Brandeis University
Financial Situation and Opportunities – Summary

After five years (FY10-FY14) of reported deficits for our operating budget, ranging from $1 million-$4 million, FY15 and FY16 saw modest operating budget "surpluses," and FY17 is projected to end close to balanced. This turnaround in our operating budget is the result of careful attention to mitigating rising costs, new purchasing policies, and other savings. While the improving financial situation is encouraging, the reported surpluses of recent years mask a longer-term underlying problem of structural imbalance at Brandeis. Even as we see audited financial statements that include an operating budget in surplus or balance, this performance would not be possible if we had not undertaken unsustainable practices to balance the bottom line.

Example: If we take the FY15 reported operating results ($2.6 million *surplus*) and use a 5 percent average draw rate from the endowment rather than the 5.9 percent draw rate that was done that year, the reported operating surplus would go from a reported $2.6 million *surplus* to a $3.9 million *deficit*. In addition, if 40 percent of annual gifts that had been raised had been directed towards endowment rather than to support the annual budget, which is typical in universities like Brandeis, the operating *deficit* would grow to just over $9 million. If we add in funds needed to address gaps in faculty salaries and under-staffing, the deficit would increase further to almost $16 million. Finally, if we began to address the backlog of deferred maintenance and invest in long-overdue IT infrastructure, the overall operating budget would be close to $30 million in deficit.

The implication of these practices is that while we have balanced our budget in the short term, we have shorted ourselves of resources for the longer term. For example, by diverting a high proportion of annual gifts towards operations rather than to endowment, our endowment has not grown as much as peer institutions. As you can see in Figure 1, in 1990 Brandeis, Tufts, Northeastern, Syracuse and Tulane had pretty similar endowments. By 2015, all were higher than ours with the exception of Northeastern. Endowments grow due to investment performance and capital campaigns. But, as you can see, if Brandeis' had kept 50 percent of annual gift revenue raised since 1995 in endowment rather than using it immediately in the operating budget, our endowment might be close to $1.8 billion rather than just half that at $915 million. That difference in endowment translates to over $45 million less endowment funds going to our annual budget. This thought exercise does not take into account what would have happened to Brandeis if those funds had not been used to cover annual budget costs. But this does highlight the fact that choices we make in the short term have longer-term consequences. In addition, as we move to a better financial situation, continuing past practices undermines our ability to achieve a more sustainable financial equilibrium.

The structural imbalance that we face does not mean that the university is not able to conduct its activities, pay its bills and continue to provide the excellent research and education we are all so rightly proud of. But it does help explain why, even with an operating surplus, faculty are being raided by other universities, it takes longer to fill many staff positions, and faculty and staff report being overworked as they contribute ever-increasing "sweat equity." In addition, in spite of the heroic efforts of our buildings and grounds staff, and new investments in infrastructure such as steam tunnels and windows, all of us on this campus are familiar with clanking pipes, faulty AC, leaky roofs, and drafty windows and doors. Figure 2 provides more information on the extent of our deferred maintenance issues on campus.

With an improved financial picture, this is the moment to tackle the challenges of this structural imbalance. Unfortunately, there are limited opportunities for new sources of net revenue. The usual sources of new revenue for a university include:

> Net Tuition – We might consider increasing the size of the undergraduate student body; however, the magnitude of change that would be required—in terms of the number of undergraduates or the socioeconomic mix—raises fundamental questions about our culture, mission, and strategy. Growth in enrollment would also require significant capital investment (e.g., new dorms). Graduate students may not require on-campus housing but would require investments in faculty and facilities.
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> Research Grants – Only a small part of sponsored research revenue is budget-relieving and therefore will not address our current situation.
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> Endowment – Reducing draw and directing more gifts to the endowment will produce enormous long-term financial benefits but restrict operating revenues in the near-term.
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> Gifts – Improving fundraising is part of the solution but cannot by itself solve the problem.
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> Other – Online learning opportunities allow us to grow our student body without many of the costs associated with a residential campus. But substantial growth will require time and articulation of its role within the overall strategy of the university.

These new revenue sources may provide some budget relief and will be important considerations in our budget process. At the same time, we will continue our vigilance to keep costs under control, including further expense reductions that do not harm our strategic goals. But cutting our way out of structural imbalance would fundamentally impact the quality of the education we provide and the research we produce in ways that would be inconsistent for the academic excellence we have achieved.

Brandeis is and continues to aspire to be a top-ranked research university that simultaneously provides a distinctive "small liberal arts college" undergraduate experience. Being a major research university requires attracting and retaining a productive faculty actively pursuing research in a range of areas. Their scholarship and creative contributions are supported with graduate students, including a critical mass of doctoral students, and non-faculty research staff. At the same time, providing our distinctive undergraduate experience requires low student-to-faculty ratios, high faculty engagement with students, and undergraduate involvement with world-class research.

Given all this, Brandeis is by definition and mission a complex organization. Complexity is very expensive, especially for smaller organizations, as the fixed costs associated with running such a university cannot be widely distributed. As you can see in Figures 3 and 4, other research universities tend to support complexity by being large, rich (in terms of endowment), or specialized. Brandeis currently has none of these attributes.

None of this should really be "news" to those who know Brandeis well. As a young university, we have achieved remarkable academic excellence in just 68 years. We were not founded with a large endowment as our peers were, and as founding President Abram Sachar said, "Brandeis could not afford to grow slowly. Whatever was needed had to be available at once — faculty support, student scholarships, buildings, equipment, administrative and maintenance assurance." Given the financial costs of establishing a university of excellence, Sachar noted, Brandeis could not, at least initially, "plan and function timidly with a bookkeeper's mentality."

We have reached the stage in our growth and development, however, where we must pay attention not only to the short run but to the medium and longer run. The challenges of maintaining our excellence and unique character as a young university require an effective framework for managing our finances. This framework needs to align investments and our operating budgets with mission and strategy. In addition, it must ensure long-term financial health, manage risk without being reckless about our future, create clear parameters within which schools and departments can make operating decisions to achieve their respective goals, and establish accountability for the outcomes associated with the funds allocated.

As we embark on this path together, there will be two principles that we will strive to maintain — transparency and inclusiveness. We all have a stake in the outcome. As such, it is important that we all understand the baseline from which we begin this effort. This level-setting appropriately began with the board last month and, with full transparency, continued in three open sessions with the entire community — faculty, staff, and students — immediately afterwards. This letter is being provided to ensure that those in our community who could not join those sessions can also benefit from the context and discussion that occurred during those times. As we look ahead, we will continue to be as transparent and inclusive as possible, especially as we move into that part of the process that will lead to difficult trade-off decision-making.

The path to long-term sustainability begins with updating the university's financial framework. Specifically, we need to more accurately understand our cost structure and ensure that decision-making, incentives and risk-management activities are appropriately placed across the university. We begin to achieve this by examining the budget model that has been traditionally used. As Kermit Daniel noted in his presentation, our current practice is a hybrid model that treats only some parts of the university as RCMs (Responsibility Center Management). We also do not attempt to allocate all of the real costs of running the university to the schools, such as operations and maintenance, and central costs such as the library, student-support services, and administration. We need to develop a consistent budgeting methodology that is transparent and predictable; incentivizes appropriate decision-making; and, importantly, allocates the real indirect costs of running the university to its constituent parts. The latter is a precursor to being able to weigh both absolute and relative financial and mission contributions of our activities. This new budgeting framework will also create financial discipline throughout and will help realize operational efficiencies — by highlighting areas where we have duplication of efforts or are simply inefficient — ultimately allowing us to allocate associated savings to faculty, financial aid, programs, and so on.

The finance team is already hard at work developing a new budgeting model that we will begin to consider with the community in the coming months. Our goal is to begin to use elements of this new financial framework to develop our FY18 budget, which will be presented to the trustees for approval in spring 2017.

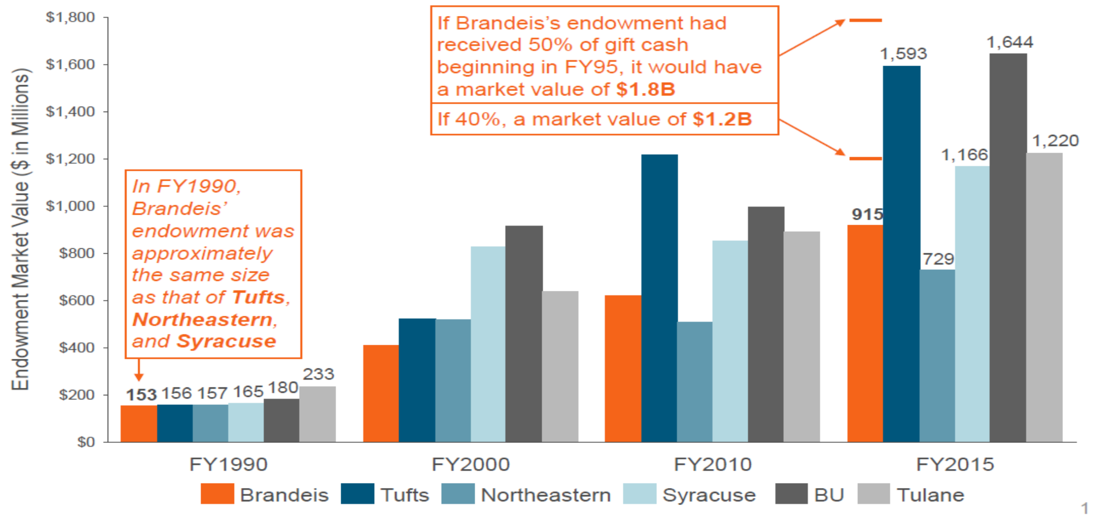
A new financial framework is a necessary but insufficient condition for resolving the structural imbalance facing Brandeis while maintaining the excellence of our education and research activities. Our new financial framework will become the foundation upon which we build multi-year budgets. As noted earlier, we need to align our financial decision-making with mission and strategy. In so doing, we will re-examine the process by which we develop work plans for next year and beyond. We want to ensure integrated development of work plans across the university, so that the individual strategies being pursued by the schools and the administration are aligned — in other words, "One Brandeis."

Note: Figures 1-4 provided by Incandscent

Figure 1: Relatively slow growth of Brandeis's endowment

Directing gifts away from the endowment further slowed endowment growth

Endowment Growth of R1s with Most Comparable Market Value



Source Data: National Association of College and University Business Officers and Commonfund Institute

Figure 2: Chronic underinvestment in the physical campus

Critical deferred maintenance is estimated to be about $220M

- Concentrated in academic and residence facilities
- Past spending too heavily weighted towards cosmetic and full-renewal – too little on critical building envelope and systems

Deferred maintenance continues to grow rapidly

- Physical campus requires about $30M - $36M per year capital spending *just to maintain current state*
- Current planning anticipates capital spending of only about $12M per year for the foreseeable future, implying about *$18M-$24M per year in added backlog*

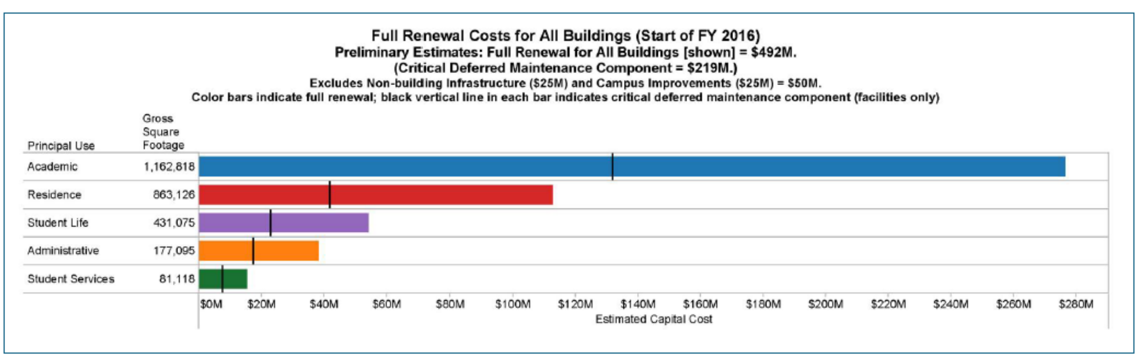
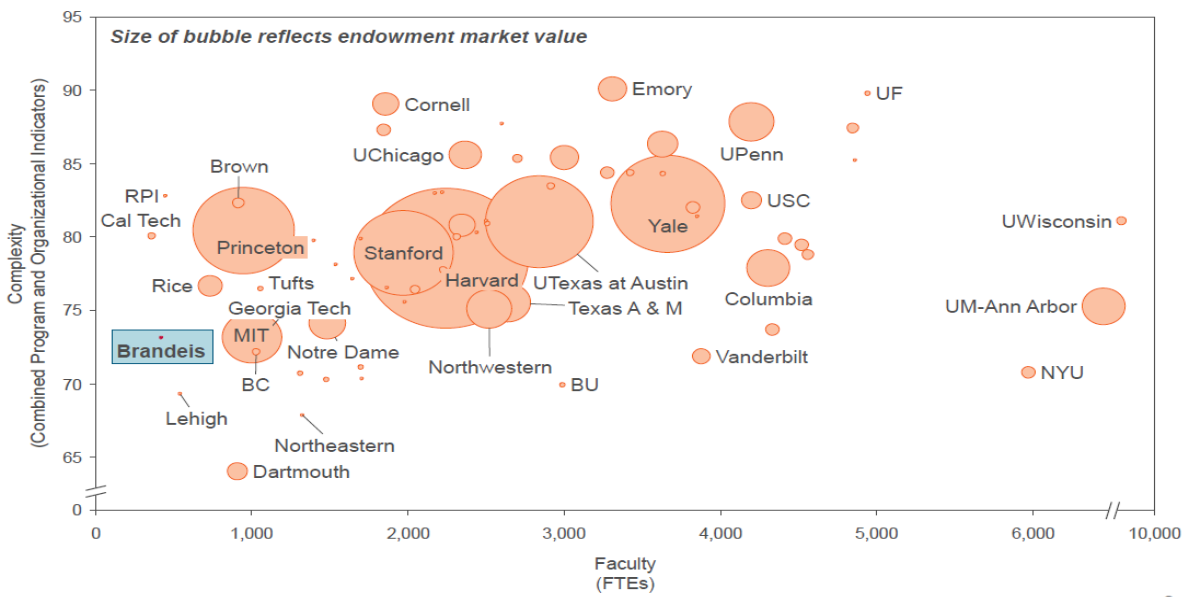


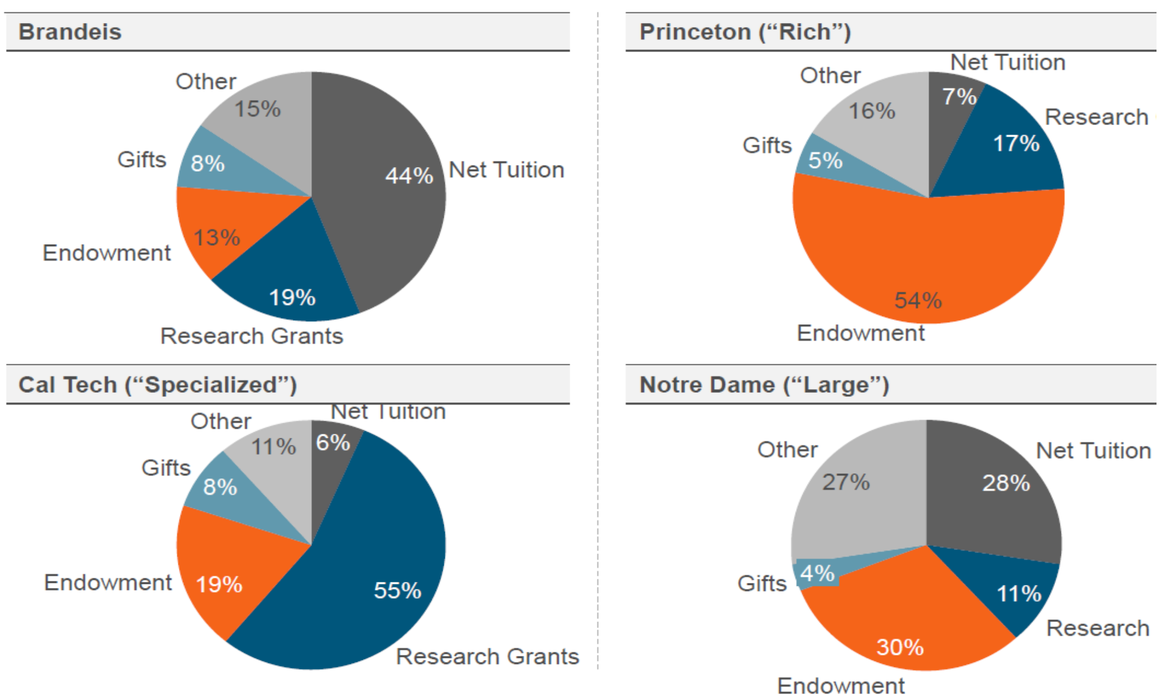
Figure 3: Brandeis is small for its level of complexity

Complex institutions tend to be large, rich, or specialized – Brandeis is an exception



Note: Program range & depth complexity index is based on the range of course offerings, where institutions that offer all courses at undergraduate, MA, and PhD levels are considered to be the most complex
Source Data: IPEDS

Figure 4: Brandeis relies heavily on tuition revenue



Source Data: Office of Budget and Financial Planning; IPEDS