

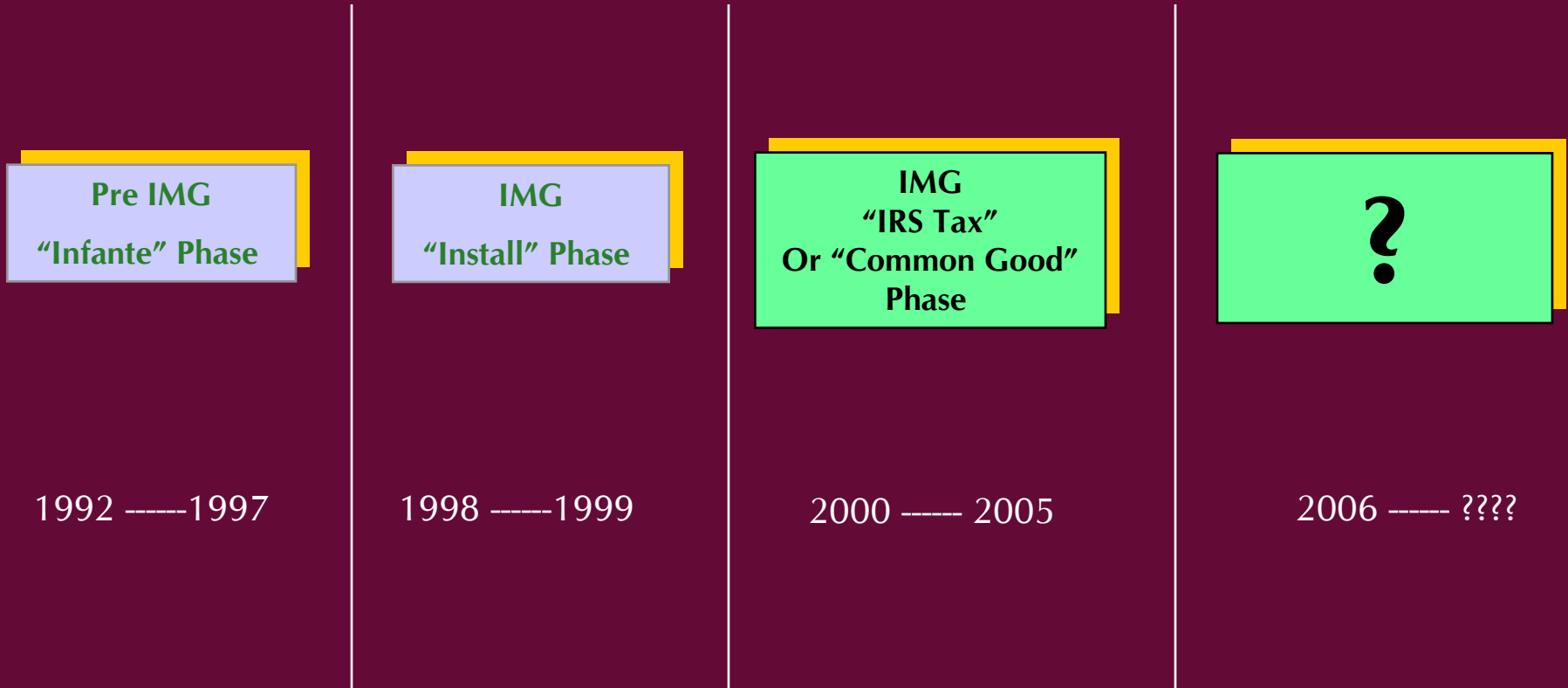
Internal Budget Model Status Report & Discussion

Briefing Materials

Agenda

- Budget Development Process 1992 to today
- IMG
- New Budget Model Status Report
- Budget Development Process 2006-07

Budget Development Activities



Incentives for Managed Growth

Principles - October 10, 1996

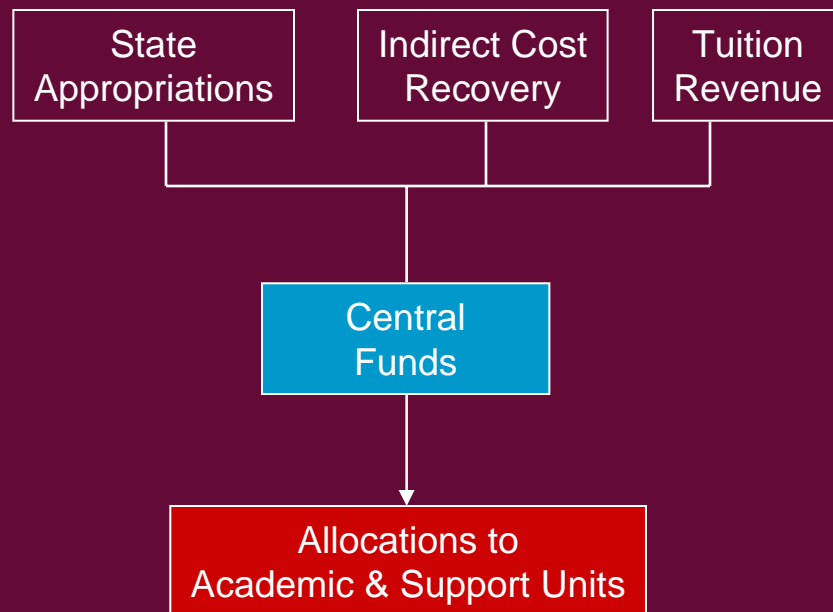
- The University cannot cut its way out of its current financial problems, but rather must grow its way out through an aggressive management of growth and growth processes.
- Proper incentives are needed for members of the university community to enhance revenues (including restricted revenues) and control costs.
- Management, budgetary, and reward structures must be created that tie resources to performance closely enough so that individuals will see how their own actions influence the security and fiscal well-being of their units and themselves.
- The management structure must be flattened and decision-making must be further decentralized so that expenditure decisions are made closer to the point of service delivery.
- The current maze of cross-subsidies and entitlements must be clarified.
- An "information-rich" discourse on the budget must be fostered.
- Service units must be subjected to constant scrutiny for efficiency, effectiveness, and proper incentives.

Reforming Resource Allocation

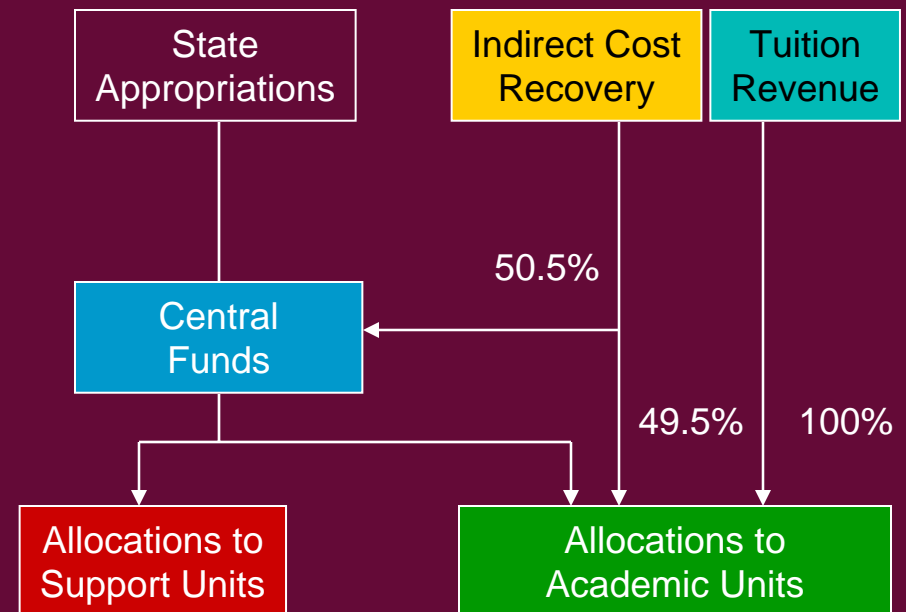
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Models for Revenue Distribution

Previous Model



Current Model

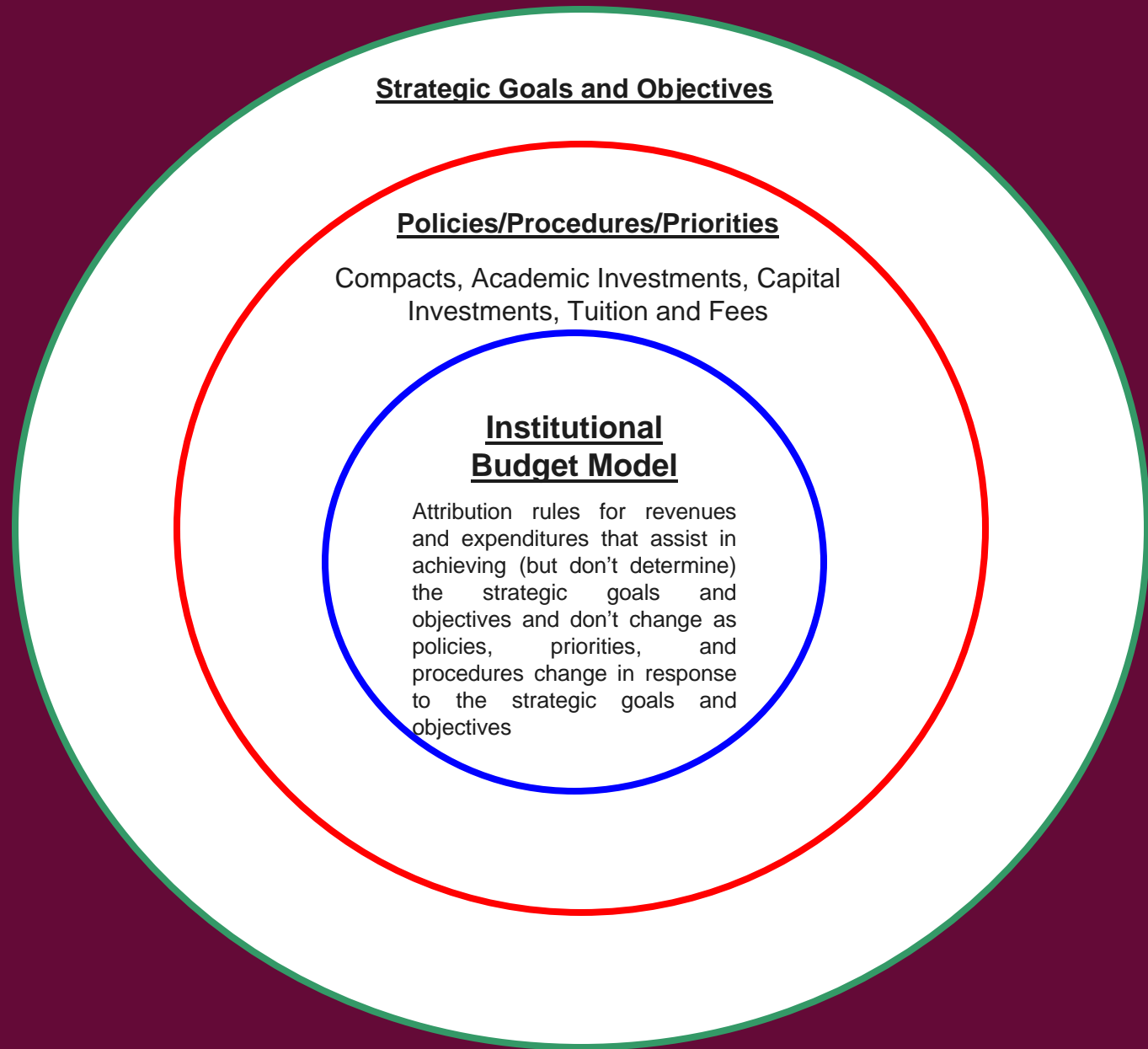


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Model Changes Since the Inception of IMG

1. We created and abandoned a facilities charge - \$5 per square foot
2. We created the Internal Revenue Sharing program to fund institutional common goods and academic priorities (FY06 estimated yield = \$99.5 million)
3. We created the University Fee to fund central student support services and other central investment needs (FY06 estimated yield = \$41.3 million on TC campus and \$11 million on coordinate campuses)

The Strategic Goals and Objectives of the University surround and direct the development of Policies, Priorities and Procedures, including a stable set of rules embedded within the Institutional Budget Model:

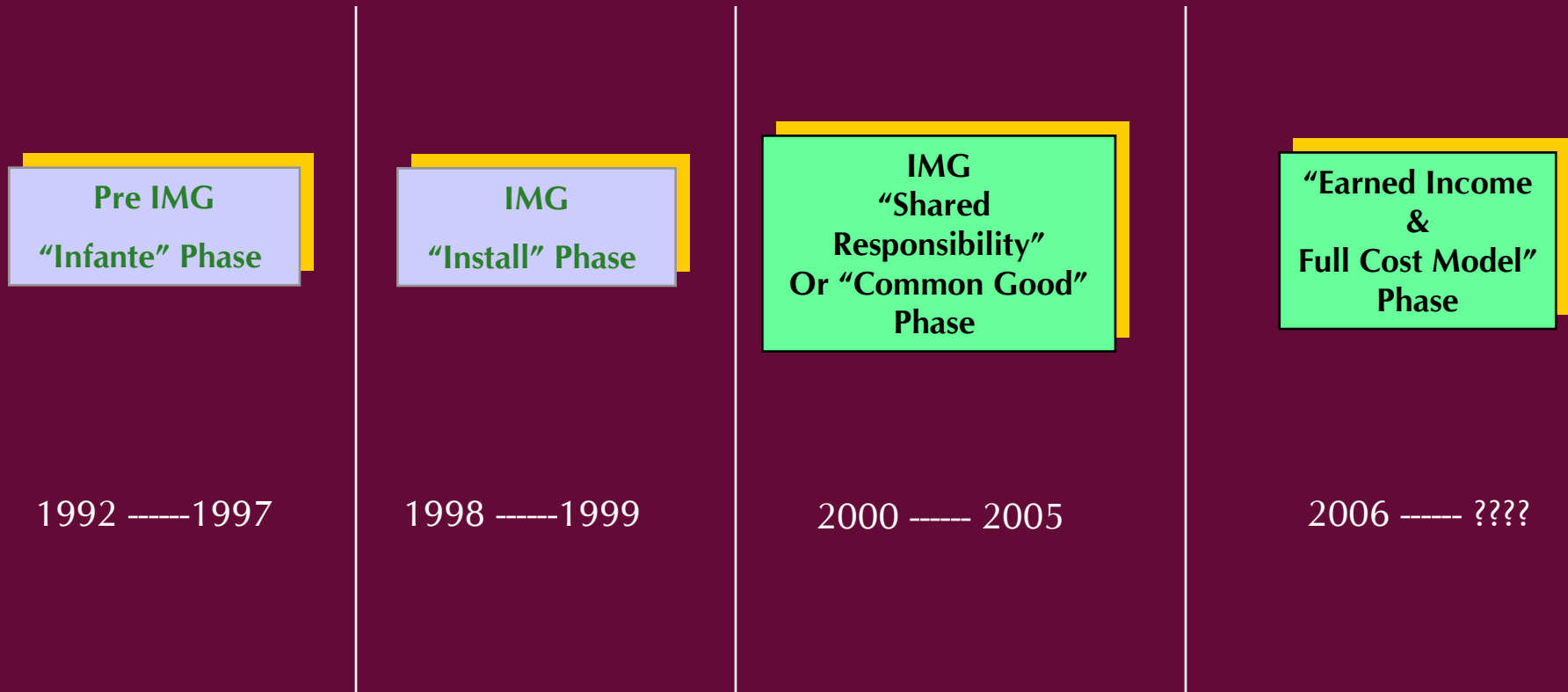


Working Principles

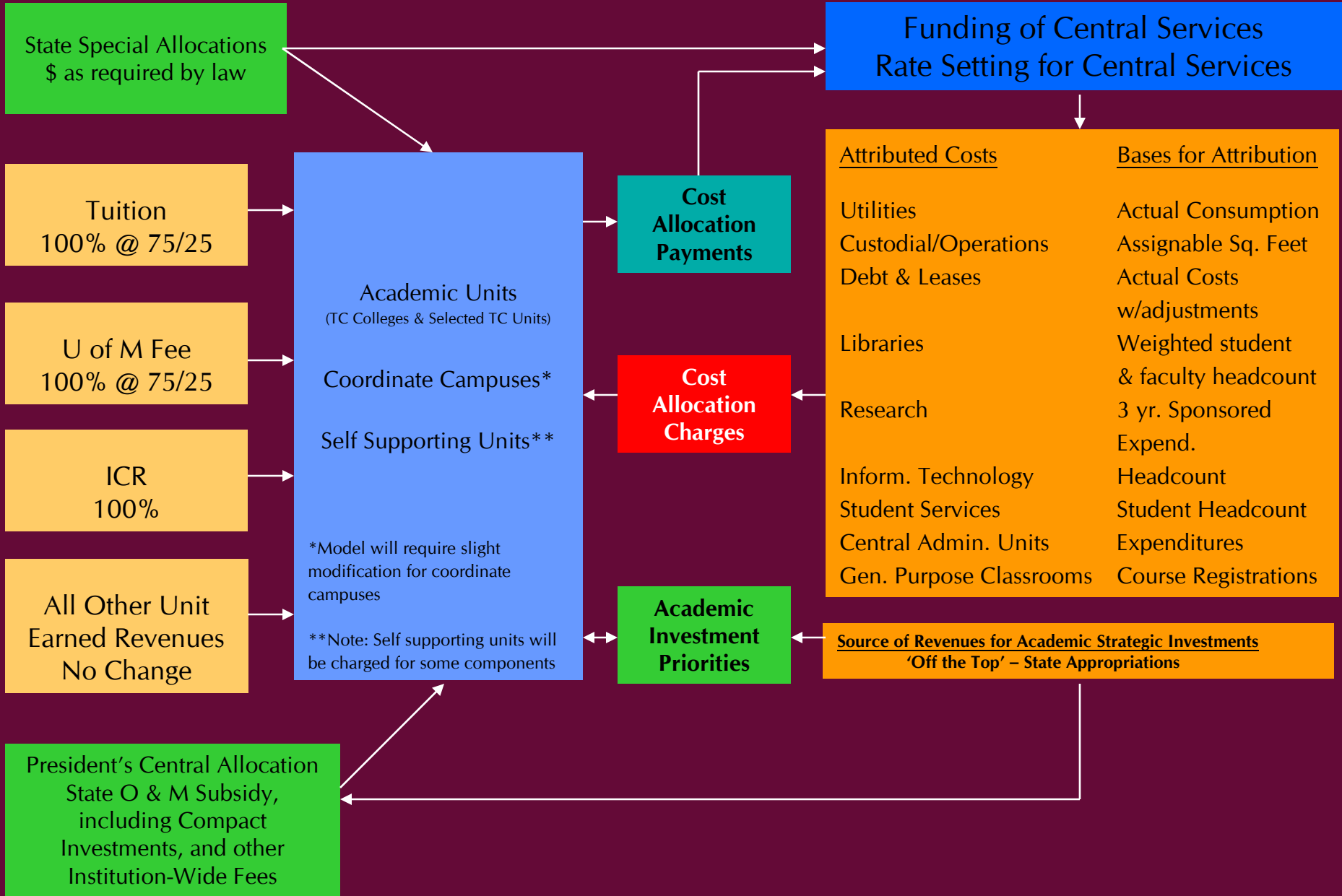
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- 1) Mission and Goals** – Model should encourage behaviors that support the University’s mission and goal to be one of the top three public research Universities in the world and the actions and strategies necessary to achieve that goal. Specific attention should be given to supporting efforts at crossing disciplinary and collegiate boundaries in working toward that goal.
- 2) Transparency** – Model should make budget decisions related to subsidies, investments, reallocations, etc., transparent and acknowledge that no units are “tubs-on-their-own-bottoms”.
- 3) Efficiency/Cost Control** – Model should optimize the use of the University’s physical, financial and technological resources; encourage excellence, service and continuous improvement; and provide clear incentives for member of the University community to control costs.
- 4) Revenue Enhancement** – Model should provide incentives where appropriate to enhance revenues.
- 5) Simplicity** – Model should be as simple as possible to understand and administer.
- 6) Predictability** – Model should result in predictable rules, consistent application of policies and clear outcomes.
- 7) Adaptability** – Model should be responsive to external “shocks”.
- 8) Central Investment** – Model should support the ability of the President to “steer the ship” through reallocations and central investments.
- 9) Information Rich** – Model should foster an all-funds discussion using detailed information related to true costs and service levels and provide good information to support fact-based decision making at all levels of the University.
- 10) Implementation** – Model should be as easy to implement as possible.
- 11) Risk** – The model should place the management of financial risk at the level of the institution that can best control the contributing factors and act to address them.

Budget Development Activities



Earned Income/Full Cost Model



State Special Allocations
\$ as required by law

Funding of Central Services
Rate Setting for Central Services

Tuition
100% @ 75/25

Academic Units
(TC Colleges & Selected TC Units)
Coordinate Campuses*
Self Supporting Units**

*Model will require slight modification for coordinate campuses

**Note: Self supporting units will be charged for some components

Cost Allocation Payments

Attributed Costs	Bases for Attribution
Utilities	Actual Consumption
Custodial/Operations	Assignable Sq. Feet
Debt & Leases	Actual Costs w/adjustments
Libraries	Weighted student & faculty headcount
Research	3 yr. Sponsored Expend.
Inform. Technology	Headcount
Student Services	Student Headcount
Central Admin. Units	Expenditures
Gen. Purpose Classrooms	Course Registrations

U of M Fee
100% @ 75/25

Cost Allocation Charges

ICR
100%

All Other Unit Earned Revenues
No Change

Academic Investment Priorities

Source of Revenues for Academic Strategic Investments
'Off the Top' – State Appropriations

President's Central Allocation
State O & M Subsidy,
including Compact Investments, and other Institution-Wide Fees

Important Points of Understanding in the New Cost Allocation Model

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- The model itself is a set of stable revenue and cost attribution rules that assist in achieving (but don't determine) the strategic goals of the institution
- A sound process for budget approval and rate development for "cost pool" units is key
- The process is dependent on strong leadership to approve cost pool budgets and to make strategic allocations of the state dollars
- The model will be implemented at an RRC level – not a departmental level
- Good performance measures and good data are essential for analysis
- Existing consultative groups will be essential to promote transparency & understanding of decisions
- Process will evolve over time – year one will largely be a conversion to the basic structure, with refinements toward goals in the future

9 Cost Allocation Pools

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Facilities – Operations & Maintenance

Utilities

Debt & Leases

Office of Information Technology

Administrative Service Units

Research

Libraries

Student Services

General Purpose Classrooms

Bases for Cost Allocation

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Discussions on cost allocation have resulted in three different types:

1) **Consumption Based Allocation** – cost allocated based on actual measurement of use

- creates direct incentive toward desirable behavior

2) **Cost Driver Based Allocation** – cost allocated based on relative share of identified cost driver variable

- variable acts as a “proxy” for use – no measurement of actual use

- no direct incentive toward any behavior – provides better management information

3) **Common Good Based Allocation** – cost allocated based on a variable accepted as reasonable measure of participation in the University community

- no direct or primary connection to incentives – just a reasonable way to fairly allocate a shared cost

Recommended FM Cost Allocations

\$119 million in FY06

Charges Allocated by ASF

- Building Services
 - Custodial
 - Waste
 - Recycling
- Maintenance
- Landcare/Grounds
- R&R

Charges Allocated by Consumption

- Energy Management
 - Steam
 - Chilled Water
 - Electricity
 - Water/Sewer

Charges Allocated as part of System-wide Administrative Cost Pool: BSAC

Charges Allocated based on Time & Materials: Services beyond 'Basic Services Standard'

(This standard to be agreed to annually within the annual budget and compact processes.) Working assumption-units “opt-in” to services unless there is a confirmed business case to “opt-out”.

Core Technologies Allocated in the Model

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\$43.8 Million in FY06

Communications

Data Network

Productivity Applications

Operating System
MS Office
File Systems
Web Collaboration
Email
Calendar (UMCal)
Portfolio
File Storage
Web Content Mgmt

Business Applications

PeopleSoft
WebCT
Imaging
Library Automation
E-Research

Student, Faculty Staff Support

Helpdesk (1-HELP)
Training
Digital Media Ctr
Computer Labs
Security

Headcount Allocation Methodology

- Annual snapshot-in-time – lagged one year (fall 2005 used for FY07 budget):
 - Student – Fall Headcount (10th day of term)
 - Staff/Faculty – Fall (9th pay period)
- Per Head Rate
- Allocate by RRC
- Single annual bill / statement to each RRC
- Two tiers – one for all campuses and a second for Twin Cities only

Administrative Service Units - \$81 Million

Part A: System-Wide Units that are “in” this cost pool

Audits	Public Safety (excluding Police)
Board of Regents	Sr. VP Academic Affairs/Provost
Budget and Finance (excluding Bursar)	(Sr. VP Office only)
Capital Planning/Project Management	Sr. VP Health Sciences
Controller’s Office (excluding SFR)	Sr. VP System Admin
General Counsel	(excluding centers)
Human Resources	University Health & Safety
President’s Office	University Relations
BSAC	VP University Services (VP area only)

Costs to be allocated based on proportionate share of system-wide total expenditures.

If college/campus A has 14% of total system-wide expenditures from most recent fiscal year end, then college/campus A will pay 14% of total approved budget for these units.

Part B: Twin Cities Campus Only Units that are “in” this cost pool

Bursar	Printing & Gen. Services
Police Department	University Stores
University Services – Finance, HR and IS	

Costs to be allocated based on proportionate share of Twin Cities Campus total expenditures.

If college B has 14% of total Twin Cities campus expenditures from most recent fiscal year end, then college/campus B will pay 14% of total approved budget for these units

Principal and Interest on Debt - \$36 Million FY06

Central Lease Payments – \$6 Million FY06

Units will be responsible for all debt/lease costs of buildings based on occupancy

Actual Direct Cost by Building with shared responsibility for 'General Purpose Classroom Space'

- 1/3 state debt requirement for University share of project assessed directly to occupants of facility.
- Calculate debt for centrally scheduled classroom space separately and add that cost to the Classrooms Cost Pool (spread on student head count)
- Principles for the appropriate use of classroom space will be disseminated as part of implementation

Research - \$14 million in FY06

Allocation Methodology – Sponsored Research Expenditures

Research Services – Costs in this Pool

- Office – Vice President for Research
- Sponsored Projects Administration
- Patents & Technology Marketing
- Sponsored Financial Reporting
- AHC - Office of Research

-
- Same rate applied to all units to cover all research support services
 - Rate calculated as a fixed percentage of *Sponsored Research Expenditures*
 - Uses a three year rolling average of research expenditures to minimize impact of annual fluctuations for academic units

(If approved budget for units above = 3% of last three years rolling average total sponsored research expenditures, then each unit will pay 3% of their 3-year rolling average total sponsored research expenditures.)

University Libraries - \$31.4 million in FY06

Proposed Allocation Methodology – Weighted Headcount

Twin Cities Campus Only

Costs Allocated based on RRC Proportional Share of:

lower division student headcount	weight = 2 (10th day)
upper division student headcount	weight = 3 (10th day)
professional student headcount	weight = 4 (10th day)
graduate student headcount	weight = 4 (10th day)
faculty headcount (broad definition?)	weight = 4 (9th pay prd)

(Based on weights developed 30 years ago and used today as part of the instructional cost study)

Headcount lagged one year

Future Planned Analysis – Revisit weighting scheme to determine validity

To meet accreditation standards, the Law Library will remain separately budgeted within the Law School. The Law School will be charged only on the basis of their faculty headcount - students will be left out of the denominator for the calculation of their charge.

Student Services Proposed Cost Allocation Methodology – Student Headcounts

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A

Allocated on Total Enrollment – all Students

Student Finance
Administration
Registrar

*Tiered formula for TC only
and coordinate campuses

Financial aid
and investment pools:

B

Allocated on Undergraduate Enrollment – TC only

Admissions
Orientation – 1st Yr
Programs
Prehlth Advising
Student Affairs



Admissions
Scholarships
Student Finance
Student Aid

C

Allocated on Graduate Enrollment – TC & Duluth

Graduate School
Operations



Grad. School
Fellowships
Grad. School
Student Investments

General Purpose Classrooms Cost Allocation 21

Methodology – Student Course Registrations

Costs included	Office of Classroom Management AHC Office of Classroom Management Debt Service on Classroom Space Utilities on Classroom Space
Methodology	Allocate combined costs of items above to Twin Cities campus academic units only based on their proportionate share of total student course registrations
Future	Potentially refine model to build in specific incentives for improved management of classroom space

Summary of Cost Allocation Recommendations

X = Primary “type” assignment

	Utilities	Facilities O&M	Debt & Leases	Tech	Admn Serv	Libraries	Research	Student Serv	Gen. Purpose Class- rooms
Consumption Based Cost Allocation	X		X						
Cost-Driver Based Cost Allocation		X		X		X	X	X	X
Common Good Based Cost Allocation					X				

Investment Pools – Proposed Methodology “off the top”

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Discretionary investment pools that fund initiatives across the institution exist within the budgets of the Senior Vice Presidents, the President’s Office and within a system-wide account (strategic investment pool).

All-University Strategic Investment Pool – Decide on level of compact pool (new investments) as part of the annual budget and compact process and incorporate investment decisions into allocations to academic units – no separate pool funded in central account but investment decisions tracked & communicated and built into compact narratives – no post-budget process

Pools Within VP Offices - Remove current pools from central unit budgets before costs allocated to academic units – decide through the annual budget process the purpose and level of each pool and make an allocation of state dollars to the relevant central units – for subsequent transfer to academic initiatives

Revenue Attribution Recommendations

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Current Attribution Category:

- Tuition
- ICR
- University Fee
- Other Institutional Fees

Recommended Methodology:

- No Changes Recommended
- Recommendation is to attribute 100% of the ICR revenue directly to the college that generates it
- ICR would continue to be recorded in collegiate accounts in the ledger
- ICR would continue to be attributed once per term
- No change recommended in the way the fee is assessed
- University fee generated on the twin cities campus should be attributed 100% to the colleges – same basis as tuition – in collegiate accts
- President can set designated fees for allocation

Notes on Allocation of the State Subsidy

- Annual decision by the President
- Strategic decision each year used to implement University priorities: leadership to be held accountable for addressing priorities through the budget
- Allocations made in support of unit level performance agreements, based on programmatic outcomes and financial management – decisions supported through unit level analysis
- Budget process, information and formatting will all be consistent across units to support decision making
- Total annual allocations cannot exceed the available state resources
- Allocation decisions cannot force a unit into a deficit for the year, but can force discussions about alternate levers in revenues and cost allocation categories.

Proposed Budget Development Timeline (Central Perspective)

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Support Unit Process In the Fall

Early October	Instructions to Support Units
Mid-Late November	Meetings w/Support Units (<i>materials submitted 1 week prior</i>)
Early December	Summarize info & prepare preliminary budget recommendations
Early January	Present materials to Sr. VPS & President for Approval
Late January	Incorporate cost allocation rates into academic unit instructions

Academic Unit Process in the Winter/Spring

Late January	Instructions to Academic Units
Late Feb. to early April	Meetings with Academic Units (<i>budget materials submitted 1 week prior</i>)
April	Build budget recommendations for academic units & balance overall institutional budget
Early May	Present President's recommended budget to the Board for Review
Early June	Present President's recommended budget to the Board for Approval

Contacts for Questions

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- Julie Tonneson, Budget Director
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- Back up slides

Timeline

University General Assessments

Fiscal Year	Enterprise Assessment	Business Serv. Tax	Sales & Serv. IRS	Academic IRS
1997-98	.7%	various	-	0.00%
1998-99	0.0%	various	-	0.00%
1999-00	.7%	revised →	2.00%	1.00%
2000-01	1.25%	-	3.25%	2.25%
2001-02	1.25%	-	3.25%	3.75%
2002-03	1.25%	-	3.75%	6.35%
2003-04	1.25%	-	3.75%	7.50%
2004-05	1.25%	-	3.75%	8.50%
2005-06	1.25%	-	3.75%	8.50%

Reforming Resource Allocation

Why Institutional Revenue Sharing?



Institutional Revenue Sharing Fiscal Year 2005-06 Approved Budget

**Academic Institutional Revenue Sharing =
Total Revenues X 8.5%**

Part 1

**Calculate revenue
yield @ 3.75% of
“Sales & Services”
Revenue***

*** [Includes Central
Support Units]**

Estimated FY06 Yield = \$12.2 m

Part 2

**Subtract “3.75%
Sales & Services”
Assessment from
8.5% IRS and collect
remaining
assessment from
collegiate/campus
units**

Estimated FY06 Yield = \$87.3 m

Total Estimated FY06 Yield = \$99.5 m