

The University of Chicago

Office of the President

12-13-27

Miss Servis: I think this is the gift letter of which you should have received a copy. The original has gone to the City Office. It was presented at the last meeting of the Board. Apparently you received a copy of the acknowledgement of the check, and possibly copy of Mr. Arnett's letter of November 17, though no note was made on the letter.

Q.S.L.

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TREVOR ARNETT  
61 Broadway  
Rm 3018  
New York City

G O P Y

November 9th  
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My dear Max:

I am writing to confirm our understanding with regard to the work among foreign students at the University of Chicago, concerning which I wrote to Mr. Woodward on October 11th that I was authorized to offer a contribution to the University for this purpose up to but not exceeding \$10,000., the exact amount to be determined after conference with you.

As a result of the conference you and I had in New York on October 28th, I understand that the amount of the contribution from New York sources to the University is to be \$9000 for the fiscal year commencing July 1st, 1927.

In the very near future, I am told, a check for \$9000 will be sent to you in payment in full of the above appropriation. It is understood that this contribution is towards the total budget estimated at \$10,265., the remaining amount being supplied by the University of Chicago.

I was sorry that a cold which descended upon me some days ago prevented me from going to Chicago last week as I had planned.

With cordial regards, I am

Sincerely yours,

(signed) Trevor Arnett

President Max Mason  
The University of Chicago  
Chicago, Illinois

TA:RE







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1976-27

# COLLEGE FINANCE

By

TREVOR ARNETT, A.B.

*Auditor of the University of Chicago*



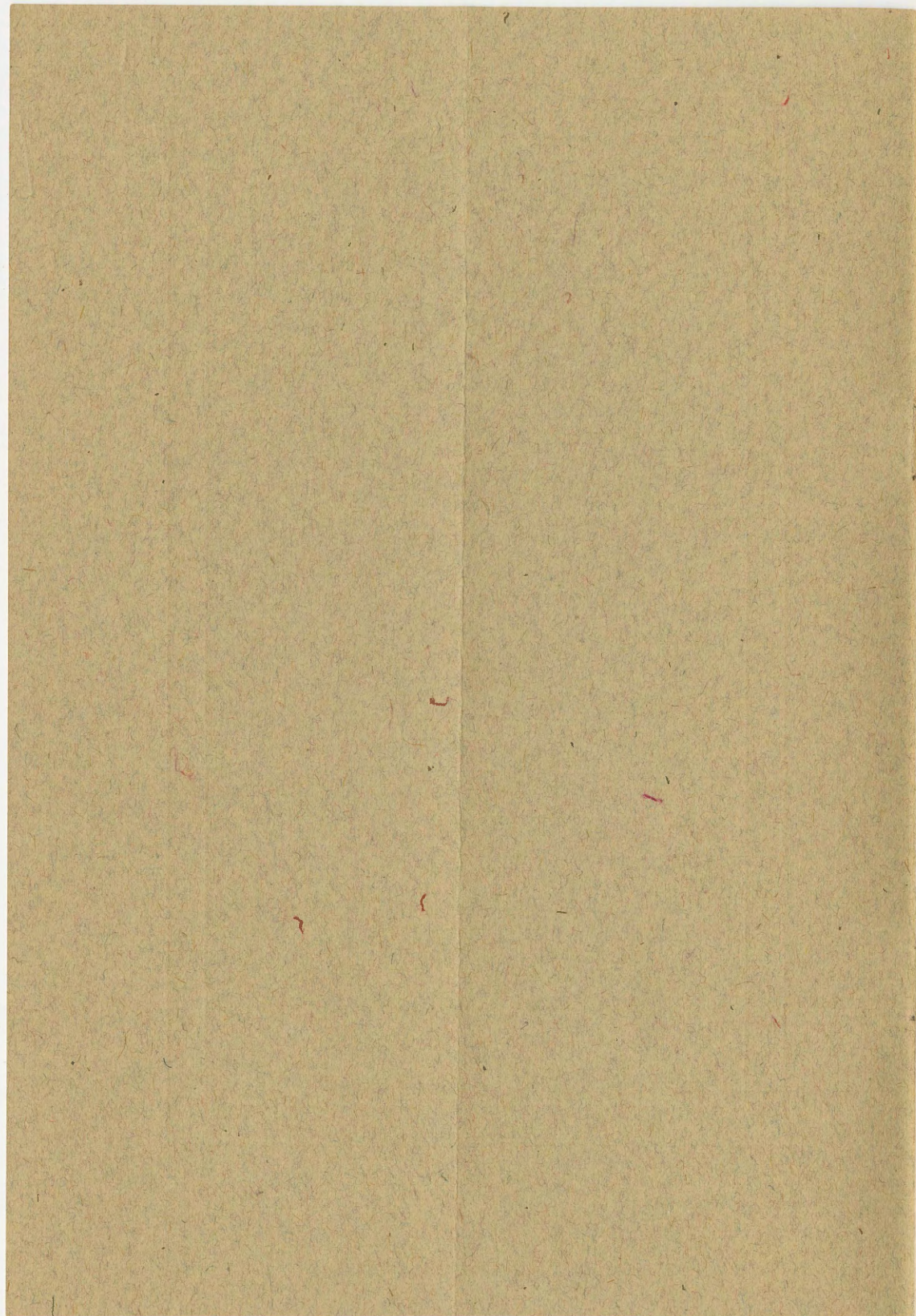
ISSUED BY THE BOARD OF EDUCATION

OF

THE NORTHERN BAPTIST CONVENTION

1915







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## COLLEGE FINANCE

**C**OLLEGE Finance, as now generally understood, is a new science. College presidents, trustees, and friends are beginning to realize the need of conducting college business in the most approved manner. Formerly the business side of the college was given little attention. The accounting officers frequently combined their fiscal duties with those of teaching, and were chosen, not because of their especial fitness for accounting, but because their time was not all taken up with their academic work, or perchance because the college felt that it could not afford to pay for the services of a good accountant. There were also other reasons for this condition: first, the poverty of the colleges, because of which there was very little business to look after, and, secondly, the scarcity of people who understood fully the peculiar financial needs of a college.

All this is now being changed very rapidly. The unprecedented growth in the material resources of educational institutions has rendered imperative a proper administering and caring for them and has led to the development of a new science, that of educational accounting. Moreover, the need of a standard in order to comply with requirements of the great philanthropic foundations, such as the General Education Board and the Carnegie Boards, has been a great factor in this development. In fact it is a pretty good test of an institution's accounting methods if it can answer readily and accurately the questionnaires of these foundations.

Under present conditions, the position of the business manager or accounting officer of a college is one of great responsibility. It devolves upon him to see that nothing is done under the guise of accounting which may tend to cover up the use of endowment funds for current purposes because of temporary exigency. He must also make clear to the president and trustees the meaning of any action of this kind on their part that may be suggested, and firmly persist until they see the result of any such action. There are many instances where endowment funds have been dissipated, by loaning them to the current account to be repaid at a future time, a "reasonable" rate of interest being allowed thereon; or by using them as security for loans from banks for the payment of current expense.



It is the duty of the accounting officers to see that this is not done, and thus to save their institutions from an experience which has brought others into trouble, and probably rendered their trustees legally and perchance criminally liable. I do not mean that the accountant should necessarily be belligerent, but he should have knowledge and courage enough to maintain his point until the trustees are also convinced.

It also devolves upon him to keep his accounts in such a way and present them in such a manner that the president and trustees are constantly informed as to the financial condition of the college, and to make the reports in such a clear and unmistakable way that all concerned may fully understand without having to spend several hours in figuring them out.

One of the distinguishing features of higher education in this country is that it is not fully supported by the fees received from students. In state institutions the deficit is made up by state appropriations, and in private institutions by income from endowments and donations. The tendency is for this deficiency to increase as the expense of higher education becomes greater. It follows therefore that the care and treatment of endowment funds are becoming increasingly more important. There are certain fundamental principles to be observed in this connection:

Since endowments are permanent funds, the income from which can alone be used, it is imperatively necessary that the principal fund be kept intact and not diminished. Otherwise the fund may be dissipated and the purpose for which it was given fail of realization. Moreover, if the principal is dissipated, the institution, from the nature of the case, has no opportunity of making it good. Therefore the primary rule to be observed in investing endowment funds is "safety first." It is unnecessary to indicate what constitutes a safe investment, because conditions vary in different parts of the country, but first mortgages conservatively placed are perhaps the safest. It is easier to define what investments should not be made in order to comply with the rule of "safety first." For example, anything of a speculative nature must be avoided. This would exclude mining stocks, stocks in companies to promote a patent, securities of a company which had not yet demonstrated its stability. Since knowledge is the chief thing in determining the value of an investment, it follows that investments which are local are likely to prove the safest, because



all the conditions are likely to be known to the trustees, and any circumstances which may arise to change the value are sure to be easily ascertained. Where institutions are situated in large cities, it is advisable to invest a proper proportion of the funds in real estate fees. First, because a good income is assured, and, secondly, the corporation being perpetual, it is likely to realize a large gain in the natural increase of value incident to the growth of the city. Certain universities have been very fortunate in this respect. In the case of bonds, bought at a premium, care must be taken to write off the premium during the life of the bond, so that at maturity the endowment funds be not depleted. On the other hand, in the case of bonds bought at a discount, it is considered more conservative not to appreciate them, but to wait until they are paid in full at maturity and then decide whether to add the amount of discount to the endowment as an increment or put it into income. The main thing is to keep in mind the sacredness of the principal and see that it is not diminished.

The second thing to be done in the case of endowment funds is to see that the greatest income possible is obtained, always keeping in mind the safety of the principal. Where there are large funds to invest, this thoughtfulness can often be exercised by a judicious selection of different kinds of securities, and a proper diversification at differing rates of interest, so that the resulting average return is good. On large endowments a difference of one-eighth of 1 per cent may sometimes mean the difference between a surplus or deficit for the year.

Another result to be sought in connection with endowments is stability of income. All well-regulated colleges and universities operate on a budget system. Under this plan, to which reference will be made later, it is necessary to know pretty accurately before the year begins what the income for the coming year will be, in order that appropriations may be made for the needs of the several departments. It is also to be remembered that a standard of appropriation for a department having been established, it is almost impossible to reduce it. It can be increased, but not easily decreased. Therefore, it is better in the long run to have an income slightly less than the average, but stable, than to have a high rate of income for a few years, and establish a high rate of expenditure, and then to suffer a reduction of income and be confronted with the almost impossible task of reducing expenses, or of incurring a deficit.



The fourth consideration in making investments is to have the income payable at different times during the year. Salaries must be paid each month and supplies must be purchased, and therefore it is advisable to invest in securities whose interest dates cover each month of the year. In other words some securities should be purchased whose interest dates are January and July, some February and August, some March and September, and so on. Otherwise the college must secure most of its income six months in advance or suffer the alternative of borrowing money at interest in order to provide for the needs of the college as they mature.

The proper treatment of endowment funds on the books of account is of importance. It is best to keep three ledger accounts for each fund, one showing the amount of it, one showing the investment of it, and the third showing the income received from the various investments. At all times the difference between the amount of the investments and the fund itself should be cash on hand represented by cash in the bank or in the office. The ledger account with the income will of course be closed out at the end of the fiscal year, because the income will be used for current expenses.

In order to prevent the possibility of endowment funds being used for current expenses, I strongly urge the plan of keeping the endowments and funds for special purposes in a bank account separate from that in which the funds for current purposes are kept. Time and again endowment funds have been temporarily or unwittingly used by a college for paying salaries because all the funds have been kept in one account, and when it was necessary to make restitution it has been found difficult to do so.

When an endowment fund is received, a full record of the conditions and purposes of the gift should be made on the minutes of the Board. If the gift is paid in cash, a reference should be made on the cash book to the minute book, or if the gift is made in securities a proper reference should be made on the journal. In the case of a gift paid in securities the figure at which they should be entered on the books of account should be the market value as of that date. If the securities are bonds or stocks, the market quotations are usually available, but if they are real estate or buildings they should be appraised by a competent authority. Securities of a doubtful value are frequently carried on the books of an institution at a face or gift value altogether out of harmony with the real value. The evil of this



course is twofold: first, it puts an inflated value on the college endowment, and when these holdings are eventually sold a big reduction in value is necessary; and secondly it makes the average return from investments appear lower than it really is.

The question is often asked whether it is better to keep the investments of each endowment fund separate, or invest all the funds together and divide the income pro rata among the funds. There are arguments in favor of each plan. Probably a combination of the plans in certain instances is best. Where a fund is large enough to admit of a sufficient variety of investments to secure safety, it should be kept invested separately. But where the fund is small, it is better to combine it with other small funds and invest them all together, the income being divided pro rata. However, if a donor makes a gift in securities with the request that they be retained, such a gift should be kept in a separate account, so that if the securities depreciate in value it would not operate to reduce the amount of other endowment funds.

The budget scheme for handling the operating receipts and expenditures of universities and colleges is coming into general use. It is peculiarly adapted to their needs, and in fact is very necessary in the case of all eleemosynary institutions, where the needs and opportunities are so great and the amount that can be undertaken is limited only by the amount of income available. In making a college budget, the first step to be taken is to make a careful estimate of the income for the coming year. In doing this there are certain rules which can be followed to advantage: first, with respect to the income from invested funds, where the funds are invested in good mortgages, bonds, and stocks, the income can be easily determined. In the case of real estate, the experience of the past few years should be taken as a guide, cognizance also being taken of any factors which in the coming year may tend to increase or reduce the income, such as leases already made at a higher rate, increase in the tax rate, need of extra repairs, etc. Where securities fall due before or during the year for which the estimates are being made, necessitating reinvestment, it is wise to allow a short time, say a month, for reinvestment, and then estimate the rate of interest at a figure low enough to be safe, so that if the investment is made at a different rate it will be a higher rather than a lower one.



Secondly, with regard to the estimate of fees from students, experience has shown that it is a good rule to take the figures for the last completed year, and use them unless the college is in possession of some information which indicates that the income will be less, in which case allowance must be made for this reduction. On the other hand, even if there is good reason to suppose that the income in any instance will be greater, it is not wise to increase the figures of the estimate, the object being, of course, to make an estimate of income which in the aggregate, at all events, will be exceeded rather than not realized. It is important that the estimate of income shall be realized, because the appropriations are made to the various departments of the university or college before the opening of the year on the basis of these estimates. It is reasonably certain that a department will spend all of its appropriation, and, therefore, if the income falls short, a deficit at the end of the year is almost inevitable.

In making up the budget of estimated expenditures, it will be found advisable and very useful to divide the expenses into sections covering the principal natural divisions. For example, in one section should be grouped the expenditures for the administration and general expenses of the college, in another the expenditures relating to the physical upkeep and care of the buildings and grounds, in still another those covering the cost of instruction and departmental expense, and in another the cost of the library and books. Further sections may be used, depending on the circumstances and needs of the college. The expenditures under each section should be divided into several accounts, as seems best suited to the case, and as far as possible complete details of each item should be included. This is advisable because it gives an opportunity to the officer in charge to watch each expenditure during the year, to see that it does not exceed the estimate, and further, when the record of the actual expenditures is kept in detail, it furnishes an accurate basis for making the budget for the succeeding year. Not only is it possible to keep an eye on the expenses when the budget is kept in the manner indicated, but an opportunity is afforded for making comparisons between the economy or waste of various departments.

After the budget estimates are all made and have been adopted by the Board of Trustees, they furnish the guide and limit to expenditures by the administrative officers and heads of departments. It will be found best to have a ledger for each year, in which there is



opened an account with each principal item in the budget, the expenditures as they are made being entered in this account. Since the amount allowed any department is a fixed sum, it is necessary to see that the sum is not exceeded unless the board makes an additional appropriation. The most effective manner to do this is to require an order or requisition to be made on the administrative officers or executive committee for each expenditure which should be approved by them before the expenditure is incurred. The cost should be estimated carefully and entered against the appropriation as a charge. The amount available for future use is the difference between the total appropriation and the total of the estimated approved orders. If this method is followed, there is no danger of unwittingly over-expending the appropriation, unless the estimates of cost are carelessly made. If no record is made of the orders placed but only of the bills paid, it is almost a certainty that in some cases the appropriation will be exceeded when all the bills are received and paid.

It is a good plan to balance all the ledgers monthly, including the budget ledger, to make statements showing the progress of the college, comparing carefully the receipts and expenditures to date with the estimates, and if they differ much to take steps to correct the tendency. A budget will not run itself, and it is of very little use to make estimates of expenditures and then take no steps during the year to see that they are not exceeded. It requires constant attention and care and frequent reports for comparison and information to make the budget plan effective. After a budget has been kept for some years, the information is at hand, so that an accurate estimate for the coming year may be made.

To sum up, the two essentials to be especially remembered in a budget are, first, a conservative estimate of receipts, and, second, constant watching of expenditures.

The reference already made to the advisability of balancing the ledgers each month suggests the matter of the financial report or statement of the college. It is of the utmost importance that the trustees of a college be kept fully and frequently informed as to the financial condition of the institution. The principal cause of trouble with the finances of a college is that the trustees are not taken into full confidence and informed of all that is going on. Probably the best way to do this is to make a monthly report. This should not



be so condensed that it is unintelligible, nor so diffuse that a picture of the principal features can not be had.

In a college report the first fact that a trustee wants to know is how the operations for the year are resulting. Is there a surplus or is there a deficit? Next he wants to know what the condition of the college is as to assets and liabilities, and whether the current assets are in excess of the liabilities; and, finally, what the total fixed assets are, what the total endowment is, and in what securities it is invested. Now to be readily understood, the answers to these questions should be in totals only, to begin with; on the following pages of the report the details of the totals may be given. The point to be always kept in mind is that the salient features or mountain peaks of the report should appear first, and then upon further investigation the details should be found. Frequently a mass of detail is given first, and the reader becomes confused or disgusted before he gets to the principal features of the report. There are certain general facts which almost everyone interested wishes to know about the financial condition of a college: first, the cash and current assets and expenses; second, the amount and nature of its plant, that is, the buildings, grounds, equipment, and furniture; third, the amount of endowment and funds for special purposes and how they are invested; and, fourth, its liabilities if any. Practically all the items which ordinarily would appear in a balance sheet can be put into one or other of the foregoing classes. As has already been said, these items should appear on the balance sheet in totals only, so that the one reading it will get easily and quickly a clear picture of the college's condition. The subsequent pages should show in detail the items making up the totals which appear on the balance sheet and should be referred to on the balance sheet by cross-reference. If the plan here suggested be followed, one can proceed from the total to the detail, and so on to the farthest extent.

The lucidity of the financial reports of a college is markedly increased by a comparison of the conditions a year ago with those of the present year, showing in appropriate columns the amounts of increase or decrease. Absolute figures rarely give one much idea of what is going on. The mind seems to need a standard or measure with which to compare. Moreover, it is possible to note at once the trend of affairs by a reference to these columns of increase or decrease. If the receipts and expenditures are increasing, the college is doubtless in a good condition, especially if the receipts are increasing faster than



the expenditures. If the expenditures are increasing more rapidly than the receipts, matters are not so favorable, and it will doubtless be necessary to scrutinize them closely in order to find the cause and if possible remove it.

In making the financial reports and keeping the trustees constantly informed of the condition of the college, the accounting officer is able to be of great service, though heretofore this function has been very much neglected. Copies of the monthly reports should be mailed to each trustee, and at the same time a letter should be sent calling the attention of the trustees to any significant features of the reports. For example, if the dining-hall is running at a loss, the trustees' attention should be called to the fact, and an explanation given if possible of the cause and whether it may be remedied soon; if it cannot be remedied, the trustees should be given an opportunity to look into the matter themselves and take such steps as they think advisable to remedy the difficulty.

Since a considerable portion of the revenue of a college comes from fees paid by students, the method of collecting and recording them is a matter of great importance. Most colleges and universities have found that the most satisfactory way is to have the student pay in advance. Perhaps the best plan is to require every student to pay his fees within the first five days of the term, or make a satisfactory arrangement with the proper officer with respect thereto. This plan, of course, puts a great strain on the collecting office in those five days and requires a flexible scheme of handling the students' accounts so that the cashiers shall know what they ought to collect, and not have to take time to find out while the student is at the window.

The practice is prevalent in some institutions of accepting notes due several years hence in payment of tuition and other fees from students. A considerable portion of these notes is never paid, and since they are unsecured there is very little chance of enforcing their payment. There is also a great reluctance on the part of the college authorities to sue former students, from sentimental and other reasons. As a result of the practice the college is in reality giving free tuition to a number of students, for which it gets no credit, and in the meantime is deceiving itself by thinking that it has a collectible asset in the form of notes receivable. It is much the better plan to insist that all students shall pay their fees in advance except those for which the college has provided scholarships. In a few cases where the cir-



cumstances are exceptional, students' notes may be taken in payment of fees, but even then they should, if possible, become due within a year. When a student leaves his alma mater with all his financial obligations to her paid in full, experience has shown that he becomes a much more loyal and enthusiastic alumnus than when the opposite is true and the college authorities find it necessary to urge him to pay his notes as they become due. The advantages of requiring students to make cash payments in advance are, therefore, twofold: first, the college has the money to use for its expenditures, and, second, it gains in loyalty and affection of the students.

When a student has been allowed time to pay his fees, he should be required to meet the payment within the time specified. Failure to pay fees within the first five days of the term, or, in the case of deferred payments, within the time specified, should result in a fine for late payment, the purpose of the fine being to induce the student to pay promptly. In case the fees are not paid, the deans should be notified and the student not allowed to remain in class. The co-operation of the deans is necessary in enforcing these rules, but under a rigid enforcement of them the amount of uncollected tuition at the close of the year will be a negligible quantity.

It will be found advisable to have all payments by students made to the financial officer of the college, and not in any case to the instructor, whether for laboratory fees, breakage, material needed, or what not. This plan relieves the instructors and also concentrates the handling and care of funds in one place and makes it easier to check and account for them.

At the close of each year the accounts of the institution should be audited by an auditor entirely outside the college and the board, in order to see that all receipts are properly accounted for, and that all the disbursements are duly evidenced by receipted vouchers, and that they are made under the authority of the board. In addition to checking the accounts, the securities owned and cash on hand should be counted and the number and amount carefully compared with the books of account to see that they are all in order and in the possession of the proper officers. The auditor should make a full report to the trustees, and the annual financial report should bear the certification of the auditor. Such an annual audit is a protection to the trustees and gives the patrons and friends of the institution confidence in its management.



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