

# ***UVM Budget Self-Study***

*December 14, 2012*

## **Institutional Context**

In his first few months on campus, President Tom Sullivan asked the Provost and the Vice President for Finance and Administration to undertake a self-study of the University's budget process and model. This self-study is now completed and contained herein. The President plans to convene a panel in early 2013, with representatives drawn from across the campus, to consider the information presented here and to provide comments and recommendations regarding the content. This self-study will also be available for public comment. After the panel's work is complete, the President will then form an external review panel, drawing experts from other higher education institutions. The external panel will review the self-study and the comments of the campus panel and then provide its input in a form to be determined by the President. All of this work will inform future decisions regarding the University's budget process, model and implementation. Both panels will be asked to use the "Areas of Presidential Focus", "Decision-Making Criteria" and "Budget Operating Principles" below as guides to their analyses.

### **Areas of Presidential Focus**

- Affordability and Financial Access to Higher Education
- Quality Enhancement
- Strategic Alignment of Budgets with Priorities
- Revenue Enhancement through expanded academic offerings and the Comprehensive Campaign
- Cost Effectiveness and Efficiency across the University

### **Decision-Making Criteria**

- Advances quality and excellence
- Reflects centrality to mission, vision and focus
- Fosters comparative advantage and multiple strengths
- Effects a positive and transformative "impact"
- Increases academic synergy and interdisciplinarity
- Satisfies cost, benefit, risk assessment and "unintended consequence" analysis, including projected supply and demand
- Promotes distinctiveness/uniqueness of the University
- Builds competencies and capacity
- Leverages multiple initiatives and resolves multiple issues
- Builds community and develops talent among faculty, staff, and students

### **Budget Operating Principles**

- Align resources and revenues with University strategic priorities
- Ensure long-term structural balance
- Promote transparency
- Advance clarity
- Achieve predictability
- Enhance flexibility
- Provide incentives to increase academic quality, enhance revenues, and promote productive creativity and efficiencies
- Provide ease of administration during times when revenues are growing and when they are shrinking

### **The University's Vision, Mission and Goals**

#### *Vision:*

To be among the nation's premier small research universities, preeminent in our comprehensive commitment to liberal education, environment, health, and public [leadership and] service.

#### *Mission:*

To create, evaluate, share, and apply knowledge and to prepare students to be accountable leaders who will bring to their work dedication to the global community, a grasp of complexity, effective problem-solving and communication skills, and an enduring commitment to learning and ethical conduct.

#### *Goals:*

**Diversity:** Build a diverse and globally aware university community sustained by an inclusive, supportive, and just campus climate.

**Academic Programs:** Increase the quality and stature of academic programs and align undergraduate and graduate education with institutional priorities.

**Scholarship:** Focus and strengthen research, scholarship, and the creative arts, and develop outstanding graduate programs that support the creation and sharing of knowledge.

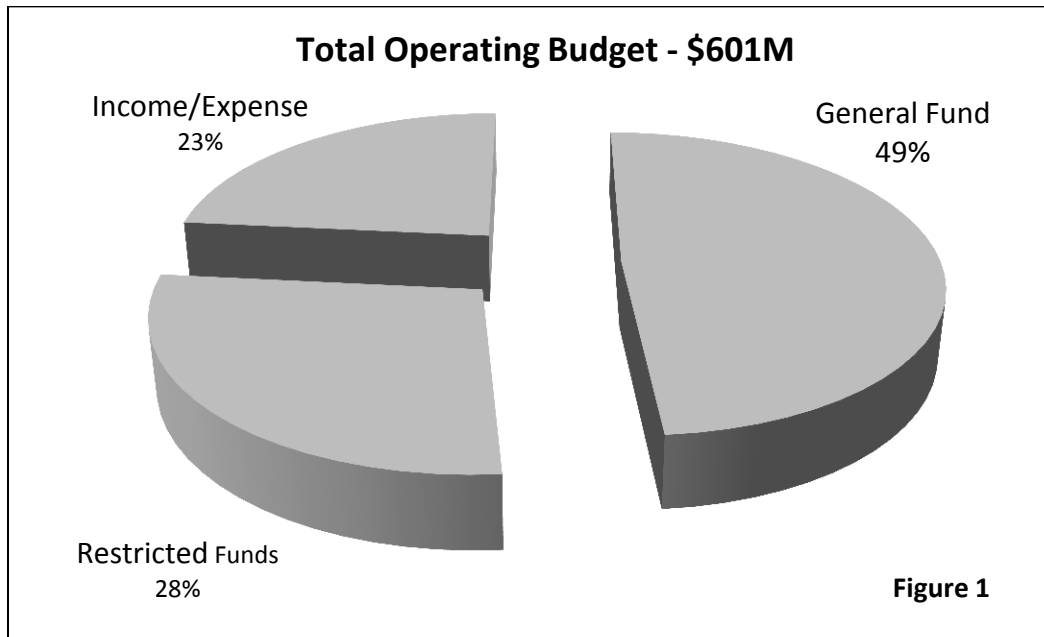
**Student Experience:** Provide a distinctive university experience that prepares students for success as accountable leaders in the 21st century.

**Institutional Efficacy:** As an institution, model the highest standard of ethical conduct, accountability and best practice, public service, and strong commitment to lifelong learning.

## Planning and Resource Allocation

### *Budget Description*

The University's total operating budget for FY 2012 was \$601 million, of which \$293 million was in the "general fund". General fund revenues are those that are not restricted for a particular purpose and it funds the day-to-day operating expenses of the University. As illustrated in Figure 1, the other half of the operating budget is split between restricted funds and income and expense accounts.

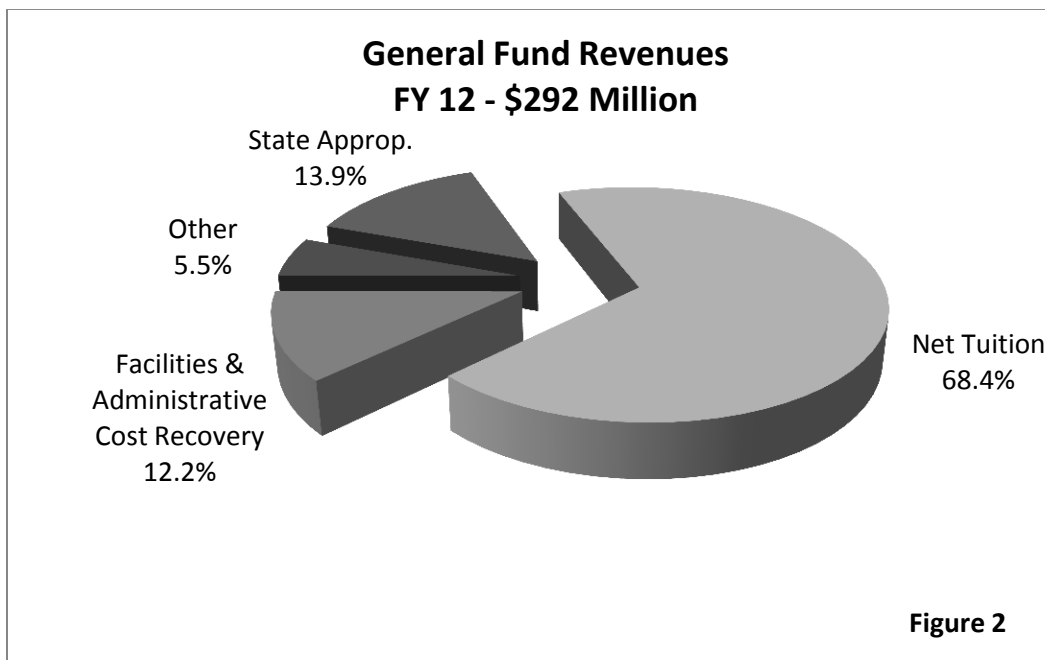


Restricted funds are comprised primarily of research grants and contracts that may only be spent for a designated purpose. When the funding for a particular grant or contract has been expended, no additional expenses are incurred. The University has nearly 200 income/expense accounts, the budgets of which total about \$138 million per year. The vast majority of these accounts are quite small but there are also some larger ones such as the \$52 million Residence Hall budget, the \$25 million Continuing Education Budget, and that of the University Store, which exceeds \$12 million. Income and Expense activities operate as individual enterprise activities that are obligated to balance their budgets. When this is not the case, they have to either generate additional revenue or reduce expenses in response to the need.

It should be noted that debt service is a component of the total operating budget within both the general fund and some of the income/expense accounts. The University's current long-term debt (all fixed rate) totals \$472 million. The current University Debt Policy calls for the debt ratio ceiling to be reduced from 6% to 5% by FY 2017. The current ratio is 5.05% so, with the modest projected increases in the operating budget (ratio denominator), there will not be room for additional debt for many years if the ratio is reduced to 5% as planned.

The University's general fund budget represents that portion of the total budget that most people think of as "the UVM budget". As illustrated in Figure 2, more than two-thirds of general fund revenue (\$206 million) flows from net tuition (total tuition minus financial aid grants). The majority of the other general fund revenue comes from the state appropriation and indirect cost

recovery from research grants and contracts. Unlike many of our peer institutions, only a little more than \$3 million (1%) of general fund revenue comes from unrestricted endowment proceeds. The other \$10 million in endowment spending is targeted to restricted purposes stipulated by donors. This, combined with the fact that the University's \$41.7 million base appropriation from the state is the lowest in the nation on a per capita basis, creates a very heavy reliance on net student tuition. Although the State of Vermont has rejected the national trend of decreasing University base appropriations in recent years, the fact that it has been flat for four years means that this revenue source represents an ever decreasing proportion of general fund revenue. The University allocates 25% of its state appropriation to the College of Medicine and another 25% to Extension and the College of Agriculture and Life Sciences, with the remaining 50% (\$20 million) used to fund scholarships and financial aid for Vermont students. Although research cost recovery rose modestly for two years as a result of federal stimulus funding it is now declining even in nominal dollars, thereby making the University more and more reliant on net tuition.



Although all net tuition revenue is important, the fact that undergraduate net tuition represents over 86% of total net tuition, and financial aid for this group is over \$85 million, it gets the most attention during budget deliberations. Graduate net tuition represents only 5% of the total general revenue both because of the relatively small number of graduate students and the fact that, on average, tuition remission and stipends for this group result in a much lower net tuition per capita.

Figure 3 illustrates the major expenditure categories of the general fund budget by function. Some people have expressed concerns that too large a portion of the UVM general fund is dedicated to “non-academic” functions. The chart below illustrates that 24.2% of the general fund budget is directed to Institutional Support. Examples of functions in these areas, which provide support across the campus, include finance, human resources, campus planning, information technology, executive staff, custodial services and support for the UVM Foundation. Although not for purposes of direct instruction, a portion of these expenditures also support instruction and research in that the debt service, utility, repair and maintenance costs of academic buildings are included herein. These costs are not directly allocated to the individual units as they are at many institutions.

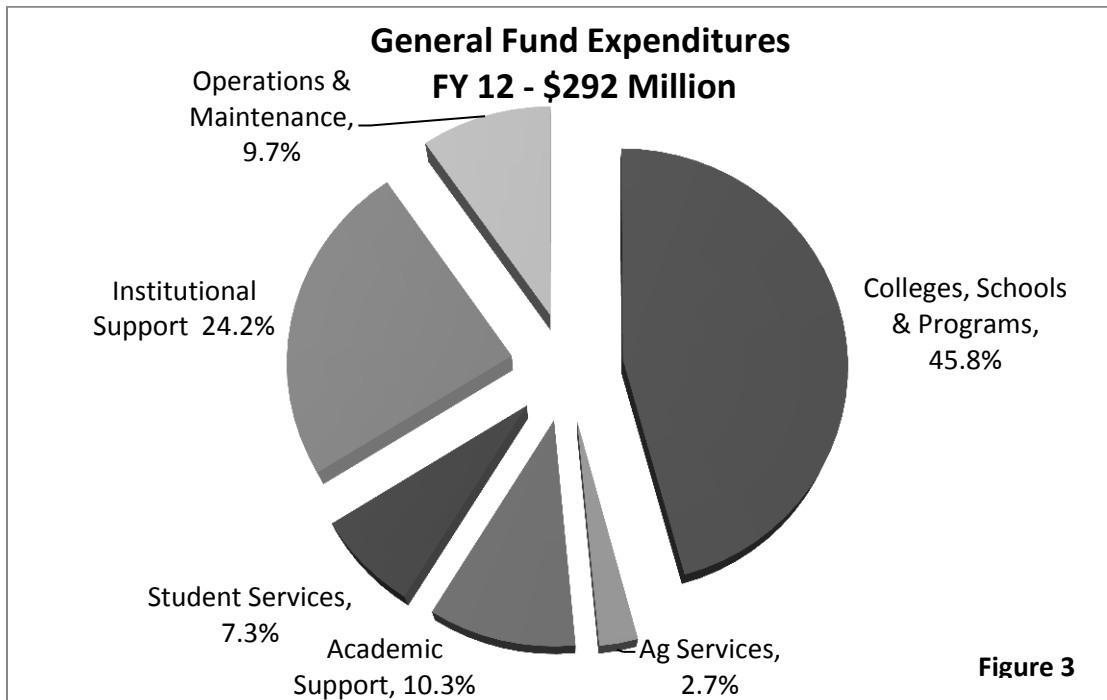
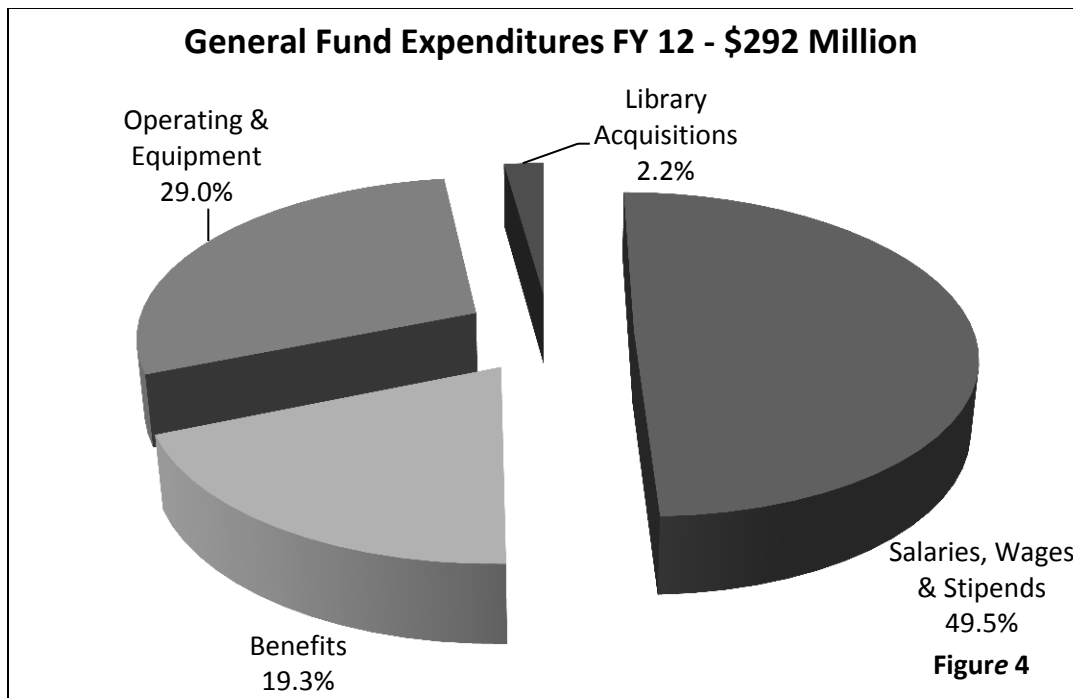


Figure 4 provides an alternative view of general fund expenditures by illustrating the major “object” categories. As is the case with all like organizations, the cost of salaries and benefits (68.8%) consumes the largest portion of the budget. Education generally, and higher education specifically, has not experienced the significant cost reductions and efficiency gains from technology innovations that have brought down the relative cost of many products produced by the private sector. This causes many to question why higher education has, in recent decades, risen in cost much faster than the Consumer Price Index, which is considered by many to be the inflation benchmark to which such costs generally should be held. It should be noted that, in any institution, quality improvements are investments that must be funded either by increasing revenues, becoming more efficient, reallocating resources, simply cutting other expenditures, or some combination thereof.



*Budget Process*

The University’s current general fund budgeting process can best be described as *incremental* and *centralized*. Although there is ongoing review of the elements of the University’s budget in a constant quest for efficiency and effectiveness improvements, the term “incremental” applies well to the UVM budget process. As a result of the Strategic Initiatives Project, there will be enhanced focus in the coming years on assessing the value of academic and administrative programs, but it is unlikely that even these efforts will result in an annual zero-based budgeting process where all the activities funded by the general fund budget are up for reconsideration every year.

The University’s budget is *centralized* in that the most significant budgetary decisions are made by the President and the Provost, subject to approval by the Board of Trustees. These decisions are supported by extensive analysis and input from a wide range of representative organizations (e.g. Faculty Senate, Staff Council, Student Government Association, and Graduate Student Senate) across the campus but final decisions about unit budgets take place centrally. The budget of the University is a continual focus of the Budget Director and his Financial Analysis and Budget (FAB) team, as well as of the Vice President for Finance and Administration (VPFA). FAB constantly monitors the status of the budget for the current year to make sure that it stays in balance and brings to the attention of the VPFA any issues that require his intervention to resolve. The Budget Director and the VPFA are also continually engaged in discussions about the budget for the coming year(s), supported by budget estimates provided by FAB. The Budget Director brings all budget policy issues to the University’s Budget Group, which is chaired by the Provost who is the Chief Budget Officer. This group meets weekly and has included the Vice President for Executive Operations, the Assistant Provost, the VPFA and members of the FAB staff.

One key step in the budget development process is revenue estimation, which is generally more difficult to accurately accomplish than expenditure estimation. The Budget Director and the VPFA work with the Vice President of Enrollment Management and his team to ascertain what level of net undergraduate tuition can be anticipated. The Budget Director and his team then gather information about other revenue categories and produce estimates of how much can be anticipated from these sources as well. The combined revenue estimate is then brought to the Budget Group and contrasted with anticipated increases in expenditures. These increases are comprised of expected inflation in the “base budget” (the cost of doing next year what we did this year) and new initiatives. After extensive consultation with the Budget Group the Provost and the VPFA meet with the President to inform him of the budget parameters and solicit his input.

The Provost and the VPFA then send a memo to all of the deans and vice presidents advising them of the proposed general budget parameters and asking that they submit within a month information about perceived budget challenges, opportunities for efficiency improvements and a plan for the use of any available reappropriations (carry over from prior years) funds. In years when the Budget Group recommends to the President that an across the board budget reduction is necessary, the memo also directs the deans and vice presidents to submit plans for reductions within their units. Again, this is an incremental process in that, even though input is sought and discussions are had about overall improvement opportunities, the focus of the discussion is about incremental increases or decreases in unit budgets. After the unit responses have been analyzed, the Provost and the Budget Group meet with each dean and vice president individually to discuss the content of the submission and seek further clarification. During this period the VPFA meets with representatives of the campus governance organizations to brief them on the budget parameters that are being considered.

The budget meetings with the deans and vice presidents and the subsequent analyses are generally complete by January, at which point the Provost and VPFA again share this information with the President. After integrating the President’s input into the budget premise, the VPFA and the Budget Director brief the Board of Trustees’ Budget, Finance and Investment Committee (BFI) at the February board meeting. It is generally at this time where the Committee begins its discussions about not-to-exceed tuition and fee levels. The results of this discussion help to guide the Budget Group in developing the proposed budget. If the Committee is generally supportive of the proposed tuition increase, the primary budget parameters may not need to be altered to any great degree. However, if the Committee wants a lower tuition level, then additional reductions necessitate another stage of the consultation process with the deans and vice presidents before a draft budget can be prepared. After considering the input of all of the aforementioned parties as well as any change in circumstances that will affect projected revenues or expenditures, the Budget Group drafts a proposed budget for consideration by the President. If the President approves the draft it is then shared with the campus governance organizations and the Provost and VPFA meet with their leadership groups to discuss the budget in more detail. The input of the governance organizations is brought back to the Budget Group for consideration and may result in modifications to the draft budget. In years when budget reductions or wage freezes have been determined to be necessary, options have been developed about which input from these groups has been sought.

After the next iteration of the budget has been developed and approved by the President, it is presented to the BFI Committee of the Board of Trustees at a special budget review meeting in

April. The Committee thoroughly reviews the proposed budget and the Provost, VPFA and Budget Director respond to questions and clarify the issues for the Committee. The Committee may direct changes in the proposed budget and, if so, another version is developed by the Budget Group and vetted again with the aforementioned parties. If the Committee is satisfied the proposal generally becomes the final budget document that is presented to the Trustees at their May Board meeting. At this meeting the budget is again vetted with the BFI Committee and then with the Full Board of Trustees. It may be modified by the Full Board at this meeting but generally the administration is able to address Board concerns prior to the meeting. Once the Board is satisfied with the budget, it votes to adopt it or not.

Every effort is made to assure that the budget process described above is as transparent as possible. Some members of the campus community would like to see more done in this area. Others indicate that the information flow from their dean or vice president is not adequate. Part of the issue is one of timing. Many believe that they should be getting information about budget challenges much earlier. The general approach has been to try to resolve some of the larger budget challenges before making them public and causing the entire campus community to be concerned about something that they, as individuals, have limited ability to affect. Some argue that the entire or a large portion of the campus should be involved in the budget decision making process. This approach appeals to one's sense of direct democracy but, because of the vast array of differing opinions and delegation of authority by the Board of Trustees, this method may not be possible or necessarily result in the best outcomes, be very efficient, meet the Decision-Making Criteria and the Budget Operating Principles or take into account the whole interest of the University at large. The goal of the process used over the past five budget cycles, which involves more of a representative democracy approach, has been to share information and seek input once there is a relatively high degree of certainty about it and preliminary option development and analysis has occurred. During the recession, when budget cuts had to be made, the existing centralized budget process allowed the senior administration to look beyond the needs of individual units to those of the University at large. It also allowed for a relatively efficient decision making process. Administrative unit budgets were cut more deeply than those of academic units but still some people in academic units wanted to see more input from the campus about which budget cuts should be implemented.

The centralized budget of the University is viewed by some as a disincentive or a barrier to creativity and efficiency. Some examples that have been cited are as follows:

1. If a dean creates a new program, and it results in the generation of additional net revenue, the money flows to the general fund and may not directly benefit the particular academic unit as it is distributed.
2. A vice president may have a plan for reorganizing a unit within her division but is less inclined to deal with the associated personnel challenges because any savings are likely to flow back to the general fund rather than to be retained in the unit.
3. Those that are responsible for a particular building are less inclined to turn off the lights and generally reduce energy consumption because their unit is not responsible for paying the utility bills (paid centrally) and, thus, will not see the savings returned to the unit budget.
4. Unit leaders are less likely to take ownership of a "budget solution" for the entire campus if they do not feel that their unit was part of the problem.



A decentralized approach would come with its challenges as well, some of which might be:

1. If units had to rely on their individual capacities to attract students to meet revenue needs while meeting University academic selectivity criteria, would they be able to adjust their budgets quickly enough in times when there was a decline in demand for their programs?
2. Would units be incented to increase program and degree requirements so as to maximize revenues, thus resulting in longer times to degree and increased cost to students?
3. Would the desire to maximize credit hours taught within units in order to generate revenue cause course or mission creep or unfair competition between or among academic units?
4. Would the President and Provost be able to achieve their goals for interdisciplinary initiatives and overall quality enhancement in a decentralized budget environment as in the current model?
5. Are all of UVM's units of an adequate scale and market appeal such that they could be self-sustaining under a decentralized model? If not, how would these units be subsidized or supported?
6. What would be the means of generating adequate resources to support centralized functions that exist for the common good?

It should be noted that there is some decentralization within the current model including:

1. Academic units are able to *carry over unspent funds* from one year to the next, a characteristic more commonly found in decentralized and incentive-driven budget models.
2. Three units (the College of Medicine, the Extension System and Ag Related Services) already utilize a *revenue-formula budget model*.
3. While the development of the budget is centralized, individual units have *decentralized discretion* to utilize allocated revenues as they desire. The one exception to this is that any new faculty lines must be approved by the Provost.
4. In addition to base budgets, academic units are awarded *Sponsored Activity Incentives*, totaling \$1.7m for the entire institution, for their ability to generate F&A cost reimbursements from grants.
5. An *Academic Investment Fund* of \$1million has been created to support strategic initiatives across the institution on a "one-time" or multi-year basis.
6. *Continuing Education* operates as a \$25million income/expense activity, essentially a revenue-formula budget model. However, the net revenue generated by Continuing Education is either moved to the general fund or put into reserves to support overall University operations, including support for all the academic units.

A quick review of some of our peer institutions indicates that Boston University, Boston College and William and Mary have a centralized budget system while Cornell, Syracuse, UConn, University of Rochester, and Tufts have some version of a decentralized system. Some of those identified as having a decentralized approach appear to be hybrids of the two models. It should

be noted that there have been substantial recent discussions at some institutions, during the recession, about the possibility of moving from their existing system to another. These types of discussions and the information in an *Inside Higher Education Article* (2010) by Jack Stripling (<http://www.insidehighered.com/news/2010/12/13/budget>) indicate that there is no one perfect system and that the unique circumstances of the institution and the state of the economy play a role.

## **Conclusions**

1. The budget process of the University of Vermont is both incremental and centralized. There are pros and cons to centralized, decentralized and hybrid budgeting processes. No one process is likely to meet the needs and desires of all of the people involved in the process. The real question is which model will result in the best means of advancing the University's Vision and Mission, and best aid the preservation and advancement of the institution over the long term.
2. Whichever budget process is eventually used it should address the Areas of Presidential Focus, the Decision-Making Criteria, and the Budget Operating Principles. The process should also be appropriately transparent.
3. Whatever budget model is implemented in the future will have to provide the means to grow revenues every year to keep pace with inflation and provide resources for new initiatives and incentives, while applying adequate controls to ensure that we are operating efficiently and effectively.