# Memo

## Budget Committee of the Academic Senate

To: Budget Committee

From: Michael J. McIntyre, Chair

Subject: Report on Budget Proposals for FY 2007 and 2008

Date: July 14, 2007

The Budget and Finance Committee of the Board of Governors (BFC-BOG) met on July 10, 2007, to discuss budget options in preparation for its July 25 meeting, when tuition rates for Academic Year 2007-08 will be set. Provost Barrett and Budget Director Kohrman made a lengthy presentation to the committee, which is available on line.[1] The BFC-BOG also discussed possible ways of closing a budget hole of around $25 million created primarily by the State's failure to provide the funds that were promised to the University at the beginning of FY 2007. Obviously, the State is facing serious budget problems of its own, due to revenue shortage. There are good reasons for concern, moreover, that the fiscal problems of the State will not go away very soon.

At the July 10 meeting of the BFC-BOG, I suggested a number of areas where the University ought to consider making cuts or enhancing revenues. I was asked by committee members and by President Reid to provide a list of those suggested cuts so that the Administration could respond to the suggestions and obtain background information in anticipation of the July 25 meeting. I provide that information in this memo. I also suggest a basic philosophy for budget cuts and raise issues that this committee might want to address at its meeting scheduled for July 20, 2007.

### 1. Suggested Budget Cuts for FY 2008

At the BOG's July 10 meeting, I suggested, in outline form, that the following budget cuts and revenue enhancements be considered as a way of reducing the expected deficit. Several of these suggestions had been raised at the June 18 meeting of this committee. Some I made on my own initiative.

- *Capture of royalties from research projects for the General Fund*. Currently, royalties resulting from joint ventures between the university and researchers end up in the budget of the Office of the Vice President for Research (OVPR), with no accounting to the BOG or

[1] Link: http://www.bog.wayne.edu/meetings/2007/07-10/bfc_doc.pdf.

the university budget office. We need a full accounting of the royalty amounts received and the way they are spent. The amounts involved are unclear, due to the lack of accounting, but I'm guessing that the average annual royalties may be around $10 million per year. I am not suggesting that all of these funds be used for deficit reduction but that they be on the table for possible use for that purpose.

- *Increase in FMRE tax, e.g., from 8.9% to 10%*. The School of Medicine collects a tax of 8.9% from funds generated by the practice plan for use within the medical school. I claim no expertise on this issue, but I understand that this tax is somewhat low relative to the tax imposed by other medical schools. I suggest we consider some increase, perhaps to 10%, with the new amounts being used in the short run to offset the deficits. In the longer run, the funds might be devoted to paying part of the interest costs for bonds used to construct a new research facility.

- *Eliminate inefficient centers.* One of the three centers funded from the so-called Research Excellence Fund has not performed well over a very long time. I understand that it has a budget of around $1.2 million per year. Eliminating this center would not result in a savings of that entire amount because a significant portion of the money spent by the center is for faculty members who have retreat rights in a department. Under prodding from a BOG member, I indicated that the center I have in mind is the Institute for Manufacturing Research. I noted that the center has failed to obtain substantial grants that provide for indirect costs and has otherwise failed to distinguish itself, despite a high level of financial support from the University for many years.

- *Rollback of special allocation to OVPR*. Last year, the University gave the Office of the Vice President for Research an increase in annual funding of $1 million. In requesting these funds, the OVPR claimed that its top priority was new faculty hiring, setups for new faculty, and retention offers. The Budget Committee asked the Policy Committee to request an accounting of how the money was actually being spent. In February of 2007, it received a fax from the OVPR indicated that $997,000 (rounded) had been spent and that none of it had been spent on faculty hiring or faculty setups.[2] The memo (dated Feb. 15, 2007, from Gloria Heppner) said that the amounts spent on setups and retention offers could not be determined until the end of the hiring season. Still, all but $3,000 of the funds (99.7%) have been accounted for.

  I suggested that this $1 million fund not be renewed for FY 2008 since the money was not being spent for what the OVPR had identified as its high-priority items. Last July, the BFC-BOG had voted to earmark the funds for setups and retention offers but that decision was overturned by the full BOG in response to serious complaints from the OVPR. It now appears that explicit earmarking was necessary if the money was to be spent for the high-priority uses.

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[2]Link: http://www.law.wayne.edu/mcintyre/Budget/budget-other_reports.htm.

- *Partial freeze on Administrative salaries*. According to the information provided by the Administration to the AAUP-AFT, administrative salaries increased in FY 2007 by 3.8%, with salaries for top administrators increasing by 8.6%.[3] Those increases are quite large, given the budget situation facing the State and the University. I suggested that the increase for FY 2008 be capped at 1%, with a fund representing 0.5% of the administrative salary pool reserved to deal with retention offers and other special cases. I estimate a savings of around $500,000 from this step.

- *Partial freeze on expenditures from plant fund and new capital outlays*. I was led to believe that the BFC-BOG would receive a full accounting of balances in the plant fund and other funds not included in the General Fund. That information was not provided as far as I can determine. In dealing with the FY 2007 shortfall, I have suggested that some plant projects that have been approved be deferred at least until FY 2008, so that the funds saved could be used to finance the 2007 deficit. The expectation would be that funds would be returned, if possible, to the plant fund and other funds early in FY 2008. The objective would be to give some flexibility to the University in coping with the $23.5 million shortfall in State funding for FY 2007. The Administration has simply called for a hold on projects that have not yet been started or approved. I am proposing a broader hold, although I do not suggest that projects be deferred if deferral would put the University at risk of significant financial losses.

- *Capture of excess reserves from auxiliaries*. There has been a practice over the years of spending the excess reserves generated by various auxiliary activities, most notably by the book store, for University purposes without the money ever going into the General Fund for allocation under normal procedures. As a result, it is likely that money is being spent for activities that do not have as high a priority as projects that are being cut on account of the University's projected budget deficits. I suggested that the excess funds from auxiliaries be turned over to the General Fund. At least some portion of those funds would be available to deal with deficits.

- *Major change in WDET*. WDET has been running a chronic deficit for years, and various plans for reducing the deficit have failed. I suggested that this auxiliary function needs to be self-supporting. If that goal cannot be achieved, then radical changes in WDET need to be considered, including its sale or disposition. In response to comments from various BOG members, I made clear that I was not making a proposal at this time for the sale of WDET. My point was that the University simply cannot afford to have its auxiliary functions draining money from the General Fund when the core functions of the University are being underfunded. WDET's projected deficit for FY 2008 is over $800,000.
- *Re-evaluation of Athletic Programs*. The University has been increasing its financial support for various athletic programs in recent years, although that increase remains controversial within the University community. In FY 2007, $4.2 million was budgeted for athletic programs. No information has been provided to the committee with respect to

[3]Link: http://www.aaup-aft.wayne.edu/newsbriefs.html.

the plans for athletic programs for FY 2008. Since athletics is not a core function of the university, it ought to be an area considered for budget cuts.

## 2. Notes on Budget Philosophy

In making recommendations on budget issues to the Administration and the BOG, the Budget Committee of the Academic Senate has been guided by the following general principles:

- *Global examination of budget issues.* In principle, all of the relevant issues relating to the budget ought to be on the table at the same time so that the tradeoffs required in setting the budget can be made in a rational way. The proposed consolidation of the discussions of the General Fund budget and the auxiliary budgets is consistent with this principle. The separation of the tuition decision from other budget decisions is not.

  No one, including members of the Budget Committee, should favor or oppose a tuition increase in the abstract. The decision depends at least in part on how the increased tuition money will be spent. I understand and support the postponement of the budget debate until September, given the uncertainty about the State funding. And I agree that our students need to be told soon what their tuition will be for Academic Year 2007-08. So the bifurcation of the tuition decision and the general budget decisions is sensible under our special circumstances, and I supported that bifurcation at the BFC-BOG meeting of June 20, 2007. But to make sure the process works properly, we need to have a firm understanding on key budget issues before the tuition decision is made.

- *Across-the-Board (ATB) cuts*. The Budget Committee generally has opposed across-the-board cuts to the Schools and Colleges. We have seen Administrations in the past use such cuts to avoid making hard budget decisions and, quite frankly, to reduce the share of the budget going to the Schools and Colleges. Our opposition to ATB cuts, however, has never been absolute. The Provost noted at the last meeting of the committee that ATB cuts can be strategic in some circumstances, especially when the data needed to make selective cuts is not available. I think there was general agreement with that position among members of the committee.

  Still, I believe that ATB cuts should be used cautiously, after better alternatives have been exhausted. The committee almost certainly prefers that the Administration make targeted cuts when there is good evidence that a particular program or project has failed or is performing badly. At the same time, the committee is likely to oppose targeted cuts that are not supported by evidence of poor performance.

  I am not pleased, for example, with the proposed cuts targeted at units that happen not to have spent all of their available funds before President Reid imposed a spending freeze. That freeze (effective June 25, 2007) created artificial year-end balances, which the Administration proposes to capture with a tax of up to 100 percent. Those cuts are

targeted, but the targeting is not strategic and creates a dangerous precedent. Similarly, the committee is unlikely to support cuts targeted irrationally at some broad category of employees, such as technical support staff.

At its meeting of June 18, 2007, some members of the committee suggested that any ATB cuts be mitigated by establishing a reserve that the Provost could use to reduce the cuts in particular units if they would create a severe hardship or undermine a particularly successful program. The committee also was told that any ATB cuts would not affect funding for tenured/tenure-track faculty. The committee has repeatedly warned about the decline in funding for the Schools and Colleges that has led to an unfortunate increase in student/faculty ratios. I could not support ATB cuts that would further increase those ratios, and I believe that most, perhaps all, members of the committee share that view.

- *Accountability*. An essential aspect of budget discipline is that units receiving funds be accountable for those funds by showing that the funds were expended for the purposes for which they were appropriated. In my view, a unit that receives funds to advance what it claims to be its top priority and spends the money for some other purpose should not receive such funds in the future.

- *Decentralized Budget Decisions*. The Budget Committee generally has favored the allocation of spending authority to the unit most capable of exercising that authority intelligently. Some spending decisions ought to be made centrally, but most should be made at the unit level because the people at the unit level are more familiar with the needs of their unit. With respect to the upcoming budget cuts applicable to the Schools and Colleges, I favor local control. In particular, I believe we will get more efficient results if we let the deans and department chairs, after consultation with the relevant faculty committee, decide where the cuts should be made.

## 3. Budget Issues to be Resolved Prior to Tuition Decision

As indicated above, I do not think it is sensible to approve a tuition increase without an agreement in general on how the tuition increase will be spent. The problem with creating proper linkage is that the size of the necessary cuts is not certain, due to the uncertainty about the support coming from the State. As a result, some ingenuity is required to approximate the results that would be reached if the tuition decision and the budget decisions were being made at the same time.

In my view, it is useful to separate out four issues: (1) Cuts for FY 2007; (2) One-time cuts for FY 2008; (3) Permanent cuts for FY 2008; and (4) Design of tuition increases under the uncertainty of State support for the University. I set forth below my preliminary thoughts on these four issues.

- *Cuts for FY 2007*. All of the cuts for FY 2007 are one-time money. The University is simply trying to pay its bills for the current year after the State shortfall of $23.5 million. The

basic plan presented to the BFC-BOG is to freeze, as of June 25, 2007, most spending over $300 per week. The result will be that year-end balances will be created. The Administration proposes to impose a tax of up to 100% on those balances. Some categories of spending, notably spending on tenured/tenure-track faculty, are not subject to the freeze. I've so far been unsuccessful in getting clarified how spending by PIs is affected by the freeze.

Another asserted source of money for FY 2007 is the utilization of reserves. No information was given on the amount of the reserves or the amount expected to be drawn from those reserves. I understand that there is enough in the plant fund alone to handle most of the FY 2007 shortfall. No figures were given on the amounts remaining in the rainy day fund.

No one can defend the tax on year-end balances except as a temporary expedient to get through FY 2007. I am not convinced that the step can be justified even as an expedient because I am not sure that there are not other, less harmful expedients. One problem with capturing the year-end balances, many of them artificially created by the spending freeze, is that units will be concerned that this step will be taken in future years and will plan accordingly by spending down their balances in inefficient ways well before the end of the fiscal year. The other problem is that this measure is not strategic — it is both unfair and unrelated to achieving the goals of the University.

To mitigate the problems with the tax on year-end balances, the University needs to put in place now a plan for making the units whole, to the extent feasible, in FY 2008. One part of that plan should be a public commitment by the University to return the funds pro rata to how they were taken if the State, as promised, refunds some or all of the $20 million it declined to pay in FY 2007 as a result of its own budget problems. A second part of the plan should be a public commitment to replace a substantial portion of the year-end balances from University funds if the State does not make good on its promise to return the $20 million. That is, the capture of the year-end balances only makes sense as a temporary measure, to get the University though FY 2007. Returning those funds in FY 2008 should be a very high budget priority for the FY 2008 budget whether or not the State keeps its promise to return the $20 million it cut from the University's FY 2007 appropriation.

- *One-time cuts for FY 2008*. As discussed above, the University will need an additional $20 million or more in FY 2008 to "repay" the units for the year-end balances that were captured at the end of FY 2007. That is, there needs to be some reallocation of funds in FY 2008 to reflect the fact that funds were recaptured in an irrational pattern at the end of FY 2007 to deal with the FY 2007 shortfall.

  For fixing the problem created by the capture of year-end balances, the University needs one-time money only, from the State or from other sources. In addition, it may need one-time money if the State makes some temporary cuts in the amounts given to the Univer-

sity for FY 2008. Given the difficult budget situation facing the State, the possibility that the University will not get all of the money promised is a real one. The University needs a plan that makes strategic sense for coping with this problem. In particular, it needs a plan for undoing the damage otherwise resulting from its tax on year-end funds and for avoiding a similar scenario at the end of FY 2008.

One potential source of one-time money is the large amounts of money given to the School of Medicine for hiring faculty members that was unused as a result of a hiring freeze at the SOM. Another source of one-time money is the postponement of building projects that could be delayed without imposing significant extra costs on the University. Several of the cuts suggested in section 1 of the memo would provide one-time money, and even some of the proposed permanent cuts could be structured as one-time cuts.

- *Permanent cuts for FY 2008*. No one doubts that the University faces significant deficits unless it increases tuition rates and makes some significant budget cuts. The size of the budget hole depends in part on the amount of State support received, and that amount is not now known. The Administration estimates that if the $3.2 million "permanent" cut for FY 2007 is continued for FY 2008 and no other cuts are imposed, then a tuition increase of 13%, coupled with budget cuts of $6.9 million, would result in a balanced budget. Of course, if permanent cuts in State support are greater than $3.2 million, then larger budget cuts or higher tuition would be required. The size of the projected tuition increase assumes that a portion of that increase would go for additional financial aid to students.

  The Administration has not disclosed in any detail how it would achieve the $6.9 million in budget cuts. It would appear, however, that most of the cuts would come in the form of an ATB cut in the budgets of all units, subject to certain exceptions, the most important being that there would be no cuts in the amounts currently spent for tenured/tenure-track faculty.

  I have suggested some permanent budget cuts in section 1, above, that would allow for lower ATB budget cuts or a lower tuition increase (or some combination of same). The advantage of my suggested cuts over the proposed ATB cuts is that mine are targeted at inefficient or ineffective programs and would not deplete resources supporting the core functions of the university. I recognize, nevertheless, that some ATB cuts are likely to be required to balance the FY 2008 budget.

## 4. Tuition Scenarios

A major problem for the Administration in presenting a tuition-rate proposal is that it does not know how much tuition revenue will be needed for FY 2008, due to the uncertainties about the level of State support for the University. So far, the Administration has not offered a plan for coping with the uncertainty. In principle, one-time cuts in State support would not justify a permanent increase in tuition to make up for the shortfall. In practice, however, it is

not trivial to design a temporary tuition increase that would be fair to most students and would not create problems for students in obtaining financial aid.

At the meeting of the Budget Committee on June 18, 2007, the Administration indicated that it planned to bring two tuition proposals to the BOG. The new plan, agreed to at the July 10, 2007, meeting, is to bring three tuition proposals. From the materials presented to the BFC-BOG on July 10, it seems a reasonable guess that one proposal will be for a tuition increase of around 13 percent. In a story running in the *Detroit Free Press*, Budget Director Robert Kohrman indicated that the Administration is considering a plan for rebating or reducing a portion of any tuition increase if State funding exceeds current expectations.

It is premature, of course, to discuss the level of the tuition increase before receiving the recommendations and supporting documentation from the Administration. I have been told that we can expect to receive the proposals on Tuesday, July 17 or, at the very latest, on Wednesday, July 18. Our committee will discuss those proposals at its meeting on July 20. Our committee may decide to make a recommendation on tuition rates to the Policy Committee, which will meet on July 23. I have invited Prof. Seymour Wolfson, President of the Academic Senate, to attend our meeting on July 20. As the faculty representative on the BFC-BOG, I will convey to that committee any recommendation that this committee or the Policy Committee may choose to make.

Given the uncertainties about the level of State funding, I think any viable tuition proposal will need to include some contingencies, either for increasing the tuition rate for the Winter Term if the State support is below expectations or rebating a portion of the tuition increase if State support exceeds expectations. In general, I do not favor a plan that would contemplate a tuition increase for the Winter Term, for a variety of reasons, including issues relating to financial aid. I see some problems with a tuition rebate, but I think it may be necessary to find solutions to those problems. If a tuition increase is justified to deal with a temporary reduction in State support, it should be structured as a one-time surcharge and not as part of the basic tuition rate. Needless to say, the method for dealing with contingencies relating to State support needs to be settled at the time the tuition increase is adopted.

The University currently charges students a flat amount per credit hour. Whether this policy is wise is unclear. On the one hand, the Administration has claimed that the costs to the University are greater per credit hour for part-time students. If the charge is to relate to costs, it would be appropriate for the tuition rates per credit hour to be higher for part-time students than for full-time students. On the other hand, part-time students are likely to be more sensitive to the tuition rate in deciding how many credit hours to take. If part-time students actually are more sensitive to tuition rates, then a lower charge for part-time students might be appropriate. I offer no advice on this issue. I would note, however, that the tuition number that seems to get the greatest publicity when rates go up is the rate for full-time entering undergraduate students.

A basic problem for the University in considering tuition increases is that the tuition "solution" is not one that the University can continue to invoke whenever State funding is below expectations. At some point — a point we may now be approaching — additional double-digit tuition increases will simply be unacceptable politically. It is important, therefore, that the University develop plans for dealing with the budget that do not rely on substantial tuition increases year after year and do not rely on a quick recovery of the Michigan economy.