UNIVERSITY OF MINNESOTA

BOARD OF REGENTS

Board of Regents Work Session

Thursday, October 8, 2009

1:45 - 4:30 p.m.

600 McNamara Alumni Center, Boardroom

AGENDA

1. Report of the *Financing the Future Task Force* - R. Bruininks/ R Pfutzenreuter/S. Rosenstone (pp. 2-33)

2. Impact of Clinical Integration on the Health Sciences - F. Cerra/B. Daniels (p. 34)

UNIVERSITY OF MINNESOTA
BOARD OF REGENTS

Board of Regents Work Session **October 8, 2009**

Agenda Item: Report of the Financing the Future Task Force

☐ **review** ☐ **review/action** ☐ **action** ☒ **discussion**

Presenters: President Robert H. Bruininks
Vice President/CFO Richard Pfutzenreuter
Vice President Steven Rosenstone

Purpose:

☐ **policy** ☐ **background/context** ☒ **oversight** ☐ **strategic positioning**

To review the final report of the Future Financial Resources Task Force.

Outline of Key Points/Policy Issues:

The Future Financial Resources Task Force was established by the President in October 2008 and charged with producing a comprehensive report addressing the following issues:

- A long-term financial model with core principles, assumptions and recommendations to maximize resources, efficiency and productivity;
- Assumptions, principles and incentives to strengthen the University's academic excellence and financial health;
- Methodological strategies for modeling and managing potential budgetary scenarios;
- Strategies for managing potential cost reductions and likely cost increases, including strategies for internal and external communication to strengthen public confidence; and
- Recommendations to strengthen budgeting, reducing overhead and ensuring creativity in managing and growing resources to achieve and support academic excellence, productivity and impact.

In its final report, the Task Force examines in depth the following five strategies:

1. Grow a larger and more diversified portfolio of revenues;
2. Grow tuition revenue while ensuring financial access for qualified students from families of modest financial means;
3. Substantially increase administrative and academic effectiveness, reduce costs, and boost efficiency;
4. Define the scope of the University's mission to advance a distinctive constellation of excellence; and
5. Develop and execute long-term financial plans, along with budget and planning processes that advance the vision, inform decision-making, track progress, and discipline the setting of priorities.

The Task Force recommends these interdependent strategies as a roadmap for the future as the University manages, develops and deploys resources in light of new financial realities.

Advancing the Excellence of the University of Minnesota

Report of the Future Financial Resources Task Force

Richard Pfutzenreuter, Vice President and CFO for Budget and Finance (co-chair)
Steven Rosenstone, Vice President for Scholarly and Cultural Affairs (co-chair)
Jordan Bronston, Student Representative to the Board of Regents
Susan Cable, Chair, Civil Service Committee
Carol Carrier, Vice President for Human Resources
Charles Casey, Chancellor, University of Minnesota Crookston
Frank Cerra, Senior Vice President for Health Sciences
John Finnegan, Dean, School of Public Health, and Chair, Twin Cities Dean's Council
Amber Peifer Fox, Senator, Council of Academic Professionals and Administrators
Patricia Franklin, Associate to the Vice President and Chief of Staff, Office of the President
Steven Goldstein, President and CEO, University of Minnesota Foundation
Robert Jones, Senior Vice President for System Academic Administration
Jay Kiedrowski, Senior Fellow, Hubert H. Humphrey Institute of Public Affairs
Kjell Knudsen, Dean, UMD Labovitz School of Business and Economics
Kristi Kremers, President, Graduate and Professional Student Assembly
Judith Martin, Chair, University Senate Finance and Planning Committee
Tim Mulcahy, Vice President for Research
Kathleen O'Brien, Vice President for University Services
E. Thomas Sullivan, Senior Vice President for Academic Affairs and Provost

Lincoln Kallsen, Director, Office of Budget and Finance
Beth Nunnally, Chief Financial Officer, Academic Health Center
Julie Tonneson, Director, Office of Budget and Finance

September 16, 2009

Advancing the Excellence of the University of Minnesota

Report of the Future Financial Resources Task Force

Executive Summary

The University of Minnesota's New Fiscal Reality

The University's financial architecture has undergone a dramatic and permanent paradigm shift. State support, historically our largest revenue stream, has been reset: it now constitutes only about 1/5 of the University's operating budget and while integral to the University's finances, it may not increase over the years ahead. Tuition is now the University's largest revenue stream and it will remain so for the foreseeable future.

Operating costs, the cost of academic excellence, and the appetite for investments in new faculty and staff, student financial aid, research support and infrastructure, technology and facilities, are now rising faster than revenue. The University's compact with the State of Minnesota to prepare the next generation of health and other professionals is at risk. And, over the years ahead, the University of Minnesota will face even steeper competition for students, faculty, and grants. If no changes are made and current trends continue, the University will face at least a $50 million shortfall in 2012 and a $1.1 billion annual shortfall by 2025. Unchecked, declining resources will lead to a decline in quality.

A paradigm reset of both our academic priorities and financial strategies is required to meet the enormous changes in revenues, rising costs, and increased competition. The challenges demand a new portfolio of academic, fiscal, administrative, and planning strategies to advance the excellence of the University of Minnesota. The Task Force has identified five such strategies designed to advance the excellence of the University, to ensure innovative research, and provide an extraordinary education for our students and dedicated service to the people of Minnesota.

Strategies to Advance the Excellence of the University of Minnesota

1. Grow a larger and more diversified portfolio of revenues. These strategies include a "new covenant" with the State of Minnesota that more clearly articulates the rationale and responsibilities of the state to support teaching, research and outreach. Additional strategies include increased private giving; development of intellectual property and real estate

assets; and increased indirect cost recovery on grants.

2. <u>Grow tuition revenue while ensuring financial access for qualified students from families of modest financial means</u>. Tuition is the revenue stream with the highest potential for significant, long-term growth, though we likely cannot sustain the high rates of growth of the last decade. To protect this revenue stream, we need to advance the quality and reputation of a University of Minnesota education, better articulate our place in the academic marketplace, and ensure that the University is the destination of choice for a smaller and increasingly diverse pool of students.

3. <u>Substantially increase administrative and academic effectiveness, reduce costs, and boost efficiency</u>. We must create more powerful incentives, reduce cost structures, increase coordination and collaboration, and build a culture of effectiveness, service, efficiency, and productivity.

4. <u>Narrow the scope of the University's mission to advance a distinctive constellation of excellence</u>. New revenues, annual budget reductions, and efficiency gains will not yield sufficient resources to replace the loss of state support, meet rising costs, fund the University's broad strategic positioning agenda, or ensure the excellence of the University of Minnesota. The University must continue to narrow the scope of its mission and direct scarce resources to activities that will ensure a distinctive constellation of excellence. We must strategically configure academic units and reporting lines to fuel the synergies needed for innovative teaching and research.

5. <u>Develop and execute long-term financial plans, along with budget and planning processes that advance the vision and discipline the setting of priorities</u>. Budget decisions must be made within the context of an overall strategic and financial framework that relies on and adheres to a realistic set of financial assumptions and parameters while also ensuring that the University can respond with agility to new opportunities.

Together, these five interdependent strategies provide a roadmap for the future – the ways we must transform the University of Minnesota in light of the new fiscal reality. Faculty and academic leadership in every unit and at every level of the University must make the tough choices needed to sharpen academic priorities. Faculty and staff across the University must fundamentally change how we manage, develop, and deploy resources. If students, faculty, and staff from across the University system work together in partnership with the people of Minnesota to implement these strategies, we will not only to meet the formidable fiscal challenges we face, but we will advance the vitality and excellence of the University of Minnesota over the years ahead.

President Robert H. Bruininks' Charge to the Task Force

"What will it take to finance the future of the University, and how can we achieve it?"

Address the following issues and others that the task force will define as important:

- A long-term financial model with core principles, assumptions and recommendations to maximize recourses, efficiency and productivity;
- Assumptions, principles and incentives to strengthen the University's academic excellence and financial health;
- Methodological strategies for modeling and managing potential budgetary scenarios;
- Strategies for managing potential cost reductions and likely cost increases, including strategies for internal and external communication to strengthen public confidence;
- Recommendations to strengthen budgeting, reducing overhead and ensuring creativity in managing and growing resources to achieve and support academic excellence, productivity and impact.

Overview of the University of Minnesota's New Fiscal Reality

1. **There has been a dramatic and permanent change in the University's sources of revenue.** State support, historically the University's largest revenue stream, has been reset. It now comprises only about 1/5 of the University's operating budget and while integral to the University's finances, future state support may not grow at even the modest 2.2% average annual rate seen over the last 20 years. The share of the University's budget funded by the state will continue to decline.

2. **Tuition now exceeds state support as the University's largest revenue stream.** In the future, tuition will continue to be the University's largest source of revenue.

The University's financial architecture has undergone a dramatic and permanent paradigm shift. The decline and reset of state support and the increased reliance on tuition revenue are permanent changes that are unlikely to be reversed. The trends are likely to continue.

3. **Operating costs, the cost of academic excellence, and the appetite for investments** (in stellar faculty and staff; competitive compensation and benefits; competitive scholarships and fellowships; extraordinary educational experiences; demand for more graduates with STEM degrees; cutting edge research support and infrastructure; technology and facilities) **are now rising faster than revenue.** If no changes are made and current trends continue, the University will face at least a $50 million shortfall in 2012 and an annual shortfall of $1.1 billion by 2025.

The University's compact with the State of Minnesota to prepare the next generation of health and other professionals is at risk. For example, at the same time that the state needs more doctors, nurses, pharmacists and dentists to care for an aging population, the resources from the state and from patient care are diminishing.

4. **Over the years ahead, the University of Minnesota will face even steeper competition for students, faculty, and research grants.**

The shift in revenues, rising costs, and increased competition are enormous challenges that require a paradigm reset in our academic and financial strategies for the future. The challenges demand a new portfolio of academic, fiscal, administrative, and planning strategies to advance the excellence of the University of Minnesota.

Overview of Strategies to Advance the Excellence of the University of Minnesota in Light of the New Financial Realities

1. **Grow a larger and more diversified portfolio of revenues**. New revenues are being developed, but they will generate only modest incremental recurring resources.

2. **Grow tuition revenue while ensuring financial access for qualified students from families of modest financial means.** Compared to other forms of revenue, tuition is the revenue stream with the highest potential for significant, long-term growth. At the same time, segments of that revenue stream are unlikely to be able to sustain the high rates of growth experienced during the last decade.

3. **Substantially increase administrative and academic effectiveness, reduce costs, and boost efficiency.**

New revenues, annual budget reductions, and efficiency gains will not yield sufficient resources to replace the loss of state support, meet rising costs, fund the University's broad strategic positioning agenda, or ensure the excellence of the University of Minnesota.

4. **Narrow the scope of the University's mission to advance a distinctive constellation of excellence.** The University of Minnesota cannot become one of the best universities in the world and meet its land-grant responsibilities without continuing to narrow the scope of its mission, directing resources to activities that will ensure a distinctive constellation of excellence, and strategically configuring academic units and reporting lines to fuel the synergies needed for innovative teaching and research.

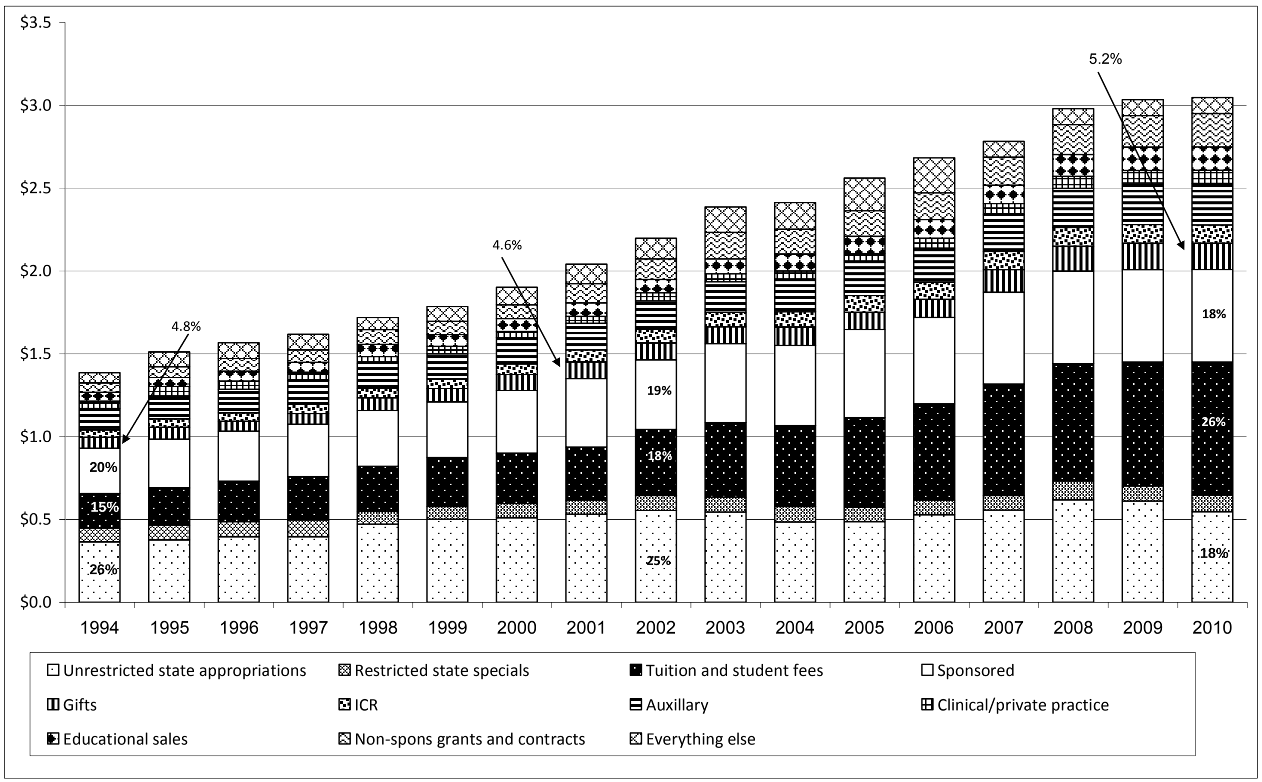
5. **Develop and execute long-term financial plans as well as budget and planning processes that advance the vision, inform decision making, track progress, and discipline the setting of priorities.**

Budget decisions must be made within the context of an overall strategic and financial framework that relies on and adheres to a realistic set of financial assumptions and parameters while also ensuring that the University can respond with agility to new opportunities.

The University of Minnesota's New Fiscal Reality

1. **There has been a dramatic and permanent reset of the University's revenues. The share of the University's budget provided by the State of Minnesota has dropped precipitously over the years from 43% of the U's budget in FY 1978, to 32% in FY 1994, to 21% in FY 2010. Unrestricted state appropriations comprise only 18% of the University's FY 2010 budget.**

Dramatic and Permanent Changes in Sources of Revenues



In $ billions
Sources: CUFS/Data warehouse, U of MN Budget Office 6/26/2009
Excludes ISO and hospital revenues; 2009 state appropriation includes mid-year unallotment;
2009 and 2010 revenues are projections based on President's Recommended Operating Budget and/or historical trends.

Over the decades ahead, state support, while integral to the University of Minnesota's budget, may not grow at even the modest historical 2.2% average annual rate. The share of the University's budget funded by the State of Minnesota will continue to decline.

- The State of Minnesota faces a potential budget shortfall of $7.3 billion for the FY2012-13 biennium assuming the buyback of the K-12 accounting shifts, the funding of current statutory programs, and inflationary increases on state spending.

- The State of Minnesota has a long-term structural budget problem. As the State of Minnesota Budget Trends Study Commission recently concluded, demographic and economic trends over the years ahead will place demand for expenditures that will likely outpace the state's growth in revenue.[1]

  i. The retirement of the baby-boom generation will produce a population with fewer wage earners generating fewer tax dollars. This older population will also place increased pressure on state health care expenditures.
  ii. The young, supported by fewer wage earners than in the past, will also place increased pressure on health care expenditures as well as on expenditures for K-12 education, economic assistance, and social service programs.
  iii. The state's economy is under-performing the nation as a whole. Minnesota's growth in per capital personal income, GDP, and employment has slowed since 2002 and now lags behind the nation. An under-performing economy produces less tax revenue.
  iv. These trends will reduce the state funds available for higher education.

- Nationally, the underlying rationale for the public funding of higher education has broken down. There is no longer a clear consensus about the social or economic reasons for public investment in higher education.[2] The covenant between the University and the State of Minnesota defining the rationale and responsibilities for state support of higher education needs to be strengthened.

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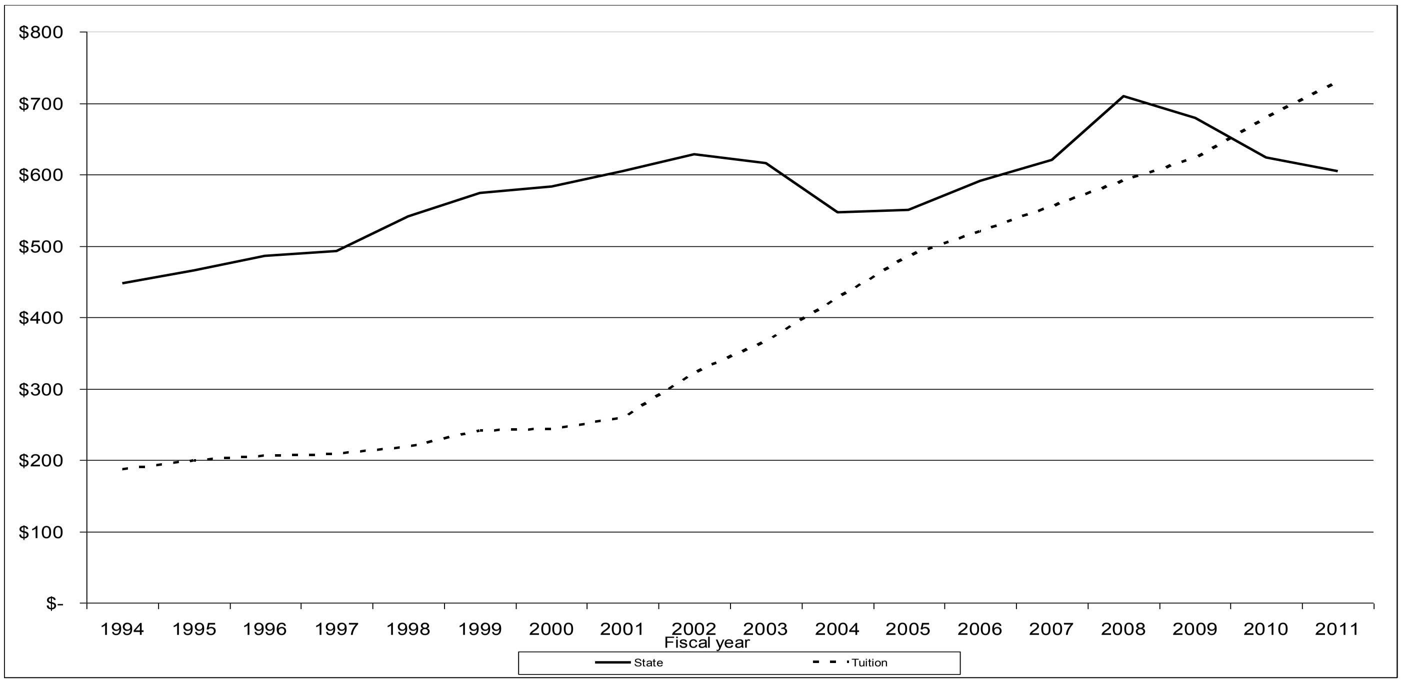
[1] State of Minnesota Budget Trends Study Commission, *Report to the Legislature*, January 12, 2009.
[2] Edward P. St. John and Michael D. Parsons, *Public Funding of Higher Education*.

2. **Tuition now exceeds state support as the University's largest revenue stream, growing from 15% of the U's budget in 1994 to 26% of the budget in FY2010.** In the future, tuition will continue to be the University's largest source of revenue. Compared to other forms of revenue, tuition is the revenue stream with the highest potential for significant, long-term growth. At the same time, segments of that revenue stream are unlikely to be able to sustain the high rates of growth experienced during the last decade.

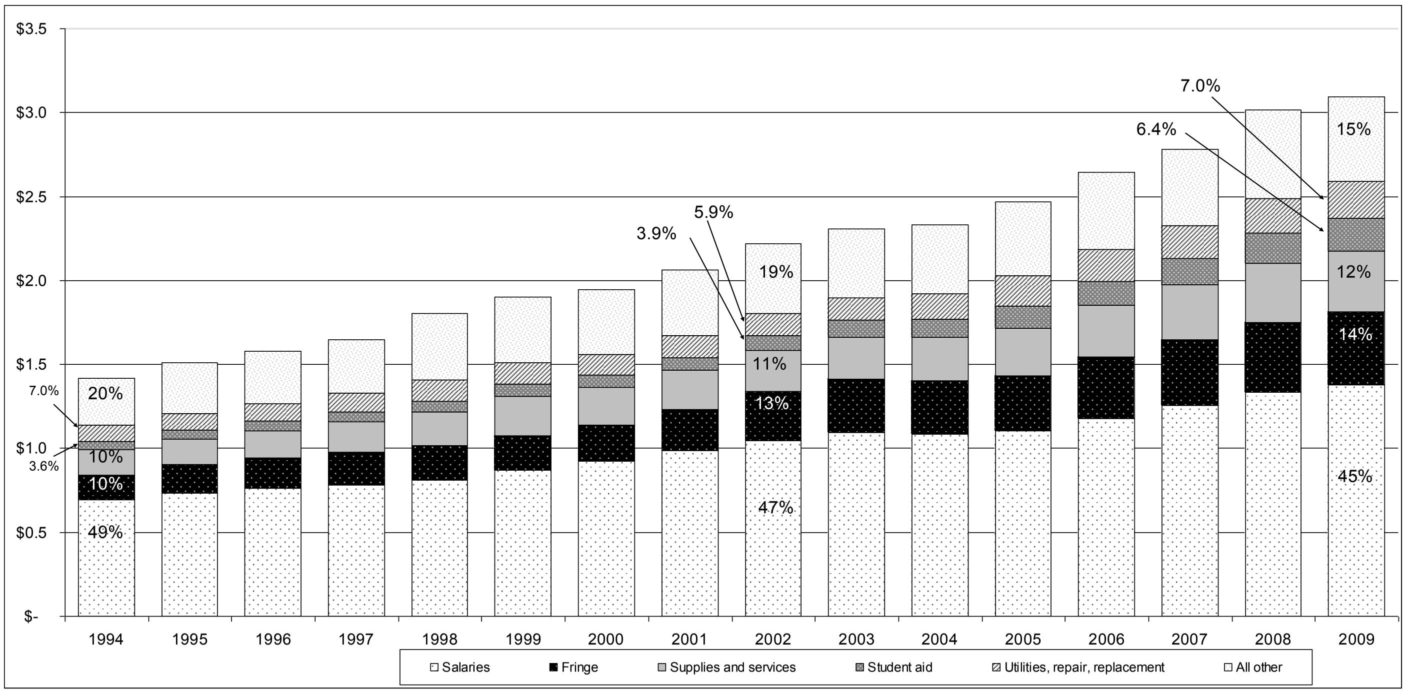
A Paradigm Shift in State Support and Tuition Revenue



Expenditures in $ millions
FY2009 is after unallotment. FY2010 and FY2011 are from the President's Recommended Operating Budget, subject to Board of Regents approval.
Source: U of MN Budget Office. 6/11/2009

3. **Operating costs, the cost of academic excellence, and the appetite for investments** (in stellar faculty and staff, competitive compensation and benefits, competitive scholarships and fellowships, extraordinary educational programs, cutting edge research support and infrastructure, technology and facilities) **are now rising faster than revenues.** These rising costs result from the increased demand for personnel, space, technology, support services, scholarships, etc., as well as rate increases.

Costs Have Been Rising 5.3% per Year

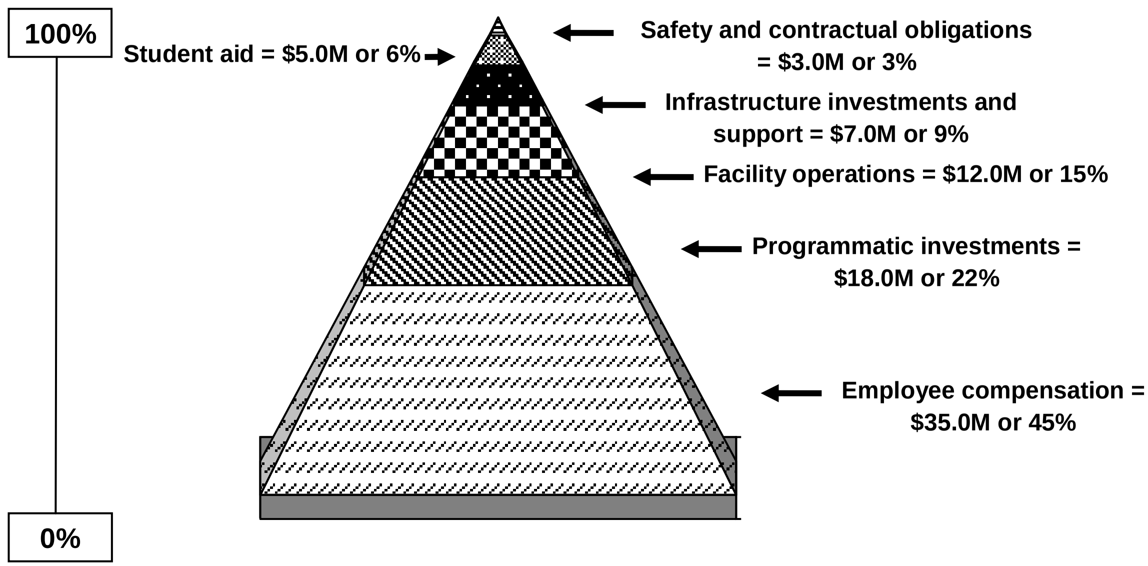


Expenditures in $ billions
FY2009 data estimated from loaded budget
Source: U of MN data warehouse/CUFS. Does not include debt service. 6/11/2009

- Between FY 1994 and FY 2009,
  - salary costs (driven by a growing number of employees arising out of increased University activities and by salary increases) have risen at an average annual rate of 4.7%

- fringe benefits costs (driven by the growth in the number of employees, salary increases, and the increasing cost of health insurance) have risen at an average annual rate of 7.6%
- facilities costs (driven by the increased amount of space and increased cost of maintenance and utilities) have risen at an average annual rate of 5.6%
- student aid costs, driven by expanded scholarship programs, have risen at an average annual rate of 9.6%.

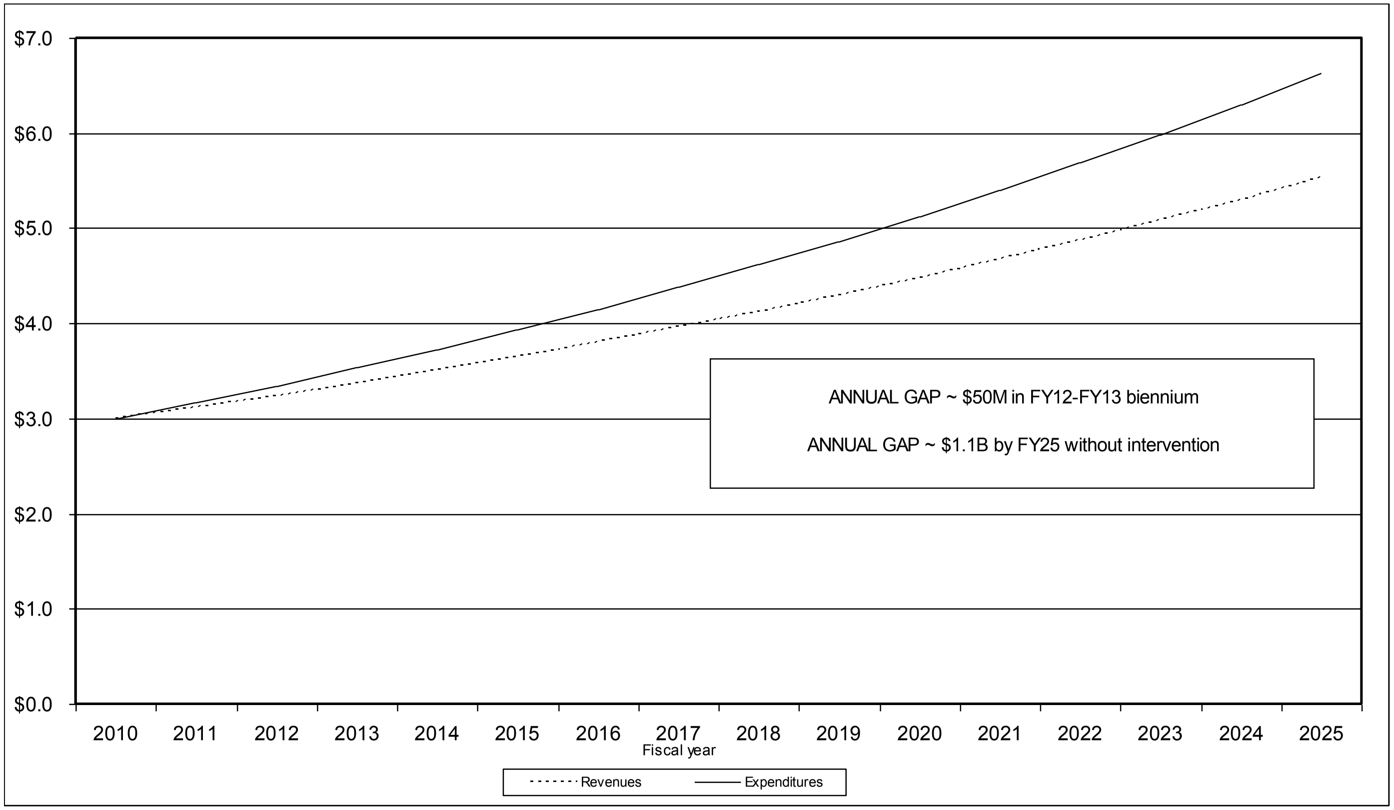
- Just to meet *incremental* costs and fund a modest level of academic investment (not fully implementing the strategic positioning priorities), the University of Minnesota has historically needed an incremental $80 million recurring each year:



- The initiatives that have emerged from the strategic positioning process require an incremental $400 million to $600 million in new and/or reallocated recurring resources.

If nothing changes and current trends continue, the gap between revenues and expenses will widen over the years ahead with the University facing at least a $50 million shortfall in 2012 and $1.1 billion annual shortfall by 2025.

Baseline Projection: If Nothing Changes and Current Trends Continue, the Gap between Revenues and Expenses will Grow



In $ billions
Assumptions:

Revenues -- constant state appropriations at FY10 levels; Tuition and fee growth of 4.5%; Sponsored and all other revenue growth at 15 year historic averages.

Expenses -- O&M costs increase at an Incremental $80M per year in FY10 dollars (assume costs go up 4.5% per year); expenditures on all other funds at 15-year historic averages. Within the $80M per year (in FY10 dollars) are $18 million for academic investments. The expenses do not included additional investments that may be made in FY12. Nor do the expenses include the $400 million to $600 million needed to implement all the strategic positioning initiatives.

Source: U of MN Budget Office. 6/15/2009

- The University's compact with the State of Minnesota to prepare the next generation of leaders in health and other professions is at risk. For example, at the same time the state needs more doctors, nurses, pharmacists and dentists to care for an aging population, the resources from the state and from patient care are diminishing.
  - Most schools in the Academic Health Center rely on clinical income to support education, but funding for health care is being cut. Government is cutting funding for medical training at the same time Minnesota needs more primary care physicians. Fewer faculty mean fewer discoveries leading to new treatments and cures.
  - Few states have funding models that specifically address medical education. Patient care provided by medical schools (faculty practice plans) has historically provided funding to help support medical education. However, changes in the healthcare industry may lessen the ability of these plans to provide this support in the future.

4. **Over the years ahead, the University of Minnesota will face even steeper competition for students, faculty, and research grants.**

- The growing excellence of the University of Minnesota means that we are now competing with better public and private institutions than in the past, but our competitors are also getting stronger and their resources are growing.
- As the baby boom generation retires from the academy over the next decade, competition for top faculty will intensify.
- The number of students graduating from high school will decline over the next decade, not only in Minnesota, but also in neighboring states. High school graduates will also be substantially more diverse. Competition for top students will intensify as institutions expand their recruitment efforts.
- The gap between resources available to top private and public institutions will continue to grow, intensifying competition for top students, top faculty, and research grants.

There has been a paradigm reset in the University's financial architecture. The decline in state support and the increased reliance on tuition revenue are permanent changes that are unlikely to be reversed. The trends are likely to continue.

The shift in revenues, rising costs, and increased competition are enormous challenges that require a paradigm reset in our academic and financial strategies for the future. The challenges demand a new portfolio of academic, fiscal, administrative, and planning strategies to advance the excellence of the University of Minnesota.

Strategies to Advance the Excellence of the University of Minnesota in Light of the New Financial Realities

Strategy #1: Grow a larger and more diversified portfolio of revenues to help the University of Minnesota compete with the best universities in the world. Implement the strategies needed to grow these revenue streams and identify the academic priorities to which these revenues should be dedicated. Ideas explored by the task force to generate net new revenue include:

Estimated Incremental Net Recurring $	Source	When Available?	Tactics
$0 million	State Support	-	• Forge a "new covenant" with the State of Minnesota that more clearly articulates the long-term rationale and responsibilities of the state to support teaching, research, and outreach. • Develop and articulate a clear set of choices for the State of Minnesota regarding its responsibilities for funding of the University. Hold the state accountable for failure to adhere to its responsibilities through the implementation of the alternative choices if they fail to make the necessary investments.
$20 - 25 million	Private Giving	3-5 years	• Increase annual giving. • Use new technologies to expand the donor base at all levels of giving. • Increase unrestricted gifts. • Increase the number of mega-gifts that advance University priorities. • Develop a financial and implementation plan to sustain these endeavors.
$12 million	Indirect Cost Recovery	1-3 years	• Do not voluntarily reduce ICR rates below the negotiated rate. • Negotiate with foundations, state, local and other governmental agencies, industry and private funders for rates more consistent with the true indirect costs.
$5 - 7 million	Intellectual Property	8-10 years	• Fund the Office of Technology Commercialization out of royalty revenue and provide bridge loans to the OTC as needed, consistent with ROI. • Pay the costs of the OTC, the Venture Center, and litigation out of royalty revenue and equity cash outs *before* distributions of royalties are made (i.e., change Regents policy from a gross to a net revenue payout).

$2 – 6 million	Real Estate Development	> 5 years	• Develop a long-term real estate strategic plan that identifies how best to use properties to meet mission critical teaching, research, and outreach priorities and ensure an effective financial monetization of assets. • Articulate in campus master plans the best use / best value for University properties proximate to each campus core. • Charge an individual to develop the long-term real estate strategic plan and engage a professional development entity to assist in this endeavor.
$ 0 million	E-Education	-	As currently configured, e-education will not yield net new revenue. Net new revenue will not emerge until the University: • Articulates e-education's role in advancing innovative, excellent, cost-effective learning for all students. • Clarifies the University's distinct place in the e-education marketplace. • Crafts an effective, system-level business strategy, academic and financial plan, and leadership model to lead e-learning activities across the University system. • Forges strategic partnerships with other e-education providers. • Charges an individual to develop and implement a strategic plan.

Increased sponsored research is not a strategy for reducing the gap between expenses and revenues. Sponsored research is core to the excellence of the University of Minnesota, to the strength of our faculty and graduate programs, and to the discoveries that serve Minnesota and the world. All the funds in a sponsored research grant provided for direct costs must be dedicated to the sponsored project. The funds the University garners from grants to cover its indirect costs – also known as F&A costs – (e.g. facilities, utilities, libraries, and administrative staff) fall short of the actual indirect cost of the research. The University's effective F&A cost recovery on research projects in FY08 was 37.7%, even though the actual F&A costs needed to support sponsored research activities was 62.9%. In dollars, the actual F&A costs were $169.3 million, but the F&A cost recovery was only $101.6 million, meaning that the University subsidized the costs of research by $67.7 million. The indirect cost rate that the University has been able to negotiate with the federal government is 51.0% – still a full 11.9% below the actual F&A costs that the University incurs when it administers research projects.

These new revenues are important, but together they will not be sufficient to replace the loss of state support, meet rising costs, fund the University's broad strategic positioning agenda, or ensure the excellence of the University of Minnesota.

Strategy #2: Grow tuition revenue while ensuring financial access for qualified students from families of modest financial means.

Tuition is now the University's largest source of revenue and is likely to need to grow over time at an *annual* rate of $35 million to $40 million (in current dollars) if it is going to meet even half of the expected incremental annual increase in costs.

<u>Strategies to grow tuition revenue</u>

- Continue to advance the quality and reputation of a University of Minnesota education by improving our academic programs and the quality of the student experience.
- Clarify the University's place in the higher education marketplace by sharpening the University's brand and what is distinctive about a University of Minnesota education.
- Continue to expand market share by making the University of Minnesota the first choice of more students and by making the University the preferred alternative for students paying non-resident tuition.
- Develop the University's long-term tuition and financial aid model and the mechanisms for providing financial access to qualified Minnesota students from families with modest financial means.
- Strategically manage undergraduate, graduate, and professional student enrollment across the system to balance capacity, demand, cost, revenue, and quality.
- Invest a steady and predictable amount of tuition revenue to improve the educational experience (particularly for undergraduates) and to advance the quality and distinctiveness of a University of Minnesota education.
- Improve the University's relationship with and ability to serve Minnesota's increasingly diverse population.
- Collaborate with K-12 and select MnSCU institutions to ensure that there is a diverse pipeline of students who are prepared for and aspire to attend the University of Minnesota.
- Develop an e-education strategy that improves learning in cost-effective ways for all students.

A long-term scenario for tuition revenue (for purposes of illustration): Assume that starting in FY 2012, annually tuition increases 3% for undergraduates on the coordinate campuses, 5% for undergraduate students on the Twin Cities campus, and 5% for all graduate and first professional students. The projected revenue increases under these assumptions are as follows:

Tuition Revenue Projections through 2022 (in $ millions)

A	B	C	D	E	F	G	H
Fiscal Year	Coordinate Undergrad (3%)	Twin Cities Undergrad (5%)	University Grad/Prof (5%)	University Total	O&M Financial Aid (13%)	Total Net of Financial Aid	Net Annual Increase
2008	$98	$271	$230	$599	$75	$524	---
2009	$105	$290	$247	$641	$83	$558	$33
2010	$113	$311	$265	$689	$90	$600	$42
2011	$121	$335	$285	$741	$96	$645	$45
2012	$125	$351	$299	$776	$101	$675	$30
2013	$129	$369	$314	$812	$106	$706	$32
2014	$133	$387	$330	$850	$111	$740	$33
2015	$137	$407	$346	$890	$116	$774	$35
2016	$141	$427	$364	$932	$121	$810	$36
2017	$145	$449	$382	$975	$127	$849	$38
2018	$149	$471	$401	$1,021	$133	$888	$40
2019	$154	$495	$421	$1,069	$139	$930	$42
2020	$158	$519	$442	$1,120	$146	$974	$44
2021	$163	$545	$464	$1,173	$152	$1,020	$46
2022	$168	$572	$487	$1,228	$160	$1,068	$48

A more aggressive tuition option might focus on undergraduate students on the Twin Cities campus, who account for 45% of the University's tuition revenue. For example, the University might consider:

- A more pronounced higher tuition / higher aid policy. Each $1,000 increase in tuition per student each year increases total revenue by about $28 million (or $14 million, if 50% were used for financial aid).
- A significant increase in enrollment. Every additional 1,000 students increases total revenue by about $9.6 million, minus the additional costs of serving these students.

Neither of these options (or various permutations) is plausible in the short-term.

Potential constraints on tuition revenue

1. Students and their families may not be willing or able to borrow more to finance their educations.
2. Morris, Crookston, and Duluth are already priced beyond market and may not be able to absorb significant additional tuition increases.
3. The number of high school graduates from Minnesota as well as neighboring states will decline.
4. Politics.
5. The quality, reputation, and distinctiveness of the academic programs and student experience on the Twin Cities campus have dramatically improved, but still lag behind the very best public and private universities. We may not be able to compete effectively beyond Minnesota at significantly higher prices.
6. A growing portion of tuition revenue needs to be invested in scholarships to ensure financial access, in student recruitment, and in improvements in the quality and reputation of academic programs and the student experience.
7. The state's reciprocity agreements significantly limit the University's tuition revenue. For example, the Madison and Twin Cities campuses have the same number of nonresident undergraduates (about 9,000), but Madison generates more than 50% of its undergraduate tuition revenue from nonresident students, while the Twin Cities campus generates less than 30%.
8. The Twin Cities campus is not geographically close to other major population centers.

Tuition policy questions

1. What is the University's long-term tuition and financial aid strategy?
2. What should tuition pay for? What should tuition pay for when tuition revenue exceeds the cost of instruction?
3. Should the University increase student headcount?
4. Should the University withdraw from the tuition reciprocity agreements?

Undergraduate

5. Should the University continue to move to higher tuition with higher levels of financial aid for students from families with modest financial means? What revenue streams should be used to support financial aid?
6. Should resident tuition rates on the coordinate campuses vary significantly from the Twin Cities campus?
7. Should we change the mix of students to include more students beyond Minnesota and the reciprocity states?

Graduate and professional

8. Should the tuition rate for professional schools be set at market levels? What is the market we should strive for?
9. Should there be resident rates for all graduate and professional programs? Should they all receive state support?

Strategy #3: Substantially increase administrative and academic effectiveness, reduce costs, and boost efficiency.

Continue current efficiency initiatives (such as health care and procurement reforms, energy conservation, and collegiate consolidations) that are improving operating efficiencies and effectiveness. Focus on the major cost drivers: personnel and benefits, space utilization, capital investment, information technology, and research infrastructure.

Create more powerful incentives

- Create explicit and consistent incentives in the internal budget model for increased effectiveness, efficiency, productivity, cost savings, and new revenues.
- Reward staff for innovative ideas.
- Increase user influence over the cost and quality of services.

Reduce cost structures

- Balance the University's principle of providing a living wage with the need to outsource or discontinue activities that are not core University competencies. An activity is a core competency only if it: provides a long-term strategic advantage to the University; makes a distinctive contribution to our ability to serve students, advance research, and serve the community; cannot be competently provided by others; is more cost effective; better reduces risk; or better balances compliance with laws and regulations with the cost of compliance. If an activity is not a core University competency, outsource it or discontinue it.
- Among the administrative, support and academic activities that the University continues to perform, determine what is best done locally, what is best coordinated across units, and what is best performed at the college, campus or system level. Organize unit-level administrative and support operations to provide cost-effective, quality service. The optimal configuration of administrative and support operations may not parallel the configuration of academic units. Priority areas include: 1) financial, administrative, and human resource support; 2) management of the curriculum; 3) use of office space, classrooms, and research facilities; 4) purchasing; 5) public relations; and 6) fundraising.
- Reduce the costs of education by simplifying degree programs, reducing time to degree, and implementing innovative, effective, and cost-efficient models of learning.

- The University's culture is one of avoiding risk through over regulation. We must better balance and define our appetite and tolerance for risk if we are going to reduce our administrative cost structure.
- Simplify systems, processes, policies, and administrative infrastructure, to reduce costs, improve effectiveness, and create flexibility. Consider whether the cost of managing nearly 100,000 individual financial accounts outweighs the benefits.
- Make better use of existing fixed-cost assets, such as space.

Increase coordination and collaboration

- Increase standardization, enterprise solutions, and the use of University-wide templates.
- Forge teams of staff doing comparable work in units across the University and empower them to work together to lead across units. (E.g. curriculum, information technology, financial operations, advising, research infrastructure)
- Consider consolidating, under a single executive officer, University-level operational units including those operational units currently aligned with senior academic officers. Consolidate central office enterprise-wide financial accounting activities under the Chief Financial Officer to better ensure the consistent application of financial practices, to streamline activities, and maximize cost effectiveness.
- Increase collaboration with other colleges and universities in Minnesota, in neighboring states, and in the CIC.
- The State of Minnesota needs to rationalize its system of higher education to clarify the distinct roles that the University of Minnesota and MnSCU play; articulate the collaborative strategies that should exist between the two systems; and identify which resources, campuses, and programs are necessary (or not) to realize the vision.
- Deploy faculty and staff expertise to help the State of Minnesota address complex state policy issues and challenges.

Continue to build a culture of effectiveness, service, efficiency, and productivity

- Develop a "culture of sharing" that focuses on meeting needs, not on who owns the entity providing the service.
- Deeply engage, empower, and reward people across the University who know most about how to improve service and productivity and reduce costs.
- Build a culture of innovation in which structures and processes advance, rather than stymie innovation.
- Decisions of all kinds must be made with an understanding of the impact that choices have on quality and effectiveness, costs and revenues, and service to students and the people of Minnesota.

Strategy #4: Narrow the scope of the University's mission to advance a distinctive constellation of excellence.

New revenues, annual budget reductions, and efficiency gains will not yield sufficient new resources to ensure the excellence of the University of Minnesota. The University of Minnesota cannot become one of the best universities in the world and meet its land-grant responsibilities without narrowing the scope of its mission and directing resources to activities that will ensure a distinctive constellation of excellence.

- The organization of the University into 5 campus, 16 colleges, 138 departments, over 400 undergraduate, graduate, and professional programs, and 289 centers and institutes reflects a legacy of decisions made over the University's 158-year history. *It offers a window into the University's past, not a deliberate strategy for its future.*
- Identify and invest in nodes of distinctive excellence and programs that have the potential to be among the best in the world and invest in those activities that are needed to support this distinctive constellation of excellence.[3]
- Articulate what's distinctive about a University of Minnesota education, about its programs of research, and about its service to the people of Minnesota and beyond.
- Every unit must identify what it will stop doing – even if this means eliminating some things that universities typically do and that the University of Minnesota has been doing for decades. Identify the programs, centers, institutes, academic units, activities, and services that will be discontinued, reduced or consolidated. Identify those that will be strengthened and/or expanded and those that will be maintained at current or slightly reduced levels of support. Set a timeline for implementing these decisions.
- As the scope of the mission narrows, identify how savings will be reallocated to higher priorities and costs will be eliminated (e.g. by taking buildings off line).
- Strategically configure academic units and reporting lines to fuel the synergies needed for innovative, excellent, and efficient teaching and research.
- Clarify and create reporting lines to the Provost that facilitate collaboration and coordinated planning across academic units.

[3] This effort should advance the momentum of strategic positioning. Deliberations should revisit the University's long-standing program review criteria. See "Criteria for Decision Making," from *The University of Minnesota: Advancing the Public Good," A Report of the Strategic Position Work Group*, February 2005, http://www1.umn.edu/systemwide/strategic_positioning/decision.html.

Strategy #5: Develop and execute long-term financial plans, along with budget and planning processes that advance the vision, inform decision making, track progress, and discipline the setting of priorities.

Strengthen the budget and planning process

- Budget decisions must be made within the context of an overall strategic and financial framework that relies on and adheres to a realistic set of financial assumptions and parameters while also ensuring that the University can respond with agility to new opportunities.
- Academic and financial planning must move beyond a single biennial cycle to take a multi-year perspective.
- Create clear and consistent incentives in the internal budget model for increasing effectiveness, efficiency, and productivity; reducing costs; developing new revenues; and implementing strategic priorities. Allow units to internally reinvest savings and new resources they create.
- Identify those academic and support units that can be financially self-sufficient and that will receive no state support. Develop and implement a model of "financial self-sufficiency" within a public university.
- Create explicit oversight by faculty and deans of the University-level support units.
- Make the unit-level contributions to University-wide initiatives more explicit to encourage assessment of the return on investment and help control costs.
- Develop academic and financial plans for reaching academic and performance goals within available resources.
- Focus budget discussions and decisions on strategic priorities and performance measures.

Increase data-rich, analytic decision making

- Strengthen U-wide measurement and reporting of effectiveness, quality, productivity, costs, and revenue.
- Develop stronger data-driven analytical capabilities to inform strategies, measure progress, and understand the consequences of alternative choices.

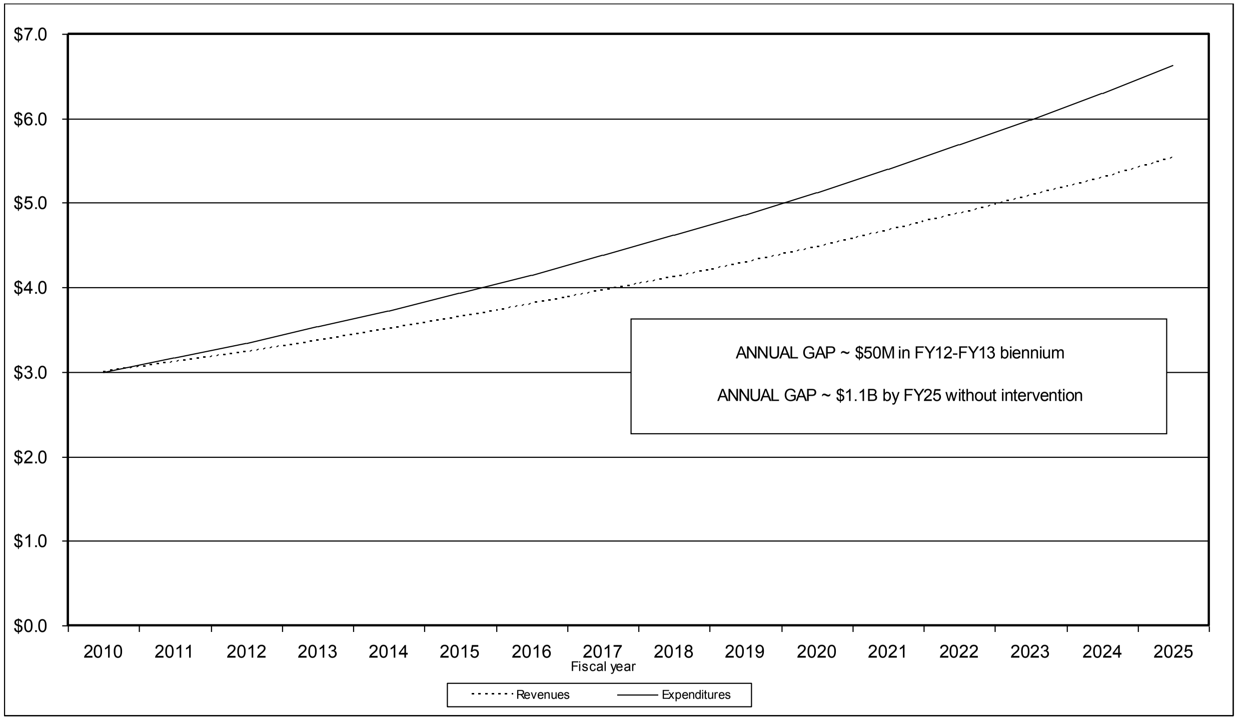
Strengthen the strategic planning process

- Periodically (e.g. in the spring of a gubernatorial election year) update collegiate / academic unit strategic plans.
- Draw upon the collegiate / academic unit strategic plans to update the University's strategic priorities.
- Align the University's legislative proposals with its long-term strategic plan.

<u>Employ long-term financial planning tools</u> that incorporate trends in costs and revenues and that model the direct and indirect, as well as short- and long-term financial consequences of decisions. Use these long-term financial planning tools to understand tradeoffs and inform decision making.

- The types of strategies, decisions, and trends that should be accommodated in the model:
    - Academic investments: faculty, research support, academic programs, advising, financial aid, etc.
    - Infrastructure investments: facilities, technology, staff, systems
    - Revenue strategies: state support, tuition, clinical revenue, sponsored research, indirect cost recovery, private gifts and endowment income, external sales, and new revenue streams.
    - Cost strategies: compensation, fringe benefits, sponsored research, sponsored research subsidy, facilities (utilities, operations, debt service), and technology.
- Develop long-term financial planning tools that are employed at the unit and campus level and, where practical, aggregated to create University system-level projections.
- An example (only for purposes of illustration) to show how the planning tool could be used to identify the long-term financial consequences of alternative strategies:

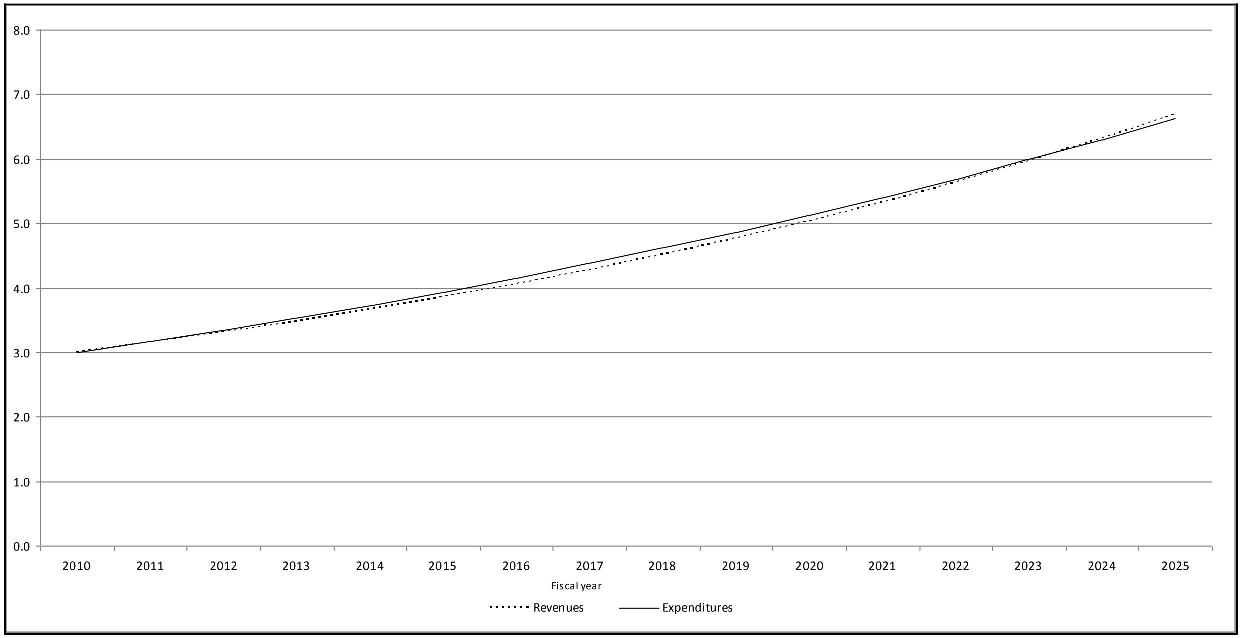
Baseline Projection Assuming Nothing Changes and Current Trends Continue



In $ billions

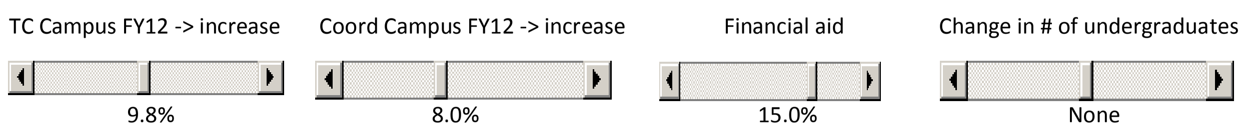
TC Campus FY12 -> increase	Coord Campus FY12 -> increase	Financial aid	Change in # of undergraduates
5.0%	3.0%	13.0%	None

By how much would tuition need to increase
if it were the only strategy used to eliminate the gap between projected revenues and expenses?



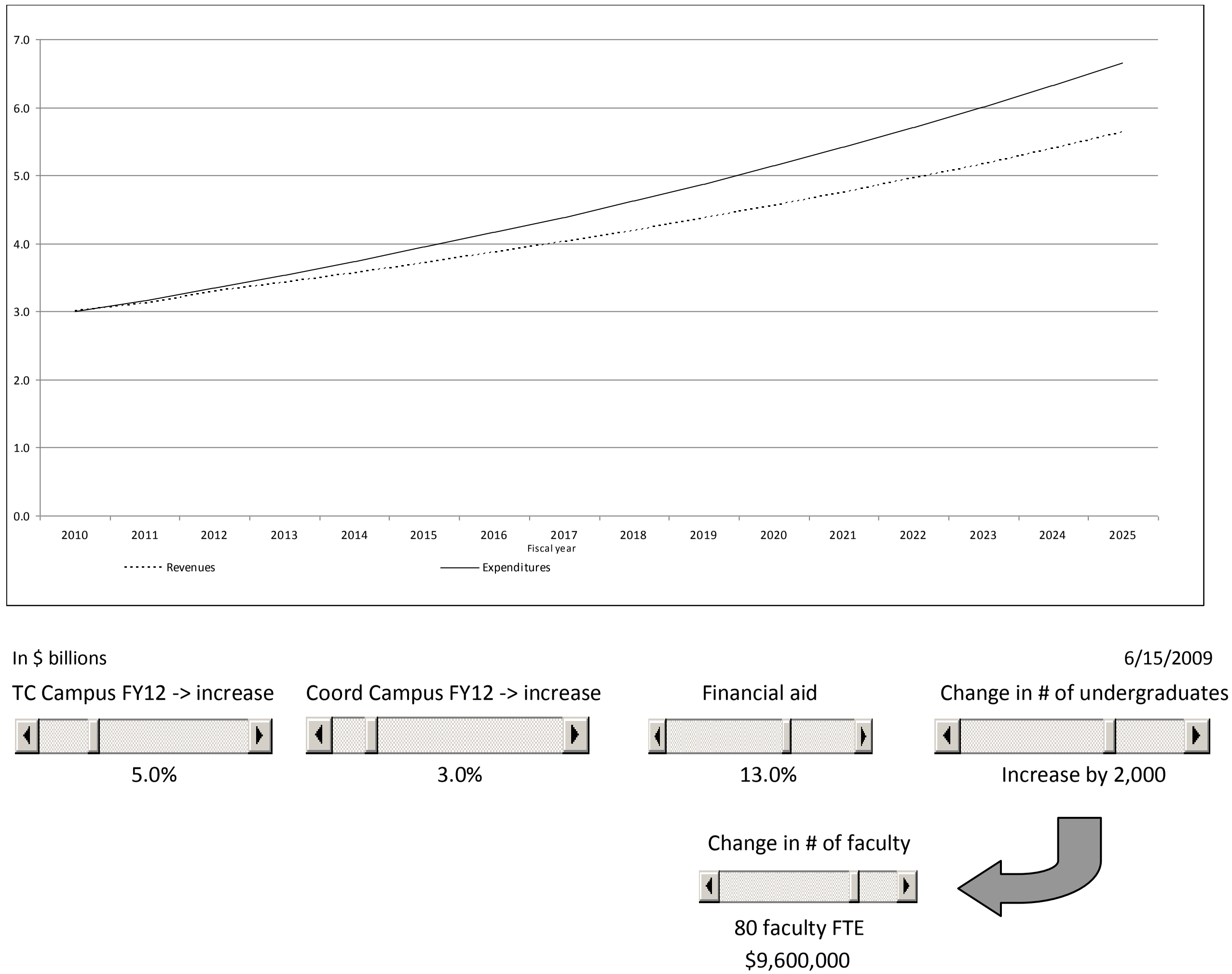
In $ billions

6/15/2009



To close the long-term projected gap between revenues and expenses, tuition would need to increase at an annual rate of 9.8% on the Twin Cities Campus and 8.0% on the coordinate campuses (assuming that 15% of all tuition revenue was used for financial aid). This is an unrealistic scenario.

How much would increasing enrollment by 2,000 undergraduates contribute to closing the gap between revenues and expenses?



The addition of 2,000 students would have a modest impact on the gap between projected revenues and expenses. Gross tuition revenue would be offset by additional financial aid; additional faculty, instructional and academic support staff; and additional facilities costs (e.g. classrooms, library space, laboratories, etc.).

Conclusions

The University's financial architecture has undergone a dramatic and permanent paradigm shift. State support has been reset and it may not increase over the years ahead. Operating costs, the cost of academic excellence, and the appetite for investments in new faculty and staff, student financial aid, research support and infrastructure, technology and facilities, are now rising faster than revenue. And, over the years ahead, the University of Minnesota will face even steeper competition for students, faculty, and research grants.

The new fiscal reality requires that we intervene in dramatically new ways. Unchecked, declining resources will lead to a decline in quality. A paradigm reset of both our academic and financial strategies is required to meet the enormous changes in revenues, rising costs, and increased competition. The challenges demand a new portfolio of academic, fiscal, administrative, and planning strategies.

Together, the five interdependent strategies described in this report provide a roadmap for the future. They are the ways we must transform the University of Minnesota in light of the new fiscal reality. They are the path by which we can advance the excellence of the University, ensure innovative research, and provide an extraordinary education for our students and dedicated service to the people of Minnesota.

Faculty and academic leadership in every unit and at every level of the University must make the tough choices needed to sharpen academic priorities. Faculty and staff across the University must fundamentally change how we manage, develop, and deploy resources. If students, faculty, and staff from across the University system work together in partnership with the people of Minnesota to implement these strategies, we will not only to meet the formidable fiscal challenges we face, but we will advance the vitality and excellence of the University of Minnesota over the years ahead.

Suggested Next Steps: Consult, Communicate, Revise, Implement

- Consult with the President's Executive Team, the Twin Cities Deans, the Faculty Consultative Committee, RRC managers, the Board of Regents, and other key leadership groups (e.g. UMF and MMF Boards). [*Begin immediately*]

- Develop and implement a communication plan that creates a sense of urgency, leads to a broad understanding of the University of Minnesota's new fiscal reality, and energizes all members of the community – students, faculty, and staff – to implement the academic, fiscal, administrative, and planning strategies needed to advance the excellence of the University. [*Begin immediately*]

- Revise the task force report to incorporate suggestions that emerge from consultation. [*Begin immediately*]

- Report to the Board of Regents [*October 2009*]

- Implement the academic, fiscal, administrative, and planning strategies [*October 2009 – September 2010*]
    - Identify an individual who will be responsible for leading the implementation of each strategy.
    - Establish an implementation timeline.
    - Set goals and outcomes that will be accomplished by September 2010.
    - Establish a leadership team to coordinate implementation.
    - Develop communication strategies to report on progress.

Key Strategic Areas for Implementation

Strategy #1: Grow a larger and more diversified portfolio of revenues.

1. State Support
2. Private Giving
3. Indirect Cost Recovery
4. Intellectual Property
5. Real Estate Development
6. E-Education

Strategy #2: Grow tuition revenue while ensuring financial access for qualified students from families with modest financial means.

1. Advance quality and reputation
2. Sharpen the perception of the U's place in the marketplace
3. Craft the University's long-term tuition and financial aid model that addresses relevant policy questions
4. Strategically manage enrollments across the system
5. Improve the connection to and service to diverse populations
6. Collaborate with K-12 to ensure a pipeline of prepared students

Strategy #3: Substantially increase administrative effectiveness, reduce costs, and boost efficiency.

1. Current initiatives that focus on major cost drivers: personnel and benefits, space utilization and research infrastructure, capital investments and information technology.
2. Create more powerful incentives
3. Reduce cost structures
    a. Outsource or discontinue activities that are not a core University competency

   b. Decide what is best done locally, what is best coordinated across units, and what is best performed at the college, campus, or system level
   c. Organize unit-level administrative and support operations to provide cost-effective, quality service.
   d. Simplify systems and processes to reduce costs and improve effectiveness.
4. Increase coordination and collaboration
   a. Within the University
   b. Collaboration with other colleges and universities
   c. Rationalize the state's higher education system
5. Build a culture of effectiveness, service, efficiency, and productivity

Strategy #4: Narrow the scope of the University's mission to advance a distinctive constellation of excellence.

1. Identify and invest in nodes of excellence
2. Articulate what's distinctive about the University of Minnesota
3. Identify the programs, centers, institutes, academic units, activities, and services that will be discontinued, reduced or consolidated. Identify those that will be strengthened and/or expanded and those that will be maintained at current or slightly reduced levels of support.
4. Configure academic units and reporting lines to fuel synergies, innovation, and excellence

Strategy #5: Develop and execute long-term financial plans as well as budget and planning processes that advance the vision, inform decision making, track progress, and discipline the setting of priorities.

1. Strengthen the budget and planning process
2. Increase data-rich, analytic decision making
3. Strengthen the strategic planning process
4. Develop and employ long-term financial planning tools

Core Financial Principles for Advancing the Excellence of the University of Minnesota

1. Financial plans and decisions advance the University's academic priorities and the excellence of teaching, research, and public service.

2. Financial plans and decisions take into account all sources of revenue and all available tools (including reduction of costs, growth in efficiency, discontinuation of programs and functions, reallocation of resources, and growth in revenue).

3. Financial plans and decisions balance short-term and long-term financial needs. Strategies recognize our responsibility as long-term stewards of the University of Minnesota and our responsibility to current and future students and the people of Minnesota.

4. Financial plans and decisions are guided by data, analytical tools, and financial projections that consider competing priorities and opportunity costs, as well as the short- and long-term academic and financial consequences of decisions.

5. Faculty and staff in every unit take responsibility for developing and implementing long-term financial plans that advance their unit's and the University's academic priorities within the overall context of realistic financial assumptions and parameters.

6. Every member of the University community is held responsible for the financial vitality of the University of Minnesota and for the effective use of resources to advance academic priorities.

7. Funding the University of Minnesota is a shared responsibility involving the State of Minnesota (through its appropriation to the University and its grants to students); students and their parents (through the tuition they pay); individuals, businesses, and foundations (through their gifts to the University); state and local government agencies and corporations (through the grants and contracts they award to advance research); patients (through the clinical fees they pay); and students, faculty, and staff (through their efficient use of resources).

UNIVERSITY OF MINNESOTA
BOARD OF REGENTS

Board of Regents Work Session **October 8, 2009**

Agenda Item: Impact of Clinical Integration on the Health Sciences

☐ **review** ☐ **review/action** ☐ **action** ☒ **discussion**

Presenters: Senior Vice President/Dean Frank Cerra
Chief Medical Officer, UMP Bobbi Daniels

Purpose:

☐ **policy** ☐ **background/context** ☒ **oversight** ☐ **strategic positioning**

To brief the Board of Regents on the impact of clinical integration on the health sciences and to provide an update on discussions underway between the University of Minnesota, Fairview Health Services, and University of Minnesota Physicians.

Outline of Key Points/Policy Issues:

The presentation will cover:

1. The potential value, goals and principles of the clinical integration
2. Why clinical integration is important to the world-class education, research, and public service goals of the University, its Academic Health Center, and Medical School
3. The potential functional model for integration
4. The evolving design criteria for an integrated academic health system
5. The status of the discussions and work underway
6. The key upcoming decisions for the Board of Regents
7. How the Medical School will continue to fulfill its land grant mission and partnerships with other health care entities in the state

Background Information:

The Board of Regents has had a series of recent work sessions on the Medical School, Academic Health Center (AHC), and the clinical enterprise. In April 2008, the Board had a working session on strategic positioning and the challenges facing the Academic Health Center, including the functional convergence of Fairview, UMPhysicians, and the AHC. In July 2008, the Board heard a presentation on the biomedical research facilities program and implementation plan. In September and November 2008, the Board had work sessions on the issues facing the clinical enterprise. In July 2009, the Board of Regents approved a resolution defining the goals, principles and objectives for an integrated clinical enterprise and directing University administration to carefully evaluate a variety of proposals to achieve an integrated health care delivery system with Fairview Health Services and University of Minnesota Physicians. In September 2009, the Board held a work session on University of Minnesota Physicians, the integrated group practice for the Medical School's full-time faculty and its relationship to the University.