Minutes[*]

Senate Committee on Finance and Planning
Tuesday, September 20, 2011
2:00 – 4:00
101 Walter Library

Present: Russell Luepker (chair), Jon Binks, Sarah Chambers, Will Durfee, Lincoln Kallsen, Judith Martin, Cody Mikl, Fred Morrison, Richard Pfutzenreuter, Gwen Rudney, Terry Roe, Michael Rollefson, Ann Sather, Arturo Schultz, S. Charles Schulz,

Absent: Kara Kersteter, Kathleen O'Brien, Karen Seashore, Thomas Stinson, Michael Volna, Aks Zaheer

Guests: none

Other: Liz Eull, Emily Lawrence (President's Office)

[In these minutes: (1) framework for the 2012-13 (FY13) budget; (2) report on vice-presidential units; (3) report of the Academic Health Center Executive Steering Committee; (4) issues for the committee]

1. Framework for the 2012-13 (FY13) Budget

Professor Luepker welcomed Vice President Pfutzenreuter at 2:05 and asked him to provide an overview of the preliminary plans for the FY13 budget.

Vice President Pfutzenreuter began by recalling that every fall, for many years, the administration starts to think about the budget framework for the next fiscal year. They have started the preliminary discussion of the framework for FY13.

Mr. Pfutzenreuter moved to a review of resources and costs. The resources are from state appropriations and tuition. The costs are non-recurring and recurring, and in the case of recurring funds, fixed (the University knows with some certainty the amounts and what they are) and variable (costs that the University has a choice about). The numbers that he is presenting, he said, make the policy issues jump out. The projections for FY13 arise from the budget President Kaler recommended to the Board of Regents (which it adopted), and the data he is presenting today have been reviewed by the President and senior officers.

-- There will be $6.1 million in non-recurring state funds, carried forward from FY12 (saved for the purpose of carrying them forward).

-- There will be $16.85 million in recurring state funds. These are the funds that were not allocated on a recurring basis in FY12 (of the $25 million in increased state funding from the special session of the legislature, $8.15 was allocated on a recurring basis in FY12, leaving $16.85 million for recurring allocation in FY13).

[*] These minutes reflect discussion and debate at a meeting of a committee of the University of Minnesota Senate; none of the comments, conclusions, or actions reported in these minutes represents the views of, nor are they binding on, the Senate, the Administration, or the Board of Regents.

-- There will be approximately $29.8 million in increased tuition revenues ($18.2 million from undergraduate tuition, assuming a 3.5% increase, and $11.6 million from graduate and professional tuition, assuming an average 4% increase across colleges). Tuition revenues are recurring.

So there will be a total of $46.65 million in recurring funds for FY13.

-- On the cost side, the proposal is to use the $6.1 million in non-recurring state funds for efficiency improvements, investments that will provide future savings.

-- It is expected that there will be a $9.9 million reduction in fringe benefit costs (as explained in earlier minutes, because of swings in calculating them caused by federal regulations).

-- On the variable (institutional discretion) cost side, the plan at present is to provide 2.5% salary increases in FY13, at a cost of $19 million (this amount is for employees on O&M funds—state funds and tuition). There would be an associated cost increase of $6.6 million for fringe benefits, but given that there will be a $9.9 million drop in fringe costs, the net change in fringe-benefit costs in FY13 will be a decrease of $3.3 million.

Professor Roe observed that health-care costs are part of the benefit costs, and employee contributions will increase significantly starting in January, 2012. Mr. Pfutzenreuter again noted that the calculation of costs, required by federal rules, will be based on FY11 data. Because there will be savings to the University with the change in health-care contributions by employees, there will likely be additional decreases in fringe-benefit costs in FY14 and FY15.

In addition, the change in contributions to the Faculty Retirement Plan will save the University money, Professor Luepker pointed out. Those will come primarily in future years, Mr. Pfutzenreuter said, because the change applies only to new employees.

While the total cost of the compensation increase is $25.6 million (salaries at $19 million and fringe benefits at $6.6 million), the net cost (to units) of the increase in FY13 is $15.7 million because of the decrease in fringe-benefit costs. Everyone he has spoken with wants to deliver a salary increase next year, Mr. Pfutzenreuter related; a fourth year of cuts or freezes is not desired. Professor Durfee asked if the increase would cover unionized employees; it would, Mr. Pfutzenreuter said, and the amounts shown on the spreadsheet relate to the costs associated with O&M funds(state and tuition $) and state special funds.

-- Another projected variable cost is $2.8 million for student aid. If the University stays at 167 National Merit Scholars, that carries a cost, and the $2.8 million would cover it, Mr. Pfutzenreuter said. This is a policy choice; the University could choose to decrease the number of such students. There is no corresponding increase in graduate-student fellowships, Mr. Rollefson observed.

-- The other variable cost increases are placeholders. One is $6 million for non-academic contractual and other investments (this covers such items as software licensing, library acquisitions, and so on—these typically increase by $4-5 million per year).

-- A second placeholder is $8.55 million for strategic investments. Of the $25-million increase in funding, the President committed about $8 million to keep tuition increases at 3.5% and reserved $8.55 for FY13 strategic investments. They have not been identified; the President, along with senior academic officers, will determine them.

-- A third placeholder is $11.1 million for academic unit investments. This is the residual of the unallocated recurring resources that would accrue to academic units, Mr. Pfutzenreuter explained, and he also pointed out that this would be aside from compensation increases, which are otherwise covered.

There is no reallocation proposed for FY13, Mr. Pfutzenreuter concluded, which would be a welcome change. That projection, however, is predicated on state revenues holding up; if an upcoming revenue forecast indicates the state will be hundreds of millions of dollars, or a billion dollars, in the hole, there will be a problem. But it does not look like that will be the case; state revenues appear to be holding steady, so the state presumably will not need to take money back. The state will produce a new revenue forecast that will cover the remaining months in the current biennium sometime in early December of the current year. If the state budget holds up, the University will have money for salary increases and academic investments and will have no reallocation.

As Professor Morrison keeps reminding him, however, Mr. Pfutzenreuter told the Committee, the federal deficit is on the horizon. What the federal government does about deficits will affect units of the University. If there is no budget agreement from the Congressional "supercommittee," there will be 7.8% cuts in non-military discretionary spending. These will not be across-the-board, but will be allocated among the various non-military budgets by the Office of Management and Budget. It seems unlikely there will be an agreement, so they must turn their attention to the potential effects of such cuts on the University. Grants tend to renew, but the total available nationally may decrease, which will make grants more difficult to obtain. Agricultural funding could drop—but it will be an election year, and it is possible Congress could change the law to prevent certain reductions.

Professor Roe said he worried about the snowball effect from cuts in NIH, NSF, and the Department of Agriculture. The average cut is to be 7.8% in non-military spending, Professor Morrison affirmed, but it will be allocated by the Office of Management and Budget (OMB), an executive branch agency. OMB must reach the 7.8% target overall, but it can cut one appropriation more than another in the non-military category. The University might be favored by such decisions—or it might not—and any decisions would override previous allotments. So it is best to think about where such reductions might hit.

Another snowball effect, Professor Morrison said, is that the state will face the same problem. Some federal grants fund nearly-essential services and activities, and if those grants are reduced, the state may have to move money around to make up for the cuts.

A third snowball effect, Professor Morrison said, is that if agriculture subsidies are reduced by 7-8%--and the reductions could be larger—that will reduce the revenue base in the state.

Winter is coming, Professor Roe concluded.

Professor Chambers reported that Global Studies has already seen a take-back in federal funds. She went on to comment that most employees will be glad to see a salary increase; how much flexibility will there be in delivering them? Could that number (2.5%) go up or down? And would it be possible for units to use non-recurring funds to pay employees back for cuts and furloughs?

With respect to the latter, Mr. Pfutzenreuter said he did not know; that is a discussion that the President would need to have. In terms of increasing the 2.5%, there would have to be more funds from the variable column (so, for example, reducing the amount for strategic investments or academic unit investments) or there would have to be cuts elsewhere.

Professor Schulz inquired about $11.1 million for academic unit investments; would that money go to colleges and departments for their use? Keep in mind the budget model, Mr. Pfutzenreuter said. All revenues except state funds are attributed to the colleges. The $11.1 million falls across colleges, depending on where tuition revenues are generated and how costs impact units. Whether there will be central decisions to move state funds around will be up to the academic leaders. But the budget model provides that the $11.1 million will fall to academic units.

Professor Schulz reported that he had read earlier in the day about the implications of cuts in Medicare reimbursements and cuts in support for residency training. Those costs will fall to the Medical School departments. And the state already cut the Medical Education and Research Costs (MERC) funds, Mr. Pfutzenreuter observed.

Professor Martin said that EFS is still being enhanced. Presumably non-academic non-recurring funds could be used for that purpose. Mr. Pfutzenreuter said he hoped they would not be. They have identified existing central non-recurring funding to cover the improvements. He has said before, he reminded the Committee, that he does not know the amount of money that will be needed for Human Resources, Student, and EFS upgrades, but they could be costly. There are choices involved, and the numbers should be clearer in November or December.

Professor Durfee asked if the University plans to close again between Christmas and New Year's. Mr. Pfutzenreuter said he has heard no discussion of doing so again. Such a closing would have no impact on these numbers, Professor Durfee asked? Professor Chambers asked if there had been a calculation of how much the University saved by closing. It was not a large amount, Mr. Pfutzenreuter said; it was the savings from the furloughs that mattered. The heat was on the entire time the campus was closed, Professor Martin observed.

Professor Durfee recalled that there had been a fixed-rate cut in salaries last year. It would be interesting to have a discussion about an across-the-board increase in salaries. Mr. Pfutzenreuter said that the increases for faculty and P&A staff have always been variable (based on merit) and Civil Service and bargaining-unit employees have received fixed percentage increases. Professor Durfee suggested there could be a discussion of a fixed increase across all employee categories, the same as the way the salary cuts were imposed. There could also be a discussion to use non-recurring funds to pay those who were hit harder by the salary reduction, Professor Chambers said.

Vice President Pfutzenreuter said that this FY13 budget framework would be used in discussions with the support units (in the compact discussions) and also would be informed and updated by the state revenue forecast and events at the federal level.

Professor Luepker inquired what percentage of University revenues come from the federal government. About 15-18%, Mr. Pfutzenreuter said. The state provides about 18%.

Professor Morrison said, in response to Professor Durfee, that the Benefits Advisory Committee has discussed a grant program for lower-income employees to partially offset the substantial shift in the cost of medical premiums (with employees paying a significantly larger amount).

Professor Martin asked if there are any big surprises the Committee should be watching for. The quarterly economic update in October for state revenues, Mr. Pfutzenreuter suggested; if those numbers appear to be stable, then the December revenue forecast will not crater. Then one must wait to see what Professor Stinson will have to say about the forecast.

Professor Schulz said that a previous meeting there was a question about the use of operating funds to provide student aid, as opposed to philanthropy and fund-raising. With the proposed increase in tuition, there also appears to be an increase in the use of operating funds for financial aid. Has there been discussion of moving financial aid to philanthropy?

Mr. Pfutzenreuter said the University spends about $80 million of non-philanthropic dollars on financial aid. To change that to an endowment would require a very large amount of money. President Bruininks made fund-raising for financial aid a high priority and a lot of money was raised. But he said he could not see the day when the University would not put operating funds into financial aid. It would be fine if there were more philanthropic dollars available, and the Foundation has set financial aid as a high priority, but it is very unlikely the University could raise enough money from private sources to offset the need for additional institutional funds to support students.

Professor Luepker thanked Mr. Pfutzenreuter for his report.

2. Report on Vice Presidential Units

Professor Luepker reported that the Committee's review of vice-presidential units will be on the docket of the University Senate on October 6.

Professor Roe commented that the budgetary data the Committee had seen was sufficiently complex that if the University were serious about evaluating it, it would bring in a consultant to look over the numbers. This is very complicated, he said. Professor Luepker agreed and said that he had thought at first that the data would sort out clearly, but any of the organization charts tells one that things are too complex to make that possible. That does not mean the institution should not look carefully at the numbers, but this Committee cannot do so. Nor can the Senate, Professor Martin added.

The fluctuations in the budgets and the number of employees raise questions about performance, Professor Roe commented. Does performance vary with the changes? In some cases, the number of employees goes up but the expenditures go down, Professor Chambers added.

Professor Martin surmised that members of the Senate, after reading the report and seeing the comments about possible duplication across administrative units, might ask how to fix the problem. People will want more detail. Professor Luepker said his response would be to say that the administration should go through these units piece by piece to determine which are fulfilling their mission in a cost-effective way. He said he believes that is President Kaler's approach, one that the Committee supports.

And what about the college level, which the Committee did not look at, Professor Martin asked? At the last meeting the Committee agreed it would invite in a selection of the colleges, Professor Luepker recalled; the Committee is aware that there are a number of parallel systems in colleges and the central administration, such human resources, communications, legal staff, and so on.

Mr. Rollefson said it was his understanding that President Kaler, when at Stony Brook, had tackled these kinds of issues with a consultant. Ms. Eull reported that President Kaler is just starting conversations with the senior officers; she said she did not know how they would evolve. The President does, however, have a significant interest in operating efficiencies.

Professor Durfee suggested that when the recommendation from the Committee is articulated at the Senate meeting, advising the administration to look at expenditures in support units, it might be asked "what administration?" It should not be each vice-presidential unit looks at itself, because that approach will not identify duplication. There should be an independent group that can look at the units as a whole, perhaps the President's office or a "supercommittee" of some kind. Professor Luepker said he thought that an excellent idea; vice-presidential units can look within but not readily at the overlap. He said he hoped the report would be helpful.

3. Report of the Academic Health Center Executive Steering Committee

Professor Luepker next said he wished to put the report of the Academic Health Center (AHC) Executive Steering Committee on the table and alert the Committee that it is a report the Committee will take up. When the Committee started its reviews of vice-presidential units, the AHC had the Executive Steering Committee looking at structure, at the request of President Bruininks, so the Committee did not have a conversation with the Vice President for the AHC.

Professor Luepker related that he has heard a number of opinions about the report and what it recommended (or did not recommend). The AHC Faculty Consultative Committee has been discussing the report, as have the AHC deans. He summarized the recommendations and suggested that the Committee educate itself and discuss the report.

Professor Roe said that perhaps a simple and appropriate question is "to what extent has the AHC been a 'cost' to the rest of the University?" It has in the past gone over budget and had commitments to tenured faculty that it did not have funds to support; does it make sense to ask such a question? It does make sense, Professor Luepker said, but it plays into the urban legend that the rest of the University rescued the Medical School. He said he did not know if that is true. The Committee may recall that at one point Senior Vice President Cerra reported the Medical School had a $20-million structural deficit, and he later reported that it had been partly addressed through a loan from the University.

Professor Morrison provided a short history of the financial issues that had arisen with the AHC in the last 40 years and said that he worried the University would see problems similar to ones that have occurred in the past. The AHC faces declining clinical revenues, the loss of state and federal funding, increased squeezing from insurers, and increased demand from indigent patients (with whom the hospital must deal, at its own cost, which is a problem both for Fairview and for the clinical faculty in the Medical School). He said he hoped there is planning underway on how the University will respond to these circumstances. Dealing with them will not be easy, especially when the University's treasury is not as flush as it was in the past.

And Fairview cannot help because it has its own troubles, Professor Martin observed.

Professor Schulz said Professor Morrison had provided a good summary and noted that there have been financial hits on medical centers in the past; there will be challenges. Dr. Cerra worked hard to reduce the deficit; the Medical School and AHC departments are working hard to balance their budgets. The Dean of the Medical School, the CEO of University of Minnesota Physicians, and the Fairview CEO have been working on ways to work more efficiently, and Fairview is now paying for residency overhead expenses, such as training directors' support. That few million dollars has helped every department. With challenges, however, has come a much stronger and more transparent examination of budgets than was the case 10-12 years ago. Vice President Friedman is able to lay out the issues.

The Medical School, Dentistry, and Veterinary Medicine are highly dependent on clinical revenue, Professor Luepker said, but as he understands it, money for AHC infrastructure expenses comes from the cost pools.

Committee members discussed several elements of the AHC budget as laid out in some of the data tables in the report.

It was agreed that the Committee wished to hear from Vice President Friedman and Ms. Nunnally, the AHC CFO, after the Faculty Consultative Committee has the AHC report with them.

Mr. Kallsen said that the Medical School revenue streams are complex and have become more so over the years, and that other AHC colleges are seeing increased complexity in revenue streams as well. The question is how to deal with fixed costs when some revenue streams fluctuate quickly?

4. Issues for the Committee

Professor Chambers said there are two issues that she would like the Committee to hear about: the 27 pay periods and Google. In the case of the latter, what are the financial ramifications of outsourcing email and so on?

Professor Luepker said the Committee will also wish to hear about developments with EFS.

Professor Roe noted that employees will soon be receiving information about health care for 2012, and some will be surprised at the numbers. The Committee should discuss them.

Professor Morrison said he could do so at the next meeting. Information about open enrollment will be provided in mid-October and open enrollment will be during November. Prices are going up substantially, about 37% for employees. The University had a good deal in the past; now it is a slightly-less good deal. For family coverage in the base plan, the cost will increase about $26 per pay check. The big change was going from two plan administrators to one; the Benefits Advisory Committee (on which he serves) looked at the cost of having a second plan administrator, about $2 million per year. So the decision was made to go with one plan administrator, Medica, and not use HealthPartners as an administrator. Employees will still be able to choose HealthPartners for medical coverage, but at a higher cost. There was considerable cross-subsidizing in the old plan; the new one largely eliminates it. The large increases in employee costs is what led the Benefits Advisory Committee to propose a grant program to subsidize part of the cost increase for lower-paid employees, on a sliding scale.

Professor Chambers recalled that there had been discussion about the distribution of the cost between premium increases and co-pay increases. Professor Morrison said that they split the difference, but recommended only modest increases in co-pays and more substantial increases in premiums.

Professor Luepker said that health insurance would be on the next agenda and adjourned the meeting at 3:45.

-- Gary Engstrand

University of Minnesota