

Minutes*

Senate Committee on Finance and Planning
August 24, 1990

Present: Virginia Gray (chair pro tem), David Berg, Arthur Erdman, Läel Gatewood, Kimberly Kantorowicz, Craig Kissock, Nick LaFontaine, Cleon Melsa, Jeff von Munkwitz-Smith, Nancy Ann Root, Charles Speaks

Guests: Senior Vice President Gordon Donhowe, Vice President Richard Heydinger, Ken Janzen (Regents' Office), Senior Vice President Leonard Kuhi, Professor Geoffrey Maruyama, Maureen Smith (Brief), Rabun Taylor (Footnote)

Professor Gray opened the meeting at 10:00 and explained that she was again chairing, this time because Professor Shapiro, although back in Minnesota, had arrived extremely late the previous evening/morning. Professor Gray started the meeting with a question about the meeting times set for next year; it was agreed that the question should be taken up with Professor Shapiro.

She then welcomed Senior Vice President Donhowe to the meeting to discuss the University's biennial request.

Mr. Donhowe distributed copies of a series of slides which had been used for a presentation to the Board of Regents and made his comments to the Committee from those slides.

He began by telling the Committee that the projected growth of state revenue is reasonably healthy although there have been no post-Kuwait forecasts made. Spending "tails" from the previous legislative sessions, however, have committed all the available funds; there is no money for the legislature to spend in 1991 (if there is to be a balanced budget). Mr. Donhowe reviewed the forecasts and numbers for the 1991-93 biennium; what basically happened, he said, is that it is if the University committed soft money fund balances to recurring expenditures, creating a base appropriation which must be covered in the future.

The Governor, Mr. Donhowe pointed out, is saying things that one can hardly argue with: balance the budget, maintain the reserve, debt service should remain at 3% of the general fund, there should be both short- and long-term management, new commitments should be funded from savings in base spending (innovate by substitution), there should be a focus on service outcomes and redesign, and there should be productivity improvements. This is a very progressive position to take which, given the circumstances, puts a very rational face on a "nasty, mean fiscal mess."

Governor Perpich has basically told higher education, Mr. Donhowe reported, that it must do better with what it has. The 1990-91 appropriation, doubled, is more or less what institutions will have. There will be flexibility in reallocating within the base (even from State Specials to the Operations and Maintenance budget--something the legislature has never approved). There will be no inflationary run-

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ups, there will be no change-orders, institutions will be asked to show how they will reallocate to best carry out their mission, and there will be an emphasis on outcomes. The Governor has also suggested greater interagency cooperation; for higher education, this would be HEAC.

The result is the reverse of what is normally true for budgets: There is a predetermined number to start with (the revenue projections for the biennium); all submitted budgets will sum to that total (rather than to a greater number which the Governor reduces to the predetermined total). The Governor, Mr. Donhowe said, reserves to himself the prerogative to reallocate among institutions in his recommendations to the legislature, based on his view of their quality and his own priorities. Technically, then, even the base is not safe.

Much turns on November events, however: There will be a new revenue forecast and there will be the election results (both for the legislature and the governor).

Mr. Donhowe explained to the Committee the several reasons why there will be no growth in the funds available for spending; this means that there will be no salary increase appropriation, no school aid formula change, and no change orders. Higher education is not being singled out. This situation, Mr. Donhowe said, will not hold; a legislature cannot not spend money--whether Democratic or Republican, it cannot do it. The salary supplement is a critical concern of AFSCME, the Teamsters, and other unions representing State employees--a critical constituent base for many Democratic members of the legislature. Mr. Donhowe dismissed the possibility that there will be no salary increase. Teachers, likewise, will not stand for no increase in school aid. If changes are made in these areas, the legislature will have to deal with inflationary run-ups elsewhere, on grounds of equity, "or there will be war between the various segments of the Appropriations Committee." There will probably be, Mr. Donhowe speculated, some sort of "revenue enhancements" and virtually no consideration given to any new proposals.

Mr. Donhowe was asked what would occur if someone other than Perpich were elected; he said that the new Governor would put together something new (in a big hurry). There will not, however, be much room to maneuver for any new governor; the picture for the University will be largely the same.

There will, in summary, not likely be any happy revenue surprises, the election results will probably not change the bleak fiscal outlook, the only planning which will lead to program changes is that which results in reallocation--for all institutions supported by the State--which tends, Mr. Donhowe observed, "to concentrate the mind marvelously." For the University, he said, this will mean "levels of reallocation substantially greater than we had heretofore contemplated."

Assuming, hypothetically, that the Governor's recommendation actually became law, the University reallocation target simply to sustain the base-before any pruning--would be about 9+% over the biennium. To do it across the board would, he said, essentially undo anything that had been accomplished over the last many years in terms of Academic Priorities or any strategic move in any desirable direction. There is no alternative to revisiting the question of reallocation "in large clumps"; even with modest news, such as inflationary run-ups, there will still be a need for significant pools of money if there is to be forward movement by the University. It would, he argued, be "an enormous mistake" if the University decided it would take "a two-year time-out in terms of the task of reshaping and redirecting" the institution.

Next Mr. Donhowe drew the attention of Committee members to several tables and graphs outlining the University's position vis-a-vis other systems.

Higher education has been losing in terms of market share of the entire State budget; from 1980 to 1990 the percentage declined from 13.8% to 12.9% of the total--a 6.5% drop. The University declined from 6.3 to 6.0% over the same period--a 4.8% decline.

Instructional amounts per student, in constant 1990 dollars, vary significantly among the systems; only the University has seen any growth during the 10 years. The University is up 13.4% over the decade and up 8% over the last 5 years--which is a direct function of the agreement with the legislature to ignore declines in enrollment when funding is calculated. The reductions in student numbers are driving the increases. The State University System is down 4% per student; the Community Colleges are down 7%. The latter two systems, facing declines in spending per student combined with significant increases in enrollment, confront very serious problems. The University is doing well and should not complain about whatever money the other systems are receiving.

Mr. Donhowe next reminded the Committee that of the University's legislative request, about 2/3 is instructional and 1/3 is non-instructional (which proportions are unrelated to the 1/3 tuition offset). The biggest pieces of the non-instructional funds are ICR, student aid, about 1/2 of physical plant, and all of the State Specials.

Tuition, as a 1/3 share of instructional costs, is automatically increased when expenditures on instruction are increased. Enrollment declines mean there are fewer students paying the existing costs of instruction. So, if tuition receipts--the same number of dollars--are to be held constant, tuition rates for 1991-92 would have to increase 1.8%.

The ideal cost-related tuition would have all instructional costs supported 1/3 by tuition income. (The University collects approximately 1/2 of all tuition dollars collected by state schools in Minnesota.) What occurs is that undergraduate and graduate students at the University pay somewhat more than 1/3 because professional school students pay only slightly over 26% of their instructional costs. Tuition for those not in professional schools would decline by 3.4% if that professional school subsidy were eliminated; the subsidy in dollars is about \$4.1 million.

One way to change the subsidy, Mr. Donhowe continued, is to change the classification of cost items from instructional to non-instructional; another would be to have a special classification of student aid for professional schools--which would permit the University to raise tuition accordingly while still maintaining access. The University has and will continue to work on these items. Mr. Berg reported that the Finance Department will permit the University to make a proposal to reclassify certain costs out of instruction.

Another way to introduce equity in tuition schedules would be to reduce everyone to the 26.4% of instructional cost paid by professional school students. That change, however, would cost the State about \$53 million. The climate for reducing the tuition offset "is lousy." The other systems have no interest in the issue and do not find resistance to the tuition they charge. The issue does not raise its head on the campus or at the legislature; the legislature perceives no groundswell of support for such a change so are uninterested in it. Despite rhetoric, the University would have no political allies for seeking the change.

This change, Mr. Donhowe said, is "not even remotely in the cards this biennium."

One alternative is a more realistic recognition of student costs in the financial aid formulas--which would concentrate resources where financial barriers are most serious, which has more support, and the cost of which is \$30 million per year (roughly equivalent to a 3% tuition offset for everyone). At present the financial aid formulas do not adequately recognize student expenses (although students, in turn, do not always choose the cheapest standard of living, either). HECB has proposed to go to the legislature and request funding to make up 1/2 the disparity between actual student budgets and what state formulas currently allow. The University will support this request--although, in Mr. Donhowe's opinion, it is unlikely to be funded.

The one point in the University's favor in terms of reclassification of instructional costs and increased aid for professional school students is that no other system has the costs so there would be no ripple effect for the legislature to other higher education systems.

Mr. Donhowe next recalled that the legislature struck an agreement with the University whereby enrollment would be reduced, the University would do internal reallocation to move funds from where it was in excess to where it was needed, and that there would be some new appropriations to help. By 1993 the University's average cost per student is supposed to be \$112 below third place in the Big Ten (currently Iowa).

Tuition policy clearly shapes the legislative request. If the share paid by tuition remains at 1/3, and tuition were to remain frozen at current levels, there would be no legislative increases for instruction. Actual spending would have to drop \$1.7 million in 1991-92 and \$3.3 million in 1992-93--because there would be a \$5 million loss in revenue over the biennium. If, however, tuition were to increase by 5% per year, actual receipts would grow by 3% or \$4 million per year; legislative funding would increase by about \$11 million per year. These increases would be less than an inflationary run-up.

If tuition were to increase 10% actual receipts would grow by 7.5% or \$10 million; the legislative increase would be approximately \$30 million per year.

The legislative outlook changes the tuition rate issue that the University has been struggling with. The question has been the maximum amount the University could charge; it actually has not charged as much as the legislature authorized. While the decline in numbers of students will require a base rate increase of 1.8% to hold tuition constant, the range of feasible increases in instructional appropriations will be lower than during the 1989-91 biennium--so the corresponding tuition increases will also be lower than the 9% of the past two years. If there is some success in obtaining reclassification of instructional expenses the rate of tuition increases may be much closer to actual inflation. Adding to the positive news about tuition is the fact that the base rate increase because of declining student numbers will, after 1993, disappear; thereafter the rate of increase per student will more closely approximate the revenue rate of increase--and tuition will be more directly related to cost. Students, in turn, should understand as consumers that increases should be related to improvements in instruction.

The tuition debate will not go away, Mr. Donhowe concluded, but the numbers will not be as inflammatory as they have been.

Asked how the University's likely plans for reallocation, and ability to demonstrate such to the State, would compare with the ability of other agencies to reallocate, Mr. Donhowe said the University was better prepared to make a presentation. The University, he said, has a good story to tell and can readily describe how funds have been spent. Both the University's reallocations and its target budgets have been well received in St. Paul.

One Committee member observed, vis-a-vis the Governor's call for increased productivity, that the objective is more difficult to achieve in higher education than it is in other activities; did he have any ideas about where such increases might occur? Mr. Donhowe said that the non-academic side of the house can look at productivity just as can any organization; on the academic side, he said, the example of a recent Michigan study might be illustrative: If there is a discipline scattered among several departments, the departments might be combined; if there are unequal workloads, they are equalized; teaching loads are a measure of central tendency rather than a ceiling and faculty who are unable--for whatever reason--to keep up in research will take on an increased teaching load and be rewarded for it.

Another Committee member said he had no doubt that reallocation would be necessary but told Mr. Donhowe he was perplexed about what strategy could realistically be used to accomplish the major 3-4-5% reallocation that would be required. There is no support for the elimination of collegiate units, no support for abolition of individual departments, and there was no support for suggestions by members of the Campbell Committee--perhaps never set to print--that what is one department at other institutions is three departments at Minnesota and perhaps the three could be combined. There is, in short, no receptivity to any kind of major changes. Are the wrong kinds of things being identified to reach the targets? Or is the climate--both in the administration and the Regents--is now such that more major changes could be considered?

Mr. Donhowe said there is no doubt the Regents are now prepared to consider major changes; several voices are saying that the rate of reallocation and reshaping is much too slow--and those voices will not be stilled. The view of the administration seems to be, at this point, that the University must do a far better job of making reallocation effective; it does no good to have a big report with units identified as targets of reallocation and then to do nothing. There must be champions of the need to reallocate, Mr. Donhowe argued, and those champions must be the faculty, not just administrators. There must be faculty voices, respected in the community, which say "I don't think that is such a dumb idea." There will be, he said, a fiscal climate which serve as a goad to everyone and which cannot be avoided. "If we all want to strangle together, equitably, we won't reallocate. If we conclude that we want to preserve the institution, and move it forward, it is in the interest of the vast majority to take the heat." The changes won't be authoritarian; that does not work. But the University cannot just decide "well, there's another idea from Morrill Hall, let's shoot that sucker down."

One Committee member recalled for Mr. Donhowe that in the last round it was the faculty plan which went much farther than the administration was prepared to go. It is not the faculty which are dragging their heels. Mr. Donhowe observed that it will be necessary to be more politically sensitive, however, because there is no point in developing plans which cannot be made to stick.

It was suggested to Mr. Donhowe that it is easier to support restructuring and reallocation when there is a vision toward which the University is working. Unfortunately, the University is always trying to "get through the next biennium" and has only one- or two-year plans. There is a need for a vision of

the institution which has the dollars chase after it.

At the last meeting, it was recalled, Mr. Donhowe was asked about the relationship between the unfunded infrastructure costs (new building maintenance, research costs, etc.) and the instructional costs which have been laid out. Mr. Donhowe said there is clearly a tie in the case of new buildings; the administration will be recommending to the Regents that with the new shared responsibility for building debt service it will be necessary to look at a building and determine its function(s). They will be instructional or research or student activity or related to a fee-generating service or something other. After the determination is made the obligation for the debt service will follow. If a building is for instruction it is an O + M obligation; funds can either come from reallocation or a tuition increase. Once a building is approved for construction the Regents approve the project and its construction costs and designate where the funds to pay the debt service will come; they will also be told what the annual operating costs will be and where those funds will come from. There will hereafter be, Mr. Donhowe said, trade-offs; new construction will have both the debt service cost and the annual operating cost. Those data will both be included in the budgetary information presented to the Board; they should also be tied to the capital budget, which will occur in 1991-92.

Mr. Donhowe was asked if some of the existing charges might be transferred, for instance, from instructional budgets to research budgets--or perhaps it is working the other way around? Mr. Donhowe responded that the revised ICR policy calls for examining research facilities built since 1987--the last time the University received operating cost appropriations--to determine what incremental costs should be a burden of ICR. There are other possibilities, he noted, such as the "popular" idea of charging rent for space. Before that step will be taken, however, the expenses of occupancy will be documented and provided to the occupants--which will require more accurate measures of use of steam, etc. The likely result, Mr. Donhowe speculated, will be discovery that the instructional units are being subsidized to some extent. This is a tough question, Mr. Donhowe said, because the costs to operate new and sophisticated buildings are very large. (For instance, the estimated annual operating cost of the proposed Basic Science building is \$1.8 million--which funds will have to come from somewhere in the budget.)

Asked about how the rental costs for academic programs which are off campus will be paid, Mr. Donhowe said it will either be a direct cost of the unit, in the case of externally-support research activities, or from the dean's budget in the case of instructional programs. Mr. Donhowe said he had not seen plans to move any unit off campus which cannot pay rent; there will be no money from central administration to pay such costs.

Professor Gray next welcomed Dr. Kuhl to the meeting to discuss the details of the biennial request; Dr. Kuhl also distributed to the Committee copies of a series of slides which had been presented to the Regents.

He reported briefly on a meeting he had been at with the academic vice presidents from the other systems; it is not clear how they will respond to the Governor's directive to request no increases.

What was presented to the Board of Regents, he told the Committee, was the thinking of the administration prior to receiving the no-increase directive. The general themes were going to be strengthening of the arts and sciences, improvement of instruction and the student experience, and delivery of more effective research and outreach programs. In the case of the first, it must be recognized

that the arts and sciences are the core of the liberal education program and central to the basic mission; concern is with recruitment and retention of faculty and improving academic support. Also included are costs of start-ups for new faculty, libraries, and academic computing and instructional equipment.

Now the thinking is that the University will comply as much as possible with the requested budget format but that numbers will be included. There are clearly-identifiable programs associated with the Undergraduate Initiative and costs associated with them; the University can explain those costs, how much can be generated by internal reallocation, and how much would be needed from the State. The schedule of presentation of the budget is such that details will be required but many of the circumstances may change between September and November.

Dr. Kuhi told the Committee that President Hasselmo had asked that any item in the request include objectives for the item, the means to achieve them, the outcomes expected during the biennium, and the expected sources of funding.

Dr. Kuhi next pointed out what has been accomplished on Academic Priorities, the set of plans for major reallocations among units which still guides actions. There will be soon a major review of Academic Priorities, probably after the current biennial request is settled in early 1991--it will be time to see where the University wishes to go for the next 5 or 6 years. The sources of funds for Academic Priorities (of the \$25.5 million spent thus far) were the legislature (\$9.6 million), reallocation (\$7.4 million), non-recurring funds (\$7 million), and program reductions (\$4 million). Of the last, \$1.4 million of the \$4 million has actually been achieved. The University has put in \$21 million of non-recurring funds over the past three years; although that money has not been "made hard," it still counts towards the goals. The \$7.4 million in reallocation comes from two large sources, the 2% reallocation and a major contribution from Physical Plant.

The Academic Priorities target was \$35.2 million, which included significant funds for the improvement of undergraduate education. There is still an unmet need, on the original goals, of about \$9.7 million.

Next Dr. Kuhi drew the attention of the Committee to a chart of expenditures on instructional improvement which have been made to date. Improving admissions--the common entry point--TA training, large class improvements, course access, renovations, advising, and instructional equipment are some of the major areas where funds have been spent; large numbers of students are affected by these improvements. The University received \$4.2 million in the 1989-91 biennium for instructional equipment; the University will seek to harden those funds.

Priorities for the next biennium include maintenance of the buying power of the current base budget, preserving access, improvement of academic salaries, maintenance and improvement of physical assets, improve instruction and the student experience, and deliver more effective research and outreach programs.

Maintaining the buying power of the base basically means obtaining the inflationary increases. The Governor's instructions indicate there will be no such increases although salary funds will be considered after the November revenue estimates. Whatever it will be, if anything, will probably be a lot less than 4.5%. The 4.5% increase would require \$81 million over the biennium; about \$56 million of the

\$81 would go directly into the instructional budget. With no formula increase, of course, there will be a net loss due to inflation--which could only be handled by massive internal reallocation and substantial program change. Or all the units could simply absorb the increases, the largest part of which is salaries.

Preservation of financial access includes support of the HECB request for 1/2 the funds to increase aid to students with unmet need, funds for professional students, reclassification of existing expenses out of the instructional budget, increased funds for financial aid (especially for minority students) from private sources--a task taken on by the Foundation. There is a gap between what Minnesota and its peers provide to students, primarily because of private support.

Preservation of access for diverse populations includes a large request for minority programs and integration of the programs into the overall budget; the idea is to work toward the President's goal of doubling the number of minority faculty and achieving a 10% minority student population. One issue is the stability of funding for programs that are already in place; many rely on outside funds, which come and go, putting the programs at risk. The request also includes a request for funds to comply with the provisions of recent federal legislation requiring institutions to provide additional support to students with disabilities.

The academic salaries request includes recognition that University salaries still lags behind its peers; on the Twin Cities campus they are 2.1% behind the Big Ten public institutions and 3.2% behind the AAU public schools. These are only averages; there are bigger problems (8-9+) in some of the individual units, especially in the professional schools and the arts and humanities. This problem must be coupled with the competition for new faculty and the increased cost of start-ups. The University had intended to ask for a 2% increase in academic salaries beyond the inflationary increase; a study of civil service salaries suggested that they are comparable with the market so there was no intent to seek increases above inflation.

Physical assets refers to repair and replacement; the deferred maintenance needs total \$300 million. It is clear, Dr. Kuhl said, that the University must start to address this problem; it is, he pointed out, one which only gets worse with time. The University has about 6,000,000 square feet of space which is over 50 years old; the backlog of maintenance "is incredible." Some funds were appropriated during the last biennium; the intent had been to ask for \$15-20 million for 1990-91. New space maintenance would have been \$6-7 million.

Instruction and the student experience includes two main areas of emphasis for each campus: speed up implementation of the Undergraduate Initiative and strengthen the arts and sciences core. A third area, on the Twin Cities, is improvement of the experience of commuter students, who make up about 80% of the student body but who have a segmented interaction with the University. There are several problems which would be addressed with this request item: There are chronic problems of underfunding in CLA and, to a lesser extent, IT; the idea is to match resources to needs and improve the student-faculty ratio. Considerable funds have already been put into advising, reduction of class sizes, etc.; it would also be desirable to see increased participation by the professional schools in undergraduate education.

Another element of the request in instruction and the student experience is in academic support: the libraries, instructional equipment, and academic computing. The libraries have the problem of increasing costs of books and journals, especially journals, and came in with a major request; the plan was

to seek \$5 million. \$4 million would have been sought for instructional equipment plus additional funds to harden funds previously received. The request for academic computing would have been for about \$5 million, with a goal to provide much more computing capability for undergraduates--much of which is currently being funded with soft money.

The research and public service request included elimination of the last offset against ICR funds (\$6.5 million); the money would go to research efforts, including a more specific program of repair of research space--an area of great faculty concern. Use of the funds would also include debt service for research space--under the shared responsibility for debt service. There would also, under this category, have been a requested expansion of State Specials in selected areas totalling \$8 million.

Dr. Kuhí then explained to the Committee the effect of the tuition limit on the size of the request. The maximum increase the University could request, given a 5% tuition increase, would be approximately \$35 million; with a 10% increase the funding increase could be about \$100,000,000. These limits, however, may now be moot.

The effect of the fiscal climate on the request was also laid out on a slide. The "normal" request, laying out the University's needs, would be about \$180,000,000. A "bare bones" request, of inflationary increases only, would be about \$81,000,000. An intermediate "reduced" request would total about \$120 million. Maintenance of the base will be the #1 priority. The reduced request would still funnel funds to instructional improvement and other priorities discussed earlier, although in smaller amounts.

The instructions from the Governor, Dr. Kuhí said, basically said that any planned new programs would have to be funded from internal changes. It would be prudent, however, to nonetheless ask for the increases, although the request will need to be couched in a different way than has been the case in the past.

The final topic is reallocation, Dr. Kuhí said. It is on the horizon, and major cuts may be required. One issue is whether there should be salary increases or programmatic changes--the issue which arose with the 2% reallocation and 80% of it returned to the units mandated for salary increases. This, Dr. Kuhí observed, was not a satisfactory solution; the 20% of the 2% did not provide much funding for programmatic change. But the issue arises again, in these circumstances: If there is internal reallocation again, is any of the money to be used for salaries? He expressed the view that it should not be.

Another issue is the 2% reallocation; the deans and many others have argued that this just nibbles away. A better approach might be to ask every unit to plan to come up with X% over the next two years or so. This may, Dr. Kuhí said, make more sense. It has proven very difficult to acquire the funds that were to be reallocated from colleges in accord with Academic Priorities; only about 1/3 of the funds have been moved (\$1.4 million of a total of \$4). Further, some of the programs slated for reductions have large political constituencies, which compounds the problem. A possibility for internal reallocation is if there is an inflationary run-up there be a "tax" on the increased funding, the proceeds from which would be used for new programs; the net effect is the same but it is less painful. Yet another possibility, fraught with difficulty, is reversion of perhaps 1/2 of all vacant positions to central administration for reallocation. The problem is complex; it might, Dr. Kuhí speculated, be better to assign targets to colleges and let them do so.

The issue of process also arises: All of the changes proposed to find money for reallocation must involve the faculty.

What the University faces, Dr. Kuhí concluded, is a major issue of generating funds internally. For example, a minimum increase in funding would be \$40 million (over an inflationary increase) for new programs. That amount could be generated by requiring all units to provide 6%--which is an enormous amount that would spell disaster for many units. How that might be achieved is something the Committee should advise on.

The Committee adjourned at noon without having had time to offer much advice. It was assured by Dr. Kuhí that the meeting on September 18 at the Arboretum would be sufficiently timely to affect the request.

-- Gary Engstrand

University of Minnesota