



RESPONSIBILITY CENTER MANAGEMENT BACKGROUND BRIEFING

FALL 2024

Responsibility Center Management (RCM)

Management & Financial Reporting at Penn

- Internal: RCM is the managerial framework for our internal budgeting and financial reporting on schools and centers
- External: University-level GAAP (Generally Accepted Accounting Principles) reporting is the basis for external financial statements used by rating agencies, resource providers, and others

History of RCM at Penn

- Implemented in the early 1970s when the University was in financial distress
- Initially focused on controlling expense
- Evolved to encourage revenue growth as well

Principles of RCM

- Majority of direct revenue and expense is at the school/center level
- Alignment of authority and accountability at the school/center level
- Transparency regarding sources and uses of institutional funds
- Academic leaders have responsibility to advance the mission of the University within the RCM framework

Budget Model Spectrum

Among Penn's Key Peers

Centralized



BROWN



CHICAGO



DARTMOUTH



JOHNS HOPKINS



PRINCETON



YALE

Hybrid



COLUMBIA



MIT



STANFORD

Decentralized



CORNELL



DUKE



HARVARD



PENN

Responsibility Centers at Penn

Revenue Generating	Non-Revenue Generating
<i>Schools, Resource Centers, & Business Services</i>	<i>Administrative Service Centers</i>
<p style="text-align: center;"><u>Expectations</u></p> <ul style="list-style-type: none">➤ Fund the direct cost of their own operations➤ Cover their share of services provided by the administrative service centers (via allocated costs and space charges)➤ Maintain internal budget balance and build appropriate levels of reserve	<p style="text-align: center;"><u>Expectations</u></p> <ul style="list-style-type: none">➤ Fund most of operations through allocated cost and space charges➤ Maintain internal budget balance and build appropriate levels of reserve

School/Center Incentives within RCM



Keep majority of their revenue and all net income



Expected to build reserves to handle fluctuations in revenues



Cut programs that are not critical to mission



Make decisions relative to their individual markets



Hold central units accountable

Stability and Long-Term Horizon

Essential to planning in an RCM environment



Stability in the parameters

Cap and floor on most allocated cost distribution methodologies smooths growth in charges

Periodic review of distribution methodologies, with changes implemented only if they are needed to realign behaviors

Tight ranges on multi-year growth parameters

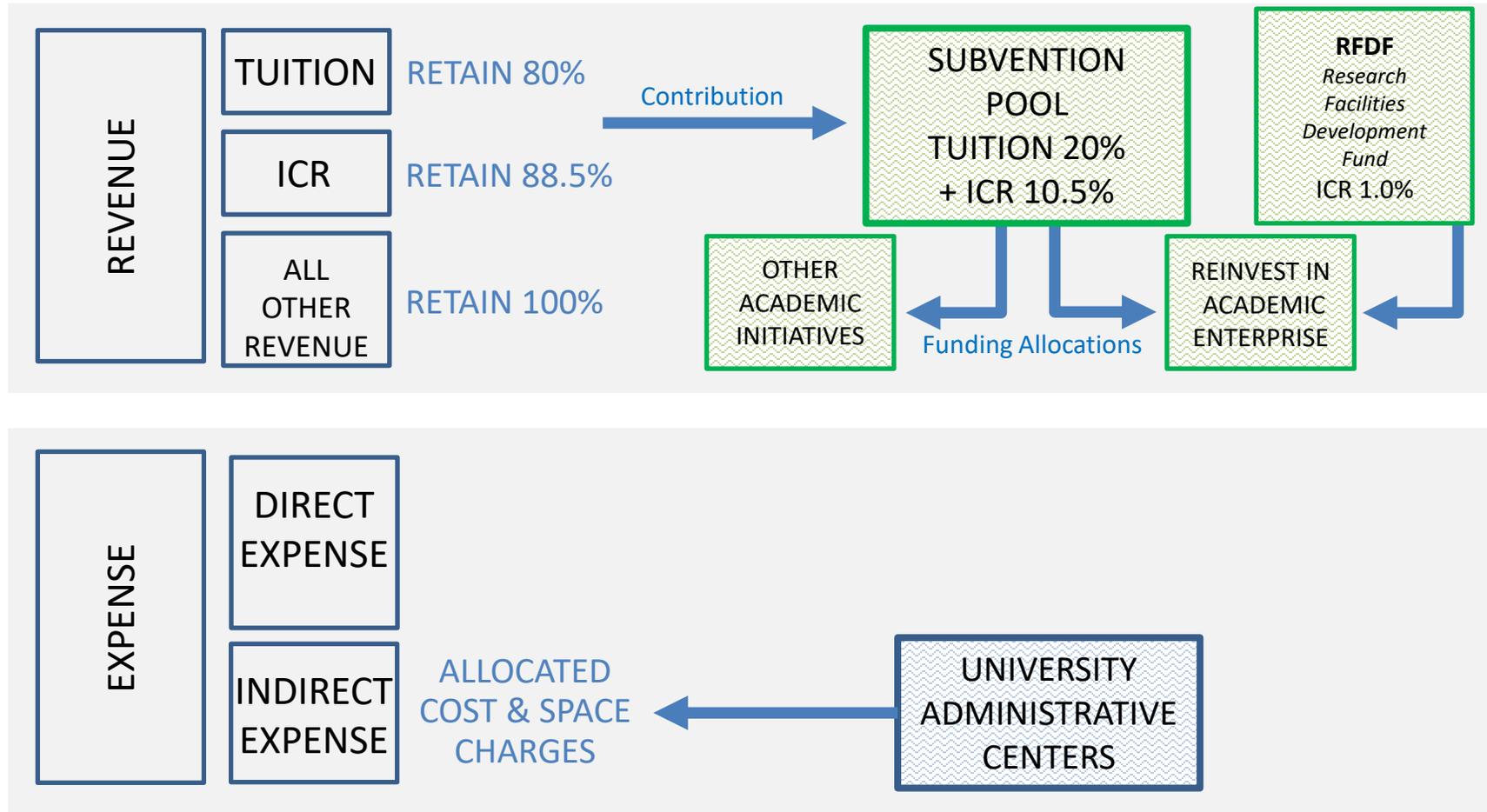


Multi-year planning horizon

Long-term implications of initiatives considered

RCM Funding Dynamics

SCHOOLS + RESOURCE CENTERS



Note: PhD tuition is not subject to Subvention Pool share.

RCM: Pros and Cons



To Be Successful in RCM

Requires ongoing engagement at school/center level and at departmental level

Leadership (Deans, VPs, Directors) need to be fiscally aware, empowered to manage, and entrepreneurial

Governance and oversight are essential



What Can Happen if not Well Managed?

Financial considerations supersede academic ones

Interdisciplinary teaching and research hindered

Competition, rather than collaboration, among academic units

Investment in unit-level plans and goals at the expense of institutional goals



Communication and Transparency Required

Maintaining open communication ensures schools and centers do not take action that impacts another responsibility center without full discussion

Who Determines Tuition, Fees, Student Aid, Admissions and Other Parameters?

University determines

- UG Tuition*
- General Fee*
- Housing & Dining Fee*
- Endowment Spending Rule*
- Employee Benefits Rate**
- Faculty and Staff Salary Increase Pool
- Ph.D. Tuition
- Discount to Tuition of UG Aid
- Allocated Costs and Space Charges
- Base Funding for Admin Centers
- Internal Borrowing and Interest Rates

*Subject to Trustee Approval **Subject to DHHS approval

Schools determine

- Professional Tuition, Aid, Admissions
- Non-Traditional UG Tuition, Aid, Admissions

Tuition Distribution

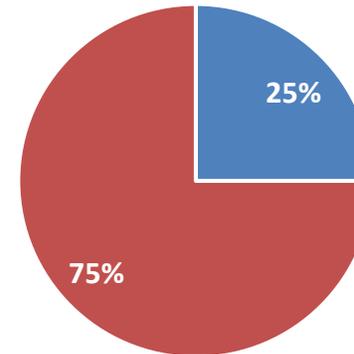
Primarily based on teaching

Undergraduate Tuition

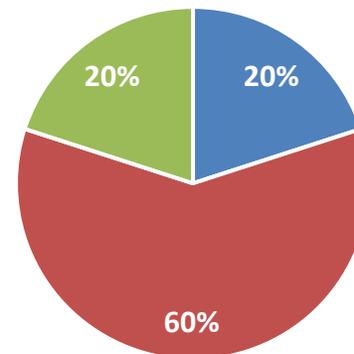
- **Tuition Block**
 - Applies to the four UG schools + two schools that administer UG majors (Annenberg & Weitzman)
 - Established base tuition level for FY19
 - Grows each year by parameter
 - Provides stability for planning
 - Recalibrated every 4 years (new base tuition level in effect for FY23)
- **Non-Block**
 - Law, GSE, SSPP, DENT, VET, PSOM
 - Based on teaching only

Graduate and Professional Tuition

- **PhD**



- **Professional**



■ Home School ■ Teaching School ■ Subvention Pool

Student Aid

Market-specific approaches

Undergraduate Aid

- **Traditional UG**
 - Grant-based aid to meet 100% of demonstrated need
 - Financial aid discount rate
 - Currently 38.5% of UG tuition net of Subvention Pool share
 - Assessment goes to UG aid pool which is administered centrally
 - Tuition is distributed to schools net of financial aid
- **Non-Traditional UG**
 - Primarily merit based
 - Centrally-incurred aid is distributed to teaching and home school

Graduate and Professional Aid

- **PhD**
 - Primarily fully funded
 - Stipends are market competitive
- **Professional**
 - Home school determines and funds aid
 - Primarily merit-based
 - Gross tuition (after subvention) flows to teaching and home school

Indirect Cost Recovery (ICR) on Research



For each \$1 of eligible* direct expenditures under federal grants, Penn currently receives an additional 62.5¢ to cover its research overhead, including space, administrative, and compliance costs

Many non-federal grants do not provide full ICR

Research ICR income is allocated at Penn as follows:

- 88.5% Dean's office of school receiving the grant
- 10.5% Subvention Pool
- 1.0% Research Facilities Development Fund (RFDF)

* Excludes equipment, student aid, and subcontracts in excess of \$25,000

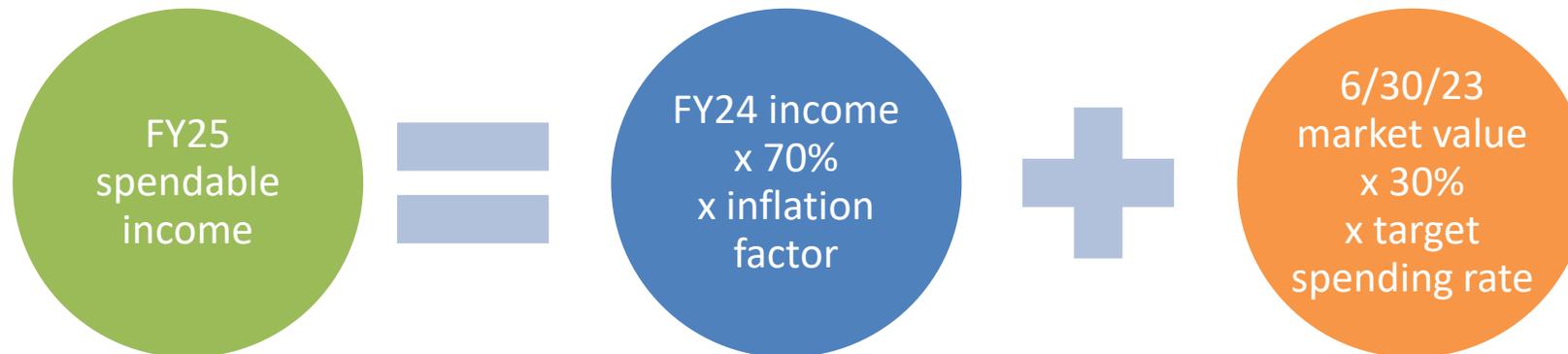
Other Revenue



- All revenue other than tuition, indirect cost recovery, and PCI income remains entirely in the school or center that generated the revenue
- **Sales and Service Revenue** and **Other Income** (e.g., clinical revenue) cover the cost of the goods or services provided; any net income can be used to support other school/center operating expenses
- **Spendable Income** from restricted endowment and **Operating Gifts** are typically subject to an indirect cost recovery policy
 - Up to 20% of an operating gift or spendable income from an endowment can be used *by a school or center* to support indirect expenses
 - While we strongly encourage full deployment of this policy, a school dean or resource center director has the discretion to exempt an endowment or gift from overhead

Endowment Spending Rule

- Penn uses a hybrid spending rule that has both income and market value-based components, weighted 70% and 30%, respectively
- This construct dampens impact of market value fluctuations on spendable income relative to formula based solely on market value
- Under Penn's spending rule, a given year's income is based on the prior fiscal year's income and the prior fiscal year-end market value, lagged one year, as illustrated below:



Subvention Pool

Funded primarily through 20% of tuition and 10.5% of grant overhead

- Subvention revenues represent only 7% of University total
- Doctoral tuition is not assessed

Allocated back to schools, resource centers, and cross-school academic initiatives as directed by President's Office and Provost's Office

- Majority of pool is committed as subvention to schools and resource centers and graduate student support to schools, with the remainder supporting other key University-wide academic initiatives

Gives President and Provost the ability to influence development and implementation of academic priorities at Penn

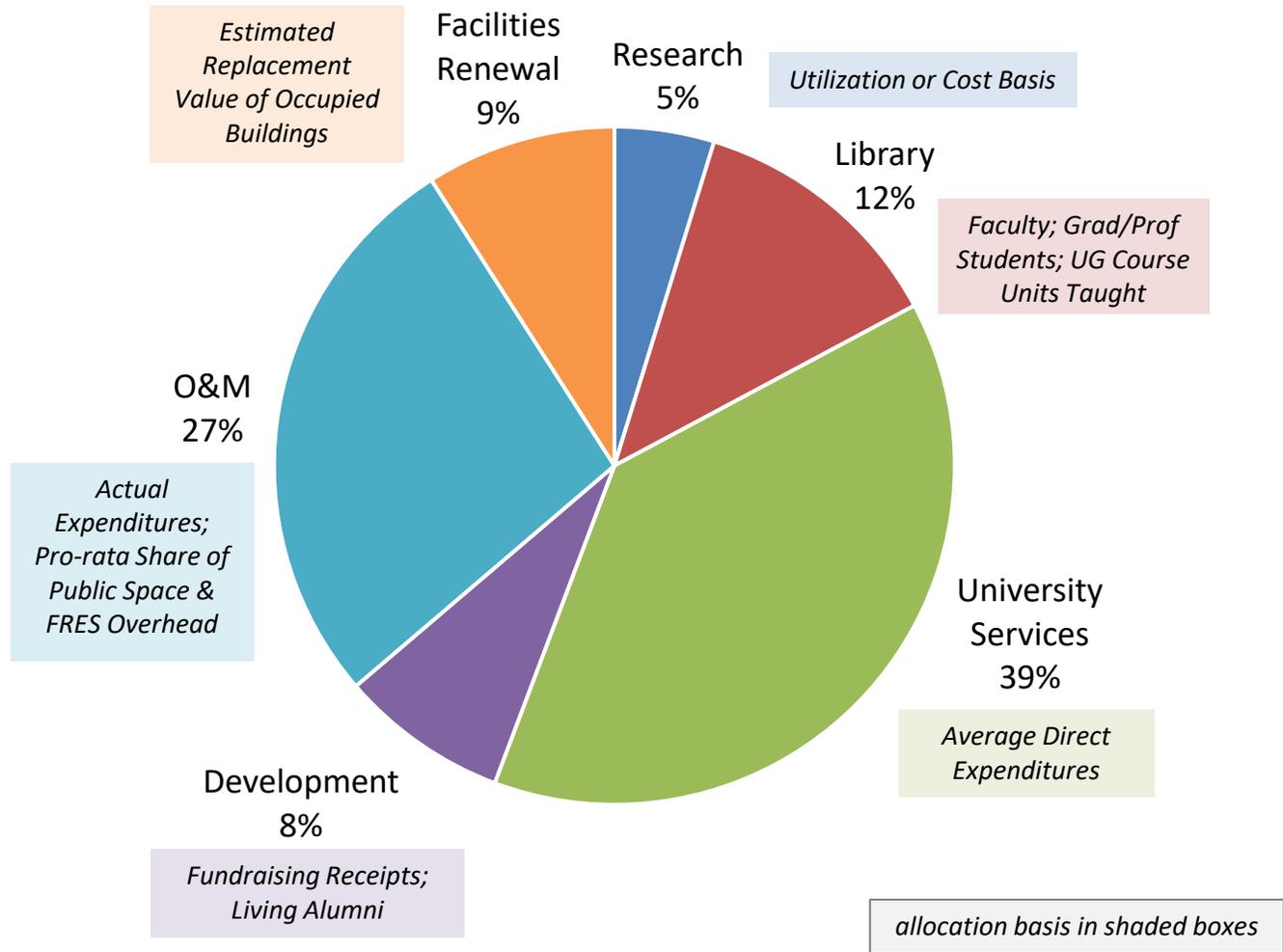
Funding of Administrative Centers

(includes President's Office, Provost Office, EVP Office, Finance, ISC, HR...)

**In order to maximize efficiency and reduce administrative costs,
Penn provides a number of services centrally**

- These services are paid for through **direct internal charges** or via **allocated cost and space charges**
 - Internal Charges: Direct billing of discrete services
 - Allocated Costs: Central services provided, charges allocated to Schools and Centers
 - Space Charges: Space is not a free good

Allocated Costs & Space Charges



RCM at Penn

Continues to evolve

Shifted central research compliance funding from ICR to allocated costs

- Too much variability in ICR revenue relative to increasing compliance costs
- Create stability in planning

Shifted a portion of IT funding from direct bill to allocated costs

- Replaced granular, time-consuming billing process with allocated charges for essential services (including network and email/calendaring)
- Little benefit to having choice for these essential areas

Changed UG tuition allocation methodology

- Gradually increased home school portion relative to teaching school portion over two decades
- Block approach for UG to eliminate barriers (real or perceived) and create stability in primary revenue source

Review allocated cost methodology periodically

- Ensure cost allocation is fair and in alignment with consumption
- Make changes where needed
- Involve schools/centers in these reviews