

Minutes*

Senate Committee on Finance and Planning
Tuesday, November 2, 2010
2:00 – 3:45
238A Morrill Hall

Present: Russell Luepker (chair), Jon Binks, Sarah Chambers, Will Durfee, Steen Erikson, Lincoln Kallsen, Kara Kersteter, Lyndel King, Kathleen O'Brien, Paul Olin, Shruti Patil, Richard Pfutzenreuter, Terry Roe, Jeremy Todd, Lori-Anne Williams, John Worden, Aks Zaheer

Absent: Devin Driscoll, Judith Martin, Fred Morrison, Gwen Rudney, Michael Rollefson, Karen Seashore, S. Charles Schulz, Mandy Stahre, Thomas Stinson, Michael Volna

Guests: Julie Tonneson (Office of Budget and Finance); Brian Swanson (University Services)

[In these minutes: (1) updates from the chair; (2) University cost drivers; (3) cost-allocation data; (4) space utilization initiative]

1. Updates from the Chair

Professor Luepker convened the meeting at 2:00 and provided updates on several matters.

First, EFS is back on the table; issues were raised at a discussion with department chairs and FCC members. Professor VandenBosch asked that this Committee have a discussion with staff who do financial work to learn their views on how things are going. The concerns are at two levels: getting reports that fulfill unit and faculty needs and how the financial staff are doing with the system.

Second, about a month ago a small subcommittee suggested that the Subcommittee on Twin Cities Facilities and Support Services (STCFSS) should be a separate committee and merged with the Classroom Advisory Subcommittee. As he has thought about it, he has come to question whether this Committee needs a subcommittee such as STCFSS; is it doing things duplicative of what this Committee does? Facilities and finances are intimately connected; the debate is whether to create a separate committee or fold the subcommittee back into this one. Ms. King, who chairs STCFSS, agreed that it is sometimes difficult to know what should be taken up here and what in the subcommittee; either the two need to be more careful on agendas or they should be merged. There is no clear path and no clear division of labor, she concluded.

Mr. Worden asked what the driving force is—cost cutting? Overlapping agendas? The ad hoc group looked at a number of committees, Professor Luepker said, and the main question for this Committee is the volume of work in a financially-tense time. But this Committee has always had a lot of business, so that is probably not new. There could be special subcommittees as needed, Mr. Worden suggested.

Professor Roe inquired if the administration had expressed interest in another committee. They were consulted after the recommendation was made and took the opposite tack, Professor Luepker said.

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Mr. Todd said that if the two were combined or disbanded, there could be sessions at this Committee devoted to the work of the subcommittees.

Third, the Committee will hear more about audits of administrative units, Professor Luepker reported. Ms. Klatt, the University Auditor, is auditing a variety of higher-level units and including some of the Committee's questions. But there are a lot of subunits in the administration. His suggestion is that the Committee consider what Ms. Klatt has done when it has its first retreat in December and then decide how deeply to pursue additional subunits.

2. University Cost Drivers

Professor Luepker turned to Vice President Pfutzenreuter and Ms. Tonneson to present information on University cost drivers, information that was presented to the Board of Regents last month.

Mr. Pfutzenreuter distributed copies of slides and explained that they made the presentation to the Board because it is interested in long-term financial planning, and to do such planning it helps to understand the factors that drive University costs.

About 60% of University costs are compensation; this is primarily a people business, Mr. Pfutzenreuter said. The other major elements are supplies/services/miscellaneous, repairs and maintenance, utilities, equipment, and student aid.

In terms of trends in University expenditures (non-sponsored accounts), there has been an average annual growth of 8.1% from 1997 to 2010 (unadjusted for inflation). Adjusted for inflation (by the Higher Education Price Index, or HEPI), average annual growth in expenditures has been 2.5% over the same period. The HEPI runs about 1.0 to 1.5% above the Consumer Price Index, although in recent years the two measures have been closer.

The key points are that University spending is heavily influenced by the nature of the mission; the University is employees, buildings, and students. The growth in expenditures is influenced by (1) cost increases, such as fuel costs, health-care costs, salaries, (2) volume changes, such as building square footage, number of employees, number of students, and (3) new program investments, such as middle-income scholarship program and new academic priorities.

Mr. Pfutzenreuter then noted the cost increases in three categories (salaries/fringe benefits, utilities, and student aid) for the same period, 1997-2010: 8.4% annually, on average. All other costs in non-sponsored expenditures rose an annual average of 5.2%. Moreover, those three items grew from 71% of expenditures in 1997 to 75% in 2010. Professor Roe inquired why those three were bundled together; Mr. Pfutzenreuter said it is because they are the ones growing the fastest and the ones that must be focused on if the institution is to contain costs.

Mr. Pfutzenreuter turned his attention to the key volume changes that have driven expenditure increases. One, the number of employees has increased, from 15,249 in 1997 to 19,157 in 2010, an increase of 25.6%. Individual salaries have not increased very much; it is the increased number of employees that has driven the increase in salary and fringe costs. He also said that the numbers are total employees, not just those paid from non-sponsored funds, so more research equals more employees. Salaries increased by about 7% per year (a combination of salary increases to employees and an increased number of employees); fringe benefits increased by 13.2% per year, which again reflects an increase in

costs plus an increase in volume. Professor Zaheer asked if Mr. Pfutzenreuter would separate the volume increases from the actual salary increases.

Two, the amount of gross square feet has gone from 24.4 million to 28.9 million in 2010, an 18.3% increase, and that means increases in utility and other costs. Fuel costs have stabilized and dropped, but overall costs have increased with 4.5 million additional square feet—and much of that additional square footage is *expensive* space. Those data are for the system, Mr. Pfutzenreuter said; the Duluth campus has added the most square footage on a percentage basis. Utilities have increased by 16.1% per year, or 12.5% when adjusted for inflation.

The third volume change in cost drivers is enrollment. In 1997 enrollments was 51,879; in 2010 it is 63,340, an increase of 22.1%. Student aid during that same period increased 11.3% per year, from \$73.9 million in 1997 to \$182.1 million in 2010. The increases were driven by programs already in place plus new programs the University has added.

Apart from the three major cost drivers, Mr. Pfutzenreuter said, the other costs increased only 5.8% per year (repairs and maintenance, equipment, supplies, purchased personnel, rents/leases, and communications/printing).

Mr. Pfutzenreuter then reviewed briefly the sophisticated long-range financial planning model that his office has developed and the key decisions that must be made before the model can provide information. The Board of Regents has a strong desire that the University prepare a long-term financial plan and update it annually. The model has been built so the input is the key cost drivers and assumptions that must be known (e.g., goals for faculty salaries, the number of students, the six-year capital plan, new investments, etc.). By populating the model with 12-15 key decisions and putting in the data, it is possible to view the impact of decisions on key financial ratios, on whether there will be a balanced budget, if key measures will go up or down. The Regents wish the model populated; his point is that that is not something his office does—that is something the President and other academic leaders must do.

Some things have just happened, Mr. Pfutzenreuter commented. No one planned on an increase in the number of students from 51,000 to 63,000.

Professor Luepker said he found this presentation very helpful. It put numbers around the small fraction the University seems to grow each year; it is particularly interesting when no one is talking about 8% growth per year.

Professor Zaheer asked what the relationship between sponsored and non-sponsored spending is. Ms. Tonneson said sponsored expenditures represent about 18-20% of total University revenue. If one goal is to increase the amount of sponsored research, Mr. Pfutzenreuter said, the institution needs to identify what it will cost to do so. The model can predict if one makes assumptions about indirect costs.

Professor Zaheer recalled that Mr. Pfutzenreuter had said there needs to be a short-term planning process before there can be long-term financial planning, so the University needs to do that as well. Mr. Pfutzenreuter agreed and added that the short-term planning should not default to the finance side of the house.

Professor Luepker commented that the data show increases driven by more employees, more students, and more facilities—but the University has not received increases in funding from the state that parallel these increases, and, in fact, state funding has decreased. What makes up the difference? Tuition contributes a sizeable amount, Mr. Pfutzenreuter said, and there have been some other revenue increases.

Tuition is up and the number of students is up, Professor Chambers observed, but students do not pay the full cost of education. They do not know how much of the costs of education students pay, Mr. Pfitzenreuter said; Professor Chambers responded that it needs to be known if strategic long-term decisions are to be made (e.g., if chasing more students increases costs, that may not be a good strategy). That depends on what college they are in, Mr. Pfitzenreuter said. It also depends on whether they are undergraduates or graduate students and the kind of pedagogy used, Mr. Kallsen added. In addition, the University has become more efficient over time; if one looks at certain ratios, it is a more efficient place.

This is a very important question, Professor Zaheer said. As state dollars decline and the University takes on more and more costs, it has to ask hard questions about tuition, rate of growth, the number of students, and how long it can continue to absorb an unfunded mandate. At Michigan, they make it clear they will take state students and discount tuition for them based on the amount of money the legislature provides, but the assumption is that students will pay full tuition. He said he was not suggesting the University take that position, because it is a land-grant institution while Michigan is not, but at some point the other shoe must drop.

For every research dollar, the University loses money, Professor Luepker said, although one can argue about the types of research that do and do not cost the institution. On average, the University also "loses" money on every student. His college, the School of Public Health, loses money on every graduate student. The Medical School costs much more per student than even the \$34,000 in-state tuition. Does the University lose money on every student?

They are trying to do a cost-accounting on that question, Mr. Pfitzenreuter said, and trying to identify every dollar that is paying for mission activities, including what it costs to educate undergraduates and graduate students. They are trying to do so by college, but it is a difficult exercise that carries a lot of assumptions. The results, however, could help illuminate where dollars go and what is paying for what and what the fully-loaded cost of undergraduate education is. They will also be able to assign revenues so it will be possible to see how much state funding supports education, how much tuition supports it, how much state funding goes to research, and so on. But there is a large number of decision rules needed to obtain those numbers.

Professor Luepker said he wished to reinforce the importance of the work Mr. Pfitzenreuter and his colleagues are doing. Schools and departments make decisions on enrollment without reference to anything like this information. He said he did not recall a plan to increase the size of the student body by 12,000; the University needs a tool like this to help understand costs, and it needs a strategic plan to decide where it is going.

3. Cost Allocation Data

Professor Luepker recalled that about a month ago he provided the Committee with an abstract of college budgets; a number of people wondered if the data were not accurate. Mr. Pfitzenreuter and Ms. Tonneson have made a number of corrections to the data, although none of the tables were initially prepared by Mr. Pfitzenreuter's office. Committee members were provided copies of four tables of financial data. Ms. Tonneson walked Committee members through each table.

The first table identified cost allocations (cost-pool charges) to each of the colleges from the FY06 cost-neutral allocation and then the budgeted amounts by college for each year since.

The second table compared FY08 and FY11 cost-pool charges and allocated state funds, by college, and calculated the difference between them; attributed tuition and Ufees were also included. This

is an interesting table, Mr. Pfutzenreuter said, and the person who prepared it wanted to show cost-pool charges versus state funds, by college. At the same time, however, tuition was increased to help pay costs, so simply comparing cost-pool charges and state-fund allocations does not tell the whole story. Some units use other revenues, not shown on the table, to pay cost-pool charges, Ms. Tonneson added. Professor Luepker said the table was originally created to show how schools need to rely on sources other than state funds to pay cost-pool charges. He noted that the dollars provided to the colleges in the revenue-neutral year of the change to the current budget model were based on history, not any formula—so everyone could blame President Northrop or some earlier administration for how much money colleges received!

The third table reported allocation of state funds by college and central units (in total) from FY07 to FY11. What was striking to him about this table, Professor Luepker said, is the grand total: It was going up until FY09, at which point it started to decline. That reflects state cuts, Mr. Pfutzenreuter said, and tuition has offset some of the cuts, so a cut in state funding did not mean, in every case, that a budget went down as well.

The fourth table provided data on the allocation of state funds, indirect costs, tuition and Ufees, and central reserve funds to central units for FY10 and FY11. Ms. Tonneson pointed out that the definition of which units are considered "central" and included on this spreadsheet is different than that used in the budget model as a whole. This list includes academic centers reporting to the senior vice presidents and various vice presidents, as well as the Minnesota Extension Service and the Agricultural Experiment Station, all of which are considered academic units within the Budget Model. The grand total for FY10 for central administrative units declined 2.59% from FY09; it increased by 1.8% from FY10 to FY11. From FY09 to FY10 the colleges and coordinate campuses declined 0.03%; they increased 1.9% from FY10 to FY11.

Professor Luepker thanked Ms. Tonneson for providing the tables and the explanations.

4. Space Utilization Initiative

Professor Luepker now welcomed Vice President O'Brien and Mr. Swanson to resume the discussion the Committee began last June and continued last August about space utilization. He noted that the Committee had asked Vice President O'Brien to pose questions on which she would like the Committee to offer advice. The questions were these:

- Should the University place restrictions on its net growth in total square footage? If so, what measures / criteria should it consider in establishing a limit?
- Should the University work to quickly consolidate its existing programs into less space to allow buildings to be decommissioned and leases terminated?
- Should the University more effectively incent innovative and efficient space use at the department level? What information would be useful to aid department level space decisions?
- Should the University's space standards be adjusted to reflect changes in how people work?
- What impediments exist that prevent faculty and staff from working from home, working off-hours or taking advantage of other innovative office arrangements?

Professor Luepker asked if Vice President O'Brien was asking the Committee to say "we agree as a committee of faculty, staff, and students that these are important things to do and that we cannot continue to grow forever"?

Vice President O'Brien said the Committee could think about answers to the questions or it could look at the principles they propose about space utilization:

- **a) Sustainable:** The University should not have more space than it can afford to operate, maintain, and support.
- **b) Aligned:** The University should provide the correct type, quality, and quantity of space required for programs to function effectively.
- **c) Managed:** The University should provide tools and incentives for maximizing the efficiency and effectiveness of its space resources.

The questions, she said, go to how they would go about implementing the principles.

Professor Roe asked what metrics would be used to consider sustainable space. Is the size more than the University can afford? Mr. Swanson said they would look to the facilities condition assessment (FCA): To maintain the existing space inventory at its existing quality level, the University should be spending twice as much money per year as it is, which suggests that the quality of space will continue to degrade if the University does not get rid of some space or put more money into the space it has.

Professor Roe recalled that the Committee heard about obsolete space about two years ago and about decommissioning buildings. The assumption that the University will try to maintain the quality of all the space it has puts a burden on sustaining quality everywhere. There is probably some space that should not see investment unless new program dollars make it reasonable to do so. That is the underlying premise of (b), Vice President O'Brien said, so they need to understand what academic programs will grow and which only be maintained or phased out. They will be triaging buildings: For some, it is expected they will be used for 15 years, plus or minus; for others, the expected use will be 50 years or more. In the latter case, there should be investment in the building (like Folwell, which is over 100 years old but is seeing investments that will make it usable for another 100 years). There must be an iteration between academic programs and facility condition information to decide what is sustainable.

Without coordinated capital and academic plans, a faculty member obtains funds to renovate his or her lab, Mr. Swanson observed, so that is a single great lab in an otherwise not-so-good building. Then another faculty member does the same thing in a different building—when one of the two buildings should probably be taken offline. Instead, the University either has to save both buildings or it has to later spend extra money to consolidate the two facilities into one of the two buildings. They want to be able to take buildings down and need academic facility plans that allow it.

Professor Durfee said that there is an emphasis on the academic side on being nimble; will facilities be more flexible? It is difficult to make an academic decision that will be binding for 50 years. That is absolutely correct, Vice President O'Brien said. For the last ten years they have focused on flexibility in both classroom and laboratory buildings so that they can be more nimble about using the space. They can set up or refresh space more quickly and more cheaply.

This is a Catch-22, Professor Luepker commented: University Services can't decide because academic plans are not decided. Mr. Pfitzenreuter has a model that he can't use yet because academic plans are not decided. Godot may not come in the near future. There need to be some principles about space that help motivate the next level so that the University gets away from remodeling one lab for a new faculty member. To develop principles and make decisions they need to work with the Facilities Condition Assessment data and academic plans, Ms. O'Brien said. They are working with the support units in some academic buildings in cooperation with the academic leadership (e.g., to tear a building

down). Their point, she said, is not that they cannot do their job until the academic decisions are made, it is that if they are to be nimble, they need to figure how to work together with the academic leaders so that academic programs have the space they need and so the University uses space most effectively. There is a considerable amount of space that is not as good as it should be.

Mr. Erikson said that it seems that people most familiar with the data are the best ones to identify problem areas and push for decisions. The leadership should tell colleges and departments about the crisis areas and that they need to do something. It appears that a lot of decisions are not being made, so they should put the issues on the table publicly and suggest some solutions.

Professor Luepker said he believed the Committee could be helpful to Vice President O'Brien and her colleagues. The financial crisis is upon the University. The Committee has heard Vice President O'Brien said there is not enough HEAPR money, and anyone who thinks the legislature will provide more money is in the wrong state of mind. Vice President O'Brien posed questions to which the Committee cannot control the answers, but should it recommend decisions about them? Should the University limit growth in space?

There are implications for students, Mr. Kallsen pointed out. If the University decides to increase enrollment by X thousand students, does the Committee wish to say "no net increase in space"? Mr. Swanson recalled that it has been reported that Ohio State has adopted a "no net new space" policy. That is distinct from "no net new space without new resources." If a great new research program comes along that includes money for both space and people, adding new space can be the right thing to do. What they would like to avoid is new space without an academic plan to pay for it so that the costs of the new space weaken the entire academic enterprise. He said that in conversations with his counterpart at Ohio State, they have established the "no net new space without new resources" as a guiding principle, not a policy set in stone or an edict.

Professor Roe said it would be useful to think about a break-even analogy: Given the history of projects, what can the University afford? When opportunities come along, they can be costed out to see if they break even if the space were to be added. The problem, Mr. Swanson responded, is that the University can't afford the space it already has. That is because of the business cycle and the space it has inherited, Professor Roe said, which should not affect long-term decisions. Mr. Erikson questioned if it makes sense to build new rather than renovate old buildings when the University does not have the money to maintain the new space. They do use that approach, Vice President O'Brien said—they did so with the Science Classroom Building and in deciding about Molecular and Cellular Biology vis-à-vis retention of Owre-Millard-Lyon. They did so with the MRRC building (now Education Sciences): It was a strong structure and it made sense to mothball it until it could be put to use, which it now has been for the College of Education and Human Development.

Professor Roe recalled that the Committee had talked a number of years ago about how it is relatively easy to build a building with bonding without considering the maintenance costs. Is that still true? The budget model is helping, Mr. Swanson said. In space management at the college level there are discussions about taking-on additional space; when units know what space costs, behavior changes. A college may have an offer for money for a new building from a donor and then realize it can't pay the maintenance costs, so it may decide to renovate existing space instead.

It also gets down to people versus space, Mr. Kallsen said; sometimes units will consider giving up space in order to save people. But units cannot just give away space, Ms. King said. That is true, Mr. Swanson agreed, but in the Medical School, for example, the dean's office has created a pool to buy back space it can use, and takes the charges for it as well, which allows them to terminate off-campus leases or

to use the vacated space for new hires. Another college is thinking about doing something similar. In doing an analysis about how it might pass space costs down to the department level the Dean's office "found" thousands of square feet that were not being used well. Space Initiative is willing to help colleges do such analyses or just provide information about space costs.

Professor Zaheer said it makes a good deal of sense to think about educational programs as a set of best practices. He said that we could build on experience with different-sized units to create say three models of best practice for the better utilization of space. The University could publicize these so that people know about the models and best practices and could offer to help the colleges implement them. They are trying to get there, Mr. Swanson said. They do a lot on the administrative side, where space costs are passed through to colleges through the cost pools—there is no harm or gain if space costs go up or down for administrative units. But there has been movement and they are looking at tools to see who grew and shrank and to provide incentives. Professor Luepker agreed that if the administration is not charged for space, there is no incentive not to grow. Professor Zaheer agreed that they needed to devise incentives. Mr. Swanson's team is looking at who grew and shrank, as well as incentives to decrease space use.

Professor Luepker agreed that if the administration is not charged for space, there is no incentive not to grow. Professor Zaheer agreed that they needed to devise incentives. Mr. Kallsen did as well but said it is harder to have those conversations because of the lack of incentives. Professor Durfee inquired about who makes the decisions; Mr. Swanson said they are made at different levels. Each department has a designated space person, and most colleges have a space coordinator, and those people are well aware of the messiness. But it is really the deans, associate deans, and finance people who decide how much space to add or eliminate. Do they need additional training, Professor Durfee inquired? Mr. Swanson said he believed they know about the implications of space use. In some cases, they have no way to control it because if a department wants to give up space, there is no one to give it to.

Professor Chambers asked, apropos of administrative units, if it the practice now to ask questions about space when they receive budget instructions. If not, it should be; is there a way to model cuts and provide incentives? Mr. Swanson said he believed there has been, to date, a disconnect between space and budget decisions at all levels. Vice President O'Brien said that Professor Chambers' suggestion is a good one that makes sense to her also. When support units are taking cuts, they need to be asked if they need all their space.

Professor Roe surmised that University Services probably has data on where space is obsolete or not being used well, but colleges see such space as capital for future expansion. What mechanism could be used to buy back space and target its use better? How are they doing at that? In the budget model, someone must pay for space, Mr. Swanson said. In the Medical School, space that is handed back is paid for by the dean's office until it can be re-assigned to a unit that can use it better, or they bring a unit back from off campus and get out of a lease. It would be possible to do that with Space Management—provided that it had funds to allow it to buy back space. They could also target buildings that should be mothballed, Professor Roe said. Mr. Kallsen said that Michigan is looking at contiguous spaces of up to 5,000 square feet, so they are only willing to buy back space that meets that criterion. If the colleges could put space together, they could then put it to the next best use.

Professor Olin said it would be helpful if they could break down space costs by the hour. They have tried to standardize hours of operation, and it would help if they could see costs per hour. Vandalism is more likely to occur on weekends and maintenance costs are probably higher then as well; the data might provide an incentive to reduce hours of operation.

Professor Luepker said he was trying to think how the Committee could be supportive of more efficient use of space. The Committee has issued statements and no one opposes more efficient use. He thanked Vice President O'Brien and Mr. Swanson, and adjourned the meeting at 4:00.

-- Gary Engstrand

University of Minnesota