Minutes

Joint Meeting
Senate Finance Committee & Senate Consultative Committee
To Consult on the Development of the Biennial Request
September 1, 1988

Present: Mark Brenner (chair), Charles Campbell, John Clark, David Dittman, Art Erdman, Lael Gatewood, Richard Goldstein, David Hamilton, Gerald Klement, Gary Kravetz, Geoffrey Maruyama, Cleon Melsa, M. Kathleen Price, Tom Scott, Burton Shapiro, Michael Steffes, Walter Weyhmann, James VanAlstine

Guests: David Berg, Acting Vice President Carol Campbell, Acting Vice President and Provost Shirley Clark, Associate Vice President Edward Foster, Gayle Grika (Footnote), Associate Vice President V. Rama Murthy, Irwin Rubenstein

Professor Brenner welcomed everyone to the meeting and then asked the several administrators attending to walk the committee members through the various handouts that had been distributed.

1. Changes in Spending Policies

Vice President Campbell began by explaining the contents of a memo from Roger Paschke, Director of Asset Management, which outlined proposed new spending policies. She noted that the Management Committee had approved the proposals; they would be presented to the Board of Regents at their September meeting.

The changes were proposed in part because of different policies used by the University and the University Foundation; since all the funds being managed are for the benefit of the University, it seemed to be wise to bring those policies into alignment. The first change has to do with the distribution to departments of short-term investment funds (the Temporary Investment Pool or (Foundation) Committed Funds). Departments will now be guaranteed a return equivalent to the 90-day rate on Treasury Bills, a rate which has recently been higher than money market funds. This guarantee, seen as achievable, will make it easier for departments to plan. On occasion, because of the size of the University's investment pool and the instruments which can used from time to time, the University may be able to obtain a rate even higher than those on T-Bills; this additional income would be held centrally by the University or the Foundation for priority programs. A department must have at least $25,000 which can be invested for at least one year; if the return is higher than the T-Bill rate, the additional income will be held. If it is lower, the department will still be guaranteed the T-Bill rate.

This proposal is, Vice President Campbell said, a little like Robin Hood, in that the central income will come from departments which can afford to invest the money, but the guarantee is an excellent one. The Foundation income from this proposal, she noted, will be used to support the activities of the Foundation; previously, it had been subsidized by income from the reserves. With that money now gone, this replaces the subsidy that the Foundation had been receiving.

The second proposal affects the Group Income Pool, which is where funds are invested for a three-year period. In the future, there will be a 1/4% annual administrative charge. With approximately

$125 million in the pool, the charge will provide about $300,000 annually. Vice President Campbell reported that the assessment of an administrative charge is the norm among the University's peer institutions.

The third change is in the rate of spending from the endowment; it will go from 5% to 5.5%. This change will mean sacrificing some future purchasing power but it is well within prudent limits on spending. It also will provide needed dollars now. Vice President Campbell was asked if this change would mean the endowment would not keep up with inflation; she said it could, very gradually, be eroded. The first 5.5% will go the departments; any additional income will be returned to the principal to grow. The University will need to look to fund-raising to maintain the value of the endowment vis-a-vis inflation. She pointed out that it could be set up so that the endowment is first protected against inflation and the remainder distributed to the departments, but the conclusion has been that the funds are needed by the departments now. She added that at a 5% distribution rate, the University is very low among its peers; at 5.5% it is about in the middle of the pack.

The fourth change simply brings the University and the Foundation policies on these changes into conformity.

One committee member observed that the second and third proposals, to withhold funds for the cost of managing the investment, seemed to be fine. The first one, however, takes income donated to departments by alumni or otherwise obtained and will be used to create reserves of the type that have recently given the University so much trouble. Vice President Campbell replied that the existence and uses of the funds will be completely disclosed. Furthermore, the committee member pointed out, the money will be taken from decentralized sources for central use; it is more like Robin Hood in reverse.

Given complete disclosure, Vice President Campbell was asked, how would the Senate Finance Committee know of the decisions about reserves? She said that the plans up to now had not been discussed with the Committee although the intent is to do so. What will happen is that the beginning balance, the income, and the proposed expenditures will be reported; a $40 million balance will always be preserved. The expenditure plans will go through the same consultative process as the regular budget, including to the Board of Regents for approval. All money in and out of the reserves will be reported monthly to the Regents. There are, in addition, two other discretionary sources: The President has $1 million and the Provost has $650,000 for academic emergencies. Expenditure over $100,000 from the reserves must be approved by the Board of Regents if it was not in the original plan. All of these decisions, she emphasized, will be made openly and with discussion of the appropriate groups.

In response to a question, Vice President Campbell confirmed that none of the proposed policy changes on spending affect the PUF money; those arrangements will stay as at present. She summarized the four major funds being discussed:

TIP (Temporary Investment Pool): short term investments, no risk, guaranteed return to departments.

GIP (Group Income Pool): longer term investments, higher rates, but some market risks (the money is in such instruments as bonds).

GIF (Group Income Fund): long term--eternity--investments, where all true endowments are placed, some market risk but all time to recover, higher rates.

PUF (Permanent University Fund): heavy investment in long-term bonds to enhance the income stream; spending was set at 5.5% in the beginning, recognizing the demand on the income.

Vice President Campbell also explained that Board of Regents policy currently allows a spending rate of between 5% and 6% Therefore, although Regents' approval is not required for these changes, it will nevertheless be sought.

A committee member expressed a concern about risks vis-a-vis the legislature; would this accumulation of reserves be a zero-sum game, so that whatever it is proposed to have available would be deducted from the state appropriation? Vice President Campbell said that she was not aware the issue had been raised by anyone, but Associate Vice President Foster reported that Vice President Heydinger had been told by a legislator, when he was testifying, that the legislature expected to see the request fitted into the context of money for the PUF chairs and justification for any additional funds. Vice President Campbell said these reserves would all along the line be fitted into the context of total University financial operations; it seems to make no difference whether the money is spent by departments or by the central administration. She said her chief concern is to maintain a $40 million reserve and to see that there is no legislative offset for reserve spending.
It was suggested that anyone representing the University at the legislature have available information from peer institutions about endowments and spending. Vice President Campbell agreed, and said the information was readily available.

2. Report of the Legislative Auditor

Discussion moved on to the report of the legislative auditor on Physical Plant. One committee member said he had read the summary and President Sauer's response and saw no proposed changes which would reduce the expenses to the departments. Associate Vice President Foster said that most Physical Plant services are not charged directly to departments, but he agreed that for laboratories there were often high charges.

Associate Vice President Foster said that the issue is the reduction of overall Physical Plant costs, not just those tied directly to departments, so as to limit the resources diverted from academic programs. One question raised by the audit that has not been addressed before is the kind of labor contracts for trades that the University has vis-a-vis other public employers. Nationally, he noted, construction workers are paid more than those in the same crafts who have 40-hour-per-week maintenance jobs in factories. Public and higher education employers typically pay the lower maintenance wages--the University does not; it pays at construction rates. It would be very costly to change this situation because wages are set by labor contracts. The choices are to renegotiate the contracts or find a way to substitute workers from another union, which would lead to jurisdictional disputes. This, in turn, could lead to strikes on construction projects and other unpleasant results. The University will not, as a consequence, decide lightly to follow the auditor's recommendation on this issue, but the report does point out a very significant aspect of overall costs. Suggestions that Physical Plant is otherwise inefficient are probably true; the present Physical Plant management believes them to be true and is addressing the problem.

Vice President Campbell added that from the perspective of a department paying the bill, the two major items of concern are the wage issue and the jurisdiction issue (e.g., must a Teamster drive a worker to a site?). One other issue is scheduling. The other questions raised by the audit, she said, would have a negligible impact on the cost to departments of Physical Plant operations.

A member of committee recalled his frustration when sitting on the Physical Plant and Space Allocation committee; Physical Plant would point the finger at Physical Planning, and vice versa, when charges were made. Professor Brenner said he expected that the Task Force on Support Services--to be appointed by SCC and the administration--would look into that problem. The Task Force, he added, would look at all support services, and look at them from an academic perspective--are needs being met? The Task Force will report to the Senate and the Provost.

3. The Operations and Maintenance (O+M) Biennial Request

Mr. Berg began by explaining some of the numbers that appeared on the handout that had also been sent to the Board of Regents by the President. He commented that there is complete confusion on the calculation of the percentage increase being sought by the University, a situation worse than he has ever seen it before. The University has always taken the position that the base for the biennial request is the second year (of the previous biennium, in this case 1988-89) doubled. The Finance Department, on the other hand, takes the total previous appropriation as the base--there is no notice taken of the increase that comes in the second year. Further, under the Average Cost Funding (ACF) formula, the University would lose money starting next year, so the "base" could be lower than the actual appropriation if the Finance Department and the legislature decide to look at the base after the ACF reduction is calculated. The University, however, will continue to use, for its own purposes, the "second year doubled" approach.

With that background, Mr. Berg said, the University's requested <u>gross</u> increase for the biennium is 16.4% (which includes no figure for inflationary increases). The <u>net</u> increase--the actual appropriation after the deductions for expected tuition and indirect cost recovery (ICR) are included--is 18.6%. The University will ask that the ICR money no longer be considered a deduct against appropriations. The gross request is for $1.074 billion; the net request is for $817 million.

Of these increases, Mr. Berg went on to point out, the O+M request is for a 14.3% increase and the State Specials would go up by 28.9%. There is, however, a $5 million item for each year of the biennium in the Specials for laboratory equipment which should really be in the O+M request; it has been put in as a Special in order that it can be kept out of the tuition base (which is O+M) so that students do not end up paying 1/3 of the cost of the equipment. The State Specials increase by 22% without that item; the O+M increase would be 15.4% if it were included in that total.

On the faculty salary item, Mr. Berg said the University has two choices, both of which were unsatisfactory. One, the University can go in with no request for inflation and accept the Governor's recommendation. The Governor will, in December or January, make a general recommendation on what inflationary increases should be; for the last biennium, his office estimated 2.5%, which was substantially lower than the actual rate. The Department of Finance will automatically then include that gubernatorial recommendation in all agency requests (and will adjust any different agency requests to that amount). Two, the University can go in with its own request for inflation. The University has chosen to use the first method; for faculty salaries, the request is for 4.75% the first year and .5% the second; the inflationary increases would be added to these amounts. If the University does not like or accept the Governor's recommendation, it can then ask that a greater salary increase be granted.

For civil service salaries, the present 1% and 1% for each year of the biennium (plus inflation) are still placeholder numbers, for the present. There appears to be information which suggests that the University is 3% behind other public employees in the state, but these data are not yet fully developed.

Mr. Berg acknowledged that for faculty salaries the faculty will wish to argue for comparisons beyond the Big Ten, and to make such an argument is not new. He said he assumes the Big Ten is losing ground nationally, although he does not yet have any data to support the claim. There is, however, a survey done each year by Cornell of 27 of the top 35 research universities in the country, which is the group the University wishes to compare itself with. He has the data for 1984-85 and 1986-87; in those two years, the University lost 2.5%. In the Big Ten, the case is less obvious: In 1979 the University salaries were at 98.8% of the Big Ten mean; in 1988 Minnesota was at 98.1%, so there was a loss of .8%. The University, however, he noted, does not <u>want</u> to just be at the average, so this difference is not merely a "shortage."

Associate Vice President Murthy next directed the attention of committee members to the requests for computing. [Much of the presentation and discussion was a repetition of the remarks made at the August 4 joint meeting and will not be presented here again.] The major points were these:

-- One objective is to replace spending from the reserves (about $2 million annually) for computing with state funding.

-- The objectives of the remaining increases being sought are for networking (both on the campus and to link the campus to national and regional data bases) and to increase access to computing on the campus.

-- If the increases being sought are granted, the University in five years will have achieved a respectable level of support (although it will still be spending significantly less than many institutions, especially the private schools), which should help in recruiting faculty and students.

A member of the committee observed that if one totalled up all of the amounts being sought for computing in the request, it would be about $33 million--or the equivalent of buying a PC for everyone on the campus. How, it was asked, can the University justify all these requests for academic, administrative, and supercomputing? Associate Vice President Murthy pointed out that in the case of supercomputing, the University had undertaken its efforts at the request of the state; the University had been given money it did not seek and was assisting the state. The University, apart from having initially said "no," did not have a great deal of control over the fact that the money was appropriated and this portion of the request should be decoupled from the other computing requests. Vice President Clark also responded by saying that distinctions can be drawn among requests and that these clarifications would be made. Another committee member commented that the funds being requested should in part be labelled Management Information Systems or some such thing because the legislature was clearly interested in seeing that the University improve itself in this area.

Mr. Berg went on to note that the arguments for release from the ACF funding formula and for the Funding Rank Adjustment (FRA) money are based on the proposition that the University spends substantially less than other schools in the Big Ten in direct instructional expenditures per student. The study is not yet finished, but it appears the University is underfunded by $20-30 million, and probably closer to $30 million. This request asks that the $2.662 million and $5.266 million that would be cut under the ACF matrix for 1989-91 be restored; between that restoration of funds related to enrollment declines, and the FRA dollars being requested, it is expected that the direct expenditures per student at the University will increase. He also pointed out that contrary to what has been said at the University, the legislature has not decoupled the University from the ACF matrix. The legislature has said, however, that it intends to restore that money to the University even if it gets nothing else--that $7.928 million over two years will be a legislative priority. Mr. Berg added that some of the other items in the request also speak to the funding rank adjustment issue, such as the $20 million for instructional equipment and part of the civil service and academic salary increases. The University has, he reported, looked carefully to be certain it is not asking for more than what it is short but it is also asking for a substantial part of the shortage. Perhaps, he said, if the whole request were granted, the funding rank discrepancy could be corrected in the biennium--although receipt of the entire request is not likely to happen.

One member of the committee asked that the request be examined in a different way. In the past few years, a number of programs have been supported or started with money from the reserves. Part of this request, presumably, includes the replacement of those reserve monies with state funds. Is there any <u>new</u> money left after the reserve dollars have been replaced, anything that can be used for Academic Priorities? Or is it a wash? Mr. Berg responded that there are new dollars, and the University does come out ahead, although he could not say by how much.

Another committee member harkened back to the matter of inflation. He noted that the Governor is always under pressure to minimize estimates of inflation in order to keep down the estimates of revenue and taxes needed. The state will develop a new recommendation, but there is never a <u>restoration</u> of funds when previous estimates were incorrect. Is there any pressure from the public institutions to correct this problem? Mr. Berg said that the higher education staffs are aware of it and that it has been discussed at the state level, including with legislative leaders. Part of it can be addressed in the funding rank adjustment argument--much of the shortage is likely due to inaccurate estimates of inflation in the past. It was pointed out that there is a difference between that which is automatic and that which the University must fight for. Mr. Berg agreed there was a flaw in the system and that an independent agency ought to make estimates of inflation. He also said that there has been discussion of going to the legislature to seek an inflationary correction.

Vice President Clark was asked if the numbers in the request can be linked to those in the Academic Priorities document. She said the request numbers do not fully reflect the numbers in Academic Priorities. Academic Affairs has been looking at the unit requests for a long time and has been cutting them down; Academic Priorities called for $33 million over five years but the requests for this biennium alone totalled well over twice that amount, so they had to pare them down because the University would have been immediately seeking more money than Academic Priorities called for over the five years. It is, she added, harder to link Academic Priorities to the State Specials requests; the latter include more creative programs as well respond to other needs--outreach, broad issues, and political considerations. She agreed, however, that Academic Affairs could put together numbers linking the request more directly to Academic Priorities.

The question of funding beyond replacing that which had come from the reserves was raised again. The committee needed to see the actual funding level for units, including the reserves, in order to see the bottom line and the impact of the reserve spending, and the biennial request, on the units. Associate Vice President Murthy said that with many items there will be more money than that which replaces the reserve funding. Another committee member observed that 1/2 of the request is for Physical Plant operations; with the legislative auditor's report, it would be hard to persuade the legislature to appropriate the money and it will have to come from elsewhere in the budget. Associate Vice President Foster said some of the items are overstated in that they as for funds for wage and price increases. After the Governor's recommendation for inflation adjustment is known, these requested increases will be lowered to ask for only the difference between the projected increase in cost and the "automatic" increase for inflation.

Committee members discussed the problem of the addition of new space without additional funds for operating it. Mr. Berg said the ACF matrix contains a factor for space, but if new space is added, after the appropriation, the money to operate it is not there. There was, one committee member observed, an institutional policy on not bringing any new space into use; Associate Vice President Foster commented that the University has not adhered to it. Mr. Berg said the Department of Finance is doing a statewide assessment of needs for facilities operation; the number in the biennial request for repairs and replacement is a placeholder, the University's guess at what Finance will determine is needed. Associate Vice President Foster pointed out that the University will ask for operating funds for new buildings. It was suggested that the operating funds be included in the capital request so there would be no surprises and that the University not build without operating funds. Mr. Berg said the state commitment has not been worth very much; the Finance Department requires that the University provide operating cost figures but the money has not been appropriated. One committee member argued that new space would be opened, heated, used; Associate Vice President Foster said that it would not be in the next biennium without retrenching from elsewhere in the budget. It would, the committee member concluded, be possible to simply leave the space empty, as a statement to the legislature; otherwise it is a way for the legislature to make the University more efficient.

Professor Brenner distributed copies of salary data based on information from the AAUP. The graphs demonstrated that the Big Ten is slipping with respect to the top research universities. He reported that he had discussed the data with President Sauer; the consensus of the Vice Presidents and Chancellors is that it is realistic, now, only to seek salary adjustments to achieve the 3rd place average in the Big Ten. It is, however, he said, time to begin to enunciate a different target and to get agreement on where the University is going. Asked again what increases at the University would achieve the Big Ten 3rd place, Mr. Berg said the 4.25% and .5%, plus inflation, would achieve that position. The drawback to the numbers is that they assume the other schools obtain only inflation plus 1/2% salary increases; if the others achieve more than that, the University will slip again. The Big Ten 3rd place average was chosen, explained Mr. Berg in response to a question, in part on the basis of how much it cost and in part because it parallels the request for 3rd place in the Big Ten for instructional expenditures per student. Professor Brenner continued by indicating he hoped the University would start a campaign to increase understanding that 3rd place in the Big Ten is only the first step if the

University is to be truly competitive. Mr. Berg commented that while, for a variety of technical reasons, he does not have a high opinion of AAUP data, these are nonetheless probably an accurate representation; they correspond with his data from the Cornell study. Asked how the University dissuades the legislature from relying on the Big Ten, Mr. Berg replied that other data have been used year after year without success.

Mr. Berg was asked if the University could demonstrate that the legislature had been unfair to the University in comparison to other public employees; he said that such a presentation, with a lot of data, was made in 1983. It could be done every biennium, although it would be difficult to do.

The important part of all this, Professor Brenner concluded, is that the Big Ten is slipping; the trend is clear. The University's problem, he said, has been that salary needs have been based on seeking a correction for inflation rather than on the market--an introspective standard rather than a comparative one. When the University moved to a marketplace comparison, it used the Big Ten; there needs to be an adjustment to use of the top research universities or, at a minimum, the top public research universities.

Mr. Berg reported that he had one study in process for FYs 75, 82, 88, and will have 1989. It includes the Big Ten plus others at the top, although it is not the elite group (it doesn't include Harvard, Stanford, Yale). He can, he said, do a comparison over the three years for which he has data; a documented slide on the part of the Big Ten with respect to that group should be convincing. Professor Brenner commented that the President is concerned about including the private schools in the comparison group of the top 29 because it leads to perceptions of elitism. The comparisons should be made with the public institutions. Another committee member, however, dissented, saying that the legislature must understand that the marketplace for professors includes the elite private institutions.

4. The State Special requests

It was pointed out that even with the adjustment for the equipment request, the Specials were increasing at a higher percentage than the O+M portion of the budget. Traditionally this is true, is it not, Mr. Berg was asked; he agreed that it was. This, the committee member observed, does not square with what the Specials are supposed to be; they are supposed to go away over time. But instead they have always gone up. Mr. Berg concurred, noting that the specials each have a constituency or they wouldn't be there in the first place.

One inquiry made was whether or not there were specials where there was no increase being requested; there are. Of the total of $76 million in specials, $17 million worth are not requesting increases. Asked if the existing specials contained a lot of new money, Mr. Berg said he did not know. A number of them, he agreed in response to a comment, do include matching funds.

Vice President Clark was asked who decided, at what level, what the increases on the state specials would be. She replied that it was not a scientific process; central administrators asked questions about what the increases are being sought for. Almost all of the requests have been reduced, and not all of those proposed appear in the request. There is a central administrative judgment on priorities, on how well developed the request is, etc. Some are cut way back. It is, she said, an item by item inspection. Some even violate the University's own guidelines on what should be a special and what should be in the O+M request; it is, she concluded, a mixture of land-grant, technology transfer, outreach, and opportunities provided by the State, with different arguments for each.

A member of the committee expressed a concern about the process, observing that if individual departments had the same opportunities to make arguments for themselves as the proponents of the specials did, the departments might obtain similar increases. The departments, however, do not have that opportunity; they get prorated increases determined by formula. The process distorts the outcomes. How, he inquired, is the English department to put a special together when it is not on the cutting edge of new technology? Some of the old specials should perhaps be moved to the O+M budget. In the end, the University's bottom line is the bottom line, so where the money comes is irrelevant. Another committee member rejoined that a lot of the dollars in the specials go to faculty and graduate students and that of the new dollars, a lot are going to faculty in existing programs; it is a way legitimate program activity can occur but different from it occurring in the department.

One committee member said he was galled that some academic programs are in the specials, and reminded the committee of Vice President Heydinger's statement that the bottom line for the University includes the specials. With 28.9%, they get a larger share of the increase; even if some of them are favors to the state, or in response to an opportunity provided by the state, they are still a part of the institution's bottom line and are coming out of something else that the University could do.

Associate Vice President Murthy remarked that departments do introduce specials; they are sometimes a unique opportunity to obtain topical or timely dollars due to interest in the legislature. Is the University to say "no" to that interest, he inquired. He acknowledged that there were hidden costs in those opportunities. It was observed that the difficulty comes when the bottom line is shrinking; then what are the University's priorities? The specials get special lobbying; there is a need to protect the center of the University. It may not be time to put out a plate with many items for the legislature to choose from.

5. The Capital request

Professor Brenner asked Vice President Clark to explain why they had received two different capital request lists and to lay out the timetable for the request and the role of the Senate Finance Committee. She told the committee that the Specials and the O+M request would go to the Regents for information at their September meeting and for action in October. The capital request, with considerable qualifications, will also go to the Regents for information in September and action in October.

Most of the central discussion thus far, she said, had been devoted to the O+M and Specials. The capital request, she reminded the committee, had been withdrawn last year, so the starting point was that request. Many feel strongly that that request was a good one; others of us, she said, want to take a look at it again in light of Academic Priorities. The two different lists sent out from her office were the capital request from last year and the Academic Affairs priority list, Twin Cities campus only. It did not include the Health Sciences or any other units; those lists would have to be spliced into the list.

The entire list of capital requests, she said, is staggering. There is a set of criteria or assumptions which are used to guide in the determination of the importance of the requests; briefly, they are:

-- will it cut life/safety/fire hazards
-- is it consistent with academic planning
-- is it part of phased concepts where the step is needed to go forward
-- what was its ranking in the 1988 request
-- is it a part of cost avoidance in operations
-- does it cut architectural barriers for the handicapped
-- does it respond to a broad range of campus constituents rather than a single department
-- is it compatible with the long-range development plan
-- is it a project with matching grants, non-state sources, or self-amortizing.

Asked if the list of criteria had been provided to deans and department heads, Vice President Clark said it had not been distributed to the deans at their recent meeting.

One committee member observed that the request bears heavily on academic issues and should receive considerable discussion in committees with faculty members. The Academic Affairs list, it was noted, did not correspond with the final 1988 list; the top item on the Academic Affairs list was #21 on the final list. Vice President Clark responded that the discussions were in a very early stage and that these lists were provided to the committee because they were what was available; they are trying to stick to the schedule and move forward. Asked if there will be some weighting or interweaving of the lists, Vice President Clark said there would be. For instance, she said, questions can be asked whether all proposals to eliminate hazards are equally important or are some excessive.

Professor Brenner inquired if the Senate Finance Committee would be able to discuss the capital request at its next meeting; Vice President Clark said that depending on meeting schedules, if would be possible, since both the O+M and Capital requests would not be going to the Regents for action until October. After some very brief but unilluminating comments on the status of the Recreational Sports building, the committee adjourned at 3:45.

--Gary Engstrand