Minutes[*]

Senate Committee on Finance and Planning
Tuesday, December 20, 2011
2:00 – 4:00
238A Morrill Hall

Present: Russell Luepker (chair), Sarah Chambers, Will Durfee, Catherine Fitch, Susan Hupp, Lincoln Kallsen, Kara Kersteter, Cody Mikl, Fred Morrison, Richard Pfutzenreuter, Gwen Rudney, Terry Roe, Michael Rollefson, Ann Sather, Arturo Schultz, S. Charles Schulz, Michael Volna, Aks Zaheer

Absent: Jon Binks, Kathleen O'Brien, Karen Seashore, Thomas Stinson

Guests: Associate Vice President Terry Bock (Academic Health Center), Richard Johnson (Capital Planning and Project Management); Julie Tonneson (Office of Budget and Finance)

[In these minutes: (1) updated on Biomedical Discovery District; (2) committee business; (3) annual financial report; (4) fully-allocated cost of mission activities]

1. Update on the Biomedical Discovery District

Professor Luepker convened the meeting at 2:00 and welcomed Messrs. Bock and Johnson to provide an update on the Biomedical Discovery District (BMDD).

Mr. Bock began with reviewing the history and goals of the BMDD.

-- Approved by the MN Legislature in 2008
-- The purpose of the program is to "further the investment in biomedical science research facilities in Minnesota to benefit the state's economy, advance the biomedical technology industry, benefit human health, and facilitate research collaboration between the University of Minnesota and other private and public institutions in this state."
-- The program is to fund projects totaling $292 million.
-- The State of Minnesota pays 75% of the capital costs.

The program goals are to "advance Minnesota's leadership in biomedical science, . . . enhance AHC [Academic Health Center] research capabilities and productivity, . . . [and] expand competitive jobs for Minnesota's economy."

Mr. Johnson provided a pictorial overview of the BMDD and the buildings that comprise it. There are areas adjacent to the BMDD that are sites for potential development in the next 10-30 years either by the University or by a private-sector research park. Mr. Bock noted that they planned the area as a campus and looked at the long-term development of the district.

Mr. Bock turned to the building that is currently under construction, the Cancer/Cardio Building and explained the research that would take place in it. Part of what the University faced in 2008, and still

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does, is a shortage of research space, especially in the Medical School, so the ability to recruit and retain faculty members as grant funding increased was limited. That is the reason the University went to the state in the first place to seek funding for the BMDD, in order to be more competitive in research.

Cardiovascular research:

-- Upon completion, the Lillehei Heart Institute and the Department of Integrative Biology and Physiology will relocate 15-20 investigators to the new space. Research examples include the following areas:

- Cardiac Regeneration
- Cardiac Development
- Muscular Dystrophy
- Congenital Heart Medicine
- Genomics

-- Depending on grant funding at the time of occupancy, additional space is being preserved for future hires in Cardiovascular research

Cancer research:

-- The Masonic Cancer Center planned its use of the Cancer/Cardio Building to focus on two specific groups of investigators:

- Chemical Biology – Eight existing faculty and up to five new faculty with a focus on studying chemical carcinogens as a cause of cancer.
- New Models to Fight Cancer – Seven existing faculty and up to five new faculty will study novel new therapeutic strategies to fight cancer– building on collaborations underway with researchers in WMBB and CMRR

-- The Masonic Cancer Center will also preserve some bench space for future hires.

In addition, a part of the Cancer/Cardio facility will be a Research Instrumentation Commons:

These facilities will be shared among all researchers in the District:

- Cellular Imaging
- Flow Cytometry
- Mass Spectrometer
- Nuclear Magnetic Imaging
- Genomics
- Long Term Study Assessment Facilities
- Primary adjacency to Center for Magnetic Resonance Research

Mr. Johnson reviewed the history of the BMDD facilities. The Center for Magnetic Resonance Research (CMRR) was built largely as planned. The cancer and cardiovascular facilities were originally planned as separate buildings, at about $85 million each, but have since been joined in one building at a cost of about $200 million. The reasons for combining them included the sharing of facilities and services and getting more for the dollar in one building because there are economies of scale.

The final element of the BMDD was to be an Infectious Disease research facility, but that has been changed to "Biomedical Research Facility Projects" and has about $38 million available. How those funds will be used has not been determined; they could be directed to renovation of biomedical research labs in space that is being vacated as researchers move from existing University facilities into the new BMDD buildings.

Mr. Johnson showed Committee members a series of slides illustrating the floor plan of the new building and talked about construction progress.

Mr. Rollefson asked about the source of the funds to pay the salaries of the new faculty members and start-up costs; that will be a major investment. Mr. Bock agreed that it will be and said they are projecting fewer new faculty members than when the project started. The Medical School and Cancer Center have set aside funds to be invested for this purpose. They have a couple of years of planning; if the building is completed in the summer of 2013, as planned, the new faculty lines and start-ups will be a budget item in FY14. They are also working with the Minnesota Medical Foundation on finding funds for recruitment packages and the University's 25% share of the facility construction costs.

Professor Zaheer inquired about the process by which the Infectious Disease facility morphed into something else. Mr. Bock explained that in the initial planning in 2008, it was clear that investments were needed in CMRR, cardiovascular, and cancer research. The remainder was unclear, and as they studied the possibilities more, a number of critical needs have emerged. They have a number of options for the $38 million: (1) Construct a program-specific facility, such as for neuroscience or infectious diseases; (2) renovate existing labs (permissible as long as they are biomedical labs); (3) build collaborative research space, including units such as Public Health; or (4) build space for computational and dry-lab research. $38 million does not buy a lot of building, Mr. Bock observed, especially if it has wet labs.

Professor Chambers asked if there is a difference between investigators and faculty, as used in the information presented, and also about the number of other employees anticipated. Mr. Bock said the two terms meant the same thing—faculty members—and that the planning assumption has been that each new faculty member would also have six additional employees, although that figure may be low.

Ms. Kersteter said she liked the research-instrumentation commons and asked if it would be limited to those itemized in the presentation or if it would be expanded. Mr. Bock said it would include the ones identified; there is a little unassigned space that could be used for other services. They asked the researchers what they need in order to develop the list. The services will be primarily Internal Service Organizations, supported through fees to departments and colleges.

Is this a Medical School project, Professor Durfee asked? Are other units involved? It is a University project, Mr. Bock responded, although investigators will come principally from the Medical School. However, Pharmacy, Biological Sciences, Psychology in CLA, and Child Development in the College of Education and Human Development may participate; the district is meant to include investigators across campus. Initially the focus has been on the Medical School because of the shortage of wet-lab space, but look to expand to other colleges if they do biomedical research.

The original plan called for two buildings at $85 million and now there is one for $200 million, Mr. Rollefson observed. The $200 million includes more than construction costs, Mr. Johnson explained; the $85-million figures were projected before he became involved and may have been only construction costs. He also said that it can be difficult to compare facility construction cost projections unless one is looking at the specific budgets for each; it can be an apples and oranges comparison. Moreover, there are economies achieved in connections to the existing infrastructure in chilled water, heat, and electricity. The size of the research-infrastructure commons also increased significantly, Mr. Bock added.

Professor Luepker asked what the cost per square foot is for the new building. It is $409 per gross square foot, Mr. Johnson said.

Dr. Fitch asked, apropos the goal of recruiting and retaining faculty, if the faculty have been retained. They have, Mr. Bock said. They also have a number of active recruitments under way. Because they are 18 months away from the opening of the building, the number of faculty members recruited may shift, depending on how things stand, but he believes they are in good shape.

Professor Roe said he understands there will be nine new faculty members and about six additional staff for each one, as well as new equipment and so on. He asked that the Committee be provided an analysis of the financial flow and the costs. The Committee would also be interested in knowing what happens to the space that people are vacating. Mr. Bock said that as they update the financial planning, he can provide the information to the Committee next year. They are looking at the freed-up space and what it would take to renovate it. They are also looking at what buildings they want to decommission and tear down, such as the VFW Cancer Research Center—so its occupants would need to be relocated. They are proposing to work with University Libraries on a major renovation to Diehl Hall, to make it into a major educational facility; it has very old research labs that will need to be moved. Repurposing the Masonic Cancer Center facility is also on the list, Mr. Bock concluded.

Professor Shultz asked about the AHC strategy for partnerships with trade groups or the facilitation of research with other entities. Mr. Bock said he was not prepared to talk about that topic; many of the activities in that realm have been shifted to the Office of the Vice President for Research. He said he is aware that there is work afoot on a potential research park near the BMDD. Some universities have come up with multi-million-dollar collaborations, Professor Shultz said, and he wondered if the University is headed in that direction as well. Mr. Bock said he surmised that it is.

Professor Luepker recalled that there had been discussion of as many as 50 new faculty members in the earlier discussions of the BMDD, but now they are talking about moving current faculty with existing grants, not new funds, and there was also discussion about private industry putting a new building next to the University facilities. There will be loans and operating costs; how will they be dealt with? That is part of planning for FY14, Mr. Bock said. Professor Luepker said the Committee will want to hear more about the planning. Mr. Bock said that they have reduced the number of new faculty because it saves money and recognizes the new financial reality. But they continue to do well on cardio and cancer grant funding.

Professor Luepker thanked Messrs. Bock and Johnson for their presentation.

2. Committee Business

Professor Luepker turned to three matters at hand.

-- He has asked Professor Seashore to expand on her concerns about the financial implications of enrollment shifts in undergraduate programs.

-- He has formulated a set of questions that the Committee could address to President Kaler. They are questions of interest to the entire campus. Committee members offered a few suggestions. Professor Luepker said he would take the suggestions into account and try to arrange a time for the President to meet with the Committee.

-- He has spoken with Professor Sheets, chair of the Committee on Faculty Affairs, about recommendations on salary instructions. He said he agreed that this Committee would await a statement from the Committee on Faculty Affairs and react to it.

3. Annual Financial Report

Professor Luepker turned now to Mr. Volna to review for the Committee the University's annual financial report.

Mr. Volna distributed copies of a set of slides containing information from the 2011 Annual Financial Report and noted that the entire report, 86 pages, can be found on the web. [http://www.finsys.umn.edu/controller/um_annualrpt2011.pdf] These statements are annually audited by Deloitte & Touche and they gave the University a clean bill of health. Some of the highlights from the report are:

-- The University's balance sheet continues to be strong and prudently managed.
-- Net assets increased by $312.5 million.
-- Total revenues increased while operating expenses were down slightly.
-- The University had positive cash flow for FY 2011.

Mr. Volna provided an overview of assets and liabilities as well as revenues and expenditures. Long-term debt increased by $189 million because of the issuance of general-obligation bonds to provide funding for various capital-related projects. With respect to revenues, a pie chart of the revenue sources demonstrates that the University has a large and varied base of revenues. With respect to operating expenses, the percentage of the University's expenses devoted to teaching, research, and service have remained very stable over many years (about 53%); academic support constitutes another 12% and operation and maintenance of facilities 9%. Auxiliary enterprises (self-supporting units) make up another 8%. The remainder is divided among student services, institutional support, scholarships and fellowships, and depreciation.

Mr. Volna also reviewed the cash flows and the assets and liabilities of "component units" (e.g., the foundations) of the report, which must be included by accounting standards and external rating agencies. He provided a more in-depth presentation on net assets, which is a balance-sheet concept that equals assets minus liabilities. Net assets are non-recurring, not fully liquid, may have to be liquidated, and may or may not be restricted or committed. The University's total unrestricted and restricted-expendable net assets amount to about $1,403 million and are comprised primarily of net receivables, student loan receivables, and investments including RUMINCO (the University's self-insurance company). To get money from the net assets, Mr. Volna explained, the University would have to collect all its receivables and liquidate all inventories and investments—at which point it would have few net assets left.

Professor Roe asked that the Committee be provided with time-series data on student loans. Mr. Volna said he could present year-to-year balances.

Mr. Rollefson noted that fund balances keep growing but employees were required to take a furlough; was any thought given to using fund balances? Vice President Pfutzenreuter said that former President Bruininks was aware of the fund balances, the issue was debated, and he made a choice.

Mr. Mikl maintained that the discussion about tuition is the first one the Committee should have.

Professor Chambers asked, apropos of declining operating expenses, if there were areas where there were savings and areas where expenses increased. The core mission expenses were consistent, Mr.

Volna said, while institutional support declined. He said he could provide comparisons with last year's data and would provide them to the Committee.

Professor Luepker said he was persuaded that the University cannot easily tap its net assets, but if they increase by 15-16%, presumably some of that increase is in negotiable securities. It is, Mr. Volna replied, but the University does not liquidate them unless a company is bought out or the University is re-balancing its portfolio; the idea is to hold assets in perpetuity. The bulk of the money is in the Consolidated Endowment Fund, Mr. Pfutzenreuter added, which money belongs to the units. If he were a legislator, Professor Luepker said, and he noticed that the University's assets had grown, he would ask why the institution is complaining about its budget. Because the University cannot get its hands on and spend most of the assets, Mr. Volna said; much of the increase in assets is because of the appreciation of the endowment and the addition of new buildings. Mr. Pfutzenreuter said he would tell Luepker the legislator that he should also look at the consolidated fund statements for the State of Minnesota; if one looked also at those statements, the state would not have had a $5-billion deficit. The state considered only one fund when it determined it had a deficit.

Professor Luepker thanked Mr. Volna for the review of the annual report.

4. Fully-Allocated Cost of Mission Activities: Part I

Professor Luepker turned now to Vice President Pfutzenreuter to begin a discussion of fully allocating the cost of mission activities.

Mr. Pfutzenreuter said that his office (along with the Office of Institutional Research and the Office of the Vice President for the Health Sciences) has been working for quite a while on the fully-allocated cost of mission activities. The University keeps track of money in a variety of ways, such as money spent on instruction, such as salaries, but not the overhead costs of instruction. The late Dr. Zetterberg did such an analysis about 15 years ago but it was not continued; they have now revived it. They will present the methodology today and the actual numbers in January.

Mr. Kallsen laid out the principles for the study:

-- Uses an all-funds, full cost and revenue approach
-- Incorporates both direct and indirect/support costs of mission activities
-- Ties to the general ledger
-- Allows analysis at the system level and where applicable the campus/collegiate (RRC) level
-- Is replicable in future years

The purpose of the study is to provide management data for use by the University's academic leadership.

Mr. Kallsen also explained how the study was organized and noted that costs will be assigned to five categories: instruction, research, public service, auxiliaries, and student aid. The allocation of cost will rely on "chart string" level data, summed to the college or campus. It will also rely on cost-pool allocations. He provided a visual representation of the concept of fully allocating costs for each of the mission activities (and also auxiliaries and student aid), which would include direct costs (e.g., faculty compensation, teaching assistants, sponsored research) and indirect costs (e.g., advisers, the Registrar, deans' offices, libraries, utilities, maintenance). There are nine primary cost-allocation pools that make up institution-level indirect costs that have to be allocated. Some are clear, such as the cost pool that includes the Office of the Vice President for Research, Sponsored Projects Administration, and so on—that one is attributed entirely to research. Similarly, the costs of general-purpose classrooms and the costs of student finance administration, honors, admissions, etc., are attributed to instruction. Others are distributed on a proportionate basis (libraries, support service units, information technology), usually based on direct costs, and some have data enabling the costs to be assigned by activity (facilities, utilities, debt and leases).

For indirect costs commonly found within colleges and campuses, but outside the cost pool charges, most are allocated in proportion to direct costs. So if 70% of a college's direct costs are for instruction, 70% of the cost of the dean's office is allocated to instruction. And so on.

In the case of fully-allocated instructional costs, they know who is teaching each course, by employee ID number, so can assign a salary cost, Mr. Kallsen said. They proposed to distinguish among undergraduate, graduate, professional, and Medical School Resident instructional costs.

Professor Zaheer asked how they split salaries between teaching and research. That is difficult for professorial salaries, Mr. Kallsen said. Where a unit has a lot of sponsored funding, the allocation of salaries is probably fairly accurate. In most areas, however, faculty salaries are paid from one chart string that is often coded as “instruction”, so in that case they are allocated 100% to instruction. They have no data on the appropriate division for salaries of most CLA faculty members, for example. So instructional costs may be slightly too high, but these are the definitions used nationally.

So "instruction" includes departmentally-funded research, Professor Morrison said. Unless it is coded separately, that is correct, Ms. Tonneson said. For all colleges that do not raise very much external funds, this formula overestimates instructional costs substantially, Professor Zaheer pointed out. Mr. Pfutzenreuter said he did not know if it would be "substantially" and said that they could do a survey and create an algorithm they could use to assign values to research and service. Mr. Kallsen said that a change might not necessarily be better; lower instructional costs are not necessarily better. If costs are reallocated so that instructional costs go down, then research or service costs will increase.

Professor Shultz said that his department did a survey of time allocation that was helpful in planning and in assigning duties. There are tools available.

Professor Morrison suggested in jest that everyone should move to billable hours like lawyers. There was an effort to capture how people spent their time, about 20 years ago; it was "not very accurate."

So when they allocate faculty costs for teaching, research, and service, instructional costs equal instructional costs plus non-coded research plus non-coded service costs, Professor Hupp asked? They could apportion faculty salaries, Mr. Kallsen reiterated. Professor Hupp said that labeling the cost as "instructional" is not accurate. Mr. Pfutzenreuter asked how much Professor Hupp would move out of the cost-of-instruction category; she said "a lot." Someone could be 60% research, 20% of which is externally funded, but they will evaluate the person on the basis of being committed 60% to research.

Mr. Kallsen said they would return to the issue. If there is a refinement, it would have to be system-wide and replicable, and they could prepare data to see the effect on the numbers.

Ms. Tonneson reviewed the allocation of revenues and pointed out that they could be presented in a way that shows how each cost category is supported as well as where the money in each of the revenue categories goes. At present, tuition and the state funds are comingled as "O&M" funds at the department level; they can be separated at the college level. For this analysis, there needs to be a decision rule about how to separately identify and assign the two sources of revenue because the system does not automatically do that at the department level, which is where spending occurs. In the category of research, "for the cost allocation analysis, research spending does not have to be further identified as sponsored vs. nonsponsored, but for revenue allocation purposes—it might be useful to separately identify them—to better understand how nonsponsored revenues flow through to support research."

Mr. Pfutzenreuter said that they have had a decision rule about allocating costs, even though they know that non-sponsored research and public service are coded as instruction; that decision rule may require attention. Ms. Tonneson said they are aware that there is a significant amount of non-sponsored research.

Their initial conclusions, which Ms. Tonneson observed are quite obvious, are these:

-- Each of our mission activities is supported by multiple revenue streams;
-- Fully allocated costs of instruction vary among colleges and campuses, and between student levels (undergraduate, graduate, professional);
-- Few institutions complete costs studies of this type, and those that do all use different methodologies. Results are not comparable between institutions, but are valid for measuring changes within the University over time. (For example, the University has cost pools; most institutions do not.)

If one were to construct a matrix, with each of the colleges on the X axis and levels of instruction on the Y axis, with the cells in the matrix containing the cost of instruction at each level and in each college, each cell would have a different number. That is neither good nor bad because different variables influence the numbers. They will identify the variables, Ms. Tonneson said.

Professor Roe said that it is likely instructional costs are over-estimated because they include non-sponsored research, so it is important to know the direction of bias in the data. Mr. Kallsen agreed and again made the point that the money is being spent, so if the cost in one category is reduced because of a change in the way it is calculated, then the costs in other categories must rise, and at present the costs of research and service are being under-stated.

Who is the audience for these data, Professor Rudney inquired? Whoever it is will ask what they are getting. There are several different audiences, Ms. Tonneson said, and they include consultation with: colleges and campuses to help understand their activities; the senior academic officers for the same purpose; and the Board of Regents, which has asked for the data because it would like to be able to compare across units and wants to use the data at a policy level to help guide the administration. For example, there could be higher costs for student support in one college; should that same level of expenditure be extended to all colleges? Or should that college reallocate its resources to some other purpose?

Professor Luepker complimented Ms. Tonneson, Mr. Kallsen, and Vice President Pfutzenreuter for coming to Committee meetings prepared with information on interesting topics and said the Committee looks forward to receiving the data. He wished everyone a happy and safe holiday and adjourned the meeting at 4:05.

-- Gary Engstrand

University of Minnesota