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TO BUILD OR NOT TO BUILD...

With facilities among the largest of campus budget categories, boards need to think strategically while staying abreast of construction finance issues.

LAST YEAR, A WEALTHY CLEVELAND TRUSTEE and philanthropist became outraged by cost overruns on a building for which he had donated the preponderance of funding. He laid the blame at the doorstep of the university's governing board, which he said was responsible for the "rotten mess" of poor management, frequent administrator turnover, and a construction price tag more than double the original estimate. He demanded that the board resign, and he withheld donations not only from the university but from the city's charities, pending a university governance overhaul.

However one might regard the specifics of this high-profile imbroglio, it is a reminder of the ultimate responsibility of boards to monitor the performance of management. The episode also suggests a need for boards to be more familiar with the issues involved in conceiving, commissioning, and monitoring a campus building project.

The concrete responsibilities of a governing board for a substantial facilities project will depend largely on the size and maturity of the institution and the nature and expertise of its staff. But in any situation, the board is ultimately responsible for several critical components.

Involved at the Start. When a board is thinking about a new project, the first question to ask is whether there is any way to *avoid* building a new building. Are there solutions that might address the problem without incurring the extraordinary expense of construction? Can functions or schedules be shuffled to rebalance underused areas with overused ones? Can an existing building be transformed more cheaply than a new one can be built?

If construction appears warranted, be aware that few projects run perfectly smoothly. A complex project requires a series of board actions. The more thoroughly trustees understand the entire picture from the start, the more

• BY SAMUEL B. FRANK •

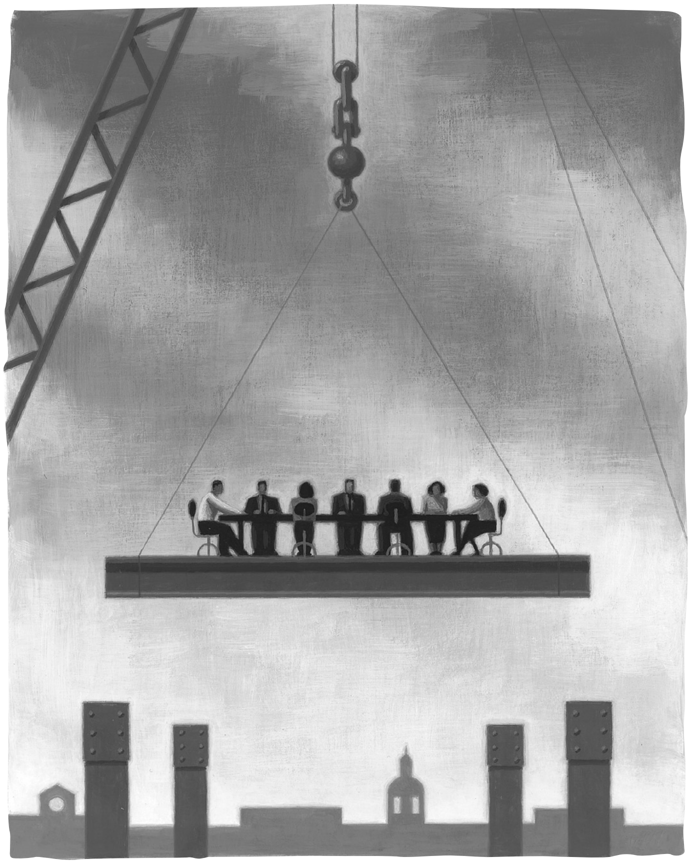
likely it is that subsequent discussions will unfold productively and according to plan.

The most ambitious projects may need to allow for phases if the pace of fund-raising does not keep up with the full project cost. Instead of revisiting a decision of whether or not to build at each phase, it is best first to get a comprehensive endorsement for the project's goals and means and then to require periodic budget review and approval at pre-set milestones. The trap of considering each phase of a project as if it were a new project to be freshly authorized risks turning a half-achieved objective into a political football.

After personnel-related costs, facilities typically represent the second largest operational costs in most institutions and the greatest investment of its assets. Yet boards generally consider facilities questions as technical ones to be delegated to those with construction, mechanical, or engineering knowledge.

Most boards have facilities committees that screen major maintenance expenditures before board authorization and oversee staff performance in ongoing maintenance and capital improvement programs. When these same committees are asked to guide and monitor the development of new facilities, they often show little mastery of the critical fiduciary issues—strategic, conceptual, and financial. (See the box on page 26.)

Dealing with these larger questions is less a matter of having special expertise than of raising the appropriate issues for discussion with the board as a whole. Once the discussion is framed appropriately, specialized expertise can be acquired as needed.



Hidden Costs. When a *construction cost* figure is mentioned (and it almost always is the figure mentioned), the first response from a board should be to ask for the total *project* cost. Construction costs cover only the amount paid to the general contractor for the direct materials and labor of construction.

"Soft" costs, the expenses other than those paid to the contractor, can be defined in various ways, but they usually are substantial enough to influence the board's thinking—or to provide a nasty surprise later. Soft costs include fees for architects, engineers, and other designers, consultants, and technical specialists. They can amount to 15 percent or even 20 percent of construction for a mid-range project, with additional costs for site acquisition, furnishings, special equipment, moving, temporary storage facilities, and various other one-time costs of getting settled into a new or renovated building.

A large institution generally will assign management costs from the facilities department to project overhead; a small institution will need to hire project-management staff for a substantial project.

Contingency allowances address unanticipated conditions or opportunities that are identified only as a project evolves through design and construction. It's a good idea to build in a generous contingency allowance during the initial stage of a project, especially in a renova-

Illustration by Scott Roberts

tion where some conditions may be indeterminate at the outset. This creates the possibility of recapturing any unused allocations later on. When construction begins, a contingency of 10 percent to 15 percent of projected construction cost is typical, but if budgeting is completed before design begins (a prudent idea), the figure should be as high as 25 percent to 30 percent to accommodate some of the details the initial broad vision fails to anticipate.

Operating-cost and revenue projections for a new facility also can help a board evaluate a project's feasibility. If an old building is being replaced, substantial savings in utilities and maintenance can be expected. A new building may provide the opportunity to increase various revenues. On the other hand, a new facility may mean staff increases and higher debt service. While small compared with construction costs, these operating budget items have ongoing rather than one-time impact and can make or break the case for a new building.

The most difficult area is probably the cost of proper maintenance. When budgets become tight, the path of least resistance often is to simply defer maintenance, a practice that essentially is equivalent to spending the institution's endowment (or perhaps more like keeping the endowment in cash in an office safe).

An appropriate maintenance budget for a mature physical plant should be from 1.5 percent to 3 percent of the appraised value of the institution's property. If such sums are not budgeted annually, the deterioration of facilities eventually becomes visible, eroding the institution's image and substantially increasing the eventual cost of correction.

A good alternative to risking future deferred maintenance is a maintenance endowment. This can be a difficult added challenge for those raising funds for a building. But to the extent it is feasible, creating such a fund can relieve the institution of the insidious cumulative operating budget burden that comes with additional facilities. Securing a maintenance endowment as part of a comprehensive campaign, especially in good economic times, can avoid an annual operating budget challenge. A figure of 20 percent of construction costs often is used for a maintenance endowment, but a fully funded figure is likely to be more than twice that.

A Board Member's Blueprint

Fiduciary responsibilities for trustees in the realm of campus buildings can be summarized in three axioms:

Know the issues. No amount of experience or knowledge in the administration will exonerate the governing board from its fiduciary responsibilities related to buildings. There are some decisions about the commitment of funds that only the board can make. Trustees should have a conceptual understanding of the building projects they will be dealing with and an awareness of the common pitfalls they can avoid.

Think strategically. The cost alone requires facilities to be measured carefully against the institution's strategic plan. New buildings should address necessities rather than merely gratify egos. But they can do much more: convey values, establish an institutional brand identity, and shape morale. The governing board is ultimately responsible for ensuring that these issues are raised and addressed and that the institution's facilities are used as a major strategic asset.

Keep in touch. The facility-creation process does *not* run itself. Trustee participation in oversight can raise critical questions of prioritization, focus, and budget before expensive mistakes get too far to correct without major cost or disruption. This becomes especially important in light of the governing board's responsibility for fund-raising. For capital campaign leadership, there can be no better preparation than participation in building planning, design, and construction management. —*S.B.F.*

Facilities creation is clearly a shared responsibility between governance and management, and sheltering the board from early understanding can cause serious repercussions later on.

A Board's Unique Role. The scale, breadth, and rarity of facilities projects and the strategic thinking, fund-raising, and financial oversight required during this process make erecting buildings something of a special case of joint responsibility between the governing board and management. For most institutions, creating new facilities is far from a core management competency. Even a large institution's facilities department addresses only the technical and operational aspects of getting a facility built.

For any institution, the critical processes of conceptualizing, planning, programming, designing, funding, and monitoring the costs of facilities require participation of constituencies beyond senior administration, and this participation starts with the board. Only a governing board has the breadth of experience and sophistication—and the standing—to ask the critical, probing questions about budget, necessity, priorities, strategy, and identity that are required to shape a successful project.

The foundation of stewardship is the board-approved strategic plan. At the next level, a physical master plan takes the strategic plan as a guide into the realm of physical planning. Only after completion of that two-level groundwork can an individual building be planned, programmed, and budgeted wisely. And only the governing board can insist on that sequence.

The extent of actual board participation in strategic and master planning as well as design and budget overview is a matter for the judgment of individual boards. All of these tools, however, are part and parcel of proper stewardship of mission and finances; they are excellent vehicles for instilling increased involvement and commitment to the institution on the part of trustees. They also prepare board members to be well informed and convincing when they solicit donors for capital gifts.

One obvious strategic objective might be to enhance identity and visibility through thoughtful representation of the values of the institution and the messages it wishes to convey in a building's design. This is more difficult than commissioning a fashionable architect to design a "signature" building. Rather than looking to an architect's signature and brand identity, a more effective approach would be to attend directly to the institution's brand.

Conserving Trustee Time. The simple message here is that the creation of new facilities—and the stewardship of existing ones—carry an important governance responsibility that goes to the essential fiduciary role of a board. The strategic, financial, and development considerations require a board to invest some time in advance of and during any process of facilities creation to avoid stress, expense, and missed opportunities.

Administrators generally try, appropriately, to protect a governing board's time and to insulate the board from too much involvement in management issues. However, facilities creation is clearly a shared responsibility between governance and management, and sheltering the board from early understanding can cause serious repercussions later on in such areas as commitment to fund-raising, informed participation in cost control, and approval of operating budgets.

Even an hour or two of a board meeting agenda or a half-day a retreat is enough to orient the board to the critical issues. It also will give trustees a fair sense of the outside expertise they may wish to engage to ensure a smooth and effective planning process that will minimize risks while maximizing impact. ◆

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