CAPINCROUSE LLP

Knowing What It Costs: The Importance of Marginal Revenue Analysis

By Tyler VanderVen, Partner, CapinCrouse and Jan M. Haas, Partner, CFO Colleague

The higher education industry is large and complex. There are many pain points that keep senior leadership teams up at night.

Institutions of all sizes need to answer these key questions:

- Do you actively monitor your Department of Education ratios and debt covenant ratios (if any), thinking the only thing you can control is your enrollment numbers or hoping that you are within your annual budget?
- Have you expanded your business model or added new programs recently?
- Have you forecasted financial outcomes for major projects or initiatives? Is your data reliable?
- Have you incurred or refinanced debt, performed a tuition reset, sold assets, or taken similar steps to make ends meet?
- Has your accreditor or governing board requested more in-depth reporting or analysis?
- Are you concerned that your institution could close in the next three to five years?
- Are you just accepting the status quo?

There is increasing pressure on higher education institutions to become more efficient.

Financial stress, increased competition, closures, downgrading, and complaints about the cost of attending college dominate higher education news. The pressures on higher education to become more efficient are mounting and it is critical to measure, analyze, communicate, and manage financial margins.

Higher education institutions need adequate margins to remain financially sustainable. Although there have been significant efforts and focus on measuring the qualitative and student success factors of programs, the trends in identifying financial contribution margins have not had the benefits of focus or clear data.

There are opportunities for higher education institutions to find efficiencies.

Higher education leaders have begun to recognize that identifying student net tuition revenue, the associated costs, and marginal contributions of their institutions is required to provide the focus and clear data needed for data-driven decision making.

An essential first step is understanding the actual revenue received and the costs of instruction. Most campus leaders do not know their net tuition revenue per student nor how that revenue is provided by program, student class, major, athletic program, etc. Similarly, there is a lack of knowledge regarding how much it costs to teach a specific class or section, or the resources needed to educate students in various programs and majors. Thus, they don't know where to begin to find efficiencies.

A recent *Chronicle of Higher Education* article stated that "most institutions — the overwhelming majority — have zero idea how they earn a living, where the margins are across programs." The article Enough 'Do More With Less.' It's Time for Colleges to Find Actual Efficiencies points out that:

> … even when you think about how we monitor what faculty do, it doesn't connect to the business model. For instance, think about the primary metric for faculty work, which is course load. That has almost zero connection to financial sustainability. But if you look at faculty throughput — how many student credit hours each faculty member is producing — and activity-based cost models of how faculty are spending their time, you understand how you're investing and what you get for that investment.

How to identify and act upon those areas of efficiency.

Higher education institutions should examine faculty throughput and identify actual student net tuition revenue less actual faculty compensation, thereby creating a marginal contribution by various characteristics. By conducting the analysis to the student class level, higher education institutions can determine the financial contribution of academic programs/departments, margin and class size by course, course-level contribution and class size by section, the financial margin by major, academic rank, instructional methodology, athletics, etc. Identifying the student net tuition revenue, faculty compensation costs, and resultant contribution margin are critical to maintaining long-term financial sustainability and are essential components of the program analysis process.

A marginal revenue analysis can provide management with data to help make decisions about the appropriate allocation, effective use, and productive investment of a higher education institution's limited resources.

This article was originally published in Christian Academia Magazine.

The pressures on higher education to become more efficient are mounting and it is critical to measure, analyze, communicate, and manage financial margins.

About the Authors

Tyler VanderVen, Partner
CapinCrouse
tvanderven@capincrouse.com
o 616.717.5764

Tyler joined CapinCrouse in 2006 and has acquired a broad range of experience through serving numerous types of nonprofit organizations. He provides assurance and consulting services to an array of clients in addition to overseeing and guiding audit teams. His expertise includes strategic planning, financial statement preparation, and compliance audits performed in accordance with Government Auditing Standards (Yellow Book) and Uniform Guidance.

Jan M. Haas, Partner
CFO Colleague
jan@cfocolleague.com
o 267.278.4650

Jan is Partner at CFO Colleague. He had two decades of experience in health care administration before serving Cairn University for another 16 years. As Senior Vice President, Finance and Administration for the Philadelphia-based university, Jan wore the various hats of Chief Business Officer and Treasurer, along with Assistant Secretary for the board of trustees, President of a real estate LLC, and board member of the Regency Foundation. He also served the industry as a board member and chairman for the Association of Business Administrators of Christian Colleges (ABACC), where he guided their growth and was a frequent presenter and contributor. Learn more at cfocolleague.com.

About CFO Colleague

CFO Colleague is a financial and operational advisory firm specializing in higher education. Since 2013, the company has helped more than 80 institutions put systems in place to make smarter, data-driven decisions that streamline costs and put strategic goals within reach. Learn more at cfocolleague.com.

About CapinCrouse

As a national full-service CPA and consulting firm devoted to serving nonprofit organizations, CapinCrouse provides professional solutions to organizations whose outcomes are measured in lives changed. Since 1972, the firm has served domestic and international outreach organizations, universities and seminaries, foundations, media ministries, rescue missions, relief and development organizations, churches and denominations, and many others by providing support in the key areas of financial integrity and security. With a network of offices across the nation, CapinCrouse has the resources of a large firm and the personal touch of a local firm. Learn more at capincrouse.com.

CapinCrouse is an independent member of the BDO Alliance USA.

© Copyright 2019 CapinCrouse LLP