacant position control, and auxiliary service monetization, but have not implemented them on a large scale. Yet, success stories in higher education show that, when implemented creatively, these measures can generate tens of millions in fungible strategic funds, not just one-time, but on a recurring basis. While not every measure is right for all institutions, their potential is too big for strategy teams not to consider anew when trying to build the war chest for big initiatives.

 3. **Developing consistent strategic seed fund formulas:** strategy teams should replace *ad hoc*, staggered consideration of proposals with a common business case template, to signal strategic priorities, improve the quality of academic planning, and surface opportunities for combining related proposals to achieve scale.

The Need for Central Funds and Coordination

Strategy Success Depends on Reliable Resource Reallocation

As Working Groups Develop Strategic Initiative Proposals, Strategy Teams Should Revisit the Strategic Budget Model

Among the most important analyses produced by strategic initiative working groups (the cross-functional teams responsible for fleshing out strategic priorities into detailed project plans) are multiyear financial forecasts, laying out each initiative's year-over-year revenue and cost estimates. These are the price tags for a differentiated value proposition and improving from as-is to target-state performance over 5-10 years, that the strategy team, finance team, and deans review, negotiate, and ultimately approve.

While strategic initiative working groups are developing these estimates, the strategy team should work in parallel on the equally important job of refining the strategic budget model, so that great ideas for strategic initiatives aren't unduly constrained for want of investable funds, or overly dependent on uncertain fundraising and tuition growth.

For Most, Strategic Investment Reserves Need to Be Larger and More Centralized for Post-Pandemic Competitiveness

In EAB's conversations with partner CBOs, many tell a similar story about what happened to their budget models over the last years, as higher education plunged into COVID shutdowns, and now emerges into the next normal.

Shutdown Phase: Taken by Surprise

- Pandemic closures take all by surprise
- No visibility about extent of operational and revenue disruption

Remote Operations Phase: Bracing for the Worst, but Not as Bad as Feared

- Budgetary "martial law" declared – spending decisions temporarily centralized and allocation formulas suspended
- Strategic reserves drawn down to cover remote delivery and health/safety costs, and subvent unit shortfalls
- Thanks to nimble internal adaptations and external one-time funds, the pandemic's financial impact proved a survivable event; bad, not worst-case

Reopening and Beyond: Adjusting the Budget Model to Grow and Stabilize Strategic Funds

- Most institutions are "re-decentralizing" budgets, but a click or two more centralized on the RCM spectrum than before
- The rationale isn't just to restore depleted subvention reserves, but because the post-pandemic competitive environment requires bigger central strategic bets

New Urgency for Larger, More Stable Investment

Student Expectations Cost More than Discretionary Budgets Allow

Looking Ahead, Strategic Funds Will Be Less about Discretionary One-Offs, More about Campus-Wide Product and Service Transformation

Historically, at most institutions, strategic investment funds were fairly or unfairly perceived by faculty to serve projects favored by the president, provost, and deans of prominent colleges. There was great leeway about scope and timing – initiatives could be adjusted larger or smaller, sooner or later, and ad hoc funding approaches usually sufficed.

Post-pandemic, the desire to fund worthy one-off projects still exists. What's different is that, in addition, there are significant new student and staff demands for flexible delivery, wraparound wellness services, and equity and inclusion that are far less-discretionary: schools need to implement them broadly, quickly, and at a high standard, or risk losing competitive positioning.

This is why so many institutions are using reactivation of dormant budget models as an occasion to realign their approaches for developing well-resourced, centrally controlled strategic investment funds.

Why Institutions Need Bigger, Stable Strategic Investment Funds Post-Pandemic

Pre-Pandemic

Some central investments seen as "pet projects" important to president or provost



Post-Pandemic

New student service expectations and differentiation pressures require investments touching every corner of campus

Flexibility about timing and scope



Initiatives must be implemented broadly, quickly, and at high standard

Funding came from tuition growth, targeted advancement and *ad hoc* budget manipulation



Can't count on funding from "new" revenues alone; budget model must create investable funds internally

Best Practices in Growing Central Strategic Funds

Overview of EAB Research

Three Budget Model Design Decisions Can Enhance the Size, Stability, and Focus of Central Strategic Investment Funds

EAB has done extensive best practice research on college and university [budget design best practices](#). From that work, three essential model design decisions stand out as opportunities to “automate” the size and stability of strategic reserves, while creating incentives to improve the alignment and planning rigor of unit proposals. Not every practice is right for every institution – there are cultural, financial and in some cases regulatory issues involved – but any strategy team with a budget model makeover already under consideration, or searching for ways to pay for new strategic imperatives can benefit from workshopping these ideas:

- 1 Migrating to a Higher Strategic Tax Rate**
- 2 Growing Fungible Investment Funds**
- 3 Developing Consistent Strategic Seed Fund Formulas**

Migrating to a Higher Strategic Tax Rate

- ▶ **EAB Guidance:** Set strategic fund “tax” of 3-5%, with phased migration path and well-publicized earmarks for popular faculty priorities

Most colleges and universities use a hybrid budget model, combining features of centralized incremental budgeting, and decentralized Responsibility Center Management (RCM.) Those closer to the RCM end of the spectrum value the ability to expose frontline academic units to financial realities, and shift resources to growth opportunities. The downside is that aggressive RCM yields few resources for central strategic investment, at times encouraging units to focus on short-term items misaligned with long-term institutional priorities.

Even before the pandemic, CBOs were concerned that secular pressures on tuition growth—the usual source of strategic investment dollars—might leave the institution unable to fund important cross-campus initiatives. Now, as institutions reckon with the nature and costs of revised priorities, they’re revisiting a core budget model feature: the size of the “tax” on allocated revenues reserved by the center to feed the strategic investment fund.

EAB’s guidance, based on hundreds of partner research interviews, is to create a central tax of 3-5% on all revenue to fund strategic reserves. The rightsizing of the tax matters more than whether it’s set aside pre-allocation or collected back after allocation—the main objective is ensuring that the end amount collected is big enough to cover must-do strategic initiatives.

Garnering Support for Growing Central Share

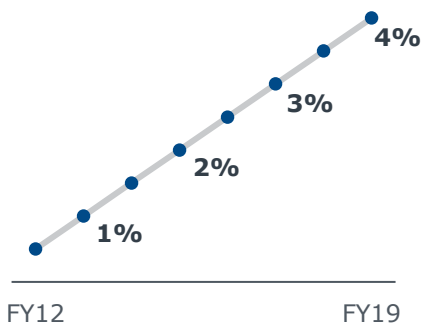
Gradual Deployment and Faculty Priorities Key to Success

Setting the tax rate is relatively straightforward; winning academic leader buy-in can be more complicated. Two provenly effective approaches for making strategy fund withhold increases more acceptable are:

Gradually Increase the Central Reserve Tax Rate over Time: Many institutions raise the reserve tax rate by 0.5% points per year until the desired steady-state rate is reached, allowing units time to adjust.

Earmark Portions of the Central Fund for Popular Faculty Priorities: Channel some of the new central reserves into earmarked pools dedicated to institutional priorities with broad faculty support (e.g., faculty retention efforts, new academic program seed funds). Faculty are more likely to endorse the strategic fund if the credible possibility exists that a compelling unit proposals, if strongly aligned, might yield funding that more-than-recoups the unit's tax contribution.

Incrementing Up Tax Rate Over Several Years



- Provost Fund financed through tax on traditional undergraduate net tuition
- In FY14, tax generated \$3M
- In FY19, tax generated \$9M

Earmarking Portion of Strategic Funds for Faculty Priorities



Faculty Equity Fund

\$1M of central dollars earmarked for a **Faculty Equity Fund**, used to help the institution become nationally competitive in the marketplace and improve faculty retention



New Academic Program Fund

Approximately 20% of central dollars are earmarked for an **Academic Program Fund**, used to develop new academic programs at the university



Growing Fungible Investment Funds

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Growing Fungible Investment Funds

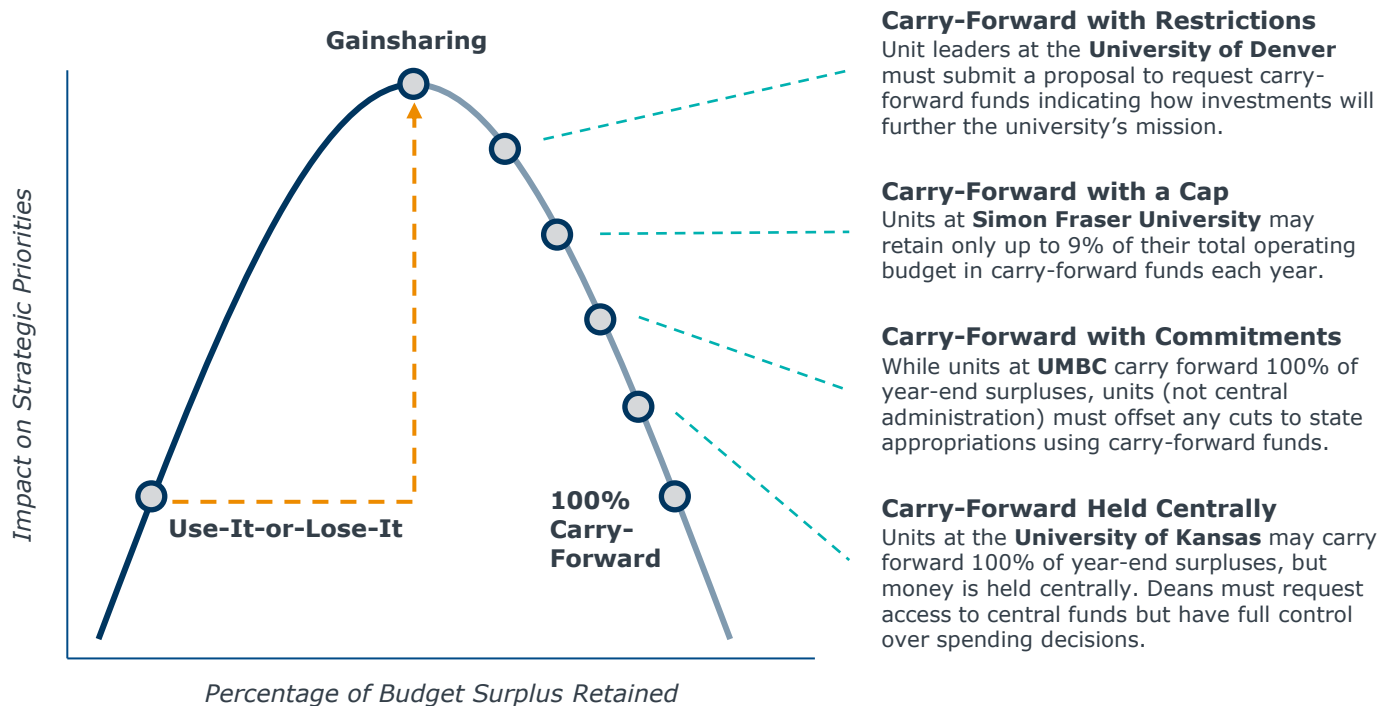
► **EAB Guidance:** Consider Gainsharing, Vacant Position Control, and Auxiliary Monetization

Even after raising the tax for strategic priorities, there might not be enough central funds to cover the new costs of important strategic initiatives. Strategy teams thus should also consider the need to generate other sources fungible funds beyond withholds.

Gainsharing unit-level budget surpluses is a multimillion opportunity that most institutions have yet to try. About 60% of EAB partners use a full carry-forward budget model, where units retain the entirety of year-end surpluses. This approach can tempt units to accumulate massive reserves, while the center is left struggling for funds. Another ~30% of institutions employ a “use it or lose it” formula, that sweeps unused surpluses to the center, creating the potentially perverse incentive for departments to spend down balances at year’s end. Only 10% of institutions employ the compromise of gainsharing, where units and central administration split surpluses, usually 50-60% going to the center.

EAB expects many more institutions to embrace gainsharing in the coming years, because it advantageously advances finance goals that are often in tension:

- Meaningful incentives for units: to look for operational efficiencies – units keep a big portion part of what they what they save
- Big source of recurring funds for the center: Gainsharing savings are routinely in the millions, not just one-time but year-over-year
- Flexibility: gainsharing formulas can be configured in many different ways to satisfy circumstances and cultural traditions

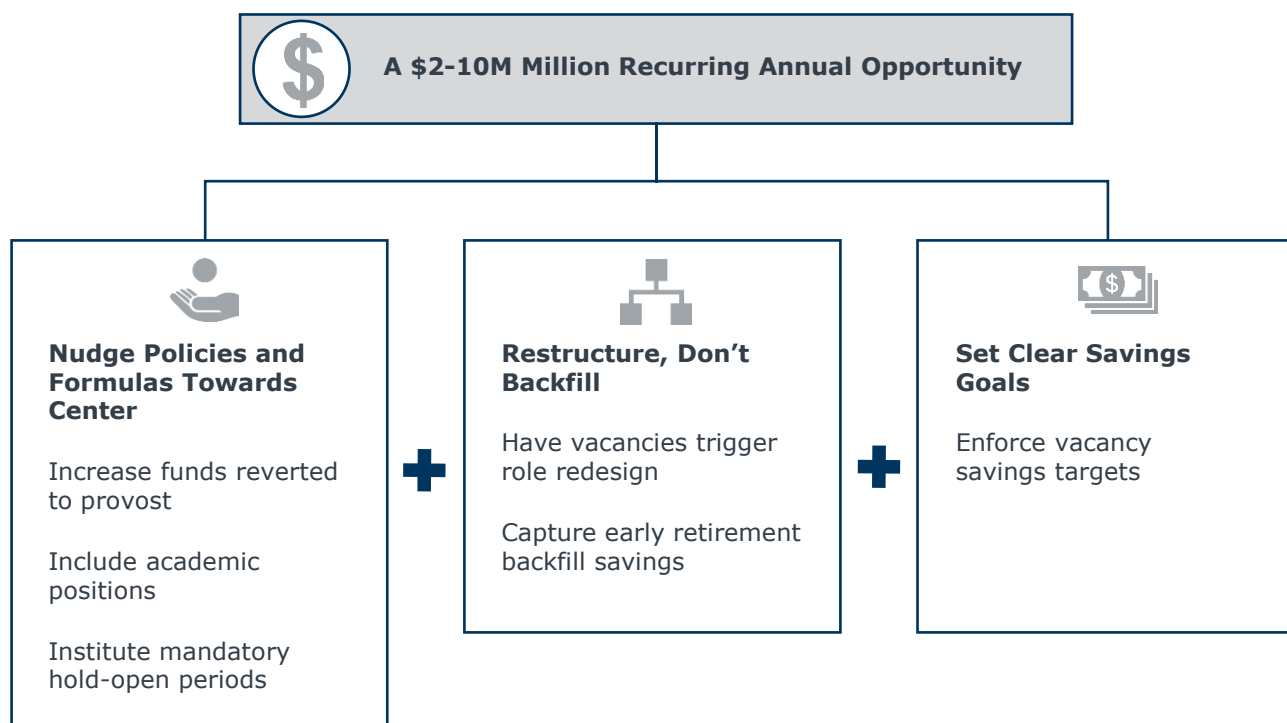


Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Vacant position control is another multi-million opportunity to create fungible funds, by reallocating a portion of open staff line salary and benefits to central strategic reserves. Aggressive, creative position control is an opportunity for strategy teams to turn the “lemons” of today’s much-lamented *Great Resignation* retention and hiring challenges into the “lemonade” of a flexible, recurring funding streams for strategic initiatives. Institutions that have not recently reviewed position control policies are highly advised to empanel a working group to identify and size these principled labor savings opportunities.

Turning Vacant Positions into Strategic Investment Funds



Nudge Policies and Formulas

Increase Funds Reverted to Provost: EAB’s most recent CBO budget model surveys, conducted prior to COVID, indicate that 80% of open position salary and benefits revert to department chairs or deans; only 20% are recovered by the provost or president for strategic reinvestment. Though those figures have likely trended upwards to the provost in the last years, the majority of institutions can find six- and seven-figure opportunities by changing policies and formulas about the percentage split of benefits and salary dollar staying with the unit versus going to central strategic reserves.

Include Academic Positions: 70%+ of institutions recover substantial portions of vacant salary and benefits for administrative positions; only 40-60% do so for academic administrative staff and faculty. Most institutions will have major opportunities by including a greater range of academic roles in position control and can manage cultural frictions through exceptions and carve-outs to general policies.

Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Institute Mandatory Hold-Open Periods: Units typically backfill positions as soon as possible, though in this labor market higher education is struggling to do so. Many institutions “round up” the pool of vacant position funds by policies that hold all vacated, non-faculty positions open for a specified amount of time to capture one-time salary savings and spur unit leaders to consider how vital the role, as constructed, is to unit productivity.

Unit leaders typically seek to backfill vacant positions as quickly as possible. By implementing a hold-open period, institutions can slow the reflexive backfill process. This often leads leaders to realize they do not need to backfill the role at all, or change work processes to better reflect unit demands.

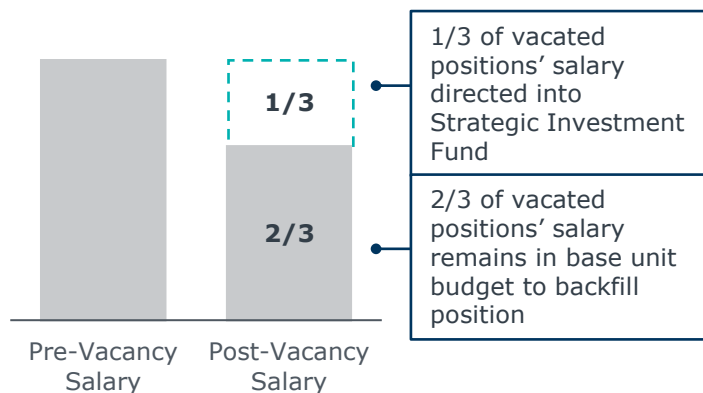
Restructure, Don't Backfill

Capture Early-Retirement Backfill Savings: Recognizing that older, higher-paid retirees are usually backfilled with less-experienced, lower-paid workers, some institutions codify recapture of the delta in salary and benefits, typically splitting the savings two-thirds to the unit, and one-third to central strategic reserves. EAB surveys suggest fewer than 10% of institutions have formal policies in place.

Early Retirement Backfill Arbitrage Nets \$5 Million in Strategic Funds at Research University

One Third of Salaries Diverted to Central Fund

Budgeted Salary for Retiring Faculty Slot



Prior Department Budget

| Department of Sociology | |
|-------------------------|-----------|
| Tenured Professor | \$120,000 |
| Dedicated to SIF | \$0 |

New Department Budget

| Department of Sociology | |
|-------------------------|----------|
| Tenure-Track Professor | \$80,000 |
| Dedicated to SIF | \$40,000 |

Have Vacancies Trigger Role Redesign: Institutions automatically place a hold on any “as-was” position request—a request to fill a position exactly as it was—and prompt unit leaders to consider ways to efficiently redesign the role, including automating, eliminating, or reassigning associated tasks. Vacancy is by far the best time to redesign positions, as shifting or automating tasks is simpler with no incumbent staff. By requiring unit leaders to review work processes as part of filling vacant positions, institutions can often refocus positions on higher-value work or sufficiently streamline roles to allow for less expensive or part-time replacements.

Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Set Clear Savings Goals

Enforce Vacancy Savings Targets: Institutions that have tapped position control most aggressively often reverse the usual process by setting a target savings amount first, achieved through a combination of central diversion of unused salary and benefits, mandatory hold-opens and redesigned/eliminated roles. Position-control reviewers are required to hit this target, and empowered to adjust policies, formulas and unit-level exceptions to deliver the number.

Predetermined targets have the dual benefit of ensuring that strategic funding is adequate and predictable – surprise shortfalls are far less likely – and ensures leaders evaluate all positions in the context of a broader institutional goal, rather than viewing each in isolation

Targets Help Pull the Right Levers Hard Enough (But No Harder)

Case in Brief: Illinois Institute of Technology

- 7,700-student private research university in Chicago, IL
- Leadership sets specific dollar target for how much money to save through vacancy review each year

Vacancy Review Savings Target

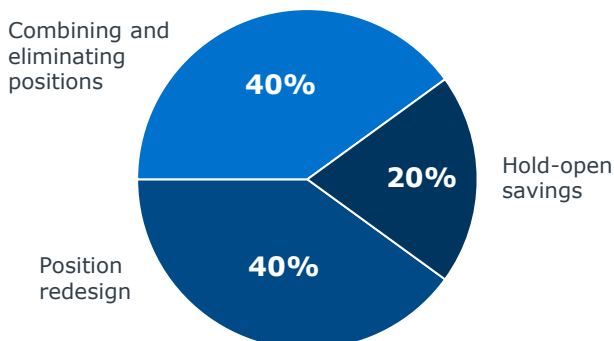
\$1.5M Savings target for vacancy review process in 2013

4% Savings target as % of IIT's non-faculty salary budget

Advantages of Pre-Set Targets

- **Maximizes Savings Potential**
Induces more thorough scrutiny of positions to achieve target
- **Forces Prioritization**
Prompts development of rigorous standard to compare competing requests
- **Provides Alternative to Across-the-Board Cuts**
Enables Central Administration to recoup needed savings through targeted position elimination
- **Offers Political Safeguard**
Equips vacancy review leaders with justification to make strategically sound but potentially unpopular staffing decisions

Breakdown of Vacancy Savings by Source



Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Diverting Auxiliary Revenue Streams Directly to Strategic Investment Fund

Another under-leveraged source of strategic fund dollars is auxiliary revenue. Absent specific state restrictions, auxiliary revenue returned to central administration is highly fungible. Accordingly, many CBOs are looking for principled ways to go beyond breaking even on small-scale services and fees to generate strategic investment funds, without passing on undue costs to students.



New Formulas for Sharing Alternative Revenue Streams

Even though these revenues can be small in absolute terms, their extreme fungibility often makes them a meaningful share of central investment funds, worth trying to expand

Representative Alternative Revenues

- Branding, Licensing, and Affinity
- Non-Traditional Educational Revenues
- Campus Operations
- Cell Tower and ATM Leasing



Outsourcing and Monetizing Auxiliaries

“To outsource, or not to outsource” is the perennial auxiliary question. Most institutions have outsourced at least one function and taken meetings about outsourcing others. Post-pandemic, strategy teams with big price tags for strategic initiatives should look anew at whether mega-leases or asset transfers to private partners with the potential to for transformational, eight-figure capital infusions and ongoing income shares make sense.

Representative Auxiliary Outsourcing Deals

- Parking
- Energy
- Facilities and Real Estate Management



Premium Service Student Fees

A handful of institutions have generated millions in student opt-in fees for premium services. Mindful to avoid the perception of “haves” and “have nots” on campus, most institutions can safely consider 10-12 unobtrusive, provenly popular fee-based services without cultural backlash

Representative Premium Services

- Vegan meal plans
- Personal chefs
- Parking spots closer to campus
- Global parking access
- Laundry and dry-cleaning services
- Textbook rental

Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Developing Consistent Strategic Seed Fund Formulas

- ▶ **EAB Guidance:** Establish common business case templates and evaluation criteria to promote proposal consolidation and academic unit self-screening

Strategic budget models should provide investment seed funds that colleges and departments can access to support new projects and activities aligned with institutional priorities. With the right best practices for proposal criteria and evaluation, seed funds can provide an excellent mechanism for:

- Educating faculty about strategic goals
- Discovering opportunities for collaboration and shared services across silos
- Securing dean commitment so that seed fund projects aren't perpetually dependent on central financial support

In practice, however, seed funds are often administered without much transparency, with inconsistent evaluation hurdles, which can lead to sub-scale proposals, weakly aligned with institutional goals. After strategy teams are satisfied that the revised budget model generates stable sources of funds, they should use the diagnostic below to identify opportunities to strengthen seed fund structure.

| Strategic Seed Fund Maturity Diagnostic | Yes | No |
|--|-----|----|
| Is the seed fund organized around strategic themes? | | |
| Do we maintain standardized business case templates for proposals that generate metadata enabling comparability across academic silos? | | |
| Do reviewers use explicit common criteria, well understood by faculty, about alignment with institutional strategy and potential for cross-unit collaboration? | | |
| Do we synchronize proposal reviews into twice-annual batches for rack-and-stack assessment, rather than staggered one-off evaluations? | | |
| Do proposal reviewers identify opportunities for combining related proposals into larger projects to achieve scale? | | |
| Do we require deans and chairs to commit their own funds in addition to seed funding, to ensure "skin in the game"? | | |
| Do we limit the number of seed fund application per college to encourage self-screening by deans and chairs? | | |
| Do we set multiyear targets for financial self-sufficiency of successful initiatives to cover their own costs by year 3-5? | | |
| Do we maintain clear standards for sunseting and redirecting funds from unsuccessful initiatives? | | |

Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

Provide Central Seed Funds Only After Local Funds Committed by Deans

An insight shared by higher education’s best seed fund managers is that dean commitment is essential, and best accomplished by proposal processes that promote high-quality self-screening and upfront pledges of college resources – both help combat the perception that central support is “free money.”

One research university accomplishes these goals in a cunning manner. When submitting seed fund proposals, deans must complete two application forms: a more ambitious proposal reflecting seed fund contributions, and a more modestly scoped proposal that the dean commits to launch using college funds alone, whether or not they receive central funding. This has the benefit of ensuring deans submit only ideas they are fully committed to, and sets a predicate for the seed fund’s target of a 60:40 split between the center and units in launching strategic initiatives.

Partners can access Strategic Seed Fund best practices and templates [here](#).

A Strategic Budget Model Workshop Agenda

Strategy teams can use the diagnostic below to assess where their current budget model might benefit from fine-tuning, and where team members should request supplementary information and expert support from EAB. Every partner keen on these issues is encouraged to contact your Strategic Leader to schedule an expert consultations or facilitated workshop sessions.

| Approaches for Increasing Size and Alignment of Central Strategic Funds | | Won't consider, don't require information | Not using at scale, want to introduce planning team to concepts | Using, but want to know more from leading practitioners |
|---|---|---|---|---|
| Subvention Tax | Levy of 3-5% on allocated revenues | | | |
| Vacant Position Control | Portion of unspent budgeted salaries diverted to central strategic initiative fund | | | |
| Gainsharing | Center shares unit surpluses generated from operational efficiencies | | | |
| Auxiliary Outsourcing | Lump-sum payments for conferring service to private provider (e.g., parking, energy, residence management) | | | |
| Diversion of Alternative Revenue Sources | Portion of non-traditional education revenue, licensing, facilities, student fees etc. diverted to central fund | | | |
| Strategic Seed Funds | Central fund with explicit criteria for unit-based proposals | | | |

Growing Fungible Investment Funds (cont.)

Review of Gainsharing, Position Control, and Auxiliary Revenue Strategies

What approaches do you use to align institutional strategic priorities with unit budgets and action plans?

| Approaches for Increasing Central Strategic Funds | Won't consider, don't require information | Not using at scale, want to introduce planning team to concepts | Using, but want to know more from leading practitioners |
|---|---|---|---|
| Cascade institutional strategy metrics to unit annual plans | | | |
| Business case templates requiring units to explain how proposal advances strategy | | | |
| Department-level strategy performance scorecards | | | |
| Tenure and promotion criteria explicitly tied to strategic priorities | | | |