

Colleagues,

As a follow-up to the discussion at the first meeting of the Internal Budget Model Working Group (IBMWG), Dr. Cerra suggested that the faculty involved with previous discussions brief the IBMWG on earlier discussions in their respective groups. What I will provide will be from the AHC Finance & Planning Committee (AHC FP) with minor comments on the Senate Finance & Planning Committee discussions related to the AHC FP proposals. Please distribute these in whatever manner you wish to the IBMWG. Professor Campbell will provide information on the Senate Finance & Planning Committee discussions of this model and other relevant items.

Principles were developed that the AHC FP envisioned as a guide to discussions on and formulation of a new internal budget model. These were forwarded to the Senate Finance & Planning Committee and eventually to the Faculty Consultative Committee for discussion and approval. The "Budgetary Principles for a Changing Economic Environment" included in the handouts for the 9/8/04 IBMWG meeting were the product of those discussions. We are all aware of both the hard lessons learned about the differential effects of O & M distribution, the effects of past O & M distributions and retrenchments, the effects of across the board cuts, the differential effects of tuition increases on the various academic units, the flawed assumptions in the "incentives for managed growth" (IMG) revenue allocation model, and the devastating effects of legislative budget cuts. In addition, we are all aware of the variable funding sources for the units within our institution and that what benefits some actually hurts others. We (AHC FP) hope the discussion below will provide the IBMWG with concise perspective on one approach to budget a model.

The AHC FP proposed what we thought was a relatively simple budget model grounded in the principles we proposed. From our perspective, the budget challenges facing the institution call for thinking beyond incremental adjustments of the existing model. The key to our proposal is that it is simple (although we acknowledge that the devil is still in the details) and it provides two critical types of incentives. They are the incentive to BOTH "actively generate revenue" (tuition, grant/contract/ICR, continuing education, unit-based clinical/service revenue, gifts, etc.) AND to "consciously control expenses". The RCM/IMG model as implemented here provides only incentives on the revenue side, but not on the expense side for the academic units as consumers of space and central services. If both sides of the equation are not addressed at the academic unit level AND at the central service level, we will never realize the necessary efficiencies to foster excellence in the academic programs in the face of declining state resources. Money wasted on inefficient use of teaching, laboratory, and clinical space, is obviously not available for the enhancement of the teaching, research and service missions of the institution. Money wasted on central programs of little use to many of the academic units (or on duplicate unit programs to be sure the unit's needs are met) cannot be spent for common goods such as libraries, classroom upgrades, and employee/student safety. These are also potential talking points for groups like the Taxpayers League.

Basically, the AHC FP model is run as a balanced budget at all levels with deans and directors making decisions within their unit on what they need and how they can get it and central administration covering common goods and central services. Also included in the AHC FP model (an addition by the Faculty Consultative Committee to the Budget Principles) is specific consultative decision mechanism on where O & M dollars will be used to supplement academic unit activities. We understand that O & M monies have a long history of incremental adjustments (retrenchment and reallocation, taxes, etc.), but we suspect there has never been a critical reassessment of where the O & M supplementation of academic programs should be. Now is that opportunity! The AHC FP model recognizes consideration of varying tuition elasticity among the academic units compared to the cost of the education delivered across these units. Nested in the AHC FP model is the need for program O & M allocation assessment and, where necessary, adjustment based on a principle-driven program evaluation (e.g. unique, central, core, necessary, or whatever other attributes may be defined).

Another aspect of the AHC FP proposal is the allocation of costs for common goods (e.g. libraries, student financial aid systems, registration systems, human resources, facilities, etc.). There are two (2) components to this. First, is "pay for what you use", not what somebody believes you need. As one of many possible examples, this could be applied to unit use costs based on how classrooms are equipped as well as peak vs off-peak rates for classroom scheduling. This is also applicable to the sophistication required for research space by the various units. Second, is cost allocation based on "proportional use". Basically, costs are assessed (only when rebalanced O & M central resources are inadequate to cover the costs of common goods) to consumers (colleges) of central services based on appropriate metrics including direct user fees for services rendered or space occupied and proportional participation in the costs of central services/common goods based on their use profile (e.g. student service costs assessed based on the number of students; human resources costs assessed based on the number of faculty and staff; library costs based on the number of faculty and students). This is different than the current model of taxes based on less specific (although probably easier) targets such as unit payroll or gross unit receipts. The goal here is to foster the perception of value for revenue expended on central services and common goods.

One major issue in the AHC FP model is the "back to basics" approach to benefit cost allocation. It is our belief that this

should be based on the pay your share based on the number of users (e.g. the cost of health insurance/employee, the cost of FICA/employee, the cost of life insurance/employee) instead of the fixed % of salary "pooled" approach without caps (e.g. money is still transferred into a pool even though the individual receives no further benefit). This is considered the cost of doing business and should not be obscured by % of salary-based benefit pools or assessments. We also must recall the surplus and deficit cycles in these pools over the years due to over or underestimation of the % needed to support the pool.

In the discussions at the Senate Finance & Planning Committee level, one of the original AHCFP-proposed principles was deleted. The AHCFP still believes that this is applicable, although potentially controversial, and that it deserves discussion by the IBMWG. It is listed below for the IBMWG consideration:

Principle #: Fully attribute revenues to units generating them and allocate costs to units incurring them

#### Proposed Actions

- attribute all forms of revenue to units where generated, including 100% of ICR
- directly and explicitly recover overhead costs for each of the mission based programs: research, education, and service & outreach

- assess actual fringe benefit costs to units where they are incurred

- define space costs equitably, including debt service, and allocate to units occupying

The AHCFP feels that this approach has both fiscal merit as well as the potential for political leverage (e.g. legislative accountability initiatives) if appropriately crafted and implemented. We accept the concern about complexity, but we request it be given due consideration to assure all possibilities for a budget model have been reviewed.

Attached are:

- 1) the graphic representation of the AHCFP proposed model based on the "Budgetary Principles for a Changing Economic Environment" including the concept of direct benefit charge (not salary-based benefit pools), and
- 2) proposed metrics for other necessary cost allocations.

Thank you for your consideration.

Dan Feeney  
2003-2005 AHC Finance & Planning Chair

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