Tuition Funds Flow Task Force Report

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Tuition Funds Flow Task Force Members

Ron Marx, Task Force Chair
Dean, College of Education

Gail Burd, Associate Dean
College of Science

Jacqueline Chanda, Associate Dean
Academic and Student Affairs
College of Fine Arts

Leslie Eldenburg, Vice Dean Designate
Eller College of Management

Jim Florian, Assistant Vice President
Budget Office

Ed Frisch, Associate Vice President
Provost's Office

Juan Garcia, Vice President for Instruction
Dean, University College

Rick Kroc, Associate Vice Provost
Institutional Research and Planning Support

Patricia MacCorquodale, Dean
Honors College

Thomas P. Miller, ex officio
Associate Provost for Faculty Affairs

Tom Peterson, Dean
College of Engineering and Mines

Jim Shockey, Associate Dean for Instruction
College of Social and Behavioral Sciences

Henrietta Stover, Assistant Dean
Finance and Administration
James E. Rogers College of Law

Mary Wildner-Bassett
Interim Dean Designate
College of Humanities

In May 2008, Provost Hay created the Tuition Funds Flow Task Force (TFFTF), providing the task force with the charge "*to investigate how we might think differently about tuition flows back to academic units in a more coordinated and incentivized way*." TFFTF was asked to report back to Provost Hay, President Shelton, and Vice-President Valdez in August.

Ron Marx, Dean of the College of Education, served as chair with 12 members drawn from academic units and the central administration. An additional member was added during the summer (see the appendix for a list of the members). In her charge to the task force, Provost Hay wrote,

> Please keep squarely in mind that there will be institutional demands that will need to be balanced. Tuition revenues constitute one of the few known sources of increased revenue that the University can anticipate in the immediate future. There are limits as to how much we could conceivably return to program units without jeopardizing other core responsibilities we have for which tuition revenues are the funding source. That said, we need to be proactive in finding innovative approaches to align revenue streams to the colleges in support of their instructional mission.

Approach

The task force met 11 times over the summer, beginning on May 30. We first discussed the challenges that we have at the UA to maximize the investments we make in instruction and to more effectively link our budget model to our instructional mission. Should we successfully create this linkage, we would stand in a better position to achieve our strategic priorities. Over the summer, we conducted three case studies of research universities that have moved to responsibility-centered budget management (RCM) including the University of Michigan, the University of Minnesota, and Iowa State University. The first two have been using such a model for about a decade or more, and Iowa State has just moved from an incremental budget model to a RCM model this fiscal year. In all cases, we read literature about the respective university budget model and then interviewed people from the university to gain a more in-depth understanding of the strengths and weaknesses of their approach. The models used at these institutions are quite different, but all include the goal to provide incentives to do more teaching and serve more students and majors. Moreover, all three employ their version of RCM to be more successful in securing research funding.

Recommendation

The benefits of a resource management model might be best explained in these terms. Right now, our budget flows do not explicitly follow any of our college related activities. The Committee believes that a model that maps some portion of revenues and some portion of controllable costs to activities would be beneficial because it would allow units to improve their welfare through their own actions. This mapping, then, provides incentives to increase revenues influenced by the formulaic method choice, and also to control costs influenced by the choice of cost assignment method. The next step is to identify a variety of potential mapping models and choose one that fits UA most appropriately. At that point, a cost-benefit analysis can be done. An advantage to a method that allows resource flows to follow activities is that we move away from the current model where activities appear to be irrelevant to resource flows when faculty realize that, in fact, there is a strong connection.

TFFTF believes that there are significant benefits of moving to a budget model that more adequately links resources, costs, and effort. Although there might be some marginal value of allocating a portion of incremental tuition in this manner, we recommend against a partial solution of this sort. The effort and work required to accomplish such a change are not likely to be worth the limited yield. Should we move toward a new approach, we recommend that it be applied at the college level, not to departments or schools. Internal allocations to units in colleges ought to be the responsibility of college leadership.

Below we outline some of the issues that need to be considered if the UA is to move from our current budget model to a model that addresses some of the concerns that gave rise to the TFFTF's charge. The fundamental issue is the lack of relationship between our budget model and our strategic plan. Other budget concerns include the recurrent battle over funding of general education; annual, demoralizing budget cuts (in many recent years we have had budget cuts either through reductions in state appropriations or through the need to reallocate internally); and lack of incentives and funding mechanisms for interdisciplinary programs and team teaching.

We begin with a consideration of the issues regarding revenues, then move to a discussion of the cost side of the ledger. We conclude with a presentation of the next steps needed should senior leadership decide to embark on this project.

Revenues. TFFTF was impressed with the complexity of moving from the current incremental budget model to an RCM approach. There are a host of difficult issues that must be addressed to make such a change work effectively. One question concerns how much of the revenue stream ought to be allocated through a RCM model. Our charge was to consider tuition, yet even for instruction, tuition is only part of the revenue picture and how much of the tuition revenue should be allocated is an issue. A significant fraction of the state appropriation (we will call this fraction of our revenue the *base budget*) is and ought to be allocated to instruction. We had considerable discussion about the value of including base budget allocations in our recommendations. Our current thinking is that both tuition and base budget need to be addressed. One reason for this is that in moving from an incremental budget model to a RCM model, it is essential in the first year to neutralize any negative impact on units as colleges begin to experience the effects of the new model. Different universities use different language to express this need for a soft landing into the new model. At Michigan they spoke of "holding units harmless," and at Minnesota they talked about "making units whole."

Another reason for addressing base budgets is that most units, perhaps all, will simply not be able to generate enough tuition to run their entire instructional program. It is essential to acknowledge that the state appropriation as expressed through the base budget provides important funds for instructional activities across the university. One could consider the base budget as an explicit representation of the support provided by the provost to the important instructional missions of the colleges.

Life in complex research universities like the UA includes inequities across colleges. There is wide variation in faculty salaries, not all of which arises from justifiable disciplinary differences. Teaching loads differ across colleges and programs within colleges. Some of these differences are perfectly sensible; few would argue with the fact that professors of medicine ought to make more money than professors of education. Similarly, different fields require different instructional approaches. Music requires individualized studio instruction for parts of its program, political science does not. Some inequities are historic and are more difficult to rationalize. All of our case study informants said that adopting a RCM model will not eliminate these inequities. At best, by putting financial decisions in the hands of college leadership, it will be possible for the colleges to make decisions that can eventually align effort and reward. Indeed, one informant from Minnesota said that their faculty members more clearly understand how their actions link to the financial viability of their unit.

At each university we examined, a pool of funding was reserved for the Provost to make strategic investments in new directions, to address inequities, and to encourage creativity and innovation.

An important decision in tuition allocation concerns the fraction that is allocated to colleges based on students' unit of enrollment (where is their major housed?) and the college of instruction (where are they taking classes?). Michigan heavily weights the college of enrollment—75% of the tuition funds—at the expense of the college of instruction—25% of the funds. Minnesota is exactly opposite—25% for enrollment and 75% for instruction. These choices have large effects on colleges that are heavily involved in general education and courses that serve majors across colleges.

Similarly, we would need to address in-state and out-of-state status. Michigan calculates a single weighted average tuition amount applicable to all colleges to reduce incentives to admit out-of-state students at the expense of in-state students. One must also determine whether undergraduate and graduate student tuition should be treated differently. It appears that universities that use RCM allocate 100% of the graduate tuition to the college of enrollment. Care must be taken so that interdisciplinary programs and programs that encourage minors in other colleges are not disadvantaged.

Another set of question regards interdisciplinary programs. Michigan has a very large number of programs, nearly 60 dual-degree programs and a large number of joint-degree programs. We were told that funding for these programs comes primarily from the colleges that contribute to them, not directly through allocations in the RCM budget model. Given the professed value of interdisciplinary research and instruction here at the UA, we would need to ensure that a new budget model would not disadvantage these programs. The same can be said of honors programs, which currently require commitments from colleges for their viability.

Finally, the direct costs of research are currently under the authority of the units that do that research, so in effect, direct research costs at the UA are already allocated using an RCM model. But what about indirect cost recovery? One way of looking at our current model is to consider that the 75-25% split to central administration and to the responsible unit is already an RCM operation, although one with a very high tax rate (75%) from the point of view of the unit generating the revenue. (The question of tax rates for costs is addressed in the cost section below.) The way in which the FY09 budget cuts were handled at the UA, wherein the cut in state funds was used to balance the loss of college ICR funds due to the change in the tax rate, is a tacit recognition that colleges use ICR funds for core activities.

Costs. Budget models address costs as well as revenues. Clearly, the salary costs associated with the delivery of instruction are borne by the unit that delivers the courses. But in addition to salaries associated with instruction are the cost pools associated with everything else at the university that needs funds, but for which there are no revenue streams. Some of these costs pools are directly related to instruction (e.g., Honors College, Library, instructional computing), and others are supportive of these functions (facilities; utilities; grounds; human resources; and the central administration, including the president's and provost's offices). And, of course, there are costs associated with the research enterprise (e.g., vice president for research).

When Michigan changed over to RCM, it included costs in its model from the very beginning. The same is true of Iowa State in their transition this summer. In the years of its RCM model, Minnesota covered costs centrally through the allocation of funds from the base budget. However, leadership at Minnesota came to realize that by covering costs through central budget mechanisms, they inadvertently removed incentives for behaving prudently. For example, if colleges do not have to bear the costs of facilities and utilities, there is little, if any, incentive to use space wisely and to conserve utilities. The same is true here at the UA. There is little relationship currently in colleges between the press for new space and the downstream costs of that new space. If a college argues successfully for a new building, the costs of operating and maintaining that building once it comes on line are borne by the central administration, not the college. In a potentially perverse way, our current budget incentivizes unrestrained demand for new space—space that is very costly initially and extremely costly later.

We were told at all of our case study institutions that the tax rate for the various cost pools is a source of discussion. Deans complain that the taxes are too high; central administration claims that they need to recover the costs of running the entire institution. Clearly, the processes used to create the cost pools and to set and increase the rates on transactions in the colleges are critical. It is essential that these processes be transparent and that they involve all of the critical stakeholders. In addition, there are technical matters of establishing the approach to calculating taxes that can have policy consequences. For example, one approach is to use three- year running averages for both revenue allocations and tax rates to smooth out the peaks and valleys of budget years.

However, in shrinking revenue cycles, colleges can be caught with insufficient funds to run their programs and pay their taxes.

The additional staff needed by colleges to manage a new budget model is a significant issue. Insofar as deans will have the responsibility for allocating and managing resources strategically under a new budget model, resources will need to be reallocated to provide staffing, data support and training.

Next Steps. Based on what we heard from the three institutions for which we conducted case studies, the TFFTF feels that it will be a long, difficult, but worthwhile process to make significant changes in resource management. A major change in resource management will need to be transparent and to include input from multiple levels (administrators, faculty, staff, and students). We heard often from our case study informants that continuous, clear, and straightforward communication with all stakeholders was key to the transition in budget models at their respective universities. One challenge for the UA will be that over the next three years, we will have a significant number of our IT and data analysis professionals devoted to making the transition in the Mosaic Project; these same individuals will be needed to assist with collecting data and providing analysis of financial plans for any new resource management system. However, working on both processes at once may ensure that a new resource management process is embedded in the university IT processes. It would be terrible indeed if the Mosaic Project were to develop a system that would produce roadblocks to a subsequent change in our budget model.

Should President Shelton, Provost Hay, and Vice-President Valdez decide to take the next steps in moving toward a system of tuition revenue allocation to colleges based on our recommendations, we suggest a number of steps. At each step we recommend that a thorough cost/benefit analysis be performed to assist in determining whether to continue to the next step.

First, the Iowa State process offers a model for planning and implementation. They began with an exploratory committee much like the TFFTF. Once they decided to take the next step, they created a budget model design committee. This committee developed the principles upon which they built their new model (using a lot of consulting and advice from Minnesota) and then designed the model. All along, they held many open meetings and maintained an open-door policy to anyone who was interested. They told us that they answered all questions—to the point of exhaustion. Yet they attribute their success in moving forward to that approach to open communication.

Once they had designed their model, they created an implementation committee. This committee did the heavy lifting to ensure that, as they went into FY 2009, they were fully prepared with data systems and the technical expertise to be successful. This required considerable training and hand-holding. Moreover, we were told that RCM requires expertise at the college level to make sure that deans and other college leaders understand exactly how the revenue and cost system operates. Such expertise is also critical to make sure that colleges are in a position to extract the maximum revenue and to control costs in order to attain financial health and stability.

Time Line

1. Explore models and set out guiding principles for interim period
    - Decide on model: tuition or tuition/IC
    - Set time line for process and coordinate with Mosaic
2. Work out cost designation and revenue flow
    - Central costs, e.g., library, police, advising
    - Associated costs, e.g., classrooms
    - Undergraduate model

      SCH and majors (75%/25%)

      Allocation for majors at lower division

      Interdisciplinary programs
    - Quality measures
    - Graduate model
3. Budget implementation period
    - Assess inequities that seem to create unreasonable losses for the model

The members of the TFFTF welcome the desire to examine the way in which our budget model supports or impedes the attainment of our strategic priorities. This document, of course, does not capture the lively debate as we worked through our deliberations. Not surprisingly, we were not of one mind when it came to the specifics of our recommendation. However, we were of one mind that a closer connection of resource allocation to effort can be of benefit to UA as we move through our current budget challenges, to emerge as a stronger institution.