Some Thought & Action readers may have heard of a new budget concept currently making the rounds in college and university administrative circles, “Responsibility Center Management,” or RCM for short. This hot concept also goes by the labels “Responsibility Centered Budgeting” or “Value Centered Budgeting.”

I first heard about RCM when a consulting firm recommended that Temple University, where I teach, adopt this approach to management and budgeting.

To justify the recommendation, the consultants told the university: “We believe that if responsibility centered budgeting can be effectively implemented, then the current situation in which some schools and colleges take minimal responsibility for recruiting, changes in enrollment and the cost to deliver instruction will change dramatically.”

They went on to assert: “Further, because each responsibility center will carry their costs of facilities and space, there will be for the first time true incentives to rationalize the use of space, with economically underutilized space being returned to the University for alternative uses.”

The principles behind RCM date back to the late 1970s and the concept of “every tub on its own bottom.” The “tub” in the case of RCM is an academic unit of a college or university and the “bottom” is the idea that each such unit must have its own bottom line, that is, be responsible for all the costs it produces and receive all the revenues it generates.

The main premise behind RCM is that unit heads, who best understand their operations, should be given greater budgetary authority and responsibility over their units. RCM supposedly encourages deans to be more innovative and develop programs that will attract more students to the institution. The

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Centers that generated a surplus could carry it over for future use. Centers with a deficit must eliminate it.

Approach, advocates maintain, will provide a financial incentive to academic units to increase the size and attractiveness of their programs and, as a result, will increase the revenue flow to the larger institution. Unit heads, in addition, will have a financial incentive to cut costs since the units will get to keep any savings.

RCM received an impetus from the widespread restructuring of higher education that took place during the 1990s. According to one 1994 survey, two-thirds of campuses reported reorganizing administrative structures and 71 percent reviewed the mission of their academic programs. RCM is, in effect, a way of restructuring the administration of a college or university.

When RCM was discussed at Temple University, the administration repeated the argument that the managers of each responsibility center would have responsibility for all center expenditures and ownership of the revenues they generate. Centers that generated a surplus would be able to carry it over for future use. Centers that generated a deficit would have to eliminate it. All budgets would be revenue-based.

Temple University opted not to adopt RCM for 1996-97, although the administration is running a "shadow" RCM budget for each responsibility center this year to see how each unit would have fared under RCM.

A number of other institutions have reportedly already adopted some version of RCM or are testing RCM on some campuses this year. Lehigh University has recently studied the approach in depth and decided not to adopt it. The administration of Southern Illinois University at Carbondale announced last fall that RCM would be tested at its law school next year, with the intention of applying the approach at the other colleges in future years.

All this occurred at Southern Illinois before the National Education Association won a fall collective bargaining election for faculty. As discussed below, collective bargaining would seem to provide a major impediment to the implementation of RCM.

At this point, I should state that I am not an expert on Responsibility Center Management—if one defines an expert as someone who has actually implemented RCM. Using that definition, there is no expert on RCM in the administration of any of the 30 or so higher educational institutions whose budgets I have analyzed.

In fact, if one stipulates that an expert should be one who has implemented RCM in an institution with faculty collective bargaining, then there may be no experts
The structure of a typical university contains three categories of units that could become responsibility centers.

The first category includes units whose mission is the teaching, research, and public service that are the core missions of any higher education institution. Typically, under RCM, each college of a hypothetical university would be made into a responsibility center that has to stand on its own legs budgetarily.

The second category of responsibility centers includes units providing services to the primary mission units. The computing center, the library, and physical plant operations are typical examples of this second category.

The third category consists of executive management. The president’s office and staff might be included in this category.

Let us consider the impact of RCM on colleges, the responsibility centers that will have the greatest impact on higher education faculty. Suppose that, in a hypothetical university, a college has direct expenses (salaries and benefits are typically 95 percent of such direct expenses for colleges) of $5 million. This college is also assigned indirect costs of $3 million. These latter costs include physical plant operations, computer services, student services, financial affairs, the Chancellor’s office, and more. The total costs charged to this hypothetical college under RCM are then $8 million.

Suppose further that the college generates $4.5 million in tuition for the courses that its faculty teach. Let us, for the time being, ignore the revenue items of indirect cost recovery on grants held by members of that college’s faculty and donations received by the college.

Under RCM, the dean of this college would be faced with a gap of $3.5 million, the difference between revenue and expenses. For the first year, under RCM, this “gap” could be plugged by allocating $3.5 million of the state appropriation to the college. In the first year, RCM would then be said to be budget neutral.

At Indiana University, on average, 60 percent of an academic center’s general fund budget comes from an allocation of state support. For a college in such an institution, the “gap” between direct revenues and direct plus indirect expenses would be even
The deans would need to be able to set salary increases in line with their estimates of the college’s future revenues.

larger than in the prior example. The problems under RCM, then, occur during the subsequent years. They are easy to identify from the above example.

For deans to be able to manage their college budgets under RCM, they would need control over direct expenses, indirect costs, and, finally, revenues. For deans to have adequate control over these items, the faculty senate, the faculty union if the faculty are unionized, the central administration, and the board of trustees would all have to cede to the deans authority that each of these other bodies presently exercise. I doubt that any of these entities would agree to give up their authority.

Let us consider the case of direct expenses first. Since direct expenses consist largely of salaries and benefits, the deans would need to be able to set salary increases commensurate with their estimates of a given college’s future revenues.

Collective bargaining agreements currently set the salaries and benefits for all faculty in a bargaining unit. To see why this cannot work under RCM, consider what reportedly happened at Indiana University after it adopted RCM. The College of Arts and Sciences lost 20 percent of its enrollments in two years after other colleges changed their required courses and reduced the number of credits their students needed to get in Arts and Sciences.

The other colleges were, as a result, able to retain a larger portion of the tuition generated by students majoring in their programs. Consequently, the dean of Arts and Sciences was unable to provide any of that college’s faculty with salary increases for two years, even though faculty in other colleges did receive increases.

The only way RCM would be compatible with collective bargaining would be for all unions at a unionized institution to replace their salary provisions with the following clause:

“Each faculty member shall receive such salary increase as the faculty member’s dean thinks the faculty member deserves and the dean can afford.”

It seems unlikely that any union would ever agree to such a clause. After all, one hardly needs a union to “negotiate” such a compensation package.

Deans at a unionized institution, in other words, would not be able to put salaries under the limits that RCM might demand. Their only other control over salaries would be over the number and kinds of staff. Here too the deans
Painful savings in direct costs could easily be overwhelmed by increases in the indirect costs.

would be stymied by a collective bargaining agreement in such areas as tenure, due notice provisions in the event they wish to retrench faculty to balance their budgets, benefits, and workload provisions.

In this setting, the use of more part-time faculty would become even more appealing to deans. Yet their increased use might adversely affect the quality of instruction.

Let us next review how the indirect costs would be assigned to each college, under an RCM approach. For starters, who would determine the formulas by which these costs are apportioned to each college? Since, on average, indirect costs would probably be about half the direct costs, painful savings in direct costs can easily be overwhelmed by increases in indirect costs.

For example, whenever a new classroom building is constructed, its classrooms would have to be assigned to various colleges who would then have to pay for their maintenance whether or not a given college believes that it needs additional classroom space. Also, how can a given college return space to the central administration if no other college wants that space?

To see how complicated and divisive the assignment of indirect costs can be, consider the following issue. Under Financial Accounting Standards Board Statement 117, depreciation is supposed to be recorded as a current fund expense. Under a full blown RCM, depreciation would have to be charged to each college for whatever space it occupies.

Suppose college A occupies space in a brand new building constructed for $30 million. Suppose this building is depreciated over 30 years. Then each year College A could be charged $1 million for the depreciation on the space it occupies.

Next consider College B, which occupies the same area in another building that is more than 30 years old. That building has already been fully depreciated so that College B pays nothing for depreciation for its space. It seems certain that the dean and faculty of College A would complain that their college is being overcharged and that the better way of dealing with this is to spread the $1 million depreciation over all responsibility center units.

If that solution is adopted, the dean and faculty of College B would be sure to complain that their college is being charged for the brand new building that another college is occupying.

There is no obvious right answer to the above cost allocation issue: The only thing that seems certain is that these sorts of issues
Would a dean experiment with faculty teaching over the Internet if the college had to pay the computer center to do it?

would provoke inter-college warfare.

Charging indirect costs, such as computing charges, to each college may also inhibit experimentation with technology in the classroom. For example, would a dean wish to experiment with faculty teaching over the Internet if the college has to pay large costs to a centralized computing operation for each such course? Does inhibiting such experimentation benefit an institution in the long run?

The short-fall between the total of the direct and indirect costs and the revenues directly generated by the college would need to be filled by using part of the state or local appropriation to the institution. Using the state or local appropriation to the institution to fill this “plug” in each college’s budget would raise two related problems.

The first is the way that the initial amount would be assigned under RCM—the difference between the direct and indirect costs and the revenues the college generates. Who is to say that the numbers used for each college in 1997-98 (or whatever year is chosen to begin implementation of RCM) are fair? Put another way, the RCM approach gives everybody their historical subsidy regardless of whether this subsidy was right or wrong and says that future budget changes will depend upon future performance alone.

This approach would mean that the past history of the growth or decline in enrollment or staffing of each college determines this initial gap. Consider the example of the college given above. Suppose that another college (called “B”) generates the same $4.5 million in revenues but has only $3 million in direct costs and $1.5 million in indirect costs. It would receive nothing from the state appropriation initially.

Is this fair, if College B achieved the much smaller direct costs by painful staff reductions and increases in faculty workload, while the first college (whose direct costs are $5 million for the same revenue) had arrived at this state by losing half of its enrollments over the past five years while its faculty size had not been significantly reduced?

How can the more efficient college be expected to yet further cut costs to the same degree as the college that may have been overstaffed to begin with? In short, the RCM approach might be equitable, in terms of the financial challenges it presents to each college if all the colleges in the institution have been treated equally over the past few years, so that current direct costs and revenues are fair relative to one another. This, needless to
There would be strong incentives to stop students in one college from sampling course offerings in other colleges.

say, is not likely to be the case.

The second problem is how future increases in the state and local appropriations would be divided among the colleges. If the increases are distributed based on the same percentage for each unit, the initial inequity mentioned above would be compounded. Would central administration “fix” the initial inequities with future distributions from increases in the state appropriation? That hardly seems likely. The present imbalances, after all, were caused by the failure to allocate past increases properly among the colleges.

Let us now examine the revenue part of the RCM equation. For most colleges, tuition would be the major component of revenues. Tuition revenues are determined by two factors, the credit hours generated by a given college and the tuition charged per credit hour. RCM would probably assign all the tuition to a college for the courses taught by that college, although some institutions have divided tuition between the college providing the courses and the college housing the subject where the student is majoring.

One institution assigned 85 percent of tuition to the college providing the instruction and 15 percent to the student’s home college. Even if a division of tuition is made, there will be intense competition among colleges to secure student enrollments. Increases in each college’s share of the state appropriation may also be tied to enrollments. This would further intensify the inter-college rivalry for student credit hours generated.

At Indiana University, this fierce competition led to a plunge in enrollments in the core courses taught by the College of Arts and Sciences. The same dynamic is likely to spin out of control anywhere RCM is implemented. There would be strong financial incentives to prevent students majoring in a given college from sampling course offerings in other colleges. This might adversely affect curricula at all colleges (with the possible exception of perhaps a law school, where I presume that virtually all courses taken by law students are offered in the law school).

In short, RCM would pit the profit motive against academic considerations of which courses a student should take and where these courses could best be taught. An example: A business school, to retain tuition dollars, might mandate that the students take business writing taught by business school faculty instead of having freshman business majors take a composition course in the English Department in arts and sciences. This might well happen even if the
Could a business school charge a higher tuition rate than a college of arts and sciences?

English faculty were far better trained to teach writing courses.

Another interesting question: How would RCM treat the tuition from athletic scholarships? One approach would be to charge the athletic department an expense equal to full tuition for all students on an athletic scholarship. This tuition money would then be assigned to the colleges providing instruction to student athletes.

A different approach would be to argue that the credit hours taught to athletes on full scholarship do not generate any actual dollars and the colleges should receive no payment for providing these courses. In turn, the athletic budget would not be charged any expense for athletic scholarships.

Deans would no doubt favor charging the athletic department tuition, while the athletic director would prefer to save perhaps millions of dollars in tuition charges by arguing that athletic scholarships do not bring in any revenue to the institution. Athletics would then be reported under RCM to “break even” while the colleges show a deficit.

It is not clear how much RCM would encourage colleges to increase their outside recruitment activities. It may well seem easier to fight over the current sized enrollment pie rather than attempt to make it larger.

Next, consider the tuition rates. Who would set them? There would be pressure to have differential tuition. Would the president and the Board of Trustees be willing to cede this power to the individual deans? Could a business school charge a higher tuition rate than a college of arts and sciences, for example? Could schools compete for students based on their tuition rates?

What about admission policies? Would deans set this also? Who would control financial aid for students? What about grading policies? Would colleges bid for students by lowering academic standards?

Let us next reconsider why a governing board and an administration might favor RCM. Some institutions have two major budget problems (and a number of minor ones as well). The two major problems: an inadequate level of state support and decreasing enrollments. Governing boards might hope that RCM would help solve one or both of these problems.

In my opinion, the adoption or non-adoption of RCM is not likely to impact future state appropriations. In February 1996, NEA released a survey, “The Politics of Remedy: State Legislative Views on Higher Education.” The chairs of the House and Senate Education
Deans and faculty would spend greater efforts trying to redistribute the current enrollment pie than enlarging it.

Committees in 49 states were surveyed by an independent research firm. Nothing in the survey results suggests that an institution’s internal budgeting system is going to affect its state appropriation.

But the survey did report that the legislatures in many states are discussing the reorganization of higher education, hoping to create a more decentralized system. RCM is consistent with this trend because it decentralizes budgetary decisions within a given institution.

The best argument that can be put forward for RCM is that it would provide an incentive for deans and faculty to work harder at recruiting. These efforts would then increase the institution’s enrollments.

RCM might indeed enhance recruitment activities, but my concern is that deans and faculty would spend greater efforts trying to redistribute the current enrollment pie than enlarging it. After all, if it were easy to get more students they would have been recruited already.

In addition, if legislation suggested by President Clinton in his State of the Union address is enacted into law, there will no doubt be a significant increase in overall college enrollments nationwide without increasing recruiting activities.

Moreover, there are other ways to increase recruiting efforts besides taking an RCM approach. The first would be to provide financial inducements for faculty to strenuously participate in recruiting. One such inducement could be to reward outstanding recruitment efforts with merit increases for outstanding service.

Colleges could also be given financial incentives. Each college could be given 50 to 75 percent of the increase in tuition generated by the college. The central administration would receive the rest to cover indirect costs associated with these students.

Finally, let us consider the impact of RCM on fund raising. Under RCM, each college would keep all of the funds it raised and could carry forward these funds from one year to the next. But doesn’t this happen under the present system? If not, a minor change in budgeting should be made to allow the colleges to keep all of the funds they raise.

For those of you that want to learn more about RCM, I would suggest reading the “bible” on RCM, Responsibility Center Budgeting: An Approach to Decentralized Management for Institutions of Higher Education, by Edward L. Whalen.

To give you a flavor of the administrative style described in the book, I will conclude with the
following quotation:\(^6\)

Of course, when responsibility center budgeting is first announced, every campus busy-body feels threatened—probably appropriately under any system—and is sure that she or he must understand it to maintain "academic quality" and protect "academic freedom". Keeping such nosy and usually noisy people under control is a dean's responsibility . . ."

The book also comments on the role of a president and provost under Responsibility Centered Management.\(^7\) "Will a president or provost cede authority to the deans sufficient for them to run their schools?" A very good question.

I include an appendix with a few suggested questions for your administration in case it suggests adopting RCM at your institution. I think that you will find that some of the questions may make campus administrators very uncomfortable. At one institution considering adopting RCM, the only thing that one high level administrator could say was that he "understood all the questions." Adequate answers, however, were never provided.

### Appendix

**Questions Concerning Responsibility Centered Management**

1. How will the state appropriation be initially allocated to the colleges?
2. How will the indirect costs be apportioned among the colleges? Who will determine the formulas for distributing these costs?
3. How will future increases in the state appropriation be distributed among colleges?
4. Who will set the tuition rates, the deans or the governing board? Will deans be allowed to set different tuition rates for each college?
5. Who will set admission and scholarship standards?
6. Who will set graduation requirements and grading standards?
7. Who will assign space to colleges when new classroom buildings are opened and who will set the rates charged to the college for this space?
8. If a college no longer needs some of its assigned space, can it give up the space (and the cost of that space) if no other college wants to assume the space?
9. If the initial allocation of the state appropriation is simply made to close the gap between a college's direct and indirect expenses and the college's other revenues, does the central administration claim that this initial distribution of the state appropriation is fair to all of the colleges?
10. If the faculty are unionized how will the deans have control over salary increases?
11. Has RCM ever been successfully implemented on a campus on which the faculty are unionized? Is the administration introducing RCM in an attempt
to undermine collective bargaining for the faculty at a unionized campus?

12. How will inter-college warfare over student credit hours generated be avoided?

13. Are the governing board and the central administration willing to cede most of their power to the deans under RCM?

14. Why has the administration suggested adopting RCM?

15. Depending upon the answer to question 14, has the administration considered less drastic approaches to achieving its objectives?

Endnotes

1 Hendrickson, 1996, 51.
2 These include Indiana University, the University of Southern California, the University of Pennsylvania, the University of Iowa, the University of Michigan, the University of Alaska, Cornell University and Virginia Polytechnic Institute

3 Whalen, 1991, 35
4 Ruppert, 1996.
5 Ruppert, 1996, 42.
6 Whalen, 1991, 93.

Works Cited

