Final Report

of the

Budget Formula Working Group

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Table of Contents

Executive Summary

The Budget Formula Working Group was appointed in the Fall of 1998 to evaluate the current budget methodology for academic units and to make recommendations for reform. This report sets forth the Working Group's recommendations and describes the work that it did over the past nine months to understand the complexities of budgeting within a major urban research and teaching institution with multiple goals.

Although the charge given to the Working Group indicated that it should focus its efforts on reform of the current formula funding methodology, the Working Group recognized early in the process that this focus must expand somewhat if the goal of meaningful budget reform was to be achieved. Thus, the Working Group has made recommendations dealing with the budget decision process, with budgeting for non-academic units, and with the allocation of funds for summer school and extension programs.

After evaluating the current formula-funding budget methodology and reviewing several alternative approaches, the Budget Formula Working Group recommends that the University adopt a historical budget model that includes a strong dynamic component. Although it has focused its attention on budgeting for academic units, the Working Group believes that its proposed methodology should be applied to non-academic units as well.

Under the proposed new methodology, a base budget would be established for each unit. It would provide funds to finance the unit's day to day operations, including faculty and staff salaries, supplies, office expenses such as telephones, graduate assistants, part-time instructional personnel, and other contractual obligations of the unit. The base budget would not include funds provided to the unit on a non-recurring basis for purposes such as the purchase of equipment, building renovations, or other special expenditures.

The "dynamic" aspect of the proposed budget methodology would require each unit to defend its current budget allocation annually and to petition for new revenues by showing that it was meeting its mission effectively. A program could not just sit back waiting for next year's allocation. Support for new or expanded programs would depend upon the availability of funds from new sources or from funds being reallocated from units that were not performing well. When faced with budget cuts or a lowered state appropriation, the dynamic adjustments might include a reduction in a unit's base budget.

The dynamic adjustments to a unit's budget would be based on quantitative and qualitative factors, such as enrollment changes (student credit hours generated, levels of instruction, cost per credit hours), productivity measures (accreditation, national ranking, degrees awarded, etc.), characteristics of its programs (laboratories, studio based), and key University priorities (strengthening research, global education). Clearly-articulated criteria for making dynamic adjustments would be developed in consultation with each unit. Each unit would be asked to define benchmarks/measures against which their success in achieving their mission can be measured. The Working Group recognizes that success in attaining academic goals often cannot be quantified; thus, qualitative measures of success may be used when appropriate. To make budget allocations based on these quantitative and qualitative measures, the Working Group recommends the establishment of a budget review committee of the type formed to review the fiscal year 2000 budget.

The potential advantages of converting to a historical base budget with discretionary adjustments are considerable. By having a relatively stable base budget, units would be able to plan for the future more securely. Because the units would have an opportunity to obtain enhanced funding by improving their programs and services, they would have a monetary incentive to work efficiently and to review their programs to ensure high quality. Although unit budgets would be subject to annual adjustments, the units would know in advance the factors and criteria that would be used by the decision making body to make those adjustments. They would have the chance to come before the budget review committee and argue their case. Confidence in the budget system should improve because it would be perceived as fair and equitable.

The Working Group recommends that the transition to the new budget model begin in the Fall of this year with the appointment of a transition team. That team would be responsible for the implementation of the new budget system. One of its goals should be to put some aspects of the new budget system in place for fiscal year 2001. In particular, it should endeavor to develop and put into operation for fiscal year 2001 a base budget for each unit. Other aspects of the proposal must be implemented over a longer period. The performance standards for the dynamic portion of the budget would be developed and refined over several years, although a preliminary method for making dynamic adjustments should be put in place for fiscal year 2002. Although the proposed implementation schedule is ambitious, the Working Group believes that prompt action is necessary to establish the credibility of the proposed new methodology.

I. Introduction

The University's General Fund budget is an important management tool, used by the University for allocating limited resources to support its most important goals. The current budget system has evolved from a system introduced in 1983. A major feature of that system, employed by the University in setting the initial budgets each funding cycle for almost all academic units, is a formula-funding methodology. Under that methodology, the amount of money initially allocated to academic units depends heavily on a formula. That formula is based on the number of student credit hours taught by the unit and on the student/faculty ratio (SFR) assigned to that unit by the University.[1] The final budget is adjusted to reflect priorities other than student credit hours. The operation of the SFR formula is described in Section III,A below.

The University's formula-funding methodology has been subject to criticism from faculty and administrators for many years. This criticism has been focused on a variety of perceived flaws, discussed in detail in Section II,A below. After the appointment of Irvin Reid as president in 1997, several changes were made in that methodology to mitigate some of its perceived weaknesses. The most important change was the appointment of a Budget Review Committee to make recommendations on budget allocations, including review of enrollment targets and allocations indicated under the formula-funding methodology.

In the Fall of 1998, President Reid, at the request of the Academic Senate, appointed a Budget Formula Working Group to make recommendations for more fundamental change in the University's budget process. A preliminary report was submitted to President Reid and Provost Williamson on July 1, 1999. The report was also circulated to the President's Cabinet, the Council of Deans and the Policy and Budget Committees of the Academic Senate for their review and comment. Comments received from members of the University community were then considered by the Working Group in issuing this Final Report.

The Working Group recognizes that many members of the Wayne State University community believe that most academic units within the University are currently receiving inadequate funds to achieve their missions. Unfortunately, a reformed budget methodology does not address the problem of systemic under funding. The most it can do is allow the University to make better use of the limited resources it already possesses. Additional resources must come, if at all, from increased private contributions, more state aid, or higher tuition.[2]

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[1]Under the formula, the number of faculty positions funded for a unit equals its AYES/SFR, where AYES is the number of academic year equated students and SFR is the student/faculty ratio assigned to the unit by the administration.

[2]Over the past decade and a half, the University has pursued a policy of stringent restraint on tuition increases, whereas other publicly funded Michigan universities have raised their tuition significantly while providing access to the disadvantaged by giving them compensating scholarship aid. An evaluation of the merits of the University's policy on tuition is obviously outside the scope of this report. The Working Group simply notes that the University's decision to make itself a low-cost alternative for students means that it is under greater budget restraints than competing academic institutions in the region with a higher tuition base. To be attractive

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The Working Group believes that its recommendations are important and worth the attention of the Wayne State University community. Although it does not offer a general cure for all of the University's budget problems, it does offer a workable solution to the particular set of problems that President Reid asked it to address.

Section II of this report provides background on how the Working Group went about the task of formulating its recommendations. Section III describes the formula-funding methodology and two alternative methodologies considered by the Working Group. The Working Group's proposed new budget methodology is set forth in Section IV, along with its other recommendations. In brief, the Working Group recommends that each academic unit be given a base budget, derived from historical experience. In addition, a unit budget would include a dynamic element which might be increased or decreased in accordance with its performance. Credit hours taught by academic units would continue to be an important element in measuring their performance. Several other factors, however, would be given considerable and explicit weight. The Working Group further recommends that a modified version of this methodology be adopted for non-academic units.

Section V discusses the practical steps that must be taken if the University decides to implement the recommendations of the Working Group. In Section VI, the Working Group addresses briefly two topics that are not directly related to reform of the formula-funding methodology but that must be addressed by the University to achieve the full benefits of any proposed budget reform. A conclusion is contained in Section VII.

II. Background

A. Pros and Cons of Formula Funding

The Working Group began its work in October of 1998. The first phase of the project was to assess the relative strengths and weaknesses of the current formula funding methodology. Through a brainstorming process, the group compiled a list of the perceived advantages and disadvantages of that methodology, based upon the experiences of its individual faculty and administrative members. This list was circulated among the deans of the 14 schools and colleges, who were invited to provide their comments and suggestions. Deans from five schools and colleges submitted written comments in addition to input already obtained from the two deans on the Working Group. In general, comments from the deans were in agreement with the Working Group's analysis and supportive of the effort to evaluate and revise the current funding methodology.

Several criticisms of the existing methodology were identified. First, the formula has not been implemented uniformly or consistently over the years. That is, some units that should have received a reduction in funding under the formula were allowed to retain their budgets

[2](...continued)
to prospective students, therefore, the University must manage its limited resources wisely. Budget reform can contribute to the wise use of limited resources.

at their historical levels, whereas other units suffered significant budget cuts in comparable circumstances. This lack of uniformity has led to a widely held belief that the existing formula, as implemented, renders inequitable results.

Second, the student/faculty ratios assigned to the units were thought to be inappropriate in many cases. These ratios are one of the key building blocks in the current methodology. The initial ratios, adopted in 1983, were based on the historical experience of the units in 1975 — a year with unusually high enrollments in most units.[3] The ratios have been modified from time to time, based in part on comparisons with other Michigan public universities. A legitimate concern expressed among the schools and colleges is that the circumstances of units at those peer institutions differ in important ways from comparable units at Wayne State. In addition, only modest adjustments have been made to the ratios for most units, typically on an *ad hoc* basis.

Third, the current methodology does not readily or easily provide an effective mechanism by which the leadership of the University can emphasize new goals or change budgetary priorities. By focusing primarily on enrollment, the methodology gives no signals as to other important priorities. One college noted that the current formula does not incorporate University research goals, although research is an important part of the University's mission.

Fourth, the current formula funding methodology can cause units to suffer a substantial drop in their annual budgets in response to short-term fluctuations in enrollment. These sudden changes can inhibit long-term planning and can affect a unit's ability to meet its critical needs.[4]

Fifth, the current model determines funding for faculty and instructional supplies but does not provide funds explicitly for other general operating expenses of a unit, such as costs for general operating supplies, recruitment, student projects, office furniture, technological equipment and support staff. These expenses are paid for through salary savings, special funds or other more inventive means which vary from unit to unit. In any event, these other elements of the budget have been under-funded.

Sixth, there is widespread agreement that the application of the formula fosters an inappropriate level of competition for students among schools and colleges. One school noted that because units “get no credit” for student credit hours generated by courses offered by other units, they have a strong disincentive toward interdisciplinary activities and cross-listing of courses among colleges. This competition for student credit hours has resulted in a duplication of course offerings and has complicated the design of a General Education program.

The Working Group also explored and discussed some of the advantages of a formula funding model. The primary advantage is that an enrollment-driven formula guarantees that the University will respond quickly to major changes in student demand for particular

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[3]Wayne State University, 1996 Self Study Report (1997), pages 20-21.

[4]During the current fiscal year, the enrollment penalties/supplements were removed, reducing the uncertainty in the fiscal year 1999 budgets for the schools and colleges.

educational programs. All members of the group acknowledge that enrollment is an important factor to be considered in allocating resources within the University.

There is a consensus within the group that any replacement for the current model should give considerable weight to enrollment trends in determining the legitimate claims of units for resources. The group also acknowledges that units may differ in the number of faculty and the instructional supplies that they need to teach a given number of students. Those differences in resource needs are captured, albeit imperfectly, with the student/faculty ratios. Finally, the group favors the feature of the current model that allows units that experience an increase in student enrollments over the projected level to obtain an increase in their budgets for the current year, without the long delays that are typical of some other budget models.

B. Comparisons with Other Institutions

In the second phase of its project, the Working Group examined and compared the funding methodologies at nine peer universities:

- Case Western Reserve,
- University of Pittsburgh,
- University of Connecticut,
- University of Illinois (Chicago, Urbana, Springfield),
- University of California at Los Angeles,
- Temple University,
- State University of New York, Albany,
- University of Southern California, and
- Virginia Commonwealth University.

Getting adequate data to assess the workings of the budget models at these institutions proved to be difficult. For some universities, only barebones information was available. The information obtained suggests that each of the universities operates in its special way in response to its own unique funding environment. The chart that follows identifies the institutions that provided data and the general type of funding methodology used to allocate resources to academic programs at those institutions. The majority of these institutions use some form of an historical funding model. None utilize a formula as the primary method for allocating resources.

Survey of Peer Institutions

Name of University	Budget ($ millions)	Annual State Funding ($ millions)	Funding Methodology (Responsibility Centered, Historical, Formula)
Case Western Reserve Cleveland, Ohio	Total: $389 Academic: $127	None	Responsibility centered.
University of Pittsburgh Pittsburgh, Pennsylvania	Unavailable	Unavailable	Historical — basic budget based on historical expenditure levels.
University of Connecticut Storrs, Connecticut	Total: $334 Academic: $146.4	$210.5	Historical — base budget based on historical expenditure levels. Requests for new funding are on competitive basis. Final decision made by Provost and Chancellor.
University of Illinois Chicago, Springfield and Urbana, Illinois	Total: $2,232 Academic: $446.4	$684	Historical (Chicago) — incremental budgeting approach with annual changes for new program funding. Final decision by Provost and President. Responsibility Centered (Urbana) — tuition directed to unit through which generated.
Temple University Philadelphia, Pennsylvania	Total: $508.9 Academic: $211	$159.1	Historical — budget model identifies existing budget monies non-recurring expenditures plus other factors (Presidential initiatives). Decreases and increases tied to enrollment shifts.
Virginia Commonwealth University Richmond, Virginia	Total: $250 Academic: $148	$150	Historical — each unit receives base budget allocation that is consistent from year to year. Occasionally, a base budget review is performed to validate budget and review performance.

During the third phase of the project, the Working Group identified the desirable features of a reformed funding methodology. In general, the reformed methodology should advance academic excellence and the University's research (retention of Carnegie I status) and urban mission. To advance those objectives, the Working Group concluded that the new funding methodology should have the following features:

- It should recognize and encourage academic excellence.
- It should encourage accountability and quality performance.
- It should be relatively easy to administer.
- It should have legitimacy within the Wayne State community by producing a distribution of resources that generally is felt to be fair and consistent with established norms.

- It should encourage long-term planning, strategic and innovative thinking.
- It should safeguard fiscal stability.
- It should encourage, or at least not discourage, inter-disciplinary activities.

C. Limited Implications of Reform

Although the Working Group is recommending major changes in the current budget system that is applied to academic units, the short-term effects of those changes, if adopted, will be modest. Most of the money currently spent by academic units is needed to satisfy existing contractual obligations and other essential operating costs. The units currently receive the money necessary to pay salaries of faculty and staff, provide supplies and cover costs of day-to-day operations. That money would continue to be made available to units after budget reform. Only the discretionary portion of the budget can be affected by the proposed reforms — perhaps in aggregate less than five percent of the total expenditures of academic units.

For several reasons, the long-term impact of budget reform could be substantial, despite its modest short-term impact on current budget levels. First, as existing fixed obligations terminate over a period of years, the amounts subject to reallocation under the reformed budget process would increase significantly. Second, even small budget adjustments, repeated over many years, can have a major effect, through compounding. For example, if the budget of a unit is increased by three percent for 24 years, its total budget will double.

Third, the signals given by the budget can have important behavioral effects without affecting the size of the budget significantly. For example, the current budget model induces fierce competition among academic units for student credit hours. The overall effect of that competition on the distribution of student credit hours, however, is probably very small, but it encourages parochial thinking in reference to an academic unit's programs. A budget reform that greatly reduces that competition might lead to better, and broader, educational programs for students without changing the budgets of any academic units significantly.

Fourth, a reformed process should increase the perception within the Wayne State University community that budget decisions are being made fairly and rationally. This perception is important in inducing members of that community to work together for common purposes. It is also important in enhancing the moral authority of the University's elected and appointed leaders.

III. Funding Methodologies

Before recommending changes to the current budget procedures, the Working Group reviewed three alternative budgeting approaches: Formula-Funding Methodology, Responsibility-Centered Methodology, and Historical Methodology with Discretionary Adjustments. These three models are described below, with some comment on their potential strengths and weaknesses.

Two of the methodologies addressed in this section — historical and formula funding — provide a procedure for setting an initial annual budget for academic units of the university. In addition, they provide some mechanism for adjusting that initial budget to account for changes in goals, programs, available funding, and other factors. For the historical model, the initial budget is referred to here as the "base budget" of a unit with adjustments made to that base budget referred to as the "dynamic component" of the budget. Under the responsibility-centered methodology, the budget of the unit is simply the amount that the unit has procured for itself in the marketplace.

At Wayne State University (WSU), all three of the methodologies are used to some degree in setting the budgets of some units within the University. The budgets for most academic units are established using a formula-funding methodology. Those initial budgets set by formula may be adjusted in an *ad hoc* manner to meet University priorities and to take account of available funding. A historical budget methodology is used for all administrative units, for the College of Urban, Labor, and Metropolitan Affairs (except for the Department of Geography and Urban Planning), and for the majority of centers and institutes. A variation of the responsibility-centered methodology is used in a small number of centers and institutes. An example would be the Developmental Disabilities Institute, which is required to obtain all of its revenue from entrepreneurial activities, without support from the general fund.

A. Formula Funding

The formula-funding methodology is intended to develop a budget based on certain selected, predetermined parameters. Examples of such parameters are student enrollment and degree production. For formula funding to operate, the parameters used in the formula must be quantified.

The simplest example of a formula-funding methodology would be a budget driven purely by enrollment. In such a model, a unit's budget would equal some measure of student enrollment multiplied by some pre-established constant. For example, a unit's budget might equal the number of student credit hours it generated multiplied by $50. This simple formula approach lacks flexibility. In its survey of peer institutions and its reading of the relevant literature, the Working Group did not encounter any institution that uses a pure formula-funding model of this type.

The methodology used at WSU in setting the budget of academic units cannot be described as a pure formula-funding model. The formula establishes a starting point which is then adjusted in many ways. Of all of the universities surveyed by the Working Group, however, it comes closest to a formula-funding model.

In simplified form, the WSU formula applicable to academic units determines the budget of a unit by reference to two key variables: (1) the number of "academic year equated students" (AYES) enrolled in the unit, and (2) the student/faculty ratio (SFR) that has been set for that unit. By dividing the number of AYES by the SFR, the WSU formula determines the number of authorized faculty positions for the unit.

Assume, for example, that the Provost's office, after discussions with the Budget Director and the Dean of College A, has estimated that College A will have 450 AYES for the coming year. Assume also that the SFR for College A is 15. Under these circumstances, the number of approved faculty positions (referred to as "faculty lines" in the budget) will be 30, computed as follows:

$$\textit{Number of faculty lines} = AYES/SFR = 450/15 = 30$$

If College A has hired exactly 30 full-time faculty members, then the amount provided in the budget of College A for approved faculty would be the sum of the contractual compensation provided to each faculty member for the year. If each faculty member is paid $60,000 per year, then the component of College A's budget for faculty salaries would be $1,800,000 ($60,000 × 30).

The actual operation of the WSU model is significantly more complex. To add one additional level of complexity, assume in the above example that College A has filled only 28 of the 30 authorized faculty positions. In that event, each of the unfilled faculty lines is funded at a "nominal" salary rate. That nominal rate is the pre-established minimum salary for members of that unit. Assume, for example, that the nominal rate for College A is $40,000. Under these circumstances, the budget component for faculty salaries for College A would be $1,760,000, determined as follows:

$$\textit{Faculty Salary Component of Budget} = 28 \times \$60{,}000 + 2 \times \$40{,}000 = \$1{,}760{,}000$$

If a unit's student enrollment is declining, the unit might have filled more faculty positions than it is authorized to fill under the SFR formula. In such circumstances, the unit would receive sufficient funding to pay its contractual obligations, notwithstanding the formula. In a future year, however, the unit might not be allowed to fill faculty positions.

The historical approach is applied in funding for non-academic staff and academic service officers. A residual "supplies" budget may be provided, but most supplies, including instructional supplies and operating expenses, are funded by formula, using a factor times the number of authorized faculty positions. Shortages in these categories are made up from unexpended salaries or other sources.

The administration has used two techniques for adjusting the budget established under the rules summarized above. One technique is to grant a unit one or more "enhancement" faculty positions. Enhancement positions allow units to hire more faculty members than are authorized under the formula.[5] Another technique is to fund new programs without reference to the formula. These techniques allow the administration to promote University goals and to mitigate inappropriate results under the formula.

[5]No enhancement positions have been awarded from central funds during the past two years.

B. Responsibility-Centered Funding

Responsibility-centered funding, also called revenue source funding, is used primarily at private institutions. Of the peer institutions surveyed by the Working Group, the only one using this budget methodology was Case Western Reserve University. Under this methodology, each academic unit is responsible for keeping track of its own revenue from tuition, research grants and contracts, indirect cost recovery amounts, endowments, and gifts. The unit is also charged with covering virtually all of its costs, including salaries, financial aid, building maintenance, utilities, and so on. In effect, each unit is treated as an independent entity that floats or sinks on its own bottom. It is given nearly complete autonomy in the management of its revenues. Those revenues can be reallocated at the discretion of the unit to meet changing conditions or to pursue new initiatives.

Although the responsibility-centered funding methodology provides for very substantial decentralization of budget decisions, it does include some centralized functions. Each unit typically pays a fee or tax to the central university to help finance certain common services, such as libraries, student services, campus police and central administration. These fees may be based on enrollment, faculty size, square footage, etc., depending on the nature of the service. In effect, these fees are a user charge for common services.

Proponents of responsibility-centered funding claim that it rewards units that attract students and manage their resources efficiently. Conversely, it punishes units that fail the test of the marketplace. The result, according to proponents of this methodology, is that the resources of the university flow to the units that can utilize them most effectively.

Opponents of this methodology claim that it discourages cooperative relationships within the university, making it difficult for the units of the university to focus on a common mission. They also suggest that it forces units to emphasize income-generating programs at the expense of important university goals. Further, they complain that units are pressured to make curricular decisions without proper reference to educational policy. In their view, educational policy tends to degenerate into a set of negotiations between the various campus interest groups, with the outcomes dependent on the political strength of those groups.

A public university that attempted to apply the responsibility-centered funding methodology would need to develop some mechanism for allocating state funds among the units of the university. If most of the resources of the university are derived from state appropriations, that allocation mechanism would become the key feature of the budget model. At Wayne State, nearly two-thirds of general fund revenue comes from state appropriations.

Adoption of the responsibility-centered funding methodology at Wayne State would constitute a major break with past practice. To implement that methodology, the university would need to charge units for the various services it now provides, or it would need to decentralize the delivery of those services. Any approach would involve major costs and dislocations. It would be necessary, for example, to upgrade substantially the administrative capacity of the units.

The Working Group is unanimous in recommending that the responsibility-centered funding methodology not be introduced to Wayne State University, given the University's current circumstances and its historical mission as a public university in an urban environment.

C. Historical Model with Discretionary Adjustments

Many public and private universities and colleges, including most of the peer institutions surveyed by the Working Group, use the budgeting method referred to here as the historical model with discretionary adjustments. For institutions using this methodology, the standard practice is to establish a base budget for each unit of the university. Often the base budget is the unit's budget for the previous fiscal year, reduced by any special support provided in the previous year on a non-recurring basis. In some cases, the budget for the previous year is adjusted for inflation.

After setting the base budget, a university typically adjusts the budget to accommodate program changes, new goals, new facilities, expanded operations, or other developments. At least in principle, the adjustments may be up or down. Almost all of the universities surveyed by the Working Group made *ad hoc* adjustments to the budget to address changing needs and conditions. Several of those universities are contemplating reforms to improve their mechanisms for making annual adjustments.

The reliance on past practice to set current base budgets is sensible, simple, and straightforward. The basic premise of that methodology is that the informed budget judgments of the past remain relevant for the present. Proponents of this methodology contend that it allows academic units to rely on a stable revenue source, without fear of the major dislocations that would undermine their ability to serve their educational missions.

Opponents of the historical approach contend that it tends to introduce undesirable rigidity into the budget process. They believe that units come to believe that they have an entitlement to the budget levels they have enjoyed in the past without regard to their current performance levels. This sense of entitlement makes it difficult for the university to adjust annual budgets to serve current priorities.

Several of the universities surveyed by the Working Group have recognized the potential advantages of adding a strong dynamic element to the historical approach to counter the risk of rigidity. In principle, the dynamic element of the budget would provide rewards for good performance and penalties for substandard performance. The difficulty lies in developing appropriate measures of performance for each unit. At one extreme, a university might develop objective and measurable criteria for judging performance. This approach is subject to easy criticism, however, because many of the intended outputs of academic units cannot be reduced to a number in any reliable fashion.

At the other extreme, adjustments in unit budgets might be made purely on an *ad hoc* basis. The university president or some council of advisors might review unit budgets annually and make adjustments based on some general impressions of the performance of the units.

The obvious weakness of this approach is that it offers the units little guidance on how it should perform to achieve budget rewards.

The middle course, favored by the Working Group, is to make annual adjustments in unit budgets based on clearly articulated criteria that have been developed in consultation with the units. Some criteria, such as level of student enrollment, can be quantified easily. Other criteria, such as research excellence, cannot. In these circumstances, some human agency, such as a budget review committee, is needed to assess the overall performance of each unit and make funding recommendations.

IV. Recommendation for New Funding Methodology

The Budget Formula Working Group has reviewed the three broad approaches described above and recommends that the University adopt budget procedures that are a modification of the historical with discretionary adjustments model for all academic units. The WSU version of the model will have a formalized dynamic element with predetermined parameters.

The rationale for this model is sound, and the method is easily understood. It provides for reasonable stability so that no unit would suffer unexpected change in its base budget, but it has a built-in process for budget adjustments to meet the University's priorities. The model is data driven; yet it recognizes that qualitative factors come into play in budget decisions by allowing revisions to be made by senior university officials in consultation with various faculty and administrative bodies on campus.

A. Development of a Base Budget

Establishment of a base budget for each academic unit is the first step in implementing the proposed reform. The starting point in developing that base budget should be the expenditures made for the preceding fiscal year to provide for the day-to-day operation of the unit. The categories of expenditures for the base budget should include:

- Faculty and staff salaries
- Supplies
- Office operations, i.e. telephones
- Graduate assistants
- Part-time instructional personnel
- Contractual salaries (salary *increases* are budgeted centrally)
- Inflation adjustment

The base budget would not include funds provided to the unit on a non-recurring basis for purposes such as purchase of equipment, building renovations or other special expenditures.

B. Dynamic Adjustment

Dynamic adjustments to the budget must be made to achieve the goals of the University in the most effective manner. Adjustments will include support for new or expanded programs. The amount of the adjustments will depend upon the availability of new funds or the amount of funds redirected from previously allocated uses. In difficult times, these adjustments may include budget reductions. To insure equity, each unit must be prepared to defend all budget allocations, including those required for maintaining current programs, for expansion of these programs, and for development of new programs.

The *dynamic* portion of the budget process provides for allocation or reallocation of funds based on clearly specified criteria for each unit. The adjustments will be based on both quantitative and qualitative factors such as:

1. *Enrollment considerations*
   - Student credit hours generated both on- and off-campus
   - Levels of instruction (lower, upper, master, doctoral)
   - Cost per credit hour in the unit

2. *Productivity measures*
   - Accreditation
   - National ranking
   - Degrees awarded
   - External research funding
   - Scholarly productivity
   - Faculty and student awards
   - Development efforts
   - Effectiveness of service and advising

3. *Characteristics of programs*
   - Laboratories
   - Studio-based courses
   - Special facilities for instructional media
   - Distance and internet-based courses

C. Budget Review Committee

The establishment of a university budget committee is a key requirement for the effective operation of the proposed new budget methodology. One of the committee's functions would be to review the performance of units relative to the pre-determined parameters. Another function would be to evaluate competing proposals and decide which proposals should be funded. To be sure, the ultimate funding decisions for the University are made by the Board of Governors upon the recommendation of the president. It is critical, however, that recommendations made to the chief executive officer on budget allocations reflect the good thinking and informed judgement of a representative group of individuals with an interest and stake in the successful outcome of the budgeting process.

The Working Group recommends that the president establish a committee with sufficiently broad representation to be perceived as fair and equitable by the Wayne State community. The committee charged with making recommendations to the president under the new methodology should, at a minimum, include the following members, all of whom serve on the Budget Review Committee formed to consider the fiscal year 2000 budget:

- Provost and Sr. Vice President for Academic Affairs
- Sr. Vice President for Finance and Administration
- Chief of Staff
- Vice President for Computing and Information Technology
- Deputy Provost
- Director of the Office of University Budget
- President of the Academic Senate, or designee
- Representative of the Council of Deans
- President of the Student Council, or designee

The chairperson of the committee should be chosen by the President. The representative of the Council of Deans should be selected by the Provost in consultation with the Council.

The informational needs of the Budget Review Committee must be carefully considered as the dynamic portion of the proposed new methodology is developed. To a large extent, the dynamic component of the recommended funding methodology will depend upon accurate, detailed information about enrollment, productivity and other characteristics of a program. To that end, the committee must have the ability and authority to obtain from the units data needed to make reasoned budgetary decisions. It must possess the authority to invite representatives of the various units or programs to attend committee meetings to explain or elaborate upon a particular funding request. In addition, it will be important for the Budget Review Committee to keep key university constituents informed as the budget is developed.

In summary, the Working Group recommends that budget allocation decisions be made by a body that (i) represents the student body, the faculty and the administration; (ii) employs in the decision-making process clearly articulated criteria that reflect the University goals and are known to the University community; and (iii) has the ability to obtain accurate and reliable information and data.

D. Extension of Proposed Budget Methodology to Non-Academic Units

The budget model that the Working Group has proposed for academic units in the University should be extended with all deliberate speed to the non-academic units. At present, the non-academic units employ a historical base budget methodology without any formal dynamic component. It is important for sound budgeting within the University, however, that all units have their budgets adjusted, upward or downward, in response to the quality of their performance.

Extending the proposed budget methodology to the non-academic units is no trivial task. Performance objectives must be established, and quantitative and qualitative benchmarks must be set for measuring performance. The Working Group recommends the appointment, in the Fall of 1999, of a committee charged with the responsibility for developing a concrete plan for introducing a dynamic element into the budgets of non-academic units.

E. Operation of New Budget Methodology

To initiate the proposed budgeting process, each unit will be asked to propose appropriate measures of its performance and productivity. These criteria should be tailored to the individual mission of each unit in consultation with the provost. As noted above, a unit would review these criteria with the Budget Review Committee, and agreement on the criteria would be reached. Development of the appropriate criteria for each unit, both academic and nonacademic, will require some time and careful thought. Further, these criteria will require regular review, with adjustments made, if necessary, to reflect the changing role of the unit.

The Budget Review Committee will assess the performance of each unit against the agreed-upon individual productivity and performance measures for that unit. Then, based on available funds and University priorities, the committee will recommend adjustments to unit budgets. Final budget review and approval will rest with the president and the Board of Governors.

V. Implementation

Moving the University to a new funding methodology will take time and substantial effort over the next several years. The Working Group recognizes that its desire to bring about immediate reform must be tempered with realism. Some time is needed to create a sound, reliable system in which the entire University community will have confidence. In order to balance the need to maintain the momentum for positive change with the legitimate goal of a well-planned transition, the Working Group recommends that proposals for reform be implemented over a period of three years beginning with fiscal year 2000 and continuing through fiscal year 2002. The proposed steps and a tentative time line are outlined in the following tables:

Fiscal Year 2000

- Assign responsibility for management and oversight of transition
- Develop timetable for implementation

- Identify base budget for each unit and division
- Determine interim methodology to allocate funding for dynamic portion
- Identify initial performance standards within context of strategic direction for university and division
- Establish guidelines for revising base budget

Fiscal Year 2001

- Utilize base budget as foundation for unit funding
- Use interim methodology for the “dynamic” portion of the budget allocation
- Identify system for collection of information
- Collect peer information and benchmarking data
- Refine performance standards and “dynamic” criteria
- Develop process for monitoring and review of budget performance

Fiscal Year 2002

- Begin second year of base budget
- Begin implementation of refined performance criteria
- Continue to refine “dynamic” performance criteria

The first step to be taken is the appointment of a transition team in Fall 1999. This team, to be appointed by the president, should be comprised of a small number of administrative leaders with responsibility for the budget and should include representation from the Budget Review Committee and the Provost's Office. This team would develop a realistic timetable for implementation of the new methodology during the fiscal year 2000 time period and should develop the specific steps needed to move to the new methodology starting with fiscal year 2001. These steps should include an examination of the problems associated with the transition to the new budget methodology and the development of procedures for the establishment of the initial base budget for fiscal year 2001. The team will also identify the initial performance standards for each of the academic units in consultation with the schools and colleges within the context of the University and division goals. It should then develop an interim methodology for allocating funds for the dynamic portion of the budget which will be used for the fiscal year 2001 budget.

During fiscal year 2001, methods for establishing the base budget will be reviewed and refined. The performance standards for each of the schools and colleges will be reviewed and refined through consultation with each of the units. Systems will be developed for the collection of pertinent data. In addition, the budget review committee, in consultation with the units, will begin the collection of peer information and the establishment of appropriate benchmarks. These data will be used to refine the performance standards and criteria necessary for the development of the dynamic portion of the budget. Finally, a process for monitoring and review of the budget against the performance standards and benchmarks will be developed. These refined procedures will be used to establish the fiscal year 2002 budget.

During fiscal year 2002, refinements of each of the above steps will be undertaken to ensure that the new methodology is responsive to the University's goals and mission. Further, it is envisioned that this review process will continue in the future so that the budget methodology can be adjusted to meet the changing University needs and goals.

VI. Other Issues

The Working Group did not undertake a comprehensive review of all of the features of the current budget model. Our focus has been on the major design features of the current budget model, with emphasis on the perceived problems of formula funding. Many important issues, such as the methods for funding research within the University, were considered to be outside the scope of our work. Two issues, funding for the extension program and funding for the summer session, were of such importance, however, that some discussion of them seemed essential. Our view, reinforced through discussions with faculty and administrators throughout the University, is that these topics need to be addressed to bring consistency to the way the budgets of academic units are set.

Section VI,A addresses budget issues relating to the extension program. The issues relating to summer school funding are addressed in Section VI,B. The Working Group recognizes the perceived problems associated with the methodologies used for funding these two activities and recommends that a separate committee be appointed to review them. The charge to this committee would be to formulate a practical plan for giving academic units the power and incentive to integrate the summer and extension programs with their academic year instructional programs.

A. Extension Enrollment Funding

A majority of the schools and colleges offer courses through the extension centers listed below and at other off-campus sites:

- Harper Woods
- Northeast Center
- Northwest Center
- Oakland Center
- Lamphere (High School) Center
- Macomb University Center

A major problem associated with the extension program is that the distinction between courses offered through extension and those offered directly by departments has become blurred by the funding methodology used. The AYES generated by courses taught off campus by full-time faculty within load accrue to the instructor's home department. Part-time faculty or full-time faculty teaching above load are funded through the College of Lifelong Learning (CLL) budget. The AYES generated by the courses they teach accrue to CLL. Thus, the funding for a given course is determined by the job status of the instructor, not by the geographic location of the classroom where the course is taught.

Additional problems arise from the rapidly-increasing use of interactive video and web-based instruction to deliver on-campus programs at off-campus sites. Furthermore, expansion in continuing education programs to meet professional development, licensing, or certification requirements may account for a substantial portion of the courses offered by a college both on- and off-campus.

The extension programs and centers are operated by CLL, and the funding for them is dependent on the number of AYES generated by CLL. As more full-time faculty teach courses at extension facilities within load, the funding for CLL decreases, despite an increase in the *overall* credit-hour production at these centers. This results in a shift in funding from CLL to the individual academic units. Because CLL bears the expenses for support of the infrastructure and operation of the extension facilities, it has difficulty providing that support at an appropriate level.

B. Summer School Funding

The University's spring/summer semester is a self-supporting activity that is operated by CLL. The total revenue generated by the program is approximately $12$13 million per year. Of this amount, $9-$10 million goes to the general fund. Then revenue is used to cover part-time faculty salaries and administrative costs for operation of the summer school. Finally, any remaining revenues are distributed as follows:

- 60% to the academic units that generated spring/summer enrollment to the extent that their revenue to cost ratio exceeds their specific target,

- 30% to the Research Stimulation Fund, and
- 10% to the President's Office for university enhancement.

In order to meet the needs of the program and the University, a standard was set that required the overall program to operate at a revenue to cost ratio of $2.40 in tuition for every $1.00 of instructional costs. This has been modified, for some colleges which have high instructional costs, to a three-tier structure with ratios of $2.40:$1.00, $2.25:$1.00, and $1.85:$1.00. At a minimum, each unit must generate enough revenue to cover its own costs. To achieve the required ratio, colleges often use part-time faculty or graduate students instead of regular faculty to teach during the spring/summer program. They may also limit upper division course offerings and eliminate graduate courses to increase the ratio of revenue to cost.

For many academic units, courses taught during the summer or taught at an extension center should form an integral part of the program of instruction offered to their students. Yet the current budget system discourages academic units from achieving this goal and even discourages some units from participation in these programs.

VII. Conclusion

In recommending the replacement of formula funding, the Working Group has attempted to avoid the major problems arising under the old system while achieving its desirable effects though other means. Its recommendation for a genuine base budget for all academic units, if adopted, should provide a beneficial level of budget stability for all academic units. At the same time, the proposed dynamic component to the budget model is intended to make budget allocations sensitive to a wide variety of valid performance criteria. The recommended extension of the dynamic component to non-academic units should bring a higher degree of accountability to those units.

Although adjustments up and down under the dynamic component of the proposed budget methodology will be based on clearly articulated criteria, they will not be based on the automatic application of a formula. Budget formulas give precise answers to what are often the wrong questions. Sensible budgeting, in the view of the Working Group, requires intelligent people making informed judgments based on the best available information.

Central to the Working Group's recommendation is its endorsement, in broad outline, of the recently instituted Budget Review Committee. The Working Group is unanimous in its recommendation that University budget decisions should be made by a body that includes representatives of key interests within the University and that operates in an open and objective fashion. In its view, the legitimacy and perceived fairness of budget decisions depend on the type of open and collaborative process that President Reid has endorsed with his appointment of the Budget Review Committee.