

VALUATION OF TENURE

presented by

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OUTLINE of TALKING POINTS

This will not be a formal presentation. We just beginning our exploration of the issues and hope your contributions will be helpful in assuring completeness of our coverage.

Tenure is a radical departure from the ordinary "at will" employment law of the USA. While not entirely accurate, tenure often is referred to as lifetime employment. The courts recognize "tenure" as a personal property right. Governments (e.g., State universities) are constitutionally prohibited from "taking" private property without due process, a public purpose, and just compensation. Tenure is different in different teaching contexts. We will focus on college professors.

We wish to focus on valuation of tenure in an arm's length transfer. Ordinarily tenure can not be transferred to someone other than the person who granted it: i.e., the employer. However, a wrongful act by either the employer or another that deprives the wronged party of use of their tenure would be valued as if it had been transferred in an arm's length transfer. Also note, a relocating professor may, in effect, transfer tenure. Additionally, this calculated value may be beneficial for institutions seeking to induce the swelling portion of their faculty that are nearing retirement to enter retirement on a more institution managed time table.

Some tenured professors exhibit mobility amongst employers; others could, but do not; some could not. The value of tenure with a specific employer moves inversely with the professor's potential mobility. Potential mobility is

influenced by variables controlled by the professor (e.g., research productivity, recognized skill as a teacher) and by variables external to the professor (e.g., household demands, market receptiveness {e.g., age discrimination}).

The value of tenure is dependant upon the professor's characteristics. (*In a fictional "arm's length" transfer the specific employer's characteristics may or may not be replaced with generic institutional characteristics, which may increase or decrease the value that could have been realized in a genuine "arm's length negotiation."*) For example, when viewed from the perspective of the market, a professor with high potential mobility may have a low mobility preference due to an external variable (e.g., children in high school).

The mean valuation of any asset is surrounded by a distribution. Market data of the mean value will embed both mobility potential and mobility preferences. Theory does not dictate that this distribution is symmetric, thus outlier effect on the mean may be profound.

Tenure signals professorial quality. The reputation value may be significant, hence a source of the professors' demand for tenure after exhibiting mobility.

The employer granting tenure influences the value of tenure. A financially secure employer with a durable commitment to the administrative unit granting tenure increases the value of the tenure. Employers with a small student base and a small endowment do make promises of work life employment with reduced credibility. The quality of the employer granting tenure is directly related to signaling effect of tenure.

The most obvious source of value is the employer's minimally conditioned promise of work life cash flows. Since employment can be gratuitous, legally, pay and tenure can be contractually separate: but, rarely is this case. However, the value contribution of employment related benefits might swamp the cash flow value. For example, a professor with an otherwise medically uninsurable spouse and an adequate alternative cash flow, may value tenure primarily for the medical insurance.

Both the front end and the back end of this career present odd valuation characteristics. At the front end, to obtain the tenure asset usually requires substantial time and resources (i.e., college, graduate school, pre-tenure). At the back end, the academic year focused employment context has produced a near global tradition of at least one-year's-notice of termination. Additionally, the traditions and legal requirements of "due process" for involuntary termination predictably add another year. Thus, at the back end, the professor's value of continued employment --due to-- tenure plummets two years prior to the

professor's anticipated retirement. The plummet is because the institution is institutionally incapable of implementing termination in less than two years. Clearly, in this two-year window employers should be able to induce retirement via negotiated exits (or mere conversion into an "at will" employment) since the institution's value of immediate termination/conversion can greatly exceed the professor's value.

Professors sell as skill set into the market. Academe is a fraction of that whole market. As measured by cash value of compensation paid per work period, for some academic disciplines, the academic fraction may be the premier employer (e.g., foreign languages), for other disciplines the academic fraction may be grossly inferior (e.g., physics). Academe is renowned for the magnitude of psychic income components (e.g., tenure, social respect, independence, moonlighting) in the compensation package. Tenure provides a risk premium that justifies a sustained pay differential. Those that prefer a smaller and stable cash flow will be drawn to academe while those that prefer a potentially much larger, but clearly more likely to be erratic, cash flow will be drawn away from academe.

Since tenure is owned by the professor personally and can not be transferred to another professor, the professor can view the inducement price of selling the professor's tenure like an option in a thin market.

The employer can view the inducement price of buying a professor's tenure like a call premium on a bond with no principle due at maturity.

The value of tenure will vary across the set of professors employed by the university. Thus, if the university offers a uniform priced "early out" provision the university should expect adverse selection in the pattern of acceptances. Accordingly, the university that offers a uniform priced "early out" must offer a lower price to reflect the greater values lost and the smaller values gained due to the adverse selection.