

Universities as Foundations—The New Model of Lower Saxony

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In Lower Saxony, the legal status of universities as foundations under public law is offered to universities because increased autonomy is a core condition for the effective and economical management of resources. Moreover, increased autonomy will attract increased amounts of private and social funding and will improve the corporate identity. A university senate can apply to have this status offered to it. A university foundation is legally responsible for the university as a corporate body. The real property is transferred as basic capital. The ministry as the supervising authority is replaced by a board of supervisors.

PRELIMINARY REMARKS

The university system of Germany from the nineteenth century to the present has been characterized by the dual status of the individual universities as self-governing academic corporate bodies, on the one hand, and dependent state institutions, on the other. Until the middle of the Twentieth Century, the head of the academic corporate body and the director of the state institution represented two different bodies. The state institutions supported the academic corporate body with all the resources that it needed for undertaking teaching and research. The state institution and its staff also did all the required administrative work.

During the period of extension of the German universities that began in the 1960s and 1970s, a framework act was drawn up by the Federal Parliament which forced the *Länder*, the instances responsible for higher education, to centralize university administration under the leadership of a rector or a president, who now became the head of the academic corporate body as well as the director of the state institution. Both institutions were united under the new concept of the university. Still, in principle, the dualism of a self-governing corporate body and a state-dependent institution remained; *i.e.*, universities did not have separate budgets, but, in financial terms, their budgets were considered as falling within the state budget.

The academic and administrative staff were employed by the state. The ministry supervised the whole administration of universities. The state administration enacted a number of rules by which to administer the budget and the staff. The last step in the hiring process of new professors was taken by the ministry. Universities could propose only three candidates. The minister would decide which one of the three was to be appointed.

A STATE-SUPERVISED UNIVERSITY SYSTEM WITH AN INPUT-ORIENTED MANAGEMENT

In the 1990s, a discussion began about the adoption of the principles of New Public Management as a new steering model for universities. These principles are characterized by contract management, *i.e.*, management by targets, deregulation, flat hierarchies, global budgets, including competitive elements, output orientation, and evaluation, rather than by rules. The general aim was to strengthen the autonomy of universities. The use of all

resources was expected to be improved by greater flexibility to increase effectiveness and efficiency. The next consequent step was to combine financial autonomy with legal independence.

THE NEW LEGAL STATUS

In 1998, through an amendment of the Federal Framework Act for Higher Education, the sixteen *Länder* (the German states) were permitted to establish a modified legal status for their universities. As this special modification of the Framework Act had been initiated by Lower Saxony, it was the first *Land* to seize the opportunity to make changes.

The Framework Act allows a change in the legal status of an academic corporate body as well in the status of the institution as it currently exists as a state institution. The view is that the legal status of an academic corporate body, based upon the membership of professors, academic staff members, students, and others, should not be changed. Lower Saxony was not aiming at any changes in this direction through its initiative for the initiation of another framework act but simply wanted to have the status of the university as a dependent state institution changed.

The corporate structure of a university is very important because of the constitutionally protected right of freedom of teaching and research and because of the right, in Germany, of co-determination in all academic affairs. The state government, however, does not need to be responsible for the provision and organization of the required resources. An independent authority like, for instance, a public foundation, could accomplish this task with greater efficiency. Thus, Lower Saxony moved in the direction of setting up private foundations in the middle of 2002.

Withdrawal of the State without Privatization

The Lower Saxony University Reform Act of 24 June 2002 offers an opportunity for the universities of this *Land* to opt for transformation from being state institutions to becoming foundations as legally self-administered public bodies. The dual status of a university as an academic corporate body and, at the same time, as an administrative body, responsible for the maintenance and advancement of itself as a corporate body, will remain unchanged. A supervisory board for the foundation will replace state supervision. Board members, appointed by the ministry on the basis of proposals by the academic senate, will assume the role played by the ministry. Such a transformation, however, is not intended as the first step towards the privatization of universities but, rather, as a paradigmatic step to reduce control by the state government over them, for, nevertheless, the state remains responsible for transformed universities. The University Reform Act makes this point very clear in its first paragraph. The role of the *Land* government is confined to two main core functions: (i) co-ordination of the university system within the scope of its responsibility for planning the university development of the *Land*, and (ii) responsibility for funding.

Unity of the Corporate Body and the Foundation

Direct responsibility, however, is handed over from the state to the foundation. The foundation and the corporate bodies do not work separately, but together in the sense of in tandem. Moreover, the University Reform Act takes great care that the guaranteed rights of self-administration of the corporate body are not affected. The foundation derives its only competencies from the *Land* government, but the latter cannot influence the corporate body

since resource administration is no longer a concern of the *Land* government. It should be emphasized that a foundation takes over tasks and assumes duties that, in the past, were administered by the *Land* government. The Reform Act even goes so far as to assign the legal supervision of the corporate body to the foundation.

Economic Management

Universities that are organized as foundations are not managed as parts of the state budget; rather, they must set up their own budgets. Still, these budgets consist mainly of state funds, used especially to cover current expenses, third-party funds for research, and teaching and institutional resources. Foundations can also have earnings from their own assets or from donations. A foundation budget is modeled according to the commercial and accounting standards of corporations. The application of the rules for public budgets is limited to three fields. These fields include warranties and loan commitments, the staff appointment scheme for civil servants, and the obligation to engage in advertised bidding.

The economic administration of the corporate body and the foundation form an entity, which means that there are no separate budgets and no separate assets. As far as assets are concerned, a distinction is made between administrative assets used for the current management of the university and the foundation capital as the general financial base.

Universities that are no longer included in the state budget are therefore not bound by the instructions issued by the ministry regarding economic management.

Financial Support

The university does not receive allowances, only calculable financial support regulated by legal rules. Financial support is calculated with fixed development and achievement targets laid down in a target agreement (a contract). The updating process of this target agreement takes the attainment of targets as a basis for setting future levels of financial support.

The target agreement is subject to public law and is drawn up between the state and the university. Because of parliamentary budgetary legislation, the agreement is subject to funding by means of an appropriate budget. When the budget is passed by the Parliament, the agreement is an enforceable legal claim—as are other arrangements for financial support. This arrangement provides great reliability for the university.

Other forms of organization, *e.g.*, legally independent bodies as in Switzerland, can also ensure the legal independence of universities in the economic sphere. The forming of private organizations, however, can be viewed as the first steps towards the privatization of universities, something, however, that is not intended in Lower Saxony.

Civil Servants

Private organizations face another, more technical barrier. The right to employ civil servants can only be conferred to organizations under public law. There is no expectation that German professors would be hired as ordinary employees, rather than as civil servants, even if doing so might be necessary *de facto*. Lower Saxony would experience a strong competitive disadvantage if the option for employing academics as civil servants were discontinued. Furthermore, the state budgets could not cope with the additional burden, since the hiring of professors as employees would actually cost an additional 33 percent more than their retention as civil servants because the future costs for pensions are not included in current budgets.

Opportunities for Foundations

The foundation form as the legal basis for the existence of a university has been chosen mainly because it presents a far more convincing step towards the concept of a civil society than any other legal form. There is also hope that a foundation might raise more private capital than a public institution.

The last fifty years of peace and prosperity have given rise to an increase in private capital. Today, €2.5–3.4 trillion is waiting to be left to heirs, or, alternatively, to institutions of public utility. Every year, 10 percent of this incredible sum is donated.

Not only testators, but other people as well are conscious of the fact that private wealth gives one grounds to feel obligated to assist the public good.

Fundraising activities in universities are, first and foremost, aimed at alumni, a practice that is very evident in American universities. It should be understood that the presumption that raising millions of dollars takes hundreds of years is a mistaken one. Even though that may have been the case for a traditional university like Harvard, if one looks at a list of about 250 selected American universities, one finds that the starting point for strong fundraising efforts was in the 1970s. Some 150 universities succeeded in raising a minimum of a million dollars each. The conditions in Europe, especially the tax levels and regulations, and the cultural background, are not the same as in the United States, but, nevertheless, it is very encouraging to find that European universities can succeed in raising funds even in unfavourable circumstances.

An example of success is that of Chalmers University in Göteborg, Sweden. Even in Sweden, in which donations have no effect on the tax liabilities of the donor, one finds a readiness to give money under the condition that a foundation, not the state, be the owner of the university.

The model of universities as foundations, adopted by Lower Saxony, is based on a built-in assumption that the *Land* is responsible for basic funding in the same way as for state-owned and organized universities. The fundraising efforts of the foundation and any other income will increase the budget of the university. Thus, it is crucial that government funding not be reduced because of the intake of supplementary income by the foundation, including interest on the capital held by the foundation. The law guarantees this situation.

To ensure that universities operated by foundations receive the same basic funding from the state as state-organized universities, it is necessary to set up a common funding formula or at least a funding system based on common criteria or indicators.

Real Estate as the Basic Form of Capitalization of a Foundation

One of the most important principles of New Public Management is joint responsibility for tasks and resources. Therefore, the Reform Act authorizes the government of Lower Saxony to transfer the property holdings of universities to them to form the basic capital of their foundations. The foundations will become owners of the estates and buildings that are needed so that the university in question can operate. Usually, the estates that will be transferred are those that are being used by the universities up to the day that the foundation begins to operate. But the Ministry of Finance will check strictly that the buildings claimed are really needed. Those that are not needed will remain the property of the state. With the transfer of properties to foundations, the responsibility of the state administration for the estates will end. It is likely that regulations will be formulated in relation to the transfer from one administration to another in order to avoid double expenses. As a rule, the

foundation will outsource many of its new administrative tasks to private companies. The new foundations will need time to manage this shift.

Universities, especially those operated as foundations, will need to be very reliable in terms of planning. Thus, they will have to be able to plan on receiving set amounts of government funding over periods of four to six years. This problem, however, is not one that can be solved easily by the *Land* government. One of the difficulties with which the state is confronted is the divided responsibility of the *Länder* and the federal government regarding the financing of new university buildings and major equipment. This problem is peculiar to Germany.

To avoid the unanticipated risks of maintaining the buildings that the foundation will own, the following steps should be taken during the process of establishing a foundation:

- the definition and the precise denomination of the estate to be transferred;
- the securing of a commitment by the state to implement the construction plans if the given university is in a phase of development, extension, or consolidation;
- assessment of the requirements concerning the maintenance and renovation of buildings in the near future or over the medium term;
- assessment of the resources needed for the maintenance of the buildings.

Nevertheless, the state government will not be able to offer more than political commitments. These concrete steps have to be negotiated when the regular contracts between the government and the university/foundation are arranged.

Lower Saxony is not able to offer any money as part of the basic capital of a foundation. Thus, the transferred real estate forms its only financial stock. This basic stock is to be consolidated by endowments made by external donors, given that the state itself, even in the future, will not be able to spend money for this purpose. At the same time, the foundation itself can decide whether or not part of the normal state funding should be used to form basic capital. To make certain that the foundation really does not need that part of state funding to cover running costs, it must put it aside for three years before using it to increase the basic capital of the foundation.

The basic value of the foundation, especially the transferred real estate, cannot be used as security for bank credit; however, the Ministry of Finance of the *Land* can authorize exceptions to this rule. It is possible for the foundation to restructure the real estate holdings without the permission of the state, if the restructuring is undertaken by a management proven to be trustworthy. Thus, the sale of a building is allowed when the proceeds are used, at the same time, to purchase or to establish another building.

The Right to Employ Civil Servants

As indicated above, the universities will have the right to employ civil servants. The exercise of this right is indicative of the fact that the universities will no longer be subject to ministerial human resources plans. Universities can elaborate their own human resources plans independently of the state. This facility applies to all employees of the university who are no longer employed by the state, but by the foundation.

The Reform Act, however, includes a caveat. All wage settlements that are applicable to public employees must also be applied to all the employees of a foundation university. The foundation will be obliged to:

- acknowledge all contractual rights and join a state-directed employers' association which is a member of the association covering all the German states (*Länder*);

—secure the rights to additional pensions, including those for surviving dependants. The foundation must set up and maintain the legal prerequisites required by the federal pension authority.

For arrangements outside the agreed scale rate, the rules governing public wage agreements apply and will be applied by the foundation under its own responsibility.

At the start, the authority of the foundation universities over human resources will be limited in another respect. The ministry in charge will still have the right to nominate professors who will then be appointed by the university. This competence can be assigned to the university foundation so that the executive board of the university, in agreement with the foundation board, can appoint new professors. This limitation is based mainly on the consideration that universities, in particular, have been hesitant as to the constitutionally mandated gender equality law. The enforcement of equal rights for women and men has been emphasized in the University Reform Act. The ministry will continue to make use of its right to supervise observance of its provisions until it is certain that the foundation universities are themselves doing so effectively.

STATUS OF THE PROCEDURE

The government of Lower Saxony intended to establish the option for foundation universities by the end of 2002, after the University Reform Act had come into effect on 1 October 2002. Thus, all the regulations for doing so were passed in December 2002. The Reform Act has determined that a university can be transformed into a foundation only when the respective university senate has voted favourably with a two-thirds majority. The hurdle thus set is high, but it is a necessary test of the acceptance of the foundation model. Six out of the twenty universities in Lower Saxony gave concrete negotiation instructions to their boards, these being the University of Göttingen, the Veterinary University of Hannover, the University of Hildesheim, the University of Lüneburg, the Medical University of Hannover, and *Fachhochschule* (university of applied sciences) Osnabrück. Intensive negotiations took place between the ministry and the universities as well as amongst the departments of the state government. These negotiations were concluded successfully with five universities. Only the Medical University of Hannover withdrew its application, considering that further negotiations were necessary.

On 17 December 2002, after the government of Lower Saxony had taken the corresponding decision, five universities were transformed into foundations, namely the University of Göttingen, the Veterinary University of Hannover, the University of Hildesheim, the University of Lüneburg, and *Fachhochschule* Osnabrück, with effect from 1 January 2003. The new government of Lower Saxony, which was elected on 2 February 2003, has already declared that it will accept this decision.

As one can easily understand, a change of mentality is required by all concerned, both at the public level as well as at the university level. Courage is needed, on one hand, to release the universities, and, on the other, to have faith in their own powers. Apart from the fact that the *Land* is not in a position to provide sufficient foundation capital, the whole model is thoroughly developed. It should be understood, however, that until only a few years ago it was beyond imagination that the *Land* government would be willing to transfer assets worth billions of euros to legally independent foundations. The replacement of state supervision by other steering instruments, namely target agreements and output control, will cause withdrawal symptoms at the public level. But the process has started, and is not reversible.

SUMMARY

- (i) The *Land* government expects universities, as foundations under public law, to use their autonomy to manage their resources more effectively and economically. The role of the *Land* government is limited to establishing target agreements and output control. Furthermore, autonomy is viewed as a value in itself. Self-responsibility leads to increased motivation and innovative power.
- (i) The legal status of a foundation under public law has been chosen in the hope that it will attract increased private and social funding. In particular, the state expects the corporate identity to be improved not only by the alumni but also by local and regional businesses. In addition, in Germany, the legal status of a foundation offers the best legal conditions for a reduced tax burden.
- (iii) The University Reform Act of 24 June 2002 does not force universities to accept transformation into foundations, but offers the option to do so. The senates of universities apply for this option. The decision of the senate has to be made by a two-thirds majority so as to enhance the validity of the decision to accept the foundation model.
- (iv) Although the *Land* government is no longer legally responsible for universities as corporations, it is obliged to directly protect them. The *Land* government protects their autonomy and freedom by setting up dispositions within the law regarding the rights and duties of staff members and the corporate community. Universities as foundations understand themselves to be units of given corporations and foundations.
- (v) The capacity to hire their staff, including the appointment of professors, without any state intervention will give universities, as foundations, greater flexibility to manage their human resources. To increase acceptance of the foundation system, the Reform Act leaves the context of public wage scales untouched. The government hopes that the model of universities as foundations will find many takers. A strong community of legally independent universities would then make an independent wage settlement of their own possible, a situation which could lead to special salary scales in science, owing to the structure and tasks of universities, for the first time in the history of wage scales in Germany.
- (vi) Universities as foundations will appoint their professors and management without any governmental intervention.

