Memo

Budget Committee of the Academic Senate

To: Policy Committee

From: Michael J. McIntyre, Chair
Academic Senate Budget Committee

Subject: Report on the FY 2008 Budget

Date: August 9, 2007

I am writing to update the Policy Committee on the budget situation and on the actions I have taken as Chair of the Budget Committee and as faculty representative on the Board of Governors' Budget and Finance Committee. In brief, the Budget Committee has voted to oppose the across-the-board cuts in the FY 2008 budgets of the Schools and Colleges. I hope that the Policy Committee is supportive of our efforts to minimize the budget reductions currently targeted at the Schools and Colleges.

To get the word out on the budget cuts facing the Schools and Colleges and our efforts to stop them, I have written a memorandum to the chairs of the unit budget advisory committees. I understand that President Seymour Wolfson has distributed that memo to the Policy Committee. In that memo, I explain the position of the Budget Committee and note the myriad ways in which the financial resources of the Schools and Colleges have borne a disproportionately heavy share of budget cuts that have been imposed in prior years or are proposed for the coming fiscal year. I have already sent the memo to those on the list of chairs that I put together last term, but I know my list is incomplete. I hope that the Policy Committee will encourage Seymour to circulate the memo to the deans and chairs and ask them to distribute it to the appropriate people. Time is of the essence, for the proposed budget gets increasingly more difficult to amend as time goes by.

Without going into great detail, I'd like to make three points about the budget. First, students are paying additional tuition of over 18 percent in the Fall and, perhaps, in the Spring and should not have the quality of their instructional programs degraded through further cuts in the budgets of the Schools and Colleges. Second, the additional tuition money is adequate to hold the Schools and Colleges harmless. The reason for the proposed cuts is to divert permanent tuition revenues to cover lower priority new spending outside the Schools and Colleges or to fund short-term revenue shortfalls. Third, the projected hole in the budget can be filled through measures that are more sensible and less harmful to the core functions of the University. I explain each of these points below.

1. Objections to the Proposed Cuts to the Schools and Colleges

At its meeting of July 20, the Budget Committee adopted the following motion:

That the committee recommends against any further cuts to the Schools and Colleges.

That motion was reaffirmed at the Aug. 2 meeting. The point was not to suggest that the various units in the Schools and Colleges should be immune to budget cuts. The Budget Committee has always favored sound budget policies, and it has prepared guidelines on how budget reviews should be conducted. If a school or college can get better return for its money by cutting some program or consolidating another, it certainly should consider doing so. Budget reform ought to be an ongoing project, and no program should be protected from it.

The point of the Budget Committee's motion is that the overall distribution of resources within the University has become unbalanced, to the detriment of the Schools and Colleges. The percentage of resources going to the Schools and Colleges has gone down sharply, student/faculty ratios have risen, and many units find themselves struggling to provide the services that students have a right to expect. In the past, the seeming solution to each budget crunch has been to take a disproportionate bite out of the budgets of the Schools and Colleges. The Budget Committee is saying, "No more."

My memo to the chairs of the budet advisory committees sets out in some detail the various ways in which the University's budget problems have been shifted disproportionately to the Schools and Colleges. I'll not repeat that list here. But I do want to elaborate on a point discussed only briefly in that memo — the somewhat sneaky way in which the proposed across-the-board (ATB) cuts have been rigged to put an unfair burden on the Schools and Colleges. In brief, the ATB formula makes an apples to oranges comparison.

The ATB formula works by multiplying the adjusted base budget of each unit by some percentage. I don't know exactly what that percentage is at this point. That percentage is reverse engineered to get the total budget cuts to be imposed under the formula. Again, I don't know that exact number. In principle, this method would impose cuts in proportion to each unit's FY 2007 budget, which, on its face, has some intuitive appeal. In practice, however, the cuts are distributed to the disadvantage of the Schools and Colleges because the base for the divisions and central accounts is adjusted for some major fixed costs, whereas the fixed costs of the Schools and Colleges remain in the base.

Slide 1, attached, illustrates the above point with a simple example, using some plausible assumptions. I will be able to refine those assumptions when the Administration provides the Board's Budget and Finance Committee with the information on the base and the ATB percentage. The clear point is that the so-called ATB cuts fall, on a percentage basis, much more heavily on the Schools and Colleges than on the more protected parts of the University.

2. Where did the Tuition Money Go?

In its presentation to the Board of Governors, attached as *Slide 2*, the Administration claimed that the revenue from the 12.8% tuition increase would go as follows:

Amount to cover State Shortfall of $3.2 million	14 %
Financial Aid	19 %
Operating Expenses	9 %
Compensation	58 %
TOTAL	100 %

As that slide shows, the revenue from the so-called contingency fee would cover the cuts otherwise required by the failure of the State to pay $10 million of the amount currently in the University's base budget. The fee actually is expected to raise $12.1 million because $2.1 million will be rebated to students in the form of financial aid.

If the Administration's slide were an accurate reflection of its budget plan, then there would be no need for any significant cuts to the Schools and Colleges because their budgets are almost exclusively spent for operating expenses and compensation. Somehow, the money that the Administration's slide claims will go for operating expenses and compensation is actually being diverted under their budget proposal for other uses.

Slide 3, which I created and which I regret to say is a bit complex, shows what is actually happening to the tuition money. In that slide, I have reverse engineered the various percentages shown from numbers obtained from the Administration. Because of a lack of detailed data on some points, I found it easier to treat the additional financial aid financed by the tuition increase as a reduction in the tuition increase. That is, *Slide 3* deals with NET tuition, after the financial aid has been paid. I have not addressed the contingency fee, because it is expected to be used to exactly replace lost revenues, without any reallocations. In addition, we do not know what will happen to the revenue from that fee if the State comes through with all of the promised money.

The point of *Slide 3* is to show what is really going on with the Administration's budget proposal. The first section, labeled "Expense Increases, 2008", shows that a NET tuition increase of 2.5% would be needed to pay for new permanent spending proposed by the Administration — namely a new fund that would be used roughly the way one-time money from year-end balances have been spent in the past. Of course, year-end balances are not likely to end with the FY 2008 budget, so the expected year-end balances now can be used at the discretion of the Administration, without the normal budget review. In my opinion, there is absolutely no justification in these difficult times for adding a $3.7 million slush fund for the Administration.

The second section of *Slide 3* shows "Revenue Reductions, 2008". The Administration has chosen to treat the State shortfall of $3.2 million as a permanent reduction in the budget, despite the governor's recent assertion that the State will return the shortfalls to the university budgets. It has also treated the drop in the Indirect Cost Recovery (ICR) as a permanent reduction in revenue, although it is spending money on research on the premise that the ICR revenues will increase. In fact, either that drop is temporary or the University will have to reduce its expenditures in programs that are supposed to produce ICR money but are failing to do so. The Administratin also treats its projected enrollment drop as permanent. I do not quarrel with that classification, although obviously the enrollment figures need to be updated to reflect information obtained since July.

The important point to be made from the second section of *Slide 3* is that a substantial part of the money obtained from the tuition increase and budget cuts is going to cover the drop in ICR revenue. It is far from clear why that cost should be shifted to instructional units (and the students they serve).

The third section of *Slide 3* shows "Revenue Increases, 2008". Investment income is expected to be up, and, with the recent decision of the Federal Reserve Board not to cut the discount rate, it may be realistic to project a greater increase in investment income. Indeed, it seems reasonable at this point to assume that the increase in investment income will fully offset the projected drop in enrollment. The items labeled "ICR Supplement from SOM" is a placeholder for the amount that the Administration plans to obtain from the chief beneficiaries of ICR money. It is not clear if this revenue source is temporary or permanent.

The fourth section of *Slide 3* shows that the proposed cuts of $9.1 million, reduced by the $1.2 million reallocated within the Schools and Colleges, represents a NET tuition increase of 5.4%. The final section shows that only about half of the proposed tuition increase is needed to fund permanent shortfalls, with the remaining half projected to be used to cover one-time expenses or expenses of uncertain duration.

The bottom line is that the Administration's asserted uses in *Slide 3* for the money obtained from the tuition increase are inconsistent with its actual plans. It is more accurate to view the tuition revenue as going into a pot, along with the money that would be saved from the Administration's proposed budget cuts. How money in that pot is spent is merely a matter of accounting, given the fungibility of money.

It seems fair to say, nevertheless, that the only reason that budget cuts are needed to balance the FY 2008 budget is that the Administration feels the need for money to cover the net ICR shortfall ($6.3 million) and to fund new spending ($3.7 million) previously financed with year-end balances. If the new and non-strategic spending is eliminated and the ICR shortfall is covered with short-term money (e.g., temporary reduction in the plant fund balances), there would be no need for ANY cuts to the Schools and Colleges or to the operating

budgets of units directly supporting the Schools and Colleges (e.g., Library, Financial Aid Office, etc.).

3. Some Better Budget-Cutting Alternatives

It is not my place, or the place of the Budget Committee, to offer up specific units for budget cuts. It is our place, however, to suggest how a budget could be constructed that would avoid the need for cuts in the Schools and Colleges. I understand that the proposed cuts total $9.1 million. Here are some ways of obtaining that money.

1. *Elimination of the $3.7 million that the Administration would use to create a new and permanent funding source for the various projects currently paid for out of year-end money*. I find this use to be baffling, given our current budget situation. The Administration's slide show indicates that the $3.7 million would be used as follows (please ignore rounding errors):

Proposed additional expenditures:

Deferred Maintenance . . . . . $1.50 M
Pres. Research Enhancement . . . . . $1.50 M
University Wide Marketing . . . . . $0.38 M
Telemarketing Contract . . . . . $0.26 M
TOTAL . . . . . $3.64 M

On the merits, none of these expenditures seem to me to have the high priority that should be given to the preservation of the current levels of instruction offered in the Schools and Colleges. The telemarketing program is not viewed as a success, the research enhancement money could be used more effectively by the Schools and Colleges, and deferred maintenance, by definition, can be deferred. The marketing enhancement has never been reviewed by the Budget Committee.

Even if these expenditures deserve a high priority, however, they do not need a new budget line. With respect to these items, there is a one-time problem created by the State's decision not to make the $20 million payment due in August of FY 2007. Because that amount was not paid in FY 2007, there were no year-end balances for that year. To finance its expenditures for FY 2007, the Administration has captured all of the year-end balances of the various units, most notably, the Schools and Colleges. As a result, the Schools and Colleges have a problem financing projects typically financed with their year-end money. That problem does not seem pressing to the Administration. On the contrary, it has chosen to ignore that problem and proposes to solve its own temporary problem by permanently reducing the budgets of the Schools and Colleges. In my view, there is no good reason to support such a proposal.

2. *Cover the temporary drop in ICR amounts with one-time money*. It seems wrong to me to use the money raised through a tuition increase to fund a drop in the ICR money. Students are not responsible for that shortfall and should not be required to pay for it. In addition, it is everyone's hope and expectation that the ICR amounts will go up next year or that the Administration will reduce funding for programs that are expected to produce ICR money but have failed to do it at the expected level. I understand that the University has no choice but to cover the shortfall in the current year. I do not understand why that shortfall should be covered on a permanent basis through a tuition increase.

3. *Make targeted cuts of ineffective or lower-priority programs and activities*. At the request of the Board's Budget and Finance Committee, I prepared a list of areas where I think it would be fruitful to look for targeted budget cuts. That list was distributed to the Budget Committee and the Policy Committee and is posted on the web site of the Budget Committee. I will not repeat that list here. As I indicated above, it is not my function, or the function of the Budget Committee, to make specific recommendations for targeted cuts. I simply noted programs that are a drain on the General Fund budget and are not noted for their success or do not seem to be part of the core functions of the University. I understand that others might prepare a somewhat different list, adding some items and subtracting others. That said, I really do not see a significant problem in coming up with $3 million or more in targeted cuts that would create far less harm to the University than the cuts proposed for the Schools and Colleges.

4. *Eliminate the $1.2 million targeted for reallocation within the Schools and Colleges*. In general, the Budget Committee has been supportive of the idea that if ATB cuts are to be imposed, then the Administration should have a fund in reserve that it could use to mitigate the harshest effects of those ATB cuts. We are pleased that the Administration has followed our advice in this respect. The $1.2 million cut for reallocation purposes, however, is only needed if there are ATB cuts. If those cuts are eliminated, as the Budget Committee has recommended, then the amount set aside for reallocation also can be eliminated.

4. Conclusion

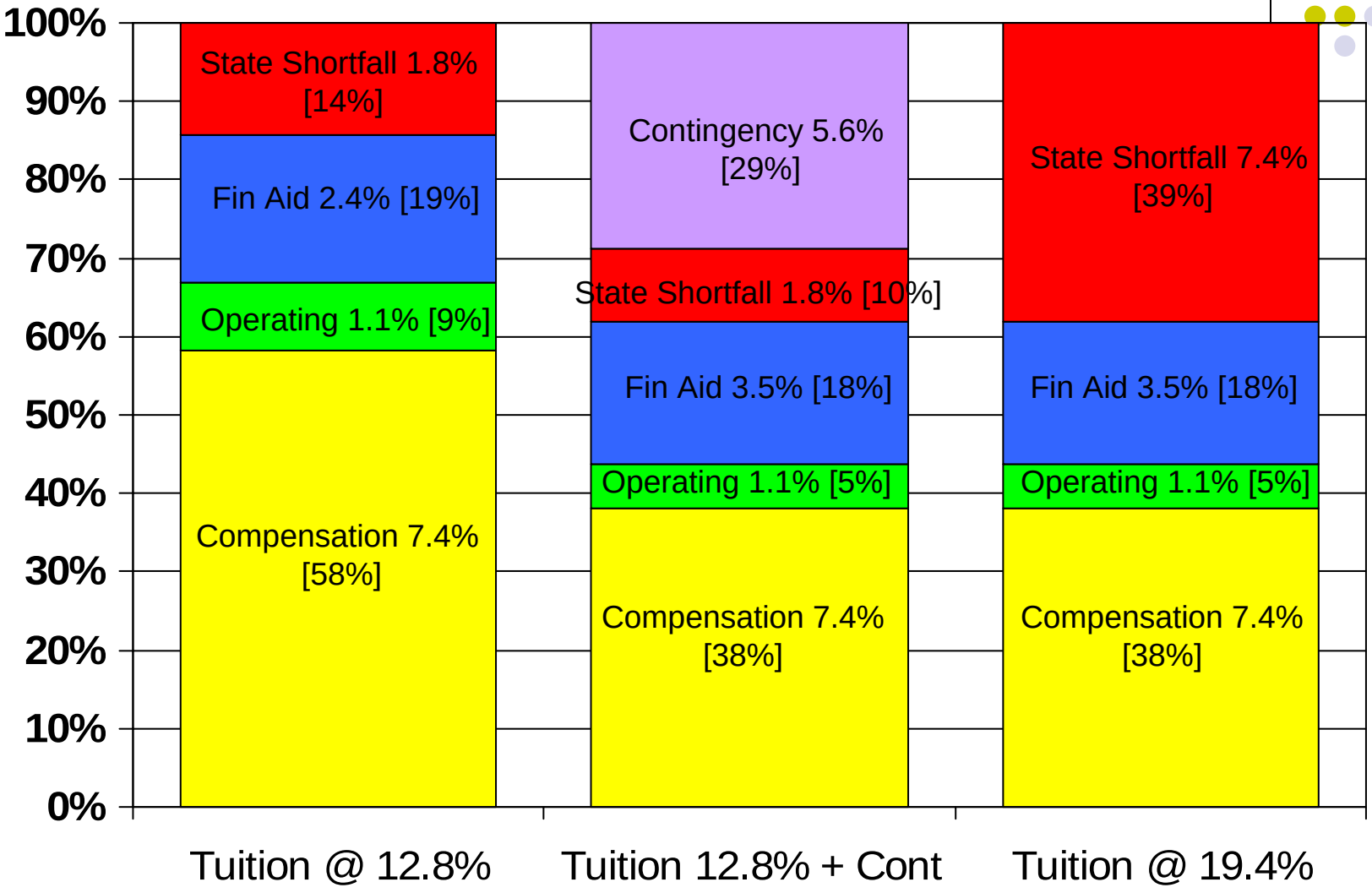
For the reasons expressed above, I do not believe that there is any good budgetary reason for imposing cuts on the Schools and Colleges. Their budgets are already stretched far too thin. I do think that the Schools and Colelges need to engage in a serious examination of their budget priorities. Even with no cuts, the resources of the Schools and Colleges will be reduced in real terms because the budget does not provide funds to cover inflationary costs. If they are to take new initiatives, they need to get the needed funds from internal reallocations. In my view, the Administration is right in forcing the deans of the Schools and Colleges to re-evaluate their spending priorities. The point of this re-evaluation, however, should be to free up money to pursue the strategic goals of the University and not to fund lower-priority activities that have happened to catch the eye of top administrators or to cover losses that the Schools and Colleges had no role in creating.

Slide 1: Flawed Allocation Formula

Base for cuts should be Net or Gross for all units

- Simplified Example. Assumptions:
  - $8 million in ATB budget cuts is needed.
  - The FY 2007 base budgets are:
    - $180 million for the Schools and Colleges
    - $100 million for academic support
    - $50 million for divisions, and
    - $125 million for central accounts
    - TOTAL = $455 million
  - Under the above assumptions, an ATB cut of 1.8 % would be yield $8 million.
- But assume that the divisions and central accounts can exclude $75 million in fixed costs from their base but the Schools and College and academic support cannot excluded their fixed costs.
  - In that event, the base in the formula would be $380 million, and an ATB cut of 2.1% is required to get $8 million. This change adds $540,000 to the cuts imposed on the Schools and Colleges and $300,000 to the cuts to academic support.
- Now assume that 50% of the base of the Schools and Colleges and academic support reflects fixed costs and that fixed costs for all units are eliminated from the base.
  - In that event, the total base is $240 million, and the ATB percentage cut is 3.3%. This change would result in the cuts to the Schools of Colleges going down from $3.78 million to $2.9 million, for a savings of $880,000.

Where Does the Tuition Go?



Tuition @ 12.8%

#1: Assumes State Shortfall of $3.2 M

Tuition 12.8% + Cont

#2: Assumes State Shortfall of $13.2 M

Tuition @ 19.4%

#3: Assumes State Shortfall of $13.2 M

Slide 3

ADMINISTRATION'S PROPOSED BUDGET, FY 2008			
	Amount (millions)	% tuition increase	Status
Expense Increases, 2008			
Compensation	$13.4	9.1%	Permanent
Operating	$2.0	1.4%	Permanent
Year-end spending	$3.7	2.5%	Unclear
SUM Expense Increases	**$19.1**	**13.0%**	
Revenue Reductions, 2008			
Announced State base cut	$3.2	2.2%	Permanent
ICR (net of S/C cut)	$6.3	4.3%	One-time
Enrollment	$2.6	1.8%	Permanent
SUM Definite revenue cuts	**$12.1**	**8.2%**	
Possible State cut #1	$10.0	6.8%	Unclear
Possible State cut #2	$10.0	6.8%	Unclear
Revenue Increases, 2008			
Investment Income	$2.5	1.7%	Permanent
ICR Supplement from SOM	$2.0	1.4%	Unclear
SUM Definite revenue increases	$4.5	3.1%	
State payback of 2007			
Possible #1 ($12.1 tuition)	$10.0	6.8%	One-time
Possible #2 ($12.1 tuition)	$10.0	6.8%	One-time
Budget cuts, 2008			
Net cuts, after reallocation	$7.9	5.4%	Permanent
Assuming no new cuts			
Permanent budget shortfall	$8.8	6.0%	Permanent
One-time shortfall	$10.0	6.8%	
Total shortfall	**$18.8**	**12.8%**	