Minutes*

Senate Committee on Finance and Planning
Tuesday, June 6, 1995
3:15 - 5:00
Room 238 Morrill Hall

Present: Fred Morrison (chair pro tem), David Berg, Thora Cartlidge, Mark Davison, Thomas Hoffmann, Karen Karni, Gerald Klement, Patrice Morrow, Richard Pfutzenreuter, Doris Rubenstein, Craig Swan, James VanAlstine

Regrets: Virginia Gray, Craig Dexheimer, Anne Sales, Thomas Scott

Absent: William Gerberich, Allen Goldman, Roger Paschke

Others: Kathy James (sitting in for Anne Sales)

[In these minutes: The 1995-96 and 1996-97 budgets]

Professor Morrison convened the meeting at 3:15 and explained that Professor Gray had asked him to chair the meeting in her absence, because he is incoming chair. He reported that Professor Gray, in turn, will remain as chair through the end of September because he will be out of the state for much of the summer and early fall. After calling for introductions, he turned to Mr. Pfutzenreuter to walk the Committee through a set of slides outlining the 1995-97 budgets.

Mr. Pfutzenreuter began by noting that this is a TWO-year plan that adheres very closely to the original partnership proposal made to the state. It balances the budget, avoids structural imbalances, and is designed to provide maximum programmatic flexibility. It also calls for a "clear delegation of financial accountability and strong stewardship of scarce resources."

He then reviewed the investments and financial needs contained in the updated partnership proposal and noted that the total costs for the two years are projected to be $8.2 million than in the original proposal. This increase is due to increased fringe benefit costs, a delay in the steam plant debt service, and miscellaneous additional expenditures, all of which net out to $8.2 million.

It was recalled that the Committee had been informed of $13 million in "additional financial pressures," items that the administration believed had to be dealt with. Are those included in these projected budgets? They are, Mr. Pfutzenreuter affirmed, although the amount has been reduced to $6.2 million. Decisions were made to scale back or eliminate some of the items that were on that list. He also said, in response to a query, that this biennial budget plan includes no funds for conversion to semesters.

Mr. Pfutzenreuter then discussed the impact of budget caps. The cap for the 1995-97 biennium

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was $908.2 million, while the 1994-95 budget doubled totals $924.3 million--which means that if the caps had been observed, the University's appropriation would have declined by $16.1 million for each year of the biennium. The legislature appropriated $968.9 for the 1995-97 biennium, but most of the increase is ONLY for the biennium, and since $16.1 million was needed to retain current spending levels, only $44 million represents new money. The budget cap for the 1997-99 biennium is $915.1 million, which means that the expenditure levels for the next two years will drop markedly if that $915 million cap is adhered to for the 97-99 appropriation. The starting point for discussions for the 1995-97 biennium will thus be BELOW the base spending in 1994-95.

If the 1997-99 cap of $915.1 million is observed, that means that $53.8 million of the funds for 1995-96 are non-recurring (the actual appropriation of $968.9 million minus the $915.1 million cap).

Factors that have affected the partnership proposal are (1) fewer resources than needed ($37.3 million), because of the lower appropriation than requested ($27.X million) and a tuition revenue shortfall ($9.X million over the next biennium), and (2) increased financial pressures of $8.2 million. The total shortfall is thus $45.5 million. At the last Board of Regents meeting, the administration presented five or six options that could be selected to close the gap.

The means selected to resolve the problem are increased tuition revenues and increased reallocation. One Committee member noted that tuition revenues could be increased by increasing the RATES or by increasing the number of students. It appears that in CLA, for example, the number of new students will be larger; does the amount expected from tuition include both rate and number increases? The original projections called for a 4.8% increase in revenues, Mr. Pfutzenreuter said, and assumed no increase in enrollment. The revised projections call for a 7.5% increase in tuition revenues (about $15 million more in revenue), and also make no assumptions about increased enrollment.

Mr. Erickson pointed out that while new student enrollment may increase, transfer student enrollment may decline. He added that the administration is tried to be VERY conservative in estimates of tuition revenue, because it is debilitating to miss the projection by $3 million; one can HOPE that tuition revenues will be greater than estimated, but the budget will not rely on that hope. Mr. Berg said that the numbers of students are projected to be up in all but one of the colleges, but the issue revolves around returning students. When the economy is healthy, students do not return in the same numbers as when it is not.

Mr. Pfutzenreuter then reviewed the reallocations proposed. The original partnership proposal had called for reallocations of $14 million for each year of the 1995-97 biennium, for a total of $28 million. The increased reallocation required by the resource shortfall will require an additional $11.4 million each year of the biennium plus an additional $7.1 million the second year. The chancellors, provosts, and vice presidents have been asked by the President to identify by September 15 where the additional reallocations will be made.

Asked if the reallocations will be pro-rata among the chancellors, provosts, and vice presidents, Mr. Pfutzenreuter said they would almost be; he said he did not know if there would be differential impacts on the colleges. He also said there are no plans for allocation of the additional $7 million in reallocation the second year of the biennium; the President and the Executive Council will discuss them. Messrs. Erickson and Pfutzenreuter were asked to carry the message to the President that the Committee would like to discuss the parameters for the reallocations.

One Committee member noted that the one piece of "good" news is that units will only be retrenched $7 million in the second year of the biennium. Mr. Pfutzenreuter said that the approximately $25 million retrenchments the first year amount to about 3.5% of centrally allocated funds (the O&M base); the $7 million the second year equal about 1%.

Discussion then turned to how the $53.8 million in non-recurring funds will be dealt with. Mr. Pfutzenreuter explained that for both 1995-96 and 1996-97, the budget work sheets for the chancellors, provosts, and vice presidents identify those funds that are recurring and those that are not, and there will be an audit trail available so that the non-recurring funds can be pulled out for the 1997-99 biennium. The units will be expected to spend the non-recurring funds in such a way that the University does not create problems for itself.

A big issue for the second year of the biennium is compensation; it may have to be a lump sum increase. Another change is that many of the funds for facilities have been changed from recurring maintenance to one-time building projects. He said this does not mean buildings will not be maintained; what it means is that funds identified in the partnership proposal to bring them up to the maintenance standards recommended in the Brenner committee report will not be available.

For 1995-96 and 1996-97 there will be $60.8 million (in both recurring and non-recurring funds) for salary adjustments and other programmatic needs. Mr. Pfutzenreuter said that the salary proposals needed to be articulated by Academic Affairs.

It must be candidly recognized, said one Committee member, that the compensation plan in the budget is a rejection of the report of the Compensation Working Group, represents an inability to implement it in any way, and that there is no progress on the report either planned or in the budget. Mr. Erickson observed that salaries in different disciplines may vary, because units can look to positions and other avenues to fund salary increases. This is a departure from past practices, when the central allocation for salaries WAS the plan; that is not the intention this year, except for civil service and bargaining unit employees.

Mr. Pfutzenreuter then outlined the proposed changes in tuition policy. One is to change the tuition band, to move to a common upper division tuition rate, and to impose a $30 registration fee. Actual tuition increases will vary by unit and level of registration. A lower division student taking 5 credits will see an increase from $354 to $400 per quarter, or 12.9%. A lower division students taking 14 credits will see an increase from $991 to $1065, or 7.4%; a student taking 18 credits will see a change from $991 to $1139, or a 14.9% increase. It was suggested that if the beginning of the new tuition band is 15 credits, there should be an example of the change for taking 15 credits; that, after all, is the rate at which students must enroll in order to graduate in four years.

The indirect cost revenues are the one bright spot in the budget, projected to be up by 5% next year; the University's rate has increased to 47% for the next four years. They are, however, threatened by federal actions, so the projected revenues have been held flat for the second year of the biennium. These funds are not affected by the grants management project, he reported. It must be recalled, pointed out one Committee member, that if there are smaller departments and fewer faculty, there will also be fewer grants and thus less indirect cost recovery money. Another observed that the ending balance for the ICR funds will be .05 of 1%; Mr. Pfutzenreuter said it is traditional to allocate all of this income.

The Committee next considered the central reserves. The balance beginning in 1995-96 will be $19.1 million; the ending balance (beginning balance for 1996-97) will be $16.6 million, with a projected balance at the end of 1996-97 of $20.4 million. Mr. Erickson cautioned that $5 million of the income projected for 1996-97 includes the sale of assets. It was noted by one Committee member that replenishing the central reserves by selling assets is a short-term option. Mr. Erickson agreed, and pointed out that there are also substantial liabilities looming in the near future. The numbers do NOT reflect additional charges to the reserves, which are likely.

Mr. Erickson also told the Committee, in response to a query, that the University is selling land which has been determined not to have research value, and that there is a real estate advisory committee. The University has huge land holdings, some in mineral rights to land administered by the DNR and some dedicated to the University mission (such as Itasca, Cedar Creek, and so on.) It was suggested that one item the Committee could take up next year is the parameters being used by the real estate advisory committee.

The deposit of funds from the sale of surplus property is part of the strategy to rebuild the central reserves, Mr. Pfutzenreuter said, as is the removal of expenditures and revenues from the reserves to O&M funds. He agreed that the Regents guideline on the central reserves, currently setting it at $40 million, should be a percentage of the O&M budget rather than a flat amount. The existing balance, said one Committee member, is worrisome, if there are indeed significant charges coming; the University could end up having to retrench in order to absorb those expenses. If that occurs, Mr. Erickson said, the University would borrow from itself rather than impose retrenchments on units. He also noted, in response to a query, that there is a $3 million general contingency item built into the budget.

Another Committee member expressed fears about the low balance of the central reserves, given the experiences with derivatives and recent news about the pyramid scam that cost a number of institutional investors. Mr. Erickson said that the University is almost completely out of derivatives and observed that it has a very good track record in investments even with the derivative losses. No one avoids ALL losses when investing; there is always a risk. Overall the University has a very healthy balance sheet. The discretionary funds are VERY limited; only the central reserves, in a conceptual sense, are truly discretionary. The individual units have balances that total over $300 million, and those funds are available to the units; all fund balances are over $1 billion, although much of the money is tied up in fixed assets. Units have worked hard to accumulate those funds. The CENTRAL reserves are small, said one Committee, but total University reserves are significant.

Committee members made brief inquiries about endowment and plant funds and then considered fees. One Committee member inquired who decides that a unit can impose fees for technology, when technology is so widely distributed across the University. There was discussion at the Executive Council, Mr. Erickson reported, and the President made the decision. It would be useful to know, as a policy matter, who can and cannot impose fees, it was said; development of policy would be one of the charges to a subcommittee on tuition and fees.

One Committee member then expressed concern about the numbers on another slide, which showed that the ending balances for non-sponsored funds declines steadily for the five years shown on the table. Does this mean that the University is drawing on reserves to avoid facing real budget problems? Mr. Pfutzenreuter said he did not know; Mr. Erickson said the numbers for the last two years may come in better than projected.

It may be that these reserves are being used for phasing in changes, Mr. Erickson said. "Phasing or ostriching," replied one Committee member. If phasing, and there is a conscious end date to the process, that is fine. If it is an attempt to get by this year, and leave the problems to the new dean for next year, then it is a problem. The University has focused on units that have structural deficits, Mr. Erickson pointed out, something it has not had the capacity to do before this.

As he exits the job of Senior Vice President for Finance, Mr. Erickson reflected, he is now getting the tools he needed as chief financial officer when he first came to the University.

Mr. Pfutzenreuter then noted the resolution on the budget that would be presented to the Regents, and said it underscores the need to move to longer-range financial planning. The change started with the partnership proposal, and the attempt will be made to at least plan on a two-year cycle.

Committee members then asked Mr. Pfutzenreuter about some of the items targeted for investment and for retrenchment; in a number of cases, those decisions will be made by the provosts and chancellors. This raises a concern, said one Committee member: there appears to be no adequate consultative mechanisms at the provostal level, so decisions are being made in a vacuum without consultation, even though they may be of institutional concern. Should this Committee invite the provosts to its meetings to discuss their decisions?

Another Committee member expressed concern at the allocations between academic programs, something that is hard to get a handle on. The Committee should not second-guess the decisions, but it should discuss the parameters by which decisions are made and it should see the cumulative impact of those decisions.

There has been a great deal of discussion of the investments and reallocations that appear in the President's budget document, Mr. Pfutzenreuter said. The only late item is the additional $11.4 million in reallocation required by the shortfall in resources.

One Committee member asked about identifying the relative allocation of funds for academic departments with faculty and students and academic activities that do not have faculty who hold tenure and students who major in them (such as the Cancer Center, the Center for Interfacial Engineering, and so on). The only way to get at that, Mr. Pfutzenreuter said, is by looking at functional categories, such as research and instruction, and those amounts are only as good as the people who are coding the expenditures. It is difficult to tell how money is being invested, it was said.

Considering the strategic investments proposed for the two year of the biennium, it was said, one is hard pressed to relate them to U2000 data. Mr. Erickson said the University continues to add to its physical plant--everyone wants a new building--and a lot of the funds are related to buildings. One issue is how to begin to cut those costs back. The University has taken more space off line in the last 3-4 years than it has the previous 20, he observed, but there is still a long way to go. The recent study demonstrates that classrooms are not well used, and similar studies of research and office space will also be conducted; there are significant funds that could be made available for the University if those costs are examined carefully. He recalled that he has many times made the point that if something is free, people are not accountable for it; that would change if the costs of space were accounted for under Responsibility Center Management.

There are a number of issues that have been put on the table for next year, said one Committee member, including the growth of administration at the academic support level (below the central administration and deans). Both Mr. Erickson and Mr. Pfutzenreuter cautioned the Committee about drawing conclusions from time series expenditure data, because there have been major changes in the classification of expenditures since the CUFS system was installed. The data from the transition year are nearly meaningless, Mr. Berg reported, and the data for the subsequent years do not compare precisely with earlier years.

It was agreed that there would be a need for summer meetings, to discuss the budget decisions that need to be made, and that the Committee would not make any comments at the Regents' budget forum on June 13.

Professor Morrison then adjourned the meeting at 4:50.

-- Gary Engstrand

University of Minnesota