Non-Traditional Partnerships in Student Housing: Why and how institutions of higher education seek partners to own, deliver and operate

Robert D. Bronstein, Jason A. Taylor, Sarah L. Samuels

On many college and university campuses, providing housing for students is integral to the institutions’ primary mission of educating them. Student housing has grown from facilities necessary for warehousing students to residential living-learning communities designed to foster intellectual and emotional growth and to build community on campus. Further, creating and managing successful, compelling campus housing communities has become increasingly important in supporting the enrollment management and faculty recruitment objectives of institutions of higher education (IHEs).

Concurrently with the emergence of student housing as an important corollary to academic goals and as a valuable recruitment tool, it is also viewed increasingly as an opportunity for partnership with third parties for its financing, delivery and management. Such non-traditional partnerships recognize that while successful student housing plays an important role on campus, it is not always one of the institution’s core competencies; rather, its predictable revenue stream can be leveraged to provide mutually beneficial outcomes to the institution and its partner(s).

While loosely structured affiliation and master-lease agreements between higher education institutions and third-party housing providers have existed for some time, approximately over the past 15 years a pronounced shift has occurred in the level of sophistication of these arrangements. IHEs view even the least structured affiliation agreements through the prisms of existing inventory, the surrounding market and the institution’s own credit and balance sheet. Increasingly, partnerships formed prior to construction can help to ensure the desired financial and institutional impact, for both the IHE and the third-party. Therefore, it is wise for any student housing provider or IHE to consider such a partnership early in the process of planning for new housing. When considering potential benefits – both financial and operational – of such an arrangement, it is important to ensure that the sometimes competing motivations of the IHE and the third-party can be aligned.

As the sophistication of these partnerships has grown, a variety of non-traditional arrangements have emerged. This paper principally seeks to examine the following questions:

- Why might an IHE consider non-traditional partnerships?
- What are the primary characteristics of a non-traditional partnership?

Motivating Factors for Institutions of Higher Education

Initially, student housing partnerships were motivated by the goal of addressing rapidly expanding student enrollment. If a school could not meet its obligation or desire to house students, it would enter into a partnership with a third party to do so. These arrangements were typically in the form of master-lease agreements or referral arrangements under which the school would direct students to the property in question – often after its own housing was fully occupied. Of course, as these same schools saw the need to address housing for an expanding student population, they also needed to dedicate significant capital and debt to addressing non-revenue generating facilities and operations such as classrooms, libraries, research labs, faculty offices and recreational facilities. Therefore, allowing third parties to invest their own capital in student housing became an attractive way for schools to address the dual needs of expanding enrollment and upgrading their other facilities, while also mitigating some portion of the risk to the IHE in such an endeavor.

Today, with hundreds of non-traditional partnerships having been executed successfully, the primary benefits such partnerships can offer IHEs fall into a handful of categories:

1. **To address an urgent need**, including higher-than-expected student enrollment, insufficient on-campus housing occupancy or other special circumstances (e.g., late delivery of new/renovated housing).
Generally, these models result in the following ownership, delivery and operations responsibilities:

3. To gain experience and expertise, particularly for IHEs that have no existing student housing or have not recently built new housing and, therefore, could gain from the knowledge base of a third party who has delivered and/or operated student housing in the recent past. Because of the variety of partnership structures available, institutions can tailor them to their needs. For example, a school with more experience in operations and less in delivery may choose to focus on that need.

4. To reduce risk, which is particularly attractive to schools with no track record of student housing on their campuses, or no track record with the specific population contemplated to be housed in the new facility (e.g., providing graduate student housing). To expedite the development process, some soft project costs. delivery process longer than that of a third-party developer and with significantly higher hard and soft project costs.

5. To preserve debt capacity, such that other capital priorities can be accomplished.

6. To obtain favorable balance sheet and credit treatment, although notably, a formal partnership will rarely be entirely off-credit and off-balance sheet for the IHE.

Characteristics of Non-Traditional Student Housing Partnerships

While there are numerous iterations of non-traditional student housing partnerships, the continuum of likely opportunities falls loosely within three models:

1. Referral: An IHE agrees to direct students to the third-party partner’s property in exchange for concessions such as discounted rent, participation in mediation prior to exiting student tenants, and/or payment of a nominal fee. Some of these agreements may result in the developer’s property operating more like on-campus housing, such as more student-friendly conflict resolution policies or renting by the bed rather than by the unit.

2. Affiliation: A more formal arrangement in which the IHE directs students to the third-party partner’s property as if it were part of its own inventory and has some control of operations — typically related to student life (resident advisors, residential policies, etc.). Sometimes, the property may be on land leased to the third-party by the institution and/or the institution may offer some guarantees.

3. Structured: A not-for-profit entity (existing or new) issues tax-exempt debt to finance the project and its board, a majority of which represents neither the IHE nor the developer, controls all facets of delivery and operations. Sometimes, the property may be on land leased to the not-for-profit by the institution and/or the institution may offer some guarantees.

Generally, these models result in the following ownership, delivery and operations responsibilities:

<table>
<thead>
<tr>
<th>Type</th>
<th>Ownership</th>
<th>Delivery</th>
<th>Operations</th>
<th>IHE Participation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Referral</td>
<td>Developer</td>
<td>Developer</td>
<td>Developer</td>
<td>Low</td>
</tr>
<tr>
<td>Affiliation</td>
<td>Developer</td>
<td>Developer</td>
<td>Varies</td>
<td>Low to Med</td>
</tr>
<tr>
<td>Structured</td>
<td>Foundation</td>
<td>Developer / CM</td>
<td>Varies</td>
<td>Med to High</td>
</tr>
</tbody>
</table>

The model which best fits the partnership is driven by the level of risk and control each party wishes to assume. Avoiding some of the risk typically requires ceding some of the control. As shown, the referral model requires the developer to be responsible for all aspects of financing, delivering and operating the project. The developer’s levels of risk and control are high in that scenario, while the IHE’s are little to none. Nonetheless, while a school can seek partners to deliver and operate housing, it cannot privatize its relationship with students. And because students and parents may find it difficult to differentiate between institution-owned housing and third-party-owned affiliated housing, it is important for IHEs to remember that referral and affiliation agreements still carry some degree of risk.

In the affiliation model, there are more options to transfer some risk between the institution and its partners. For example, the IHE might provide security, management and/or infrastructure (usually technology) services at minimal or no cost in return for greater control of operations. Of course, the IHE’s willingness to accept some risk and increase its resultant level of participation is based entirely on its motivation to seek a partnership. An affiliation could be as loosely structured as a requirement to adhere to certain residential policies, or as strongly structured as a master-lease agreement for the IHE to control and operate the project or portions of the project. In some cases, the school itself may be contracted to manage some or all of the operations.

Finally, the structured model represents a complete transfer of risk to a not-for-profit foundation, resulting in a ceding of control to the foundation’s independent board, on which the developer and IHE could sit and retain some limited veto authority. The structured model also limits financial return solely to the foundation and its not-for-profit beneficiaries — typically the IHE.

While the developer has responsibility for project delivery in each model, the IHE may share some decision-making authority. The IHE may offer a partnership only for projects built to its specifications, including materials, finishes, building components, tele/data, labor requirements (e.g., union and/or prevailing wage laws), LEED standards, floor plans, program space, and other design and construction criteria. In any event, the IHE may require its review and approval of these specifications before agreeing to any partnership.

Further, in evaluating a prospective partnership it is also important for both the IHE and the third-party provider to understand the impact of the proposal to the institution. This impact is directly related to the level of participation of the IHE in the partnership. Depending on motivating factors and the partnership model executed, IHE participation could comprise control of and responsibility for management duties and in-kind services, potentially including marketing, leasing, room assignment, security, maintenance, residence life or billing/collection.

The IHE may also consider providing some guarantees such as the assumption of debt repayment, rental collection risk, delivery risk, construction overruns and/or first-year occupancy, in return for greater control.

The degree to which IHE participation through management duties, in-kind services and guarantees impacts its risk is generally described as follows:

<table>
<thead>
<tr>
<th>If IHE Participation is:</th>
<th>High</th>
<th>Medium</th>
<th>Low</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of capital</td>
<td>Low</td>
<td>Med to High</td>
<td>High</td>
</tr>
<tr>
<td>Student rates</td>
<td>Low to Med</td>
<td>Medium</td>
<td>High</td>
</tr>
<tr>
<td>On-credit?</td>
<td>Yes</td>
<td>Partially</td>
<td>Unlikely</td>
</tr>
<tr>
<td>On-balance sheet?</td>
<td>Likely</td>
<td>Unlikely</td>
<td>No</td>
</tr>
<tr>
<td>Return to IHE</td>
<td>High</td>
<td>Medium</td>
<td>Low</td>
</tr>
<tr>
<td>Control by IHE</td>
<td>High</td>
<td>Medium</td>
<td>Low</td>
</tr>
</tbody>
</table>
Typically, an IHE will weigh the credit and balance sheet impact of its participation along with its motivating factors in order to determine the most desirable partnership. Ultimately the IHE must decide on the model that provides it with the optimum blend of control, long-term cash flows, credit impact and ability to achieve institutional goals.

About the Authors

Robert D. Bronstein is a principal and President of The Scion Group and has over $1 billion of experience in consulting, financing and development of not-for-profit facilities. He is also a founding member of the Real Estate Center at DePaul University and has lectured on matters relating to affordable housing, urban redevelopment and student housing to graduate-level students of the Illinois Institute of Technology, Kent State University and DePaul University.

Jason A. Taylor is a Senior Associate for The Scion Group, and has nearly ten years combined experience in consulting, project management and marketing communications, all focused on campus housing. He has worked with over 60 educational institutions, not-for-profit foundations and private developers on matters of demand and feasibility, program development, financial modeling and operations planning.

Sarah L. Samuels is a Consulting Associate at The Scion Group, focusing on public-private partnerships in student housing. As a graduate student at Northwestern University, she studied nationally the relationships between institutions of higher education and third-party housing providers, including various financing, ownership and operating structures and their impact on each institution and its goals. She was previously a Student Programs & Events and Campus Life staff member at the University of Chicago Graduate School of Business and the School of the Art Institute of Chicago.

About Scion

The Scion Group LLC is a real estate services partner to higher education – as well as businesses serving not-for-profit institutions – providing consulting, facility planning, financial services, operational reviews and development management. Scion’s expertise enables clients to improve financial performance while remaining focused on providing and enhancing a quality learning environment.

Founded in 1999, Scion consists of a unique combination of seasoned experts from the fields of higher education administration, market and corporate real estate, and property management, offering a level of financial and real estate sophistication not previously readily available from consultants to not-for-profit entities. Concentrating particularly on campuses with challenges to new or existing student housing – including high barriers to entry such as urban markets, faculty/staff housing, housing for students with dependents and schools creating housing for the first time – Scion combines state-of-the-art real estate analysis and modeling with understanding and sensitivity to the unique nature, mission and special considerations of schools and other not-for-profit institutions.

A member of NACUBO (National Association of College and University Business Officers), CCBO (Community College Business Officers association), NACAS (National Association of College Auxiliary Services), ACUHO-I (Association of College and University Housing Officers – International) and a participating sponsor of the ACUHO-I 21st Century Project for envisioning housing of the future, Scion is a recognized leader in the financial and operational analysis of educational housing and auxiliary facilities. To date, Scion has completed engagements on more than 80 campuses in the United States, Canada, Mexico and the United Kingdom, encompassing approximately $2 billion in facility construction and renovation.

For more information, contact The Scion Group at (312) 704-5100 or info@thesciongroup.com, or visit us on the web at www.TheScionGroup.com.