



TOPIC: UMUC Request for Approval of Creation and Investment in a New Company to Commercialize Analytics Technology and Services

COMMITTEE: Committee of the Whole

DATE OF COMMITTEE MEETING: September 18, 2015

SUMMARY: Over the last four years, UMUC has invested in building a market leading business intelligence capability that has provided a strategic advantage for the University. This capability was essential in helping UMUC chart a path forward as the University experienced increased enrollment volatility and great uncertainty over the last few years. There is a gap in the market for vendors focused on assisting higher education institutions to leverage analytics to support critical institution outcomes.

UMUC plans to create a company to introduce an industry specific product offering to help institutions navigate fiscally challenging times and improve decision making. This new venture aligns with UMUC's strategic priority to diversify its revenue portfolio and increase stability in a world of changing student populations and a shrinking military component. Revenue realized from this company will potentially enable creation of an endowment at UMUC to increase access to higher education for Maryland residents.

The new company will require the services of sixteen current UMUC employees, including two University vice presidents. One of the two vice presidents will be an employee of the new company, and the other who will be a member of the new company's board of directors but remain a UMUC employee. Approval of these two current UMUC vice presidents participation in the new company requires Board of Regents approval.

This new company satisfies the requirements and intent of the High Impact Economic Development Activities (HIEDA) policy and has received the Chancellor's certification as a HIEDA entity. The HIEDA policy enables the institution to manage conflicts of interest and contracting practices in such a fashion as to allow creation and operation of new activities and entities such as the one proposed by UMUC. Based on UMUC's projections, the new company will create 20 or more jobs in the state of Maryland, generate more than \$1 million of annual gross revenues and will facilitate the licensing and potential commercialization of a promising new product.

ALTERNATIVE(S): The Board of Regents could refuse approval for the creation and necessary investment in the new company.

FISCAL IMPACT: UMUC would invest funds in the company.

CHANCELLOR'S RECOMMENDATION: That the Committee of the Whole recommend that the Board of Regents approve the creation of, and investment in, a new company; find that the participation by two of UMUC's senior staff is necessary to the success of the company and that any conflicts of interest can be managed consistent with the State Ethics law.

COMMITTEE RECOMMENDATION:

DATE:

BOARD ACTION:

DATE:

SUBMITTED BY: Joseph F. Vivona (301) 445-1923

UMUC Request for Approval of Creation and Investment in a New Company to Commercialize Analytics Technology and Services

Background Information

Over the last four years, UMUC has invested in building a market leading business intelligence capability that has provided a strategic advantage for the University. This capability was essential in helping UMUC chart a path forward as we experienced increased enrollment volatility and great uncertainty over the last few years. There is a gap in the market for vendors focused on assisting higher education institutions to leverage analytics to support critical institution outcomes. UMUC plans to create a company to introduce an industry specific product offering to help institutions navigate fiscally challenging times and improve decision making.

UMUC believes that NewCo satisfies the requirements and intent of the High Impact Economic Development Activities (HIEDA) legislation and agrees that this is the best mechanism to establish the new company. Based on our projections for NewCo, the new company will create 20 or more jobs in the state of Maryland, generate more than \$1 million of annual gross revenues and will facilitate the licensing and potential commercialization of a promising new product. In addition, NewCo embodies the intent of the HIEDA legislation to foster a thriving startup community in Maryland.

A. Statement of the benefit to UMUC

NewCo is an important opportunity for UMUC that has the potential to yield many benefits. Listed below are the main drivers that support the creation of this new company:

- 1. Revenue Diversification** - Among the top initiatives in the UMUC Strategic Plan drafted in January 2015 is to diversify the revenue portfolio. After experiencing the impact of years of enrollment volatility, this strategic initiative is more important than ever. UMUC believes that NewCo offers a long term opportunity to achieve this objective by opening up a separate revenue stream for the university.
- 2. Commercial Opportunity** – UMUC has the opportunity to monetize its significant investment in building a market leading business intelligence capability. Many universities do not have the talent, resources or monies needed to build a like capability and UMUC believes there is a significant market opportunity to commercialize this product at scale for the benefit of higher education, including possible adoption by other USM schools which could be provided at reduced cost.
- 3. Brand Elevation** – Launching NewCo will bring prestige and national attention to both UMUC and the University System of Maryland. UMUC has long been an innovator in distance education and now has the opportunity to showcase its expertise and advancement in higher education analytics. Analytics in higher

education is among the top topics in many industry forums and UMUC will demonstrate a competency that puts them among the leaders in this category.

4. **Endowment Funding** –UMUC believe that with moderate success, there will be an exit opportunity that can potentially yield between a significant return on its initial investment in NewCo within 5+ years. These monies will fund the UMUC endowment and be used to reduce tuition costs for Maryland residents and ensure that UMUC remains a very healthy and financially viable institution.
5. **Venture Roadmap** –The creation of NewCo will provide a roadmap to launch other ventures to market by UMUC as well as other USM institutions.

B. The organizational form

UMUC intends to establish NewCo as a Limited Liability Corporation. This will be an independent legal entity wholly owned by UMUC (single member) at formation. This corporate structure offers many advantages to UMUC:

- **Limited Liability** – UMUC will only be held accountable to the extent of its investment made in the form of capital contributions to the company and it is not directly responsible for the debts and actions of NewCo.
- **Ability to Generate Capital** If needed, NewCo will have the ability to raise additional funds through the sale of stock to further invest in the business or acquire targeted companies. In addition, as a possible exit strategy, this will allow NewCo to either be sold to a third party or ‘go public’ through an initial public offering (IPO).
- **Attractive to Potential Employees** - NewCo should be able to attract and hire high-quality and motivated employees because they offer competitive benefits and performance based merit compensation in the form of bonus pay or possible equity interests in the form of options or grants.

C. The involvement and roles of current UMUC employees

UMUC will divest the current Office of Analytics staff in its entirety to form and run the new company. All sixteen current staff members will be offered job opportunities within NewCo. One current VP at UMUC will lead the organization and his current direct reports will hold leadership positions within NewCo. The exact organization structure is to be determined and will be approved by the newly formed Board of Directors.

The university will appoint a UMUC Senior Executive as non-compensated Board member. This executive will represent the best interests of the university and will have a fiduciary responsibility to NewCo.

Both individuals have completed the process and been granted exemptions under the UMUC Conflict of Interest Policy.

Finally, UMUC will contract back to NewCo for its current analytics services. This will

include maintaining and enhancing the technical platform and providing data analysis services. Once finalized and executed, UMUC staff will manage the contract and ensure that NewCo is meeting its contractual obligations.

D. Compensation arrangements and decision-making authority for employees of the new company, including any current UMUC employees

The compensation structure for NewCo employees will be determined by the Board of Directors. The expectation is that employees will receive base salaries plus merit compensation. The total compensation package is intended to offset the risk to employees leaving state employment and joining NewCo, and to reward them for meeting performance objectives.

All employees will be paid directly by the new company and will no longer have a formal relationship with UMUC or the State of Maryland outside of any contractual obligations related to the sale of services. Each employee who leaves UMUC to work for NewCo will complete the process for an exemption under the UMUC Conflict of Interest policy.

E. The governance structure for the new company

The new company will include a multi-tiered management structure that will govern all facets of the company:

- **Board of Directors** - NewCo will have an independent board of directors, appointed by UMUC, comprised of a UMUC executive representative, higher education industry experts and venture capital/commercial market representatives. NewCo will need to determine the obligations of each board member, board level compensation, fiduciary responsibilities, voting rights and procedures, by-laws, meeting frequency and structure, and other strategic and operational details upon starting the company. The UMUC President will appoint the initial board members upon approval of the new company by the Board of Regents.
- **Advisory Board** - In addition to the Board of Directors, NewCo will recruit a panel of public and private sector leaders from academic and commercial industries to their Advisory Board. The primary role for this board will be to promote NewCo's value proposition externally to potential customers, and provide input and direction to the NewCo leadership across topics including product development and industry trends.
- **NewCo Management Team** - The current management team will be led by a current Vice President. NewCo will have four business divisions, which include: Sales and Marketing, Professional Services, Product Development and Data Engineering. Each division will be led by a Vice President-level leader. The specific leaders for each division will be finalized prior to launch.

The NewCo management team will run the daily operations of the company and be fully responsible to achieve the company's performance objectives.

Outside of appointing the Board of Directors and maintaining one seat, UMUC will have no direct management and decision making authority within NewCo.

F. UMUC's expected business relationship with the new company

UMUC will initially contract with NewCo to provide analytics services to the university on a renewable term. The university will divest its current Office of Analytics and contract back to NewCo for these same services. Through the negotiated contract, NewCo will maintain and enhance the technical platform and provide similar data analysis services to UMUC as are provided currently.

In addition, as permitted under USM Policy IV-3.20 and UMUC Policy 190.00 on Intellectual Property, UMUC will grant a broad license to NewCo to use and develop software, as well as any business processes, branding, websites or other materials created during the development of the product.

G. UMUC's plan for investment and funding of the new company as well as any associated 'de-risking strategies'

Based on expense and revenue assumptions in the draft pro forma income statements, NewCo is forecasted to require \$10 million in funding. This range is based on different market scenarios and growth trajectories for NewCo and provides the company with both reserve funds and monies to cover operating deficits in the first three years. This seed funding will provide working capital for NewCo to start the company and ramp up ahead of, and in support of, growth projections.

Logistically, UMUC plans to provide a single lump sum investment of \$10 million to position NewCo to achieve its growth scenario. UMUC does not expect to invest additional monies going forward. These funds will be managed by the company Board of Directors and management team. The Board will review and approve a budget, operating plan and performance objectives annually and will review progress towards achieving goals on a quarterly basis. Company objectives will have specific measurable metrics around new customer acquisition, retention of existing accounts and financial performance.

Any monies spent in excess of the approved budget will need to be explicitly approved by the Board. While the initial funding will be provided in one lump sum, the spend authority will be granted annually and performance will be monitored regularly.

H. UMUC's expectation and plan for recovering its investment and possible investment return

UMUC will receive an annual net savings compared to the FY2015 budget by acquiring analytics services via a contract with NewCo versus retaining the current Office of Analytics. The savings from the synergies provided by NewCo will offset the net investment to UMUC by a material amount.

In addition, UMUC will be entitled to take an annual dividend from NewCo, once profitable, to reduce or recover its net investment over time. Company performance will dictate whether this approach is a prudent measure or if the monies should be reinvested in the company to accelerate growth.

UMUC believes that if NewCo achieves moderate success, it will be valuable to the market and can be monetized accordingly.