Minutes*

Senate Committee on Finance and Planning
Thursday, June 14, 2001
9:00 – 11:00
238A Morrill Hall

Present: Charles Speaks (chair), Jean Bauer, Stanley Bonnema, Charles Campbell, Daniel Feeney, Stephen Gudeman, Wendell Johnson, Joseph Konstan, Michael Korth, Eric Kruse, Elo Charity Oju, Richard Pfutzenreuter, Jane Phillips, Susan Carlson Weinberg

Regrets: Brittny McCarthy Barnes, David Chapman, Terry Roe, Rose Samuel, Cory Stingl, Michael Volna, J. Peter Zetterberg

Absent: none for a summer meeting

Guests: Executive Vice President Robert Bruininks, Professor Fred Morrison (Faculty Consultative Committee)

Other: Suzanne Bardouche (College of Liberal Arts), Florence Funk (Office of the Executive Vice President and Provost)

[In these minutes: the budget]

The Budget

Professor Speaks convened the meeting at 9:00, welcomed Executive Vice President Bruininks and Professor Morrison, and turned to Mr. Pfutzenreuter to begin the discussion.

Mr. Pfutzenreuter said that budget plans are being made assuming the University will receive about $110 million from the state, about $90 in O&M funds and about $20 for the Academic Health Center from the tobacco endowment funds. There has been a rumored "lights on" proposal, which would provide the University with $62 million; there are no plans being made for that contingency. There are various versions of shut-down plans being considered, with various contingency plans, but the approach is not to panic and to take no action on July 1 because it is assumed the state will get the situation straightened out shortly.

Mr. Pfutzenreuter said he believed the University should plan around the $110 million and bring the Board of Regents, on June 26, a budget using that number. If there is no legislative agreement, so be it, he said, but eventually there will be. If the amount appropriated is different, then recommended adjustments will have to be brought to the Board. The plan now is to bring the entire budget package to the Board with the understanding that it is subject to legislative action.

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

In developing the internal budget they have been going through a variety of options, Mr. Pfutzenreuter related, on how to fashion the Internal Revenue Sharing (IRS) tax, tuition, and how much of tuition will be taken by central administration--the internal distribution of revenues. The $110 million, he noted, is not enough for the President's investment plan, which includes a 3% general salary increase for employees, separation from the state for health care (which actually saves an estimated $11 million over the biennium), a minimum annual compensation level for University employees, and small investments in undergraduate education (faculty, advising, classrooms). There are other costs which must also be paid: opening new buildings, paying debt, paying the increase in utility bills.

Will the libraries and technology components of the biennial request be funded, Professor Speaks asked? There will not be substantial new funding for them, Dr. Bruininks said. His view, with which Senior Vice President Cerra agrees, is that these items should be a top priority in the compact process. There will be about $2 million in recurring funds available next year; depending on what happens with tuition and the biennial request, there could be $3-4 million in the second year of the biennium. There will be nothing for the libraries in the budget allocation, Dr. Bruininks agreed with Professor Morrison, but emphasized that he wants to identify ways to put money in them out of the compact process. Professor Campbell pointed out that the serials crisis in the libraries could consume the entire $2 million. Dr. Bruininks said he needed advice on whether budgets should be cut elsewhere to deal with that problem. Of the $110 million, he noted, $20 million is committed to the Academic Health Center so cannot be touched.

Mr. Pfutzenreuter reported that the President had also asked that the budget models also include an additional 2% (above the 3% general salary increase for all employees) for faculty salary increases next year and an additional 3% the second year. Are those to be merit or special merit, Professor Speaks asked? More special merit, Dr. Bruininks said, to deal with recruitment, retention, and market conditions; the money will be allocated to the colleges to be distributed by decision at the local level; deans and chancellors will decide how to use the money.

How will the increase be funded, Professor Speaks asked? All money is green, Mr. Pfutzenreuter said--it will come from the IRS tax, tuition, state funds. The legislature will ask what the University spent its state funds on but the University does not segregate the funds when it pays costs; the state funds could be attributed to facilities or salaries or however one wanted to assign it. There was a proposal to fund salary increases in proportion to the amount of a college's budget that came from tuition, Professor Speaks observed; that is the plan being considered. In terms of the 3% general salary increase, if one subtracts the part that is proposed to be covered by tuition, Mr. Pfutzenreuter said, it equals $29 million, or the amount of the first-year appropriation for the next biennium (assuming the $110 million).

Dr. Bruininks said that balancing the budget will be accomplished roughly in thirds: by increasing tuition, from state funds, and by cost reductions/cuts/internal reallocation. On the latter, he said, the University said it would do it, the legislature expects it will do it, and the University will do it. There will be a need for hard decisions.

Other investments to be made include 10-13 new computer and information science faculty, Mr. Pfutzenreuter told the Committee, core needs in the Academic Health Center (the endowment will generate about $5.6 million the first year, about $14 million the second, and over $17 million the third year; Dr. Cerra has identified how the money is likely to be spent). Some funds have been earmarked by the legislature for state specials (although a very small part), some funds will have to be used for financial aid because tuition will be increased, there is $10 million in one-time budget needs, and there are other recurring University financial needs such as leased space, legal costs, technology needs, and commitments that must be kept. The challenge is to figure out to pay for these investments.

There will be natural growth in the IRS, and the central administration's share of ICR funds; there is also about $3 million in one-time money, state funds will increase by $110 million, and there is tuition. The assumption is that there will be a significant increase in tuition. The Committee discussed with Dr. Bruininks and Mr. Pfutzenreuter the possible rate increases that might be considered.

Professor Speaks noted that the University had requested $221 million for the biennium; with tuition increases at certain levels, plus $110 million, much of that request could be covered. Mr. Pfutzenreuter explained that that was not quite true. The initial figure, for University needs, was about $274 million; when $30 million in internal reallocation and about $23 million in additional tuition revenues (a 3% increase) were subtracted, the net biennial request was $221 million. However: there are additional University needs that it has not asked the legislature to support (e.g., increased financial aid with a tuition increase, lease costs, legal costs, technology needs) and one needs to add about $55 million to the original $274 million figure, so the total is about $329 million. If one presumes $110 million from the state and perhaps $108 million in tuition, there remains $111 million in costs that are not funded. This means that some will not be; there will not be additional dollars for, among other things, Facilities Management for building maintenance and for new faculty, and faculty salaries will not be increased an additional 4% (above the 3% general increase) each year of the biennium.

Professor Campbell said he would repeat a point he has made before: when all of the discussion about development of the budget has taken place, it was never said there was an additional $55 million in costs that needed to be covered. To put the $55 million in perspective, Mr. Pfutzenreuter said, each year there seems to be about $12-15 million in things the University must pay for and for which it cannot ask the state for the money; $15 million continued into the second year of the biennium, plus $15 million in the second year, totals $45 million; when an additional $10 million in non-recurring items arises, the total is about $55 million in items that the University cannot ask the state to pay for.

It may not be able to ask the state for the money but it would help those who participate in the planning and consultative process to know about those numbers, Professor Konstan said. Dr. Bruininks agreed that one could say these items will crop up every year but one cannot anticipate all that will arise in a $2 billion budget. What one CAN know, Mr. Pfutzenreuter agreed, is that there will ALWAYS be this $12-15 million in expenses. Professor Campbell agreed with Dr. Bruininks' observation that the University could build in a "stuff happens" budget line. Dr. Bruininks said the budget model is becoming more mature (e.g., it accounts for funding building depreciation) and there are central costs--which are not the idea of some administrator about how to spend more money; one example is a significant rise in costs of interpreters. Many of these unpredicted central costs arise as a result of pressure on academic units and the list of them to be paid has been pared by about half so far; if the list is cut any further, he cautioned, units will see bad things happen. While the budget model must include a way to fix problems, the University must also curb its appetite, Dr. Bruininks said.

The University must set aside reserves for contingencies, Professor Gudeman said; if it knows X% of the budget will routinely arise, that amount should be planned for. Dr. Bruininks agreed and said his only point is that there is a lot of shared responsibility for those costs and they will not go down. The costs of a university do not reflect the CPI, he added; to be on the cutting edge in research and recruit the best people it can are more costly.

Most of the items that Dr. Bruininks mentioned--labs and salaries--are carried by academic departments on fixed budgets, Professor Morrison observed. He also said he was happy to hear that an item would be built into the 2003 budget for unanticipated expenses; if there is an item, people responsible for commitments must live within that budget rather than hand the list to Mr. Pfutzenreuter and tell him to find the money. This will force these items within a budget, which is very important. finally, Professor Morrison said he had heard nothing about assessing the value of what the University is doing; if the budget is this tight, one can ask if the University must open its new buildings rather than lock them and postpone opening them for a year, or if the University should be putting $8 million into intercollegiate athletics when other universities are meeting gender equity guidelines by cutting programs rather than adding them. Is the University looking seriously at such options? Or is it spreading the pain all around, affecting all programs? Mr. Pfutzenreuter again noted that the budget would be balanced by allocating one-third of the problem to tuition increases, one-third to state increases, and one-third to cost-savings and reallocation. The latter includes a target of $6 million in cuts in recurring funds the second year of the biennium.

With respect to tuition increases, is the projected amount the maximum that could be expected--does it assume student behavior will remain the same, Ms. Phillips asked? Dr. Bruininks affirmed that the tuition number assumes behavior will remain the same. There is some concern that there may be a drop in demand. But the University has work to do: students take too long to graduate, they take too few credits, and there are high costs for that, both for the University and the student. The half-price tuition for the 13th and subsequent credit was an attempt at an incentive for students to take more; the University must work very hard to make sure the numbers do not drop.

The University is checking with other institutions; it appears that most public institutions in the Midwest have been underfunded for 20 years and are going to push the limits on tuition. If there is a financial safety net, and the actual DOLLAR increase is not prohibitive (perhaps $500 per year next year at the University), the impact on behavior should be minimal. Professor Speaks suggested that with the decision on tuition coming so late, the impact on enrollment next year may be misleading; any impact will more likely be seen the following year.

Professor Campbell asked, apropos enrollment and tuition, if there was liable to be a shortfall and another penalty (part of the one-time recurring costs the University must pay is a penalty to the state for not meeting enrollment goals)? Mr. Pfutzenreuter said the possibility exists. Is the University taking steps to avoid the possibility, Professor Campbell asked? He said that the large undergraduate colleges surpassed enrollment targets but the University still suffered the $6 million penalty. There appears to be a communications problem. Mr. Pfutzenreuter said he would welcome advice from the Committee on this issue. Dr. Bruininks agreed that the University should not create problems because of prediction errors.

Professor Speaks then observed that if, under Incentives for Managed Growth (IMG), all agree that funds for central administration for all-University costs must be identified, what models are being contemplated for deriving those funds? Mention has been made of the IRS. Second, he recalled that the Budget Management Task Force, chaired by Dean Rosenstone, recommended a single, all-funds tax.

Mr. Pfutzenreuter said his office has modeled many different ways to balance the budget and deliver revenues. The President asked for four options; Mr. Pfutzenreuter distributed a one-page handout laying out four possible ways to structure the budget to pay for central costs. Those four alternatives were:

A: Use the budget model for this fiscal year; there would be no change in the attribution of tuition but the academic unit IRS rate would increase from 2.25% to 4.75%. The general tuition increase would be 13.8%.

B: Central administration would implement a $200 annual "enrollment fee," calculated for each semester as $10 per credit up to 10 credits, and the academic IRS rate would increase from 2.25% to 3.75%. The general tuition increase would be 10.1%.

C: 25% of the GROWTH in tuition revenues between the current year and next year would be transferred to central administration; the academic IRS rate would increase from 2.25% to 3.75%. The general tuition increase would be 13.8%.

D. 65% of the growth in tuition revenues between the current year and next year would be transferred to central administration and the academic IRS rate would remain at 2.25%.

Models A and D "are viewed as the two bookend options for comparison purposes," according to the handout. In none of the models would there be any change in the Enterprise Systems Project tax; all four options would generate about the same amount of money for central administration to pay for all-University expenses, approximately $25 million.

The handout also identified on a table, for each college and campus, the net impact of each option after calculation of the IRS, tuition income, and state funds (in all cases holding the Enterprise Systems Project tax constant). Professor Gudeman observed that the table of data indicated there is tremendous differential in the impact of the options on different colleges, varying with how dependent a unit is on tuition revenues and state funds. He also said that there are bigger issues involved than simply who gets what, such as what happens with support units and the environment for units that are more tuition-dependent. These require planning discussions about the direction of the University.

[A few illustrations from the table; ( ) indicates a net negative impact of the option, numbers without parentheses indicate a net positive result from the option]:

	A	B	C	D
Duluth	(418,705)	151,689	375,773	60,372
Morris	(1,178)	133,490	148,093	50,291
COAFES	(347,644)	(308,181)	(262,064)	(123,842)
Carlson	673,369	931,833	380,630	(85,458)
General Coll	(599,590)	(688,369)	(502,950)	(347,915)
IT	981,360	642,897	548,318	(139,583)
CLA	1,492,815	225,752	408,070	(1,322,199)

Dentistry	(436,715)	(336,574)	(310,749)	(107,777)
Medical Sch	(1,795,940)	(1,050,701)	(998,412)	284,522
Pharmacy	553,247	465,092	466,497	328,420
Vet Med	(502,427)	(252,184)	(291,849)	46,916
Ag Exp St	(1,206,381)	(739,822)	(739,822)	(39,983)
MN Ext Svc	(1,089,402)	(667,430)	(667,430)	(34,471)

Dr. Bruininks noted that tuition remains 15-20% of the revenue base. There have been commitments to the units in the past; one can, however, raise questions about what will happen in the future. Professor Gudeman said his question is not about "values" but is more pragmatic: what kind of university can this be in this kind of environment. Dr. Bruininks said there is not agreement on the issues and a need for conversation about them. The people of the state may not accept the idea of a different kind of university.

Professor Speaks said the underlying point is that the central administration has bills to pay and must have revenues; the table of four options demonstrates the different distributional effects of alternative ways of generating that revenue.

The table puts the cart before the horse, Professor Morrison opined. It is useful but if one is going to talk about allocating revenues there must be an understandable system that is built on some kind of principle (rather than on whose ox is being gored). Who should be contributing to the overall costs of the University? Should the money come from overall University revenues or only from what the students pay? If the University uses the fee (option B) or 65% of tuition, one is saying that the costs of services that are partly or largely not tuition-based should be borne by the students.

One could make that argument, Dr. Bruininks agreed, but one could also make the argument that all cost increases are attributable to students--financial aid, faculty salaries, and so on. The costs for buildings that house research facilities (e.g., heating, lighting), Professor Morrison pointed out, are also borne by students when tuition is taxed. Part of the costs must be paid by a general assessment on all revenue sources, he maintained; as for tuition, should it be based on a % of the revenue or on headcount (as with the fee, option B)?

There are no simple answers, Dr. Bruininks said. Decisions made last year will remain intact; the question is what to do about tuition, on which there is a split in opinion. Tuition needs to be added to the funding model to some extent because it is increasing as a source of revenues to fund the University, if one makes the assumption that a new funding model is evolving. Other models are being considered, Dr. Bruininks said, such as attributing more costs to units and increasing the IRS on that basis.

Why not a tax on all funds, Professor Speaks inquired? He also asked if there is any plan for a tax on balances. Mr. Pfutzenreuter said that the University has $10.2 million in one-time needs that must be paid; his office has developed a methodology for apportioning that cost to central and academic units and each will be sent a bill. How the units pay the bill is up to them. Is the amount assessed each unit based on balances, Professor Speaks asked again? It is partly based on balances, partly on revenues, Mr. Pfutzenreuter responded.

Professor Konstan said that there are different short-term and long-term models. For the short term, the valves are all locked and the pressure is building. One can increase tuition because tuition is available, but it is mostly in the undergraduate colleges. There is a very different long-term question: is putting 100% of tuition income in the colleges the right way for a university to budget? Answering the latter question will take more than two weeks. Right now the consideration is about a band-aid.

Dr. Bruininks agreed but said the point does not go deeply enough. Tuition is available but the University must also cut costs. Any assessment model will have long-term effects and the University should not raise tuition because it is convenient. At the same time, there has been a conscious decision over the last 20 years about public higher education; if one looks at the gap between needs and revenues, it has been largely made up with tuition, sponsored funds, and gifts. The argument is about what kind of university this institution will be.

Professor Morrison said he agreed with Professor Konstan and the point is tied to what principle will be used--something that cannot be solved this year. These plans are unstable, he pointed out, and in two years another band-aid will be needed. (For example, if the central administration is dependent on taxes on INCREASES in tuition, it will receive very little if the tuition increase is 4%; model C works only when there are large tuition increases, thus delivering significant revenues for central costs.) The University must work toward a system that will produce a predictable result, as recommended by the Budget Management Task Force.

In a more tuition-dependent environment, what has the legislature done about allocating money for financial aid, Professor Gudeman asked? There will be only inflationary increases, Mr. Pfutzenreuter told him. If tuition is increased significantly, some of the money must be set aside for aid, Professor Gudeman then commented. Dr. Bruininks pointed out that part of the capital campaign includes funds for student financial aid, although that part of the campaign has been less successful than others and needs to have a higher priority. He agreed that more money needed to go into financial aid.

Professor Campbell said that the asymptotic limit on central administration revenues will be 25% of tuition, under option C: as time passes, and the administration takes 25% of the increase in tuition revenue each year, the total taken will begin to approach 25% of ALL tuition. He said that it appears the University is giving up, on short notice, on one principle it worked very hard on: IMG. All who looked at the budgets recognized the need for the administration to have revenues; the question is how they should be generated. The options identified will be a shock to the system and will mean giving up a substantial portion of IMG with very little discussion.

Moreover, Professor Campbell said, taxes on balances are about the worst possible principle to adopt and it cannot be justified without notice. It will lead units to determine that they will not, in the future, have balances. (Dr. Bruininks expressed doubt that because the administration taxes balances once, at a few percentage points, units would decide to eliminate balances.) Professor Speaks agreed with Professor Campbell: units that have not engaged in wise financial planning will be immune from the tax and units that have deficits will be protected. He said he would prefer to see a non-recurring surcharge on the IRS to pay one-time costs than a tax on balances. Mr. Pfutzenreuter said the model relied .36 on the IRS but that could, for example, be doubled. He surmised, however, that bill to the deans, however derived, would be paid with funds in balances. This has been argued internally as well, Dr. Bruininks observed, and can be revisited--in the next five days, because there is a problem that needs to be fixed.

A more long-term, philosophical question, Professor Feeney said, is that it seems no matter what option is selected, it affects units differentially. Fixing the problem for one unit creates problems for another, as the results of imposing different options demonstrates; there appears to be no one model that works for all units.

Dr. Bruininks agreed. Not all revenues are included, such as endowment funds; building debt is not included. If the Academic Health Center taught more students, the results would be changed. He said he is not proposing any change in what the units do but only pointing out that there is much that is buried behind the numbers for each of the models. He agreed that option A cannot be the only one used to generate revenue for all-University expenses, but at the same time the choice should not destroy the incentives built into IMG; it may be necessary to use a combination of options.

One lesson for him, Mr. Pfutzenreuter related, is that the University cannot develop a taxing mechanism that makes everyone happy. With these models they have made everyone mad at each other. He said that he is an "IMG purist" and would allocate costs and then use option A, with the administration generating sufficient funds to deal with problems that arose.

Professor Bauer said that if all four options generate about the same amount of money, then one need look only at the distribution effects. The options with fewer distribution effects will be easier to explain to the University community.

Dr. Bruininks said that the University cannot spend its energy arguing over these options each year; it must develop an assessment mechanism. The President believes the system was flawed when it was implemented (because the central administration has too few resources to pay all-University costs) and this argument should not be necessary every year. The President maintains that there must be funds for central needs and the administration should not have to beg for them every year. The system needs to be refined so that the other big questions facing the University can be addressed. The administration is looking at cost attribution. The President is also coming to the view that the University needs a different funding strategy; it will not necessarily be easy to convince people that this is the way the University should proceed.

A formula cannot solve the problem, Professor Konstan said; it is good at creating incentives but the University still needs leadership to say what will be emphasized and what will not. For example, whichever formula is chosen will affect the Medical School and the Extension and Experiment Station in the same way; the University must first decide whether it wants to treat those units similarly or differently, rather than depend on a formula that cannot distinguish among them. He maintained that option A was simplest but that the University must be sure under option A that there is enough money centrally to help the units that are disproportionately hurt and need help.

Dr. Bruininks said that the administration was listening carefully to the deans and this Committee and trying to develop a model that would work in the future. He said, however, that he could not get a reading on what the Committee wished. Option A could be adopted because it is a simple tax; options B and C may not work in future years; the effects of A could be smoothed out; more costs could be attributed to units. Should the administration attribute more costs and lower the IRS? The unattractive part of that option is that some units would receive a mandate without additional funds.

These are all new questions that would lead to a shock to the system if imposed for this biennium, Professor Campbell objected.

Professor Speaks asked what the Committee's preferences were. Professor Feeney said he hoped for a one-year fix and then consideration given to a more permanent solution. He urged adoption of the KISS principle advocated by former Senior Vice President E. F. Infante: Keep It Simple, Stupid. His preference is for the model that has the least differential impact. He noted that FCC has asked this Committee to be more involved in working out a solution.

On a show of hands, Committee members cast 6 votes in favor of option A, 2 in favor of B, 2 in favor of C, and none in favor of D. At least one Committee member abstained.

Professor Speaks noted that the Regents will meet on June 26 for a preliminary review of the budget. He suggested, and the Committee agreed, that it would meet again on Monday, June 18, to consider the options that have evolved by then, before materials go to the Regents. Professor Speaks said he would be out of town; Professor Campbell agreed to chair the meeting on June 18. He said he would, in the meantime, draft a statement for the Committee to consider.

Professor Speaks commended Committee members for setting aside self-interest and for trying to look at the broad interests of the entire University. That approach continued at this meeting, he concluded, and adjourned the meeting at 11:00.

-- Gary Engstrand

University of Minnesota