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Lessons for Academic Leaders from Modern
Restructuring Practice

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Abstract

Financial distress has hit higher education. More and more universities and colleges are facing existential challenges as the competition for a dwindling number of students has put a strain on revenues. Unlike leaders in other industries, the presidents and chancellors of a financially distressed institutions of higher education cannot explore the possibility of a Chapter 11 filing under the Bankruptcy Code to restructure their obligations so that they align better with their revenues. Federal law prohibits Title IV loans – the lifeblood of virtually every university and college – from being made to students who attend a school that is in an insolvency proceeding. Yet academic leaders can take lessons from modern Chapter 11 practice: they can, in advance of financial distress, ensure that their boards of trustees have members who can provide advice to the schools' leaders as to the difficult choices that they face; they can employ restructuring professionals who have experience in turning around operations without a bankruptcy filing; finally, given that many of these institutions have relatively few creditors, they can attempt to negotiate a restructuring support agreement that would restructure the schools' debts without a bankruptcy filing. The options available to leaders in the higher education space are not as robust as the options available to leaders of private enterprise, but they do exist and can be useful in confronting financial distress.

Lessons for Academic Leaders from Modern Restructuring Practice

Robert K. Rasmussen¹

Colleges and universities have a complex relationship with chapter 11. Those institutions that operate on a not-for-profit basis (not all schools do) cannot be forced into bankruptcy via an involuntary petition. The Bankruptcy Code (the “Code”) prohibits such filings against corporations that are not “moneyed, business, or commercial” in nature, and thus not-for-profit schools are immune from being hauled into bankruptcy court without their consent.² The Code itself, however, does not put any further restrictions on the ability of institutions of higher education to access its provisions to address issues of financial distress. That said, it is common knowledge that chapter 11 provides no meaningful relief to an institution seeking to restructure its debts and continue to educate its students.

The de facto restrictions on access to chapter 11 lie elsewhere. Federal law prohibits the disbursement of federal loans to an institution that has filed for relief under the Code.³ Changes in the student lending market in recent years have created a system where the majority of students at virtually all colleges and universities who borrow money to finance their studies do

¹ J. Thomas McCarthy Trustee Chair in Law and Political Science, University of Southern California Gould School of Law. From 2007 to 2015, I served as the Dean of the USC Gould School of Law. I would like to thank Tobias Rushing for excellent research assistance on this piece.

² 11 U.S.C. § 303(a) (2012). Furthermore, if public schools are considered public agencies or instrumentalities of the state, they can only proceed under chapter 9. *See* 11 U.S.C. § 109. An entity cannot be forced into chapter 9, and can only pursue chapter 9 relief if the state has authorized it to do so. *Id.*

³ For a description of this limitation as well as an argument questioning its merits, see Matthew A. Bruckner, *Bankrupting Higher Education*, 91 AM. BANKR. L.J. 697 (2017) and Scott F. Norberg, *Bankruptcy and Higher Education Institutions*, 23 AM. BANKR. INST. L. REV. 385 (2015).

so from the federal government. The federal government stepped into the funding gap that arose at the onset of the Great Recession, guaranteeing loan students up to the full cost of attendance.⁴ Other providers of student loans left the market after this action, and the federal government continues to be the primary funder of higher education. This reliance on federal funds means that, for any given college, if federal loans are not available to attend that institution, students by and large will choose to go elsewhere. To illustrate the effect that losing access to federal loans can have, consider the fate of ITT Educational Services. This for-profit education provider had been in business for fifty years. Due to concerns with how it was running its operations, the Department of Education decided to stop loaning money to students who wished to attend its schools. ITT closed its doors two weeks after it lost access to federal funds.⁵

While the federal loan program makes chapter 11 unavailable as a practical matter to schools that seek to continue as a going concern, chapter 11 can be used by a college or university that has decided to shutter its operations.⁶ The capital structure of even a small

⁴ It is unclear whether this policy will remain in place, at least for graduate and professional students. Recent legislation introduced as part of the reauthorization of the Higher Education Act would cap the amount that most graduate and professional students could borrow at \$28,000 per year. See Andrew Kreighbaum, *Reversal on Graduate Lending*, INSIDE HIGHER ED, Dec. 11, 2017, <https://www.insidehighered.com/news/2017/12/11/house-gop-higher-education-overhaul-would-cap-graduate-lending-and-end-loan>. Such a cap, or even a cap at a higher level, would have profound effects on the financial stability of many graduate and professional programs.

⁵ Danielle Douglas-Gabriel, *ITT Technical Institutes Shut Down After 50 Years in Operation*, WASH. POST, Sept. 6, 2016, https://www.washingtonpost.com/news/grade-point/wp/2016/09/06/itt-technical-institutes-shut-down-after-50-years-in-operations/?utm_term=.5440745c095c.

⁶ See, e.g., Andrew Scurria, *Dowling College Files for Chapter 11 Bankruptcy*, WSJ, Nov. 29, 2016, <https://www.wsj.com/articles/dowling-college-files-for-chapter-11-bankruptcy-1480464552>; Stephanie Gleason, *Corinthian Colleges Files for Chapter 11 Bankruptcy*, WSJ, May 4, 2015,

school can be complex, and the school can use chapter 11 to monetize its physical plant, endowment and intellectual property, and then to sort out which creditors get what proceeds.⁷ What cannot be done, however, is to file a petition under chapter 11 as part of an attempt to rehabilitate the school and enable it to continue to pursue its mission of education.

It is far from clear that such limitation on the access to the bankruptcy court is wise public policy.⁸ For the purposes of this paper, I want to put this issue to one side. Assuming that chapter 11 remains unavailable as a practical matter for schools facing financial distress, I want to focus here on what lessons leaders of higher education can learn from restructuring practices applied in the realm of for-profit, non-educational business corporations. Ever since the passage of the Code, many companies have been able to restructure their debts without filing for bankruptcy, as have many schools of higher education. Moreover, recent years have seen a transformation of how businesses deal with financial distress. Creditors, especially senior creditors, can often dictate the course that a business restructuring takes.⁹ An entire profession of turnaround managers has been created.¹⁰ These professionals parachute into a

<https://www.wsj.com/articles/corinthian-colleges-files-for-chapter-11-bankruptcy-1430746291>.

⁷ For example, Dowling College filed for chapter 11 to wind down its affairs. It chose to use chapter 11 because the chapter 11 process would assure buyers that they were getting clean title. Its Oakdale campus, which was secured by bond debt, sold for \$26.5 million in April 2017. See Scurria, *supra* note 6.

⁸ I find the arguments put forward by Professors Buckner and Norberg persuasive. Indeed, many of the devices discussed for restructuring outside of bankruptcy would be even more effective if the school had a credible threat to initiate a chapter 11 proceeding.

⁹ See Robert K. Rasmussen & Douglas G. Baird, *Private Debt and the Missing Lever of Corporate Governance*, 154 U. PA. L. REV. 1209 (2006); Harvey R. Miller & Shai Y. Waisman, *The Creditor in Possession: Creditor Control of Chapter 11 Reorganization Cases*, 21 BANKR. STRATEGIST 1 (2003).

¹⁰ See Douglas G. Baird & Robert K. Rasmussen, *Chapter 11 at Twilight*, 56 STAN. L. REV. 673 (2003).

company in order to tackle its problems, with the goal of making tough decisions needed to stabilize, and possibly save, the business as a going concern. Boards of directors have become increasingly attuned to the strategies available to a business that runs into financial pressures. Prearranged deals among the company and its various creditor groups have become commonplace.¹¹ Devices such as restructuring support agreements and plan support agreements have allowed affected parties to craft solutions in advance of bankruptcy filings.¹² The tools described here can well be deployed to combat financial distress, even without access to chapter 11.

One note of caution, however, needs to be sounded at the outset. It is true that private restructuring practices can provide models and lessons for leaders in higher education, but such tools are no panacea. Bankruptcy law exists to solve a collective action problem.¹³ Disparate creditors pursuing their collection rights could force a viable concern to liquidate and chapter 11 provides a forum to prevent such action. The problem of uncoordinated creditors, however, is not coextensive with the problems of financial distress that many schools are facing. Just as chapter 11 cannot solve all the problems that private companies face – as the current spate of retail bankruptcy liquidations illustrates – not all the problems faced by colleges and universities can be solved through debt restructuring. For many institutions, the problems lie more on the operational side rather than having a capital structure that needs adjustment. To

¹¹ See *id.* at 678; Douglas G. Baird, *Bankruptcy's Expanding Universe*, 87 TEMPLE L. REV. 975, 978 (2015).

¹² See Douglas G. Baird, *Bankruptcy's Quiet Revolution*, (Coase-Sandor Working Paper Series in Law and Economics No. 755, 2016).

¹³ The canonical work remains Thomas H. Jackson, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* (Harvard 1986).

the extent that there are fewer (and poorer) students seeking a four-year undergraduate degree,¹⁴ there will be fewer students enrolled in such schools. Moreover, financial pressures may lead some schools with strong reputations to expand their market share at the expense of other institutions. To be sure, there is always the prospect of innovation as schools that witness a decline in traditional students pursuing traditional degrees will have an incentive to seek out new, previously underserved, students and create new degrees designed to deliver education at differing points in peoples' careers. Still, many schools will lack the resources or insight necessary to enter new markets. The decrease in students will put financial pressure on a number of schools, and it may well be that some schools will not make a go of it in the new competitive landscape. Restructuring tools can undoubtedly aid many schools as they confront turbulent times. Active boards, innovative leaders, and tough decisions can save some schools. They will not, however, ensure that all schools will survive.

I. The Economics of Higher Education

A. The Structure of Higher Education in the United States

At a certain level of generality, higher education does not differ from other businesses. Like other businesses, the providers of higher education sell a good – in this case education – to willing customers. To remain viable, the business has to generate revenues that exceed its costs. The salutary purpose of higher education¹⁵ does not grant it immunity from the basic

¹⁴ See *infra* note 28 and accompanying text.

¹⁵ See Jonathan R. Cole, *THE GREAT AMERICAN UNIVERSITY: ITS RISE TO PREMINENCE, ITS INDISPENSABLE NATIONAL ROLE, WHY IT MUST BE PROTECTED* (Public Affairs 2009); Fareed Zakaria, *IN DEFENSE OF A LIBERAL EDUCATION* (Simon & Schuster 2015).

laws of economics. Innovative schools such as Black Mountain College can be long on intellectual capital but short on financial capital.¹⁶ An abundance of the former cannot compensate for the lack of the latter. Colleges and universities, at least those that are private, tend to be relatively simple businesses. They produce a product – education – with a mixture of hard assets – land and buildings – and human capital – faculty and staff. They pay for these expenses primarily through tuition and contributions from the school’s supporters – *i.e.* current donations and returns on endowments donated in the past, which add to a school’s revenue. While endowments at some schools, such as Harvard and Yale, are substantial, the reality for most schools is that they have little in the way of revenue outside of their core business of education.

Higher education in this country is very decentralized. In 2014, there were over 4,600 schools of higher education in the United States. Taking a more fine-tuned look at the structure of higher education, one sees important differences from other industries. Perhaps the most significant difference is that there are three types of providers – private, not-for-profit schools; public schools; and private, for-profit schools.¹⁷ Perhaps the most salient of these to the general public is the private, not-for-profit sector. The nation’s oldest colleges and universities are private, not-for-profit entities. Schools such as Harvard, William and Mary, Yale, Penn, Princeton, Columbia, Brown, and Dartmouth all predate our country’s founding. These colleges and many others have, by any measure, shown a remarkable degree of longevity. No private

¹⁶ See Helen Anne Molesworth, *LEAP BEFORE YOU LOOK: BLACK MOUNTAIN COLLEGE 1933-1957* (Yale University Press 2015); *BLACK MOUNTAIN COLLEGE: EXPERIMENT IN ART* (Vincent Katz et al. eds., MIT Press 2013).

¹⁷ See Bruckner, *supra* note 3, at 11.

company in this country can rival their span of existence. Of course, not all private, not-for-profit schools have roots that stretch back centuries; many are of more recent vintage. Regardless of their age, however, private not-for-profit schools are the most common type of higher education schools in the country. During the 2015-16 academic year, there were roughly 1,300 four-year private, not-for-profit schools.¹⁸

The organizational structure of these schools is fairly standardized. They are run by a CEO, most often called a president or a chancellor. The ultimate legal authority for these schools, though, rests in a board of trustees. The school operates under a charter granted by the appropriate state, and state law requires ultimate authority to be vested in the board. The board can delegate day-to-day responsibilities to the president/chancellor, but it must remain the final arbiter of major decisions. The board is a self-perpetuating body. Unlike directors of a corporation, trustees of a university cannot be removed by an outside constituency. They may have term limits written into the school's governing documents, but the trustees are the ones who pick their successors. There is no fear of a proxy contest in higher education. The election of directors in a private company is the subject of much current debate and activity. Corporate governance advocates vigorously debate whether it should be easier for outsiders to replace current directors.¹⁹ Not so with not-for-profit schools. While trustees take their jobs seriously,

¹⁸ See *Characteristics of Degree-Granting Postsecondary Institutions*, NATIONAL CENTER FOR EDUCATION STATISTICS (May 2017), https://nces.ed.gov/programs/coe/indicator_csa.asp.

¹⁹ Issues such as staggered boards and proxy contests dominate the corporate law literature. See, e.g., Lucian A. Bebchuk, *The Myth that Insulating Boards Serves Long-Term Value*, 113 COLUM. L. REV. 1637 (2013) (arguing that devices that decrease the ability of outsiders to oust current directors decrease firm value); Martin Cremers & Simone Sepe, *The Shareholder Value of Empowered Boards*, 68 STAN. L. REV. 67 (2016) (arguing that, for certain firms, protections that make it difficult for outsiders to replace directors can enhance firm value). For reasons explained in the text, these issues do not arise with not-for-profit schools.

they do not have to worry about removal by an outside group that believes the organization needs to rethink its current operating plans.

The number of layers of bureaucracy that any higher education institution has below the president/chancellor depends in large part on the size and structure of the school. Universities with multiple schools and colleges tend to have provosts who oversee deans who, in large units, oversee department chairs. In smaller colleges, there may be one administrator between the faculty and the president. Decisions as to a school's academic programs tend to be the product of consultation and dialogue. Faculty members cherish their ability to have input into the direction of their unit. For many faculty, the contributions they make in this decision-making process represent an important part of the legacy of their careers. Most, if not all, schools depend on the willingness of faculty members to make institution-specific investments toward the common goal. The American Association of University Professors ("AAUP") – the trade association for professors – touts its commitment to academic freedom and shared governance as two of its primary objectives.²⁰ Another key objective for the group, which can well be at odds with restructuring needs when a school hits financial shoals, is the promotion of job security for faculty.²¹

The academic program, however, does not constitute the entire operations of any school. There is also the administrative side of running the school, consisting at least of a CFO who

²⁰ "The mission of the American Association of University Professors (AAUP) is to advance academic freedom and shared governance. . ." About the AAUP, *American Association of University Professors*, <https://www.aaup.org/about-aaup>.

²¹ See *id.* (Describing that another mission of the AAUP is "to promote the economic security of faculty"). For an insightful discussion of how tenure rights would be treated in a Chapter 11 case, see Matthew Adam Bruckner, *Terminating Tenure: Rejecting Tenure Contracts in Bankruptcy*, 92.2 AM. BANKR. L.J. (forthcoming 2018).

oversees the budget and an admissions professional charged with attracting and enrolling the student body. Some schools add other professional, non-academic personnel, such as athletic directors, communications specialists, general counsel and development professionals. The faculty, however, traditionally have little input into the administrative side of the school's operations. Few faculty members could tell you what the tuition discount rate is at their institution, describe the admissions model the school uses, or explain the intricacies behind fund-raising numbers. The administration sets the tuition and enrollment goals, with little to no faculty input.

While private schools lead the list in terms of the number of institutions of higher education in the United States, when one measures institutions by the numbers of students educated, the prize goes to the nation's public schools. In the spring of 2017, over 7.6 million students attended a public, four-year college.²² Another 5.4 million attended public, two-year programs. These numbers are roughly four times the number of students attending private, not-for-profit schools.²³

The funding and governance of public schools differ markedly from those of their private-sector counterparts. Public schools get some (though in recent years a declining) percentage of their revenue from the public fisc. Like private schools, they are led by a chancellor or a president, and have internal organizations similar to their private counterparts. The ultimate authority, like in the private setting, rests in a board. This board, however, differs significantly from those overseeing private, not-for-profit schools. In most states, an elected official

²² See NATIONAL STUDENT CLEARINGHOUSE RESEARCH CENTER, TERM ENROLLMENT ESTIMATES: Spring 2017 4, <https://nscresearchcenter.org/wp-content/uploads/CurrentTermEnrollment-Spring2017.pdf>.

²³ *Id.*

appoints the board of a public institution. In four states, voters directly elect the board members. In either scenario, however, there is a connection between the board and the voters of the state, and there is the threat of removal.

There is another salient difference as well. Private, not-for-profit schools tend to have one or at most two campuses. They are not geographically diversified. In contrast, public schools are often organized into systems that encompass many campuses across the state. For example, the University of California system has ten separate campuses. While these schools are often part of a larger organization, that organization is contained within the boundaries of a single state. While they are all located in the state, the head of the system has the ability to allocate resources among the schools, a flexibility that her private, not-for-profit counterparts lack.

The third sector of American higher education – private, for-profit schools – has taken aim at what many view as a complacent and inefficient market. For the past few years, there have been bold predictions that the for-profit schools were going to displace the more staid business model of higher education. For example, Minerva, a start-up from the Bay Area led by a CEO who had great success in e-commerce, seeks to compete with the most selective schools at roughly half the price.²⁴ Many observers believe that MOOCs – Massive Open Online Courses – are the way to bring higher education to the masses. While they may be pursuing different strategies, as a group, private for-profit schools boast that they are going to unseat the long-standing purveyors of the four-year degree. By and large, the disruption and transformative

²⁴ See Graeme Wood, *The Future of College?*, ATLANTIC (Sept. 2014), <https://www.theatlantic.com/magazine/archive/2014/09/the-future-of-college/375071/>.

change that these efforts have promised has yet to materialize, though it is fair to say that these efforts continue to evolve. Amazon lost money for years before becoming one of the world's leading companies that is now in large part responsible for the rapid decline of traditional retail outlets.

In the spring of 2017, four-year for-profit schools educated just under one million students. For-profit institutions are organized like their for-profit business counterparts. They are led by a CEO, who answers to a board of directors. These directors, in turn, are put in place by, and can be removed by, the shareholders of the company. Unlike their not-for-profit competitors, these for-profit institutions are funded by investors who seek a return on their investments. The motivations of those who enter this investment arena may be laudable – providing education to more people at a lower price – but the returns they seek are financial as well. The cheerleaders for these schools embrace the profit motive. For them, it is market discipline spurred by potential financial rewards that emboldens the risk taking that will lead to new, innovative, and disruptive ways of delivering education.

Private, for-profit schools can range from single schools to wide-ranging enterprises with operations in multiple states. The University of Phoenix has dozens of campuses spread across several states. In recent times, these schools have seen their operations altered extensively. Periods of aggressive expansion have been followed by painful contraction. The leaders of these entities focus on the health of the overall operation and are quick to close under-performing units. Whereas roughly three to five private, not-for-profit schools have closed on

an annual basis in recent years, the University of Phoenix alone has closed over one hundred of its campuses with a single decision to streamline its operations.²⁵

B. Sources of Financial Distress

Until recently, higher education in the United States enjoyed continued robust growth. Higher education, it seemed, was impervious to the economic cycle. During good times and bad, tuition increased relentlessly. Parents heard for decades that the path to a successful and rewarding life for their children wound through college. If anything, the volume of this message increased over time. Leaders of higher education faced challenges but they were the challenges of competing in a growing market. Leaders struggled with questions such as: How do you increase market share? How do you inspire your faculty? What new amenities need to be added? How can the educational program be enriched? They occupied a market position not unlike the big three automakers in the 1950s. They competed against each other, but there was no sense that they faced an existential threat.

Today, however, higher education is facing the winds of financial distress. Endless growth is being replaced by thoughtful retrenchment. State schools have been particularly hard hit. State and local government revenues plunged during the Great Recession. As their budgets shrank, one of the frequent targets was higher education. To be sure, as these headwinds have dissipated in recent years, states have begun to increase their investments in their schools. Even with these recent increases to college budgets, however, state funding, adjusted for

²⁵ See Joseph Flaherty, *University of Phoenix Phasing Out Campuses; Current Students Not Affected, School Says*, PHOENIX NEW TIMES, Sept. 25, 2017, <http://www.phoenixnewtimes.com/news/university-of-phoenix-phasing-out-more-campus-9722920>.

inflation, is billions of dollars lower today than it was at the onset of the Great Recession.²⁶ But such pain is by no means confined to the public sector. The Great Recession brought an increased focus on the costs of higher education for all types of schools.²⁷

One reason that all three types of providers of higher education have been under pressure in recent years is the declining numbers of traditional students applying to college. The number of students graduating each year from high school began a projected decade-long stagnation in 2013.²⁸ While the number of high school graduates is expected to increase from 2024 to 2026, after that brief hiatus, another decline is expected. Indeed, the predictions are that from 2027 to 2032, there will be fewer high school graduates each year than there were in 2013. In addition to this decline, the high school graduates in the coming years are expected to be more diverse and less affluent than their predecessors. These changes have already put financial pressure on some schools, and these pressures will continue.

Not only does each college or university have to contend with a shrinking pool of potential students, but it has to contend with competition from fellow schools. As the pool of prospective

²⁶ See Michael Mitchell et al., *A Lost Decade in Higher Education Funding*, CENTER ON BUDGET AND POLICY PRIORITIES, (Aug. 23, 2017), <https://www.cbpp.org/research/state-budget-and-tax/a-lost-decade-in-higher-education-funding>.

²⁷ See, e.g., Steve Odland, *College Costs Out of Control*, FORBES (Mar. 24, 2012), <https://www.forbes.com/sites/steveodland/2012/03/24/college-costs-are-soaring/#34de831e1f86>; Dylan Matthews, *Introducing 'The Tuition is Too Damn High,'* WASH. POST, Aug. 26, 2013, https://www.washingtonpost.com/news/wonk/wp/2013/08/26/introducing-the-tuition-is-too-damn-high/?utm_term=.18751c9d13cc; Marc Joseph, *It's Too Expensive to Go to College Anymore*, HUFFPOST (Nov. 17, 2013), https://www.huffingtonpost.com/marc-joseph/its-too-expensive-to-go-t_b_3935231.html.

²⁸ See Rick Seltzer, *High School Graduates to Drop in Number and Be Increasingly Diverse*, INSIDE HIGHER ED (Dec. 6, 2016), <https://www.insidehighered.com/news/2016/12/06/high-school-graduates-drop-number-and-be-increasingly-diverse>.

students shrinks, it may well be that every school trims its enrollment. Under this scenario, a school might tighten its belt a bit and finds ways to make do with less, but that is not the only possibility. Some schools—those with demand that exceeds supply—could well increase the number of students that they admit. At a minimum, they may decide to keep enrollment steady, thus taking a larger share of the smaller pool. Under either scenario, schools further down the food chain may confront an ever-dwindling pool. The pressure to date has been felt perhaps most acutely in the for-profit sector of higher education. Their enrollment has declined by more than twenty percent over the past three years.²⁹

The decline in students has, not surprisingly, lead to a decline in pricing power on the part of the schools. Colleges and universities tend to have large fixed costs. As in the case of overcapacity in the airline or hotel business, an unfilled seat or room saves little in terms of marginal cost. Those running the operations recognize that it is better to generate some revenue than none. Thus, when faced with a decrease in demand, they have discounted their product. Indeed, the average discount rate on freshmen tuition at many private, not-for-profit schools hovers around fifty percent.³⁰

²⁹ Part of this decline can be attributed to the Obama Administration's decision to increase oversight in the for-profit sector. The Trump Administration is seeking to loosen some of these regulations. See Valerie Strauss, *For-profit Colleges May Be Headed for a New Boom Cycle – Thanks to the Trump Administration*, WASH. POST. (Dec. 11, 2017), https://www.washingtonpost.com/news/answer-sheet/wp/2017/12/11/for-profit-colleges-may-be-headed-for-a-new-boom-cycle-thanks-to-the-trump-administration/?utm_term=.92627bc59fdc.

³⁰ See Rick Seltzer, *Discounting Hits New Highs*, INSIDE HIGHER ED (May 16, 2017), <https://www.insidehighered.com/news/2016/05/16/discount-rates-rise-yet-again-private-colleges-and-universities>.

Higher education faces much more than a cyclical downturn in student enrollment. Higher education has been in the cross hairs of Silicon Valley for over a decade. The hope was that new, start-up ventures could provide cheaper education. The goal was both to broaden education as well as to disrupt incumbents. Technology has changed many industries; many have predicted that technology will have an equally dramatic impact in higher education. One does not have to endorse some of the bolder claims to recognize that leaders of higher education have to have a strategy for dealing with this threat.

One response to this threat is that schools have moved more of their product online. Some schools have been able to generate significant revenues through this approach. For example, more than five years ago the University of Southern California reported that it was generating more than \$100 million in revenue on an annual basis through online graduate education.³¹ Starting up an online program, however, requires a significant upfront investment, the type of investment that is out of reach for struggling, and especially small, schools.

The other response that the higher education sector has made has been to increase the size of the pool of prospective students by openly welcoming and aggressively recruiting students from other countries. In the 2016-2017 academic year, there were more than one million foreign students enrolled in American colleges and universities. This comprised over five percent of the total national student population.³² While there has been noticeable growth in this segment over the past decade, it may well be that the number of foreign students looking

³¹ See Merrill Balassone, *USC Embraces Online Graduate Education*, USC NEWS (Sept. 17, 2012), <https://news.usc.edu/41400/usc-embraces-online-graduate-education/>.

³² See *International Student Enrollment Trends, 1948-2016/17*, INSTITUTE OF INTERNATIONAL EDUCATION (2017), <https://www.iie.org/Research-and-Insights/Open-Doors/Data/International-Students/Enrollment>.

to come to America has stabilized.³³ The reality is that, although the inflow of international students has buoyed the fortunes of many schools, it seems clear that there is not an inexhaustible supply of such students willing to pay the price of an American education.

More troubles are on the horizon. Since the onset of the Great Recession, the federal government has been willing to lend to all students the full cost of attendance. Both the Obama Administration and Congress have proposed lowering the maximum amount that students could borrow, but this legislation has not gained much traction. Few expected meaningful action to be taken until after the 2016 presidential election. Congress is now turning its attention to this issue. Recent legislation introduced in the House of Representatives would cap the amount that graduate and professional students could borrow from the federal government in any given year at \$28,500. The extent to which private lenders would be willing to fill the gap between \$28,500 and what each student needs is unclear. It is safe to assume, however, that private lenders would not be willing to fund all students, regardless of the student's or their parents' financial status. Not surprisingly, non-profits dedicated to higher education are aggressively lobbying for changes to the legislation,³⁴ but few if any observers think that the current system of federal funding for higher education is going to remain as it is.

A decrease in the availability of funds would directly translate to fewer students applying to schools. To be sure, private lenders would cherry pick the more attractive credit

³³ See Stephanie Saul, *Fewer Foreign Students Are Coming to U.S., Survey Shows*, N.Y. TIMES (November 13, 2017), https://www.nytimes.com/2017/11/13/us/fewer-foreign-students-coming-to-us.html?_r=0.

³⁴ See, e.g., *AccessLex Institute Calls for Substantial Improvements to House Higher Education Act Reauthorization Legislation* (Dec. 4, 2017), <https://www.accesslex.org/xblog/accesslex-institute-calls-for-improvements-to-house-hea-legislation>.

risks, but many prospective students would lack the means to finance their education. While there are ways to ameliorate some of the harm that would be caused by the decrease in funding sources, few expect that the demand for education would remain unchanged. A drop in demand, coupled with the other threats facing higher education, would likely tip more schools into financial distress.

II. Modern Chapter 11 Practice

As more schools and colleges face financial pressures, leaders of higher education will look for new and creative solutions. One obvious place to look is corporate restructuring practice. In the eyes of many, the United States has the most robust system for dealing with financial distress.³⁵ At the heart of our country's reorganization practice sits chapter 11. Chapter 11 is first and foremost about adjusting debt. Its primary purpose is to scale back a company's debt so that the business can continue to operate rather than shutting down. The basic intuition is that the operations are generating, or with sensible adjustments can generate, a going-concern surplus. The enterprise is worth more if kept together than if it were liquidated in a piecemeal fashion. While it may be in the interests of creditors as a group to see the business continue, collective action problems prevent such a solution.

Given the practical inability of a college to seek bankruptcy relief and remain in operation, it is important to recognize that not all corporate restructuring is done through a bankruptcy proceeding. One study suggests that in the latter part of the Twentieth Century,

³⁵ As one example of this, last year Singapore amended its restructuring laws by enacting reforms which were based heavily on the principles underlying chapter 11. See Paul Apathy & Emmanuel Chua, *Singapore Enacts Key Restructuring Law Reforms*, (March 16, 2017), <https://www.herbertsmithfreehills.com/latest-thinking/singapore-enacts-key-restructuring-law-reforms>.

roughly seventy percent of distressed firms sought to restructure their debts outside of bankruptcy.³⁶ Over time, the proportion of debtors who utilized out-of-court restructurings as compared to chapter 11 reorganizations has shifted, with an increasing number choosing out-of-court workouts. Thus, even firms that have access to chapter 11 are often able to resolve their financial distress without a bankruptcy filing.³⁷

In thinking about what role restructuring practice could play in addressing the financial distress of colleges and universities, it is necessary to have some sense of the capital structure of schools. Larger schools often tap the public markets for debt. Approximately five hundred schools in the United States have issued public debt. These bonds have generally been a safe bet for investors. Since 1986, there have been only three colleges or universities that have defaulted on their bonds. Even Sweet Briar College, which famously announced that it would close because it believed that it could not service its debt in the future, has remained open. Standard and Poors has upgraded its bonds.³⁸

Out of more than 4,000 schools of higher education, however, the vast majority do not issue public debt. This does not mean that they are debt free. Rather, their debt is privately held. Typically, the school has a mortgage on its real estate. This type of financial restructuring can be handled without resort to bankruptcy.³⁹ Small colleges are like small businesses. Most of

³⁶ See Stuart C. Gilson et al., *Troubled Debt Restructurings: An Empirical Analysis of Private Reorganization of Firms in Default*, 27 J. FIN. ECON. 315 (1990).

³⁷ See Stuart Gilson, *Coming Through in a Crisis: How Chapter 11 and the Debt Restructuring Industry Are Helping to Revive the U.S. Economy*, 24 J. APPLIED CORP. FIN. 23 (2012).

³⁸ See Amanda Albright, *Sweet Briar College, Which Almost Closed, Gets a Rating Upgrade*, BLOOMBERG (Dec. 18, 2017), <https://www.bloomberg.com/news/articles/2017-12-18/sweet-briar-college-after-near-closing-now-sees-rating-inch-up>.

³⁹ For example, Virginia Intermont College closed without filing for bankruptcy. It took twenty-seven months. It sold its land for \$3.3 million, which was not enough to cover its \$4 million

these either restructure or fail without filing for bankruptcy. The collective action problem that exists when debt is widely held does not arise for most schools. It is easy for them to bring their creditors together. The challenge is crafting a course of action for the future. While debt payments often have to be delayed or scaled back, operations need to change as well.

Financial distress in state schools presents a problem distinct from that in the private sector. State schools get a portion of their funding from the state, and the level of education that they seek to provide their citizens is a matter of state policy. Indeed, in the case of municipal debtors, the Code gives less power to bankruptcy courts and greater leeway to debtors than it does in the private context. The aspiration is to leave policy judgments in the hands of elected officials rather than courts and creditors. Thus, even if the federal loan program were amended to allow a state institution to continue to receive funding despite a bankruptcy filing, deference should still be afforded to public officials. Public institutions should be allowed to restructure under chapter 9.

Modern chapter 11 practice has changed radically over the past twenty years.⁴⁰ Conventional wisdom used to be that chapter 11 was a venue for managers to escape the pressure of their companies' creditors and execute a plan for the future. Reorganization under federal bankruptcy law was seen as a way that those in charge of the company could keep the

bank debt and the \$6 million it owed to others, including employees who worked for months without being paid. See *Virginia Intermont Sold at Auction for \$3.3 Million*, WJHL.COM (Dec. 15, 2016), <http://wjhl.com/2016/12/15/virginia-intermont-sold-during-auction-for-3-3-million/>.

⁴⁰ See Douglas G. Baird, *Bankruptcy's Quiet Revolution*, *supra* note 11; Douglas G. Baird & Robert K. Rasmussen, *The End of Bankruptcy*, 55 STAN. L. REV. 751 (2002); Douglas G. Baird & Robert K. Rasmussen, *Chapter 11 at Twilight*, 56 STAN. L. REV. 673 (2003); Douglas G. Baird & Robert K. Rasmussen, *Antibankruptcy*, 119 YALE L.J. 648 (2010).

creditors at bay.⁴¹ Some worried that managers would dissipate the company's value in pushing for a low probability turnaround. They would benefit should the turnaround occur, but should the more likely liquidation happen, it would be the creditors that bore the brunt of the loss. Even if some of the claims of the debtor being in complete control of the bankruptcy process were overstated, few questioned that managers had a strong hand to play in chapter 11 in dealing with a company's creditors. Such a state of affairs is certainly not the case any longer. Chapter 11 today is not a refuge for beleaguered managers; rather, it has become just one part of the restructuring process.

In looking at these changes, I want to start with those changes that are most removed from the actual filing for bankruptcy. There has been renewed focus on the role of directors of a company in financial distress.⁴² Gone are the days when the board was a bystander as the company descended into financial distress. It once was the case that the board was seen as a passive group whose members were by and large put in place by the CEO. Some referred to boards as the friends and family plan. Yet the days of quiescent boards reflexively approving

⁴¹ See Lynn M. LoPucki, *The Debtor in Full Control – Systems Failure Under Chapter 11 of the Bankruptcy Code?*, 57 AM. BANKR. L.J. 99 (1983); Barry Adler & Lawrence Weiss, *The Debacle of Corporate Bankruptcy*, 15 REGULATION 54 (1992); Barry E. Adler, *Financial and Political Theories of American Corporate Bankruptcy*, 45 STAN. L. REV. 311 (1993).

⁴² See Stephen Hessler, Partner, Kirkland & Ellis LLP, Statement Before the Subcommittee on Regulatory Reform, Commercial, and Antitrust Law, Committee on the Judiciary, United States House of Representatives 7 (March 23, 2017) (“[I]n my experience as a practitioner representing very large Chapter 11 debtors, the knowledge, expertise, and commitment of the company’s prepetition directors and officers are indispensable to effectuating a soft landing into, and orderly passage through, bankruptcy”) (transcript available at <http://docs.house.gov/meetings/JU/JU05/20170323/105758/HHRG-115-JU05-Wstate-HesslerS-20170323.pdf>).

whatever the CEO put before them are long gone. Today, board members are expected to be active monitors of the CEO. In times of crisis, the board often rises to the fore.

One of the major duties of the board of any institution is to pass judgment on the leader.⁴³ It is up to the board to determine when the CEO is not up to the challenges confronting the company. Indeed, removal of a CEO who is not the right fit for a company can prevent further erosion. Prompt dispatching a poor choice can help arrest the downward trajectory.

A second change that has occurred in reorganization practice in recent years has been the creation of a community of turnaround professionals.⁴⁴ These professionals come onto the scene well before a bankruptcy petition is filed. They are tasked with righting the ship. They look for areas of value that need to be maintained and enhanced, and areas where the firm should no longer focus. They have expertise in dealing with companies in distress, and they are comfortable making radical changes to a business's operations if they conclude that such changes offer the greatest chance for turning the enterprise around. It is not uncommon to appoint a chief restructuring officer and have her make substantial changes, thereby avoiding bankruptcy. Active and dedicated boards monitoring CEOs and turnaround professionals joining the company will have a significant affect on the operation of the business.

One of the innovations of the Code was the creation of the prepackaged bankruptcy case. In such a situation, the debtor and its creditors reach an agreement outside of

⁴³ See Douglas G. Baird & Robert K. Rasmussen, *The Prime Directive*, 75 U. CINN. L. REV. 921 (2006).

⁴⁴ Douglas G. Baird & Robert K. Rasmussen, *Private Debt and the Missing Lever of Corporate Governance*, 154 U. PA. L. REV. 1209 (2006).

bankruptcy, and then filed for bankruptcy with a plan of reorganization in hand. The understanding was that the bankruptcy proceeding was not a place to address the operational issues of the company; rather, the trip through bankruptcy was only to take advantage of the provisions of the Code, which enabled a super-majority of creditors to bind dissenters, something that cannot be done outside of bankruptcy. Over the years, the use of prepackaged plans has increased.

These deals have expanded from simply adjusting the capital structure to even including the sale of the company to a willing buyer. TWA filed for bankruptcy precisely so that it could consummate its sale to American Airlines. Chrysler filed for chapter 11 to deliver itself to Fiat. The details of the transactions were largely worked out in advance, and the sale through chapter 11 was simply the vehicle by which to implement these deals.

More recently, the reorganization community has been using prepackaged bankruptcies in connection with restructuring support agreements (“RSAs”). An RSA is an agreement by creditors in advance of a bankruptcy filing to vote in favor a plan of reorganization that will be proposed once the debtor is in bankruptcy. The key aspect is that parties bind themselves in advance. They decide the fate of the company and how their interests in the company will be handled prior to any legal proceeding taking place. If anyone walks away from the agreement, that party will have breached the contract.⁴⁵

The driving force behind RSAs are usually the companies’ creditors. This one of the techniques they have devised that allow them to exert pressure on management. In particular,

⁴⁵ For more on enforcement of such agreements after the company has filed for bankruptcy, see Kenneth Ayotte, et al., *Bankruptcy on the Side*, 112 NW. U.L. REV. 255 (2017).

they capitalize on the power they have to declare default under the terms of their lending agreements. The price of waiving a default or getting an amendment to avoid a default is often to take actions that better protect the lender's investment. Such influence continues up to and through the bankruptcy case. When it comes time for the company to seek funds to carry through an upcoming bankruptcy case, the prebankruptcy lenders assist with the process of finding debtor-in-possession financing.⁴⁶

III. The Lessons for Higher Education

The tools outlined above can well be of use in the higher education arena. To be sure, these practices arose in a setting where there was always the legitimate threat of filing a chapter 11 proceeding. However, many of these tools can still be utilized with colleges and universities. The first place to start is with a traditional restructuring of the outstanding debt.

If the college has issued public bonds and needs to restructure the debt, the lack of access to a prepackaged bankruptcy does not mean that a meaningful restructuring cannot take place. Consider the recent restructuring of Education Management Corporation ("EMC").⁴⁷ EMC owned a number of for-profit schools. It had \$1.5 billion in outstanding debt. The parent company (EDMC) owned two subsidiaries (Education Management, LLC and Education Management Finance Corporation). Its secured debt was roughly \$1.3 billion governed by a credit agreement executed in 2010. The loan was an enterprise loan and all of the assets of the enterprise were pledged as collateral.

⁴⁶ See Kenneth M. Ayotte & Edward R. Morrison, *Creditor Control and Conflict in Chapter 11*, 2 J. LEGAL ANAL. 511 (2009).

⁴⁷ The description of the facts leading up to the dispute over EMC's restructuring efforts are taken from the Second Circuit's opinion in the case. See *Marblegate Asset Mgmt. v. Educ. Mgmt.*, 846 F.3d 1, 2-4 (2d Cir. 2017).

The two subsidiaries executed more than \$200 million in unsecured notes. The parent guaranteed those notes as well. The company, however, could not generate sufficient revenues to service its overall debts of \$1.5 billion. Had EMC been in a business other than higher education, it would have been a prime candidate for a prepackaged bankruptcy. As we know, however, EMC could not pursue that route. Like most other higher education institutions, it received a majority of its funding from tuition paid with student loans issued by the federal government. Filing for a prepackaged bankruptcy would have destroyed its students' eligibility for such loans.

In 2014, the secured creditors entered into a new, amended credit agreement. As part of this agreement, the parent agreed to guarantee the secured debt.⁴⁸ The secured lenders already had a claim that was senior to that of the noteholders. The guarantee did nothing to increase their priority. However, the guarantee that the noteholders received had a "tag-along" provision. It provided that, if there was a release of another guarantee issued by the borrower, this release would have the effect of releasing the noteholders' guarantee as well. The granting of the guarantee to the secured lenders basically cocked the trigger on the tag-along provision, taking direct aim at the guarantee held by the noteholders.

At the same time, the parent entered into negotiations with a group of creditors that, collectively, owned over eighty percent of the secured loan and eighty percent of the

⁴⁸ Although the decisions in the district court and the court of appeals are not entirely clear on this point, it appears that EDMC was not a guarantor under the original credit agreement, but rather one of the borrowers. It was only in the 2014 amendment that the parent guaranteed the obligations of the subsidiaries under the credit agreement. Since the bank lenders already had a direct claim against the assets of EDMC, this guarantee provided little additional enhancement of the banks' position.

unsecured notes. All agreed that, because of the federal loan restrictions, filing for bankruptcy was not an option. The company received 78.6% of its revenues from federal loans to students. Instead, the parties hammered out an agreement. The agreement presented the creditors with two options. The first option could only be exercised if *all* of the noteholders, both secured and unsecured, agreed. Under this option, the secured lenders would exchange their existing \$1.3 billion in claims for a \$400 million secured loan and seventy-seven percent of the parent's stock. The unsecured noteholders would receive nineteen percent of the parent's stock in exchange for their notes. The parent estimated that this exchange would represent a forty-five percent reduction in the value of the holdings of the secured lenders, and a sixty-seven percent reduction in value for the noteholders, at least when one compares the face value of the old obligations to the new ones. Of course, few if any thought that the old obligations were worth anything close to their face value.

The second option was a complicated mechanism, designed to nudge (or, more accurately, shove) the creditors in the direction of the first option. Under the second option, the secured creditors who consented would exercise their rights under the 2014 credit agreement and foreclose on the parent's assets, which of course included the stock of the two subsidiaries. These creditors would also release the guarantee that they had received from the parent. As previously stated, the effect of this release would be to release the noteholders' guarantee as well. The noteholders could no longer look to the parent to satisfy their debts.

The parent would then create a new subsidiary. The collateral agent who foreclosed on the assets of the parent would sell the same assets to the new subsidiary in exchange for new debt and equity. These new notes would be distributed only to the consenting creditors.

Secured creditors who did not consent would receive new debt issued by the new subsidiary. This debt, however, would be junior to the debt that the consenting secured lenders would receive. The incentive for the secured creditors to accept the deal was obvious. It is always better to be at the top of the waterfall. Thus, it is not surprising that all secured creditors agreed to the restructuring.

As to the noteholders, those who consented would receive notes executed by the new subsidiary. Those noteholders who did not consent would not have any claim against the new subsidiary. Rather, they would be left with the worthless claims against the two subsidiaries, who would have lost all of their assets by virtue of the transaction. Receiving nineteen percent of the stock of the parent under the first option was clearly better than a collection suit against a shell company. Almost all the noteholders accepted the deal.

However, one noteholder, who owned notes with a face amount of \$14 million, did not consent. Failing to receive unanimous consent on Option No. 1, the parent began to implement Option No. 2. The objecting noteholder sued. It argued that Option No. 2 ran afoul of the Trust Indenture Act (the "TIA"). Section 316(b) of the TIA provides, "the right of any holder of any indenture security to receive payment of the principal of and interest on such indenture security . . . shall not be impaired or affected without the consent of such holder" Surely, the loss of all of the borrowers' assets "impaired or affected" its right to payment. The district court agreed,⁴⁹ but the court of appeals reversed.⁵⁰ The Second Circuit held that the right protected by the TIA was only the legal right to payment. The noteholder who did not offer its

⁴⁹ *Marblegate Asset Mgmt. v. Educ. Mgmt.*, 75 F. Supp. 3d 592 (S.D.N.Y. 2014).

⁵⁰ *Marblegate Asset Mgmt. v. Educ. Mgmt.*, 846 F.3d 1 (2d. Cir. 2017).

consent still had the exact same legal right – the ability to sue the issuer of the note. What had changed was the ability of the issuer to satisfy its legal obligations; the obligations themselves were untouched. Whatever one thinks of the hardball tactics that EMC used to attempt to induce consent, the lesson of this case is clear. Educational institutions that have issued public debt can attempt to restructure that debt through such tactics and not run afoul of the TIA.

Another lesson in restructuring bond debt without the use of bankruptcy law comes from the law school world. Thomas Jefferson School of Law, a stand-alone, not-for-profit law school, built a beautiful, state-of-the-art law school building in downtown San Diego. The school did not have the wherewithal to pay for the building upfront. Rather, it borrowed the money, issuing over \$90 million in bonds. The building was beautiful, but the timing was atrocious. Soon after the completion of the new facility, the bottom fell out of the law school market. Law school applications plummeted, and few schools were hit harder than Thomas Jefferson. Two years after opening, it missed its enrollment target by over thirty percent, triggering a default under the bonds.

The bondholders were entitled to foreclose on their collateral – the new, state-of-the-art building. It turns out, however, that a law school building, even in a prime location in a major American city, is not easily or cheaply repurposed to other commercial uses. After exploring all of their options, the bondholders decided that the highest use of the building was as a law school. They agreed to restructure the debt. The parties struck a deal in which the creditors received title to the law school building and then leased it back to the borrower. This transaction had the effect of reducing the school's debt service by half. Prior to the

restructuring of the bonds, it had paid \$12 million in principal and interest on an annual basis. After the deal, its rent and other charges were only \$6 million.⁵¹

Both of the restructurings, in EMC and Thomas Jefferson, could have been accomplished relatively quickly through a prepackaged bankruptcy if that tool had been available to them. There would have been no need to coerce the creditors with Option No. 2 in the EMC case. Two-thirds in dollar amount and over fifty percent of the number of holders of claims are required to achieve class acceptance of a plan.⁵² With over eighty percent of both classes voting in favor of Option No. 1, this arrangement could have been implemented much more quickly through a prepackaged case. There certainly would not have been years of litigation that followed the rejection of Option No. 1.

Educational institutions can also utilize another tool from the insolvency community's playbook, the use of turnaround or financial restructuring experts. Whether it is hiring these professionals or changing the composition of the board, schools need financial expertise that they can draw on in troubled times. In the private sector, directors are usually chosen for what they can bring to the operation of the business. They have deep business experience and, when they are in step with the CEO, they can be helpful allies in navigating financial distress. Boards of trustees of educational institutions, on the other hand, tend to be prominent alumni and other notables. They are usually selected, at least in part, based on their contributions to and affinity for the school. Indeed, the boards tend to be larger than the boards of private firms.

⁵¹ See Gary Warth, *Dean Optimistic about Law School's Future*, SAN DIEGO-UNION TRIBUNE, December 12, 2014, <http://www.sandiegouniontribune.com/news/education/sdut-dean-predicts-restructured-debt-will-save-law-2014dec12-story.html>.

⁵² See 11 U.S.C. 1126(c) (2012).

They are not accustomed to exercising power. Thus, when hard decisions need to be made about future operations of the school, there is no guarantee that the trustees will have in their midst the necessary business experience to draw upon.

One can imagine a number of creative approaches that a school facing financial distress may want to explore. For example, it might form a consortium with other schools to share resources. In years past sharing agreements would only be feasible among schools that were physically close to one another, but technology has expanded the options. One could explore, say, having one school close its English department and a second school close its Philosophy department, allowing students at the first school to take English courses remotely from the second school, and allowing students at the second school to take Philosophy courses remotely from the first school. The schools might even pursue a formal merger, if it promised cost savings. Businesses today are under tremendous pressure to continually explore ways to reduce costs. Board members who have operated in this environment could generate new ideas for the college or university leadership to consider. Few academics who ascend to the top position at an academic institution have been exposed to the types of strategies that private companies have adopted in recent years to reconfigure aspects of their operations. Schools should look for trustees who have training in finance and business strategy and are comfortable making hard decisions. Moreover, both new and old trustees should receive training so that they can more fully discharge their monitoring and advising roles.

A change in orientation must come from the top, with the president of the university or college embracing this change. Boards tend to replicate themselves, and if the institution would benefit from trustees with profiles that are different from those of current board members, it

will be the president who will have to push for the change. At one level, this change may be attractive to the president who would benefit from the additional perspectives that new people bring. At another level, however, some presidents may recoil from the prospect of change. After all, the board has the power to replace the president, and a president with a fully supportive board may be reluctant to push for new trustees who ask hard and uncomfortable questions about the direction of the school.

The board should do more than expand its array of talent in confronting today's challenges. It should also reject the traditional conception of who can lead a university. The traditional career path of many university presidents has not prepared them for today's realities. They often come from the faculty. While one can find some faculty whose work touches on financial issues,⁵³ that is not always or indeed usually the case. Some faculty may acquire relevant skills when they serve as administrators beneath the presidential level – few faculty ascend to the presidency without any administrative experience – and those individuals can be nimble in the current landscape. Still, a president should not be required to have served as a faculty member somewhere in order to serve as a leader. In the private sector, the responsibility of the board is to identify the most pressing challenges and opportunities the institution faces and select the person best suited to address these. Fortunately, it is becoming more commonplace to look beyond faculty members for university leadership. This trend should continue.⁵⁴

⁵³ Bankruptcy scholars who have gone on to lead colleges or universities include Ron Daniels (John Hopkins), Karen Gross (Southern Vermont College) and Tom Jackson (Rochester).

⁵⁴ For a contrary argument, see Benjamin Ginsberg, *College Presidents Should Come from Academia*, N.Y. TIMES, March 3, 2016,

In addition to having the right leadership (at both the board and presidential level), all options have to be on the table when an institution is in financial distress. Debt restructuring by itself will not solve the problems that many schools face. To the extent that the school's operations are not cash flow positive, debt relief only postpones the inevitable. Operations have to be adjusted so that current revenues exceed current expenses.

One option that some schools have taken has been to pare back programming. A department that once made sense for the school may need to be terminated. Extracurricular activities that seemed like a positive enhancement to the student experience during flush times may need to be curtailed. Combining schools is an aggressive and rarely used strategy. Companies often use chapter 11 to facilitate a sale because the debtor cannot make it as a stand-alone company, but some of its assets and employees can survive as part of another business. For years, the Claremont schools have provided a quality education while combining central services to create efficiencies.

Another option is to hire turnaround consultants. There are at least two benefits of bringing in an outsider to assess a school's condition. First, the outsider may well see things that insiders miss. What may seem perfectly sensible to longtime trustees and presidents may strike someone with a fresh pair of eyes as an opportunity for constructive change. Second, an outsider can quickly add needed skills to the task. Enhancing the financial acumen of boards and finding new presidents skilled at turnaround situations is a process that can take years. A consultant can be hired much more quickly.

<https://www.nytimes.com/roomfordebate/2016/03/01/college-presidents-with-business-world-ties/college-presidents-should-come-from-academia>.

Of course, colleges are just like other companies. In times of crises, CEOs can act swiftly. Colleges are not used to radical changes. Faculty expect to be consulted about fundamental issues facing the school. Even decisions that do not formally require faculty approval are more likely to be met with success when the faculty and staff understand the need for departures from past practice. Very few faculty view themselves as employees. They see themselves, quite rightly, as the indispensable community that lies at the heart of every school. This reality places a premium on the communication skills of the president/chancellor. A president/chancellor who takes drastic action that fundamentally alters the mission of the college will make little headway without a “buy-in” from the faculty. She needs to clearly articulate the challenges that the institution faces, set forth her thinking, and welcome constructive feedback.

In summary, although educational institutions cannot take advantage of chapter 11, they can utilize many of the same tools that it has spawned. Leaders seeking to corral various interested parties into a new path for the school could attempt to formulate a restructuring support agreement. Committing to put together a plan for the school with input from faculty, alumni, staff, and lenders could allow the leadership team to reach a global agreement with all constituencies. For example, a lender may be willing to consider reducing what it is owed if it is convinced that the school has taken a hard look at compensation. By the same token, faculty and staff will understandably be reluctant to bear the brunt of the restructuring, unless they are assured that the pain will be shared. A president committed to shuttle diplomacy among the various parties, with a shared goal of reaching a settlement that everyone will endorse, could well be able to steer a school away from the shoals of financial distress.

IV. Conclusion

College and university presidents are facing challenges that few could have foreseen a decade ago. Declining demand for much of the school's traditional offerings, outrage from parents as to the cost of tuition and the opacity of the financial aid process,⁵⁵ faculty with secure contracts who may have little knowledge or concern about general trends in the education arena, and lawmakers often intent on scoring political points rather than seeking cooperative solutions are all part of the landscape confronting today's leaders. While there is undoubtedly cause for concern, there is cause for optimism as well. Nimble and creative leaders can use this crisis to take bold actions and, working with their constituents, recommit to the values of higher education in a new age. One of the enduring lessons of restructuring practice is that financial distress does not inevitably lead to extinction. Painful changes and concessions, coupled with a willingness to explore new ways of doing things, can lead to a new future.

Higher education is undoubtedly one of the most important institutions responsible for America's growth. It has spawned ideas that have impacted every life across the globe. It has provided pathways for countless people to have successful and meaningful lives. There are undoubtedly things that it does wrong, but there are a lot of things that it does right. Careful and creative use of the lessons of restructuring practice can help reduce the former and increase the latter.

⁵⁵ See Ron Lieber, *Why It's So Hard to Calculate What You'll Pay for College*, N.Y. TIMES, Jan. 19, 2018, <https://www.nytimes.com/2018/01/19/your-money/paying-for-college.html>.