



REPORT OF THE AD HOC BUDGET REVIEW COMMITTEE

APRIL 9, 2014

Members

Deborah Larsen, Co-Chair, College of Medicine
Jozef C. Raadschelders, Co-Chair, John Glenn School of Public Affairs
Anil Arya, Fisher College of Business
Morgan Cichon, Council of Graduate Students
Donna Hobart, Office of the President
Shane Ingalls, Undergraduate Student Government
Betsy Lindsey, College of Education and Human Ecology
Marie Mead, College of Engineering
Robert Perry, College of Arts and Sciences
James Phelan, College of Arts and Sciences
Kris Devine, Office of Business and Finance, ex officio
Brad Harris, Office of Academic Affairs, ex officio

Staff Support

Suzi Ballinger, Financial Planning and Analysis
Dawn Romie, Financial Planning and Analysis
Jim Schiefferle, Financial Planning and Analysis

■ EXECUTIVE SUMMARY

The Ad-Hoc Budget Committee was convened by the Senate Steering Committee and charged with reviewing the current budgeting principles and budget model of the university. The committee approached the review by developing an in-depth understanding of the university budget, examining the historical context of the last five years, and conducting a detailed data analysis. In addition, colleges were surveyed regarding their viewpoint of the budget model. Next, the committee evaluated the outcomes of recommendations from the last budget review conducted in 2008. Then, the committee had extensive discussions on the risks, challenges and opportunities with the budget model. After this review and analysis process was completed, the committee developed our recommendations.

Overarching Recommendation

1. The guiding principles and design of the university budget model are fundamentally sound. The committee recommends the budget model should be retained. To fully take advantage of the budget model, central university decisions must be made in a coordinated, holistic, transparent manner with the impact of decisions on colleges and support units modeled prior to the decisions being finalized.

Annual Planning and Review Process

2. The Senate Fiscal Committee (SFC) should comprehensively review annually the tax and all assessments in the budget model (for example, student services, research administration, and physical plant assessments) and other assessments outside of the model, both cash and PBA (present budget allocation) based.
3. A robust multi-year projection model should be developed that can be used by colleges to model budget scenarios based on a variety of inputs.
4. The review process for central administration offices should include a subsequent review focusing on the impact of the recommendations.
5. Three institutional risks, the Wexner Medical Center and the changing healthcare environment, the cost north residential housing, and the ongoing cost of STEP, should be carefully evaluated and monitored to ensure their impact is understood, and strategic decisions should be made to minimize the impact to the model.

Budget Model

6. Assessments outside of the budget model should be limited.
7. The subsidy allocation methodology should be re-evaluated when the Ohio Board of Regents (OBOR) methodology is finalized.
8. A “re-basing” analysis should be completed for all colleges.

Management Reporting and Training

9. Colleges should have a college level committee for fiscal and budget issues with adequate department level faculty and staff representation.
10. To increase transparency, fiscal presentations by college leadership, such as the dean and senior fiscal officer, to faculty and staff are desirable and expected.
11. Financial training for unit leaders, including deans, associate deans, department chairs and senior fiscal officers, should be implemented.
12. Centralized financial reports that are easily accessible and provide multi-year data by college and department should be developed and maintained.
13. The Senate Fiscal Committee should review the recommendations above in early FY2016 to determine the status of the implementation of these recommendations.

■ SECTION 1: BACKGROUND AND CHARGE

In FY2003 the university implemented a new budget system. The university budget system is comprised of two distinct components: the *budget model*, which is a responsibility-based model allocating revenue and expenses to colleges and support units based on a series of allocation methodologies commonly known as “budget restructuring”, and *strategic allocations*, which are strategic investments in colleges and support units made by the president and provost. The university budget system is just one component of the entire university operating budget and focuses on general funds revenue, comprised of tuition and fees, state subsidy, and indirect cost recovery from sponsored projects, totaling \$1.5B for colleges and support units combined. For some colleges, general funds are a significant portion of their overall budget and in other colleges, general funds are a much smaller portion with those colleges having significant non general funds revenue streams including endowment, gifts, and sponsored research. The total operating revenues for the university are budgeted at \$4.3B in FY2014, with over half, \$2.4B, attributed to the OSU Health System and OSU Physicians, Inc.

The original principles and recommendations for the budget system are detailed in “*University Goals and Resource Allocations*”, November 1999. The recommendations included a requirement that the university review the budget model every five years. The first review was completed in 2004 by the Ad Hoc Budget Restructuring Review Committee. The last review was conducted in 2008 by the Budget System Advisory Committee (BSAC).

The current Ad Hoc Budget Review Committee was appointed by the Senate Steering Committee in September 2013. The charge is:

Review the current budgeting principles and budget model of the university. Consider all parts of the university budget that do not currently fall under this budget model.

■ SECTION 2: REVIEW PROCESS CONDUCTED BY COMMITTEE

Understand the university budget - Given that many of the members of the committee were unfamiliar with the university budget, including the principles and components, meeting agendas were developed with topics aimed at providing the committee members information and context on all facets of the university budget. Meetings included invited guests and conversations about the budget system and areas of potential risk to the university’s finances.

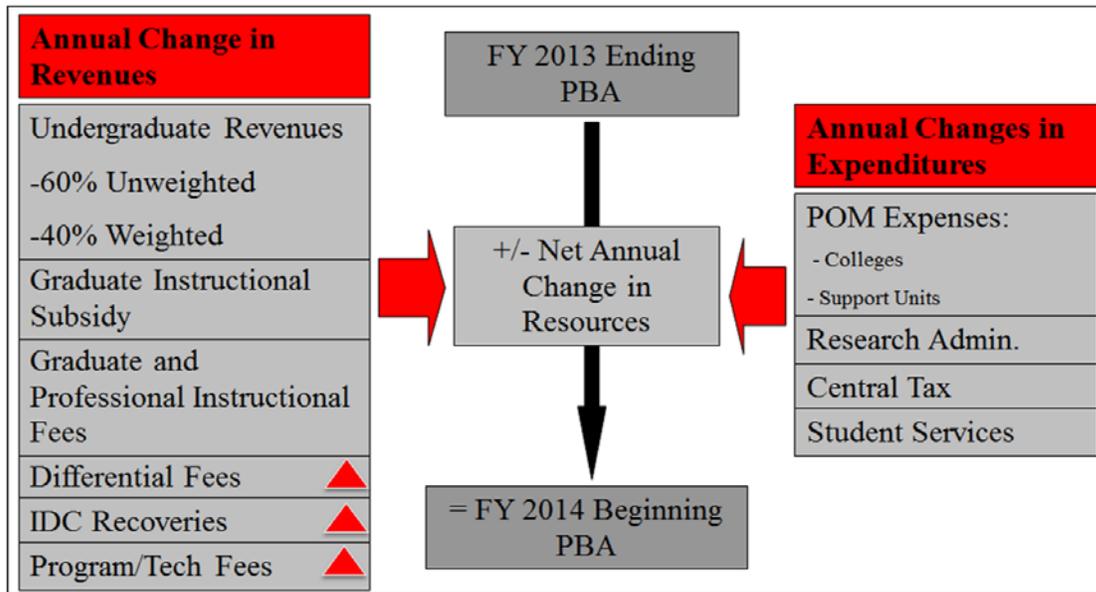
Areas covered are listed below.

- OSU Revenue Structure, University Budget System Overview and University Budget Model – Jim Schiefferle, Senior Director, Financial Planning and Analysis
- Management reports, including College Profiles and Sources & Uses – Donna Hobart, Special Assistant to the Interim President
- History of the University Budget System – Bill Shkurti, former OSU Senior Vice President, Office of Business and Finance and Chief Financial Officer
- Office of Student Life Budget – Dave Wiseley, CFO, Office of Student Life, and Donna Lewis, Director, Budget and Planning, Office of Student Life
- University Athletics Budget – Pete Hagan, Associate Director and CFO, Athletics
- President and Provost Strategic Reserves – Donna Hobart, Kris Devine, Deputy Chief Financial Officer, and Brad Harris, Assistant Provost and Chief Administrative Officer, Office of Academic Affairs

Understand the University Budget Model and Budget System – The university’s budget system is comprised of two components: a modified responsibility center management (RCM) model and the strategic investment of central funds. The university budget model allows for decentralized decision making and control of financial resources at the individual college and support unit level. Colleges are incentivized to increase their resources by teaching more credit hours and increasing research activity and decrease expense by releasing unneeded space back to the university. **Chart 1** provides a visual representation of the university budget model to allocate general funds revenue and expenses to colleges. Marginal revenue from tuition and fees, indirect cost recovery and college specific fees are allocated to the colleges. Marginal changes to expenditures for centrally provided services are also allocated to colleges, including a central tax, research administration, student services, and physical plant. The net of the marginal resources less marginal expenditures is the net marginal revenue (NMR) allocated to each college annually. The colleges’ general funds budget allocation, known as PBA (Present Budget Allocation), changes annually according to the changes in the NMR. It is important to note that PBA can increase or decrease annually based on the NMR calculated through the university budget model.

Chart 1

Budget Process for Colleges: The Big Picture



▲ Revenue not subject to central tax

Understand Historical Context of Last Five Years – Based on a review of the data, both internal and external events of the last five years contributed significantly to the budget outcomes. The historical context is discussed in Section 3.

Understand the Data – Given the vast amount of data available to analyze, a subset of the committee, comprised of the senior fiscal officers who have a high level of expertise with the budget, focused on the data analysis and presented those results to the entire committee. The details of the analysis are discussed in Section 4.

Survey the Colleges – Consistent with the BSAC report, the committee solicited the viewpoints of colleges regarding the budget. The deans were interviewed in person by college cluster (Arts and Sciences, Professional, Health Sciences). The deans, in collaboration with the college senior fiscal officers, were also asked to answer seven questions about how they manage their budgets. In addition, all department chairs were sent a brief survey to complete. The details of the surveys and discussions are discussed in Section 5.

Evaluate the BSAC Recommendations and Outcomes – The committee reviewed the BSAC recommendations and evaluated the outcomes to determine if the recommendations were implemented and successful. This evaluation is discussed in Section 6.

Discussion of Risks, Challenges and Opportunities – The committee identified risks, challenges and opportunities that are discussed in Section 7.

Formulation of Conclusions and Recommendations – After completing the process above, the committee developed a list of conclusions and recommendations forming the basis of this report. The recommendations are discussed in Section 8.

SECTION 3 - HISTORICAL CONTEXT OF THE BUDGET FROM 2008 – 2014

The committee reviewed the historical context of the university budget from FY2008 to FY2014 to better understand and evaluate the impact of the budget model on colleges. The budget model was directly impacted by both internal and external forces since FY2008, and the combination of these forces formed what the committee refers to as the “perfect storm of FY2012.”

External Forces

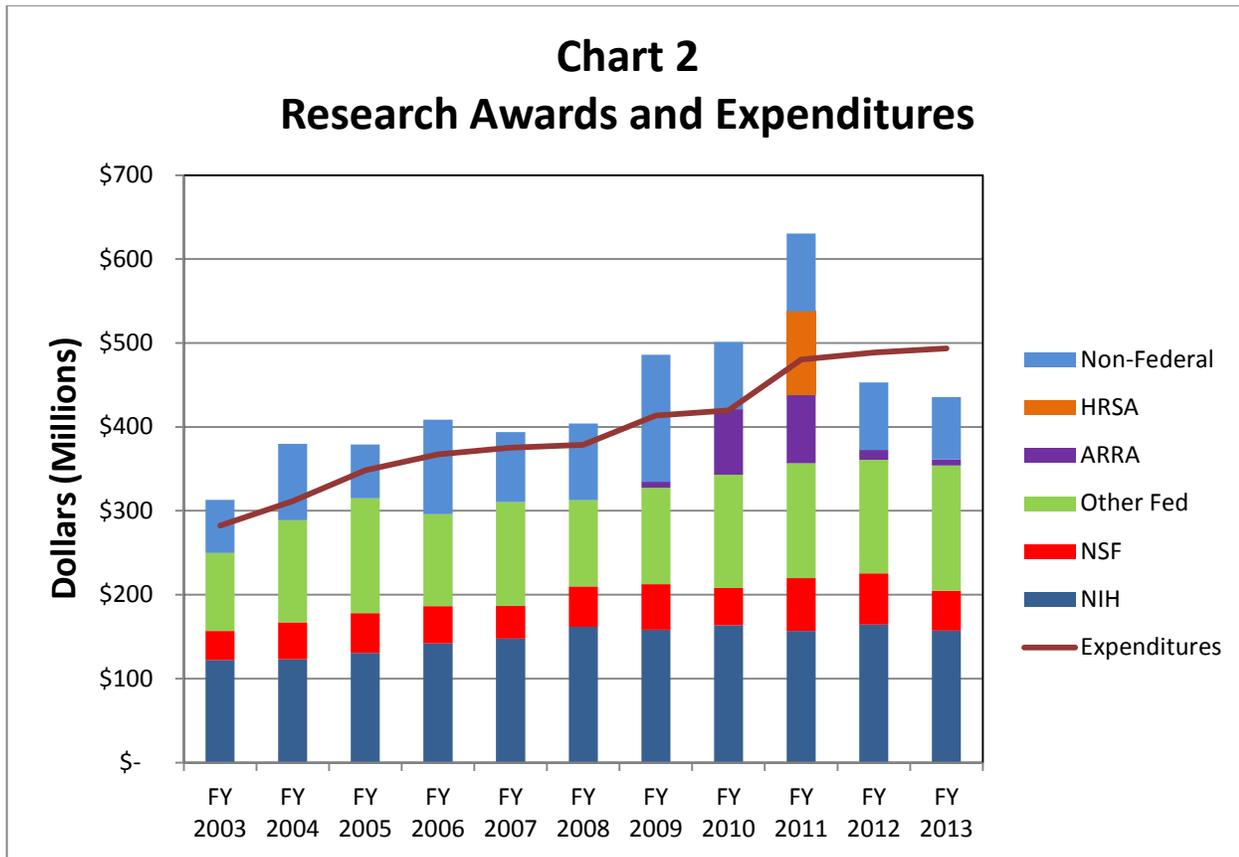
The most significant external event impacting the budget was the financial recession beginning in 2008 and lasting for several years. The recession had many negative effects, but the most notable were a decline in state funding, a decline in federal funding for research, a decline in endowment earnings, and the pressure to keep tuition growth low in order to minimize the student debt load.

Beginning in FY2011, the state funding to the university, known as the State Share of Instruction or SSI, was cut 15 percent, representing a significant funding decline. In FY2011, the SSI funding gap was covered by one-time federal funds. The university used this one-time infusion of funds to keep SSI allocations at their pre-cut levels for FY2011, but in FY2012 the 15% reduction, which totaled to \$64M, was passed on to the colleges, and in turn, also impacted support units through a reduction in the taxable revenue. Although this reduction was unavoidable, it presented colleges and support units with significant challenges whose effects are continuing to be felt.

The decline in federal and state funding for research grants has also impacted colleges. Beginning in FY2009, federal funding increased due to the American Recovery and Reinvestment (ARRA) funding. However, after

ARRA funding ceased, overall federal funding has declined. Since the budget model directly allocates both direct research expenditures and the marginal change in indirect cost recovery to colleges, the decline in funding has negatively impacted their revenue streams.

Chart 2 below displays the trends of research awards and expenditures. The university received \$185M in ARRA funding over five years beginning in FY2009. In FY2011, the university also received one-time federal funds from HRSA (Health Resources and Services Administration – a unit of Health and Human Services) to fund a capital investment in radiation oncology in the hospital.



During this time period, as we noted above, negative economic factors converged with pressure from students, parents and legislators to limit tuition increases, especially for undergraduates, and the university responded accordingly. Since FY2008, undergraduate tuition for Ohio residents was frozen for three years, and the average annual increase over the seven years has only been 2.3%. The committee understands the societal concerns with increasing student debt load and the need to mitigate tuition growth. However, since tuition is a sizable portion of the university budget model, limits on tuition growth negatively impacts college budgets.

In addition to the impact of the recession, the Ohio Board of Regents (OBOR) has changed their SSI funding model twice in the last five years. These allocation changes directly impact how much SSI the university receives. In FY2010, the OBOR SSI allocation model changed to increase the number of subsidy categories based on cost of instruction and academic subject. The university, based on recommendations from Senate Fiscal Committee, changed the allocation methodology to mirror the OBOR changes. The changes included expanding the number of subsidy categories based on average statewide cost of instruction and moving to

credit hours completed rather than enrollment based on 15th day data. In FY2013, the OBOR allocation model changed again to shift the emphasis onto degrees completed, the education of at-risk students, and the development of on-line academic programs. These more recent changes to the OBOR model are still being evaluated to determine the impact on the university's SSI revenues.

Internal Forces

Several internal forces have affected the funding allocated to the colleges via the university budget model. Based on the recommendations of BSAC, the university implemented a three-year budget reallocation plan to create strategic reserves for the president and provost. Beginning in FY2011, all colleges and support units reallocated 1% of their total base PBA back to the provost (colleges) or president (support units). This amounted to slightly more than a 3% PBA base reallocation over three years.

The university implemented an undergraduate enrollment plan over five years beginning in FY2011, the same year as the start of the PBA reallocation. The enrollment plan primarily invests in undergraduate scholarships with the overall goal of increasing both the quality and number of undergraduate students. The total cost of the enrollment plan is \$26.3M over 5 years. The majority of this cost is being added annually to the student services allocation in the university budget model, and therefore, passed directly on to colleges. In addition, the university is funding centrally \$25M in one-time need-based cash distributed equally over a four year period at \$6.25M annually beginning in FY2013.

The effects of these undergraduate scholarships on college budgets are magnified by the way in which they are implemented in the budget model. Tuition that is not received is credited in the same way as tuition that is collected. Marginal tuition changes are taxed. The colleges are then charged for increases in general funds scholarships through the student services assessment. Thus, the university is not receiving revenue for scholarship students, colleges must pay the central tax and student services assessment on scholarships as if it was actual tuition. It may be appropriate to handle the scholarships in this manner, but the impact on colleges should be modeled and fully understood.

Despite the external forces described above, the university has provided annual salary increases through its Annual Merit Compensation Program (AMCP) along with the associated increases in benefits. During the period FY2008-FY2014, compensation increases ranged from 2% to 4% annually, with the average annual increase being 2.7%. These increases are funded from college budgets, typically with revenues associated with tuition and SSI which were declining over the same period. Support unit AMCP costs are provided from central university funds. Simultaneously, benefits rates continued to rise, and these increases had to be covered by the colleges. While the university must remain competitive with both faculty and staff compensation compared to the external market, doing so during a period of declining state and federal funding, and negligible tuition increases had a major negative impact on college budgets.

Alternate sources of funding, such as the parking monetization, and the affinity agreements with Huntington Bank, Nationwide and Coke, are providing large annual revenue streams that are being invested back into the core academic and research mission of the university. The revenue from the asset monetization of the parking operations provided the university with \$483M, which has been invested to generate \$23M annually for strategic investments in faculty hiring in the discovery themes areas, in eminent scholarships and student support, in the arts district and in ongoing support for transportation operations and sustainability.

Notably, the university implemented semester conversion in FY2013, resulting in a downturn in credit hours, particularly during the summer. May term was also implemented and was tuition free up to three credit hours for students enrolled in spring semester. The opportunity revenue loss for May term was modeled at \$21M, comprised of \$7.6M for undergraduates and \$13.4M for graduates. However, based on benchmark data for

participation rates when charging students, realized revenues will likely be less. A more realistic revenue gain from charging tuition using an 8.5% participation rate would be in the range of \$11-\$12M.

“The Perfect Storm of FY2012”

FY2012 was a perfect storm of combined external and internal forces that resulted in a significant decline in budget availability to colleges and support units.

1. State funding from SSI declined 15 percent with the elimination of the one-time federal cash in FY2011.
2. Undergraduate resident tuition was frozen at FY2011 levels.
3. FY2012 was the second of three years of the funding of the 1% PBA reallocation.
4. FY2012 was the second of five years for funding of scholarships associated with the enrollment plan.
5. Compensation (AMCP) increases of 2% along with associated benefit rate increases were given to faculty and staff.

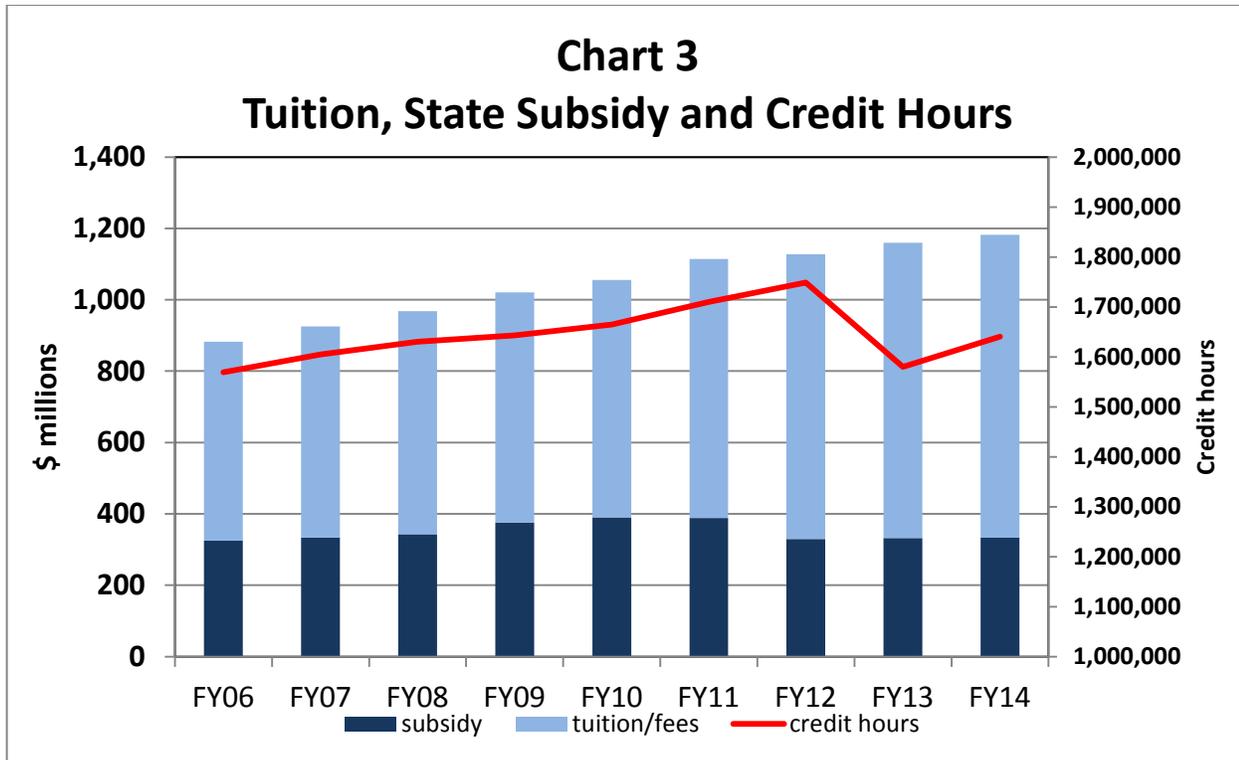
The combination of these five elements all resulted in an overall budget decrease through the university budget model of \$21.6M to colleges. AMCP cost an additional \$8M just for faculty and staff, thus, resulting in a funding gap of \$29.6M for all colleges combined. Only two of 14 colleges had a positive marginal change after AMCP.

SECTION 4 - DATA ANALYSIS AND OBSERVATIONS

In analyzing the data, the committee focused on several key questions. The budget allocations both within the budget model and budget system (allocations outside the budget model) were examined, plus specific revenue streams and assessments within the budget model were examined. The analysis focused on colleges in total, not individual colleges. We did not consider differential impact of the budget model and strategic investments on individual colleges in any detail. Nor did we attempt to link allocations with quality measures to assess how well the budget model is supporting our academic plan.

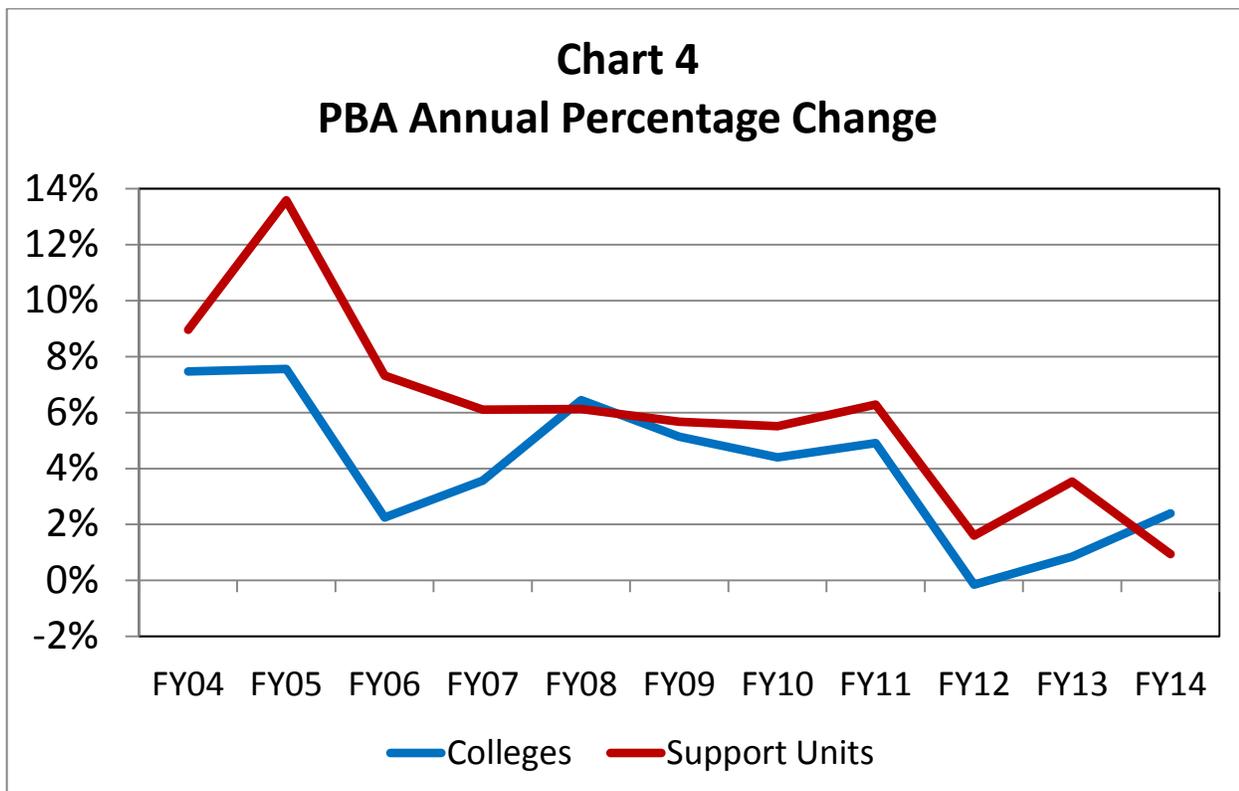
What has been the change in tuition and State subsidy compared to credit hours? The change in tuition and subsidy includes both the total funding combined and the percentage share of each.

In **Chart 3**, the tuition, State subsidy and total credit hours are displayed for FY2006 through FY2014. Tuition continues to increase proportionately compared to state funding. In FY2006, subsidy was 37% of the total, and in FY2014 it declined to 28%. Total credit hours continue to grow over time and appear to be rebounding after FY2013 semester conversion.



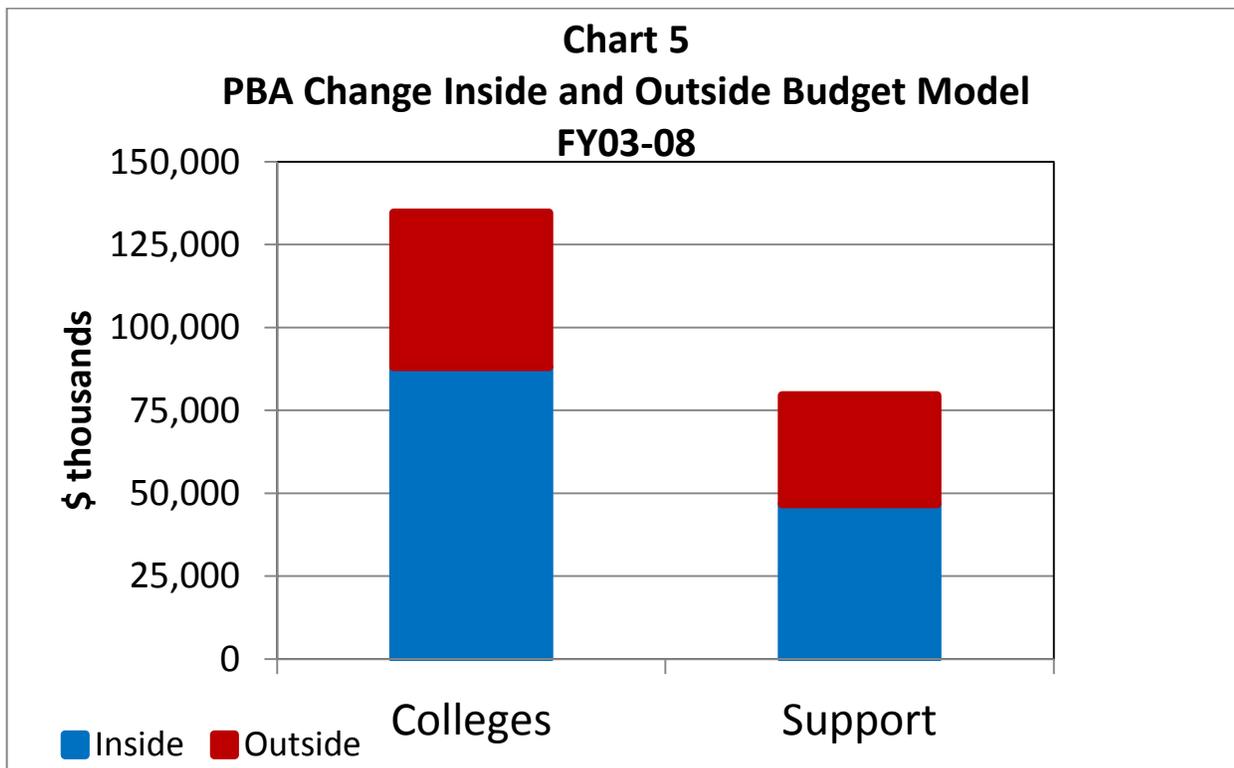
What has been the percentage change in PBA over the last 10 years for colleges and support units? The percentage change includes both components of the budget system – allocations via the budget model and strategic allocations outside of the budget model.

In **Chart 4**, the annual percentage change for support units has generally been higher than colleges every year except in FY2014, even though the slopes of both lines are similar. In FY2004 to FY2006, several large PBA funding adjustments were made to support units that did not impact colleges, including the funding of graduate fellows and Office of Sponsored Programs. This resulted in higher percentage increases in those years. The overall rate of PBA growth has declined since FY2008 due to low tuition rate increases, decreases in SSI and increasing assessments. In FY2014, it was determined that support units would not receive PBA to fund their AMCP from central sources, since the alternative would have been to force colleges to absorb the approximately \$8 million reduction in SSI that year.



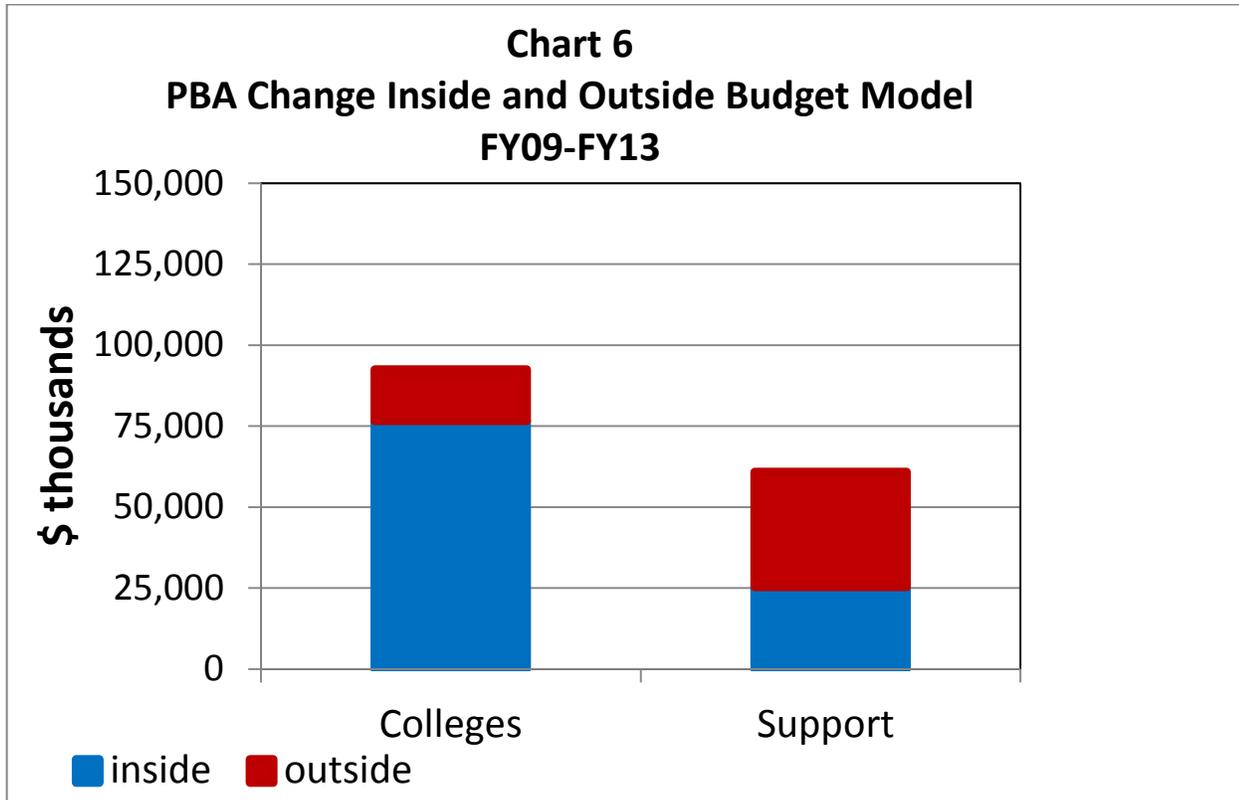
What has been the PBA change via the budget model versus the budget system? Colleges and support units receive funds through the two parts of the budget system (budget model and strategic allocations). The data is analyzed in five year increments. FY2003 – FY2008 represents the first five years after the implementation of the new budget system, and FY2009-FY2013 represents five years immediately after the BSAC report.

In **Chart 5** for FY2003 – FY2008, colleges received \$135M in PBA with about two-thirds from the standard allocations of the budget model and about one-third allocated strategically. Support units received about \$79M in total with slightly more than half allocated strategically.



In **Chart 6** for FY2009 – FY2013, significantly less PBA was distributed overall. Colleges received \$92M, with over 80% allocated through the model and under 20% allocated strategically. Support units received \$61M, with over half allocated strategically.

Although the amount of PBA allocated strategically declined significantly in FY2009 – FY2013, it should be noted that strategic allocations totaling \$96M in cash were distributed to colleges. The decline in the distribution of PBA during this time was a strategic decision to ensure Academic Affairs had sufficient resources for future investments.



What has been the annual revenue to colleges from program, technology and lab fees? The annual revenue to colleges from these fees has almost tripled since FY2009. This revenue comes directly to colleges untaxed and is used directly to support academic programs. In Chart 6, colleges received about \$75M in PBA increase through the budget model, but a substantial component was the revenue from student fees.

Chart 7 displays the annual PBA revenue and growth for college specific fees.

Chart 7
Annual Fee Revenue from Program, Technology and Lab Fees
\$000s

FY	Amount	% change
2009	\$12,994	NA
2010	\$17,581	35%
2011	\$21,762	24%
2012	\$24,474	12%
2013	\$29,156	19%
2014	\$32,391	11%

What has been the trend of the assessments via the university budget model, including the physical plant assessment, research administration assessment and student services assessment?

Chart 8 displays the physical plant assessment trends. The growth rate has leveled out over the last five years. The largest growth component is utility costs. The physical plant assessment is reviewed annually by Senate Fiscal Committee.

Chart 8
Physical Plant Assessment per Assignable Square Foot (ASF)

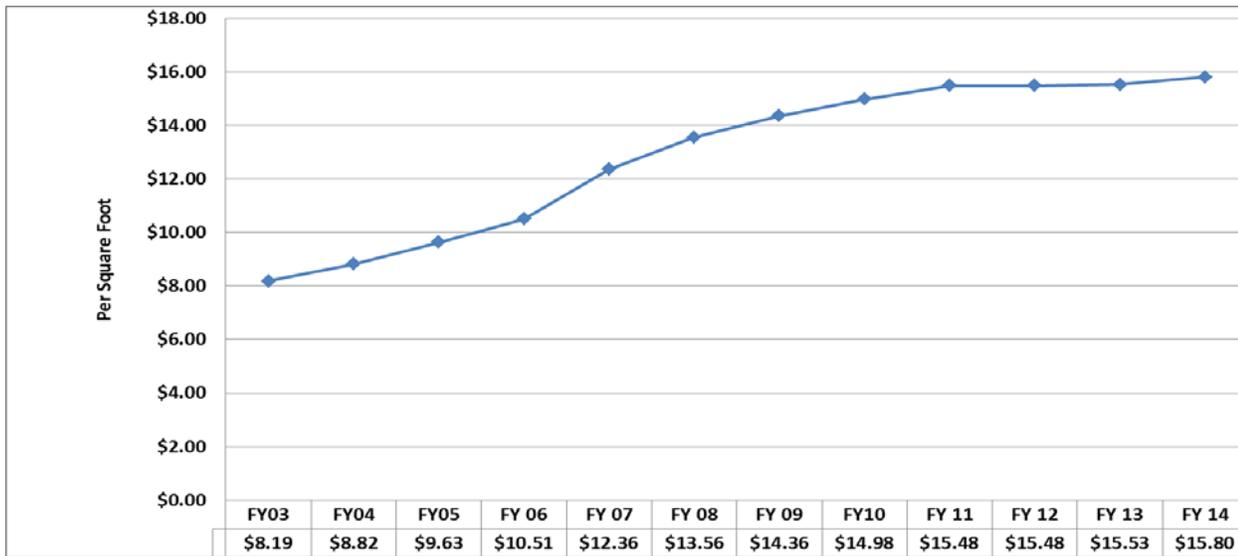


Chart 9 displays the trends in the research administration assessment compared to marginal indirect cost recovery (IDCR) revenue. This assessment is calculated based on each college’s relative percentage share of total research expenditures. Therefore as shown below, even during periods of low marginal change in IDCR, colleges still pay the research administration assessment. In FY2013, the impact of a decline in federal funding is clear. It is also important to note that the actual realized IDCR revenue is significantly less than the federal negotiated rate which was 52.5% for FY2009 – FY2013. The realized rate ranged from 27.2% to 30.2% during the same time period.

Chart 9
Research Administration Assessment compared to the
Indirect Cost Recovery Marginal Change

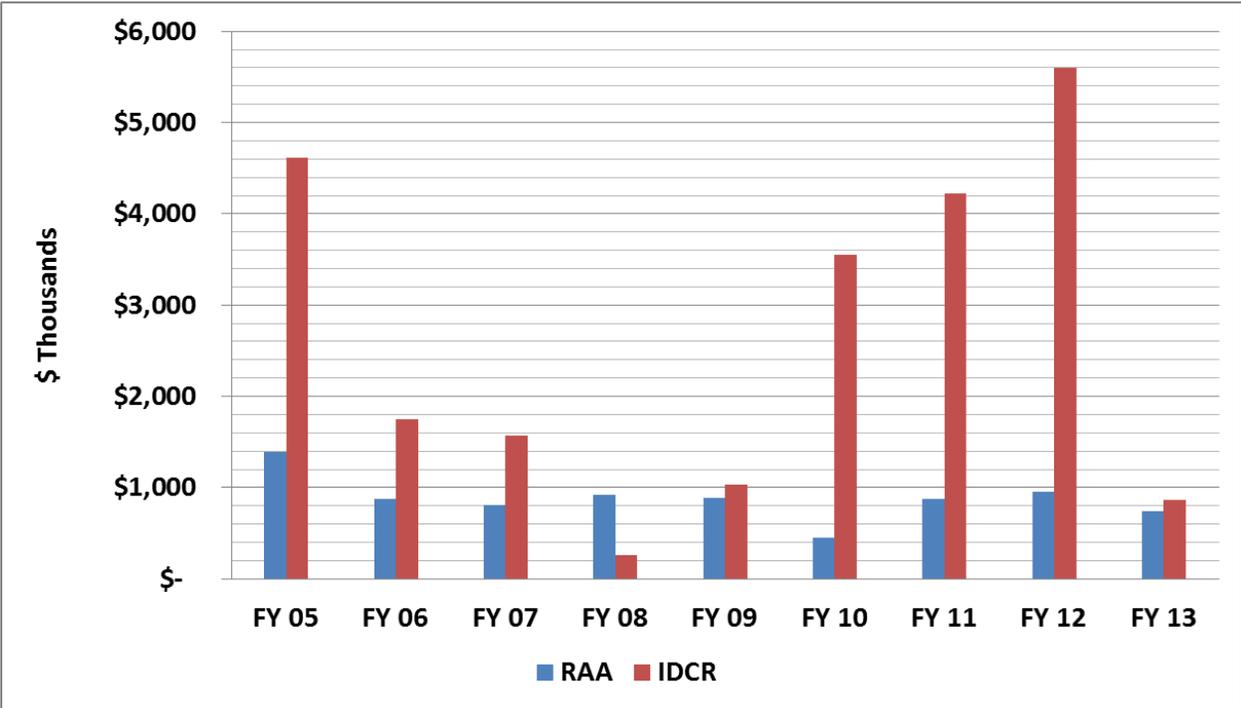


Chart 10 displays the student services assessment trends. This assessment is based on credit hours and has had the most significant impact on colleges' total assessments. The marginal change in FY2009 is low due to the reduction in graduate non-resident fee authorizations with the implementation of post-candidacy credit hour requirements lowered to three credit hours. Beginning in FY2011, the funding for the five year undergraduate enrollment plan, totaling \$26.3M, was added to the student services assessment at an annual marginal cost between \$5.8M and \$6.1M. Beginning in FY2014, the undergraduate enrollment plan was partially funded with central cash, thus, reducing the overall student services assessment.

Chart 10
Marginal Student Services Assessment – All Colleges

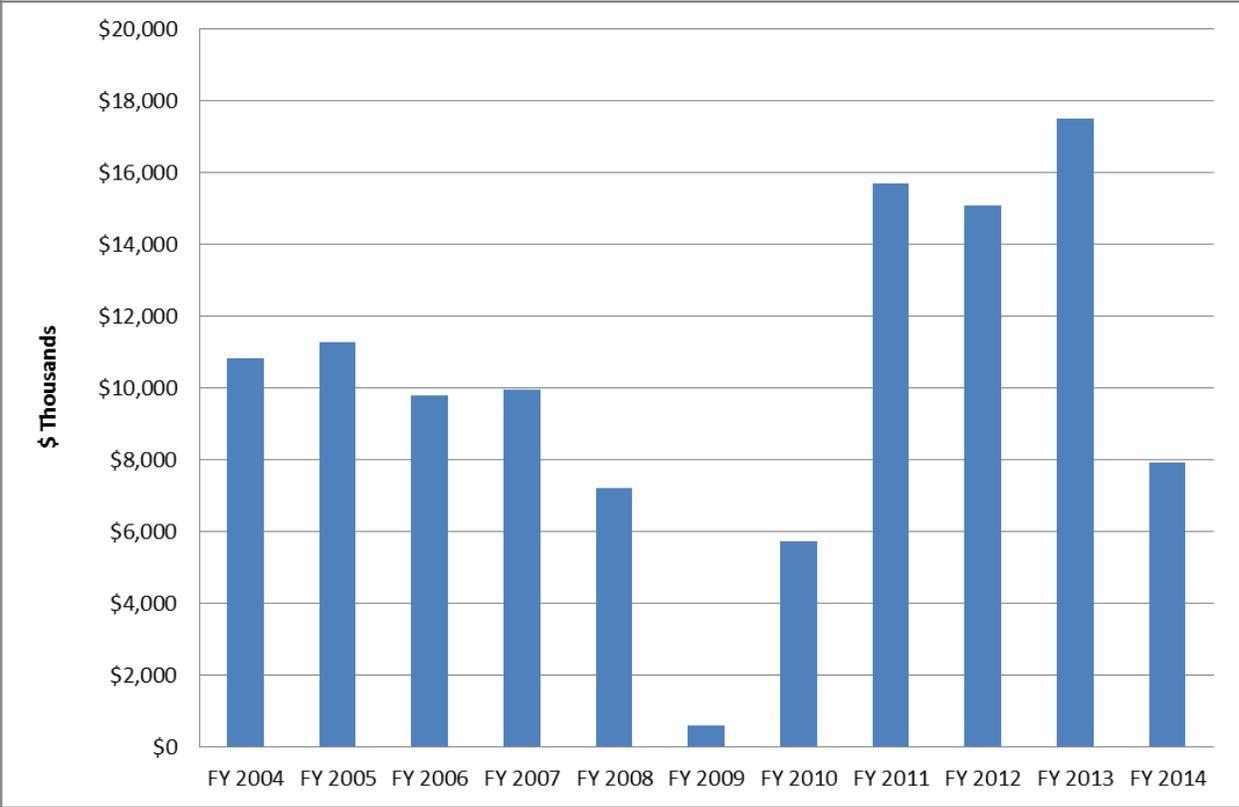


Chart 11 summarizes the central tax and ongoing assessments in the university budget model and the involvement of the Senate Fiscal Committee in the holistic review and oversight of the tax and assessments. Portions of some of the assessments are reviewed annually; however, the overall effect of the tax and assessments is not reviewed comprehensively.

Chart 11 – Budget Model Tax & Assessments

Budget Model Tax and Assessments	Tax/Assessment Description	Review Annually by Senate Fiscal
Central 24% Tax	credit hour subsidy and fee revenue	No
Student Services Assessment 1	undergraduate credit hours (per cr hr)	Partial review
Student Services Assessment 2	graduate credit hours (per cr hr)	Partial review
Student Services Assessment 3	all credit hours (per cr hr)	Partial review
Physical Plant Assessment	non-earnings, non-leased university owned space (per ASF)	Yes
Research Administration Assessment	% of OSP MDTC as of March applied to a RAA marginal budget	No

What has been the overall tax and assessment rate on the total marginal revenue? All of the revenue, taxes and assessments detailed above come together to impact the actual NMR distributed annually to colleges. And from that NMR, colleges fund compensation increases and expenses necessary to carry out their missions. It is important to recognize that a portion of the taxes and assessment is allocated back to colleges and support units strategically. The central tax is comprised of a 19% tax plus a 5% tax to fund the Provost’s reserve, and most of these central funds then are differentially distributed to colleges and support units.

Chart 12 displays the overall tax and assessment rate for colleges. FY 2012 is shown as “*” as the tax and assessment rate exceeded the marginal revenue. The central tax of 24% has not changed since the implementation of the budget model.

**Chart 12
Overall Tax & Assessment Rate (Colleges)
Marginal Tax and Assessments as a % of Marginal Resources**

FY	Rate
FY05	51%
FY06	64%
FY07	61%
FY08	65%
FY09	33%
FY10	41%
FY11	56%
FY12	*
FY13	93%
FY14	67%

Chart 13 displays the total marginal revenue and tax and assessments for FY2005 to FY2014 for all colleges combined. The difference between the two bars each year represents the NMR to the colleges for that year. In FY2012, colleges had more tax and assessments than marginal revenue. As discussed in Section 3, FY2012 was a perfect storm of events with declines in SSI, no undergraduate tuition increase, year 2 of the enrollment plan funding and 1% PBA base reallocation, and a 2% AMCP increase with associated benefit rate increases.

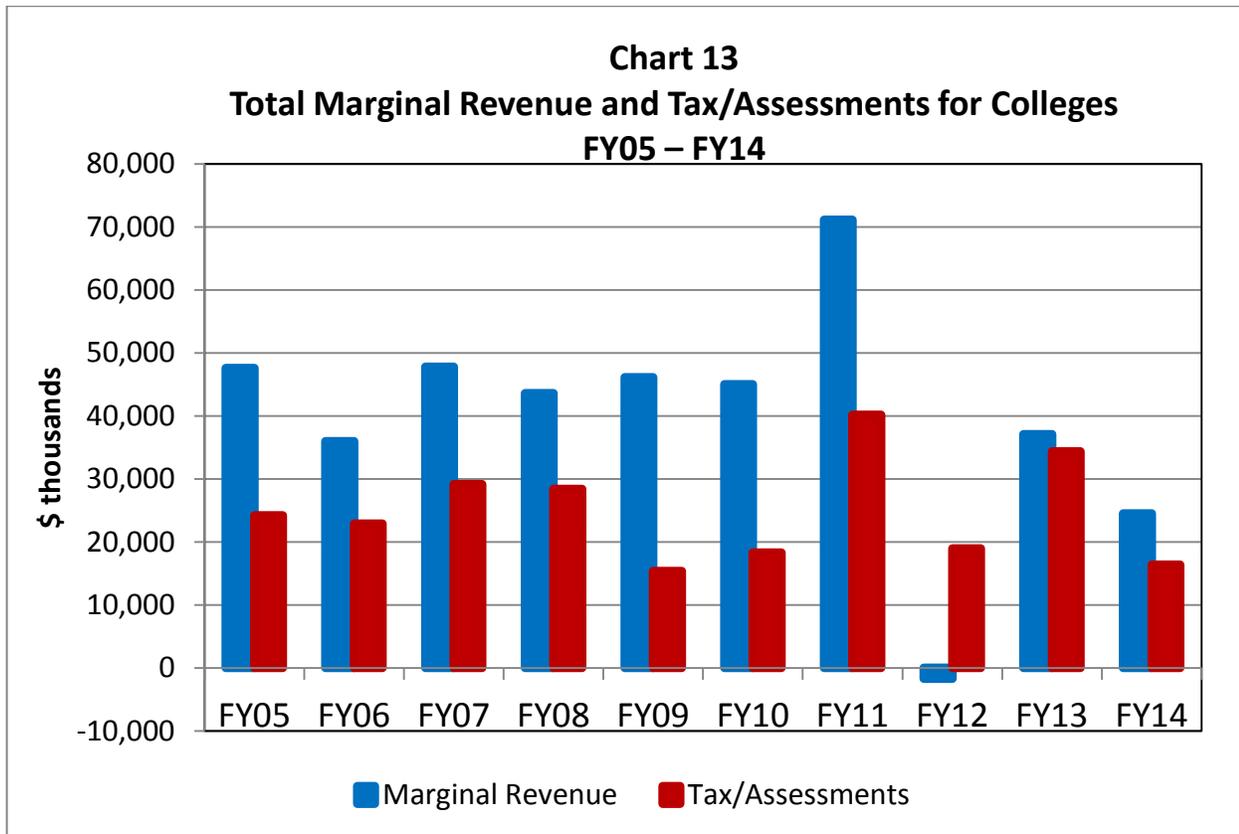


Chart 13A displays the total NMR for FY2005 to FY2014 for all colleges combined. This chart represents the difference between the two bars in chart 13. FY2012 clearly illustrates the perfect storm with only a slow rebounding in growth for FY2013 and FY2014 with NMR of \$2.7M and \$8.2M respectively for all colleges.

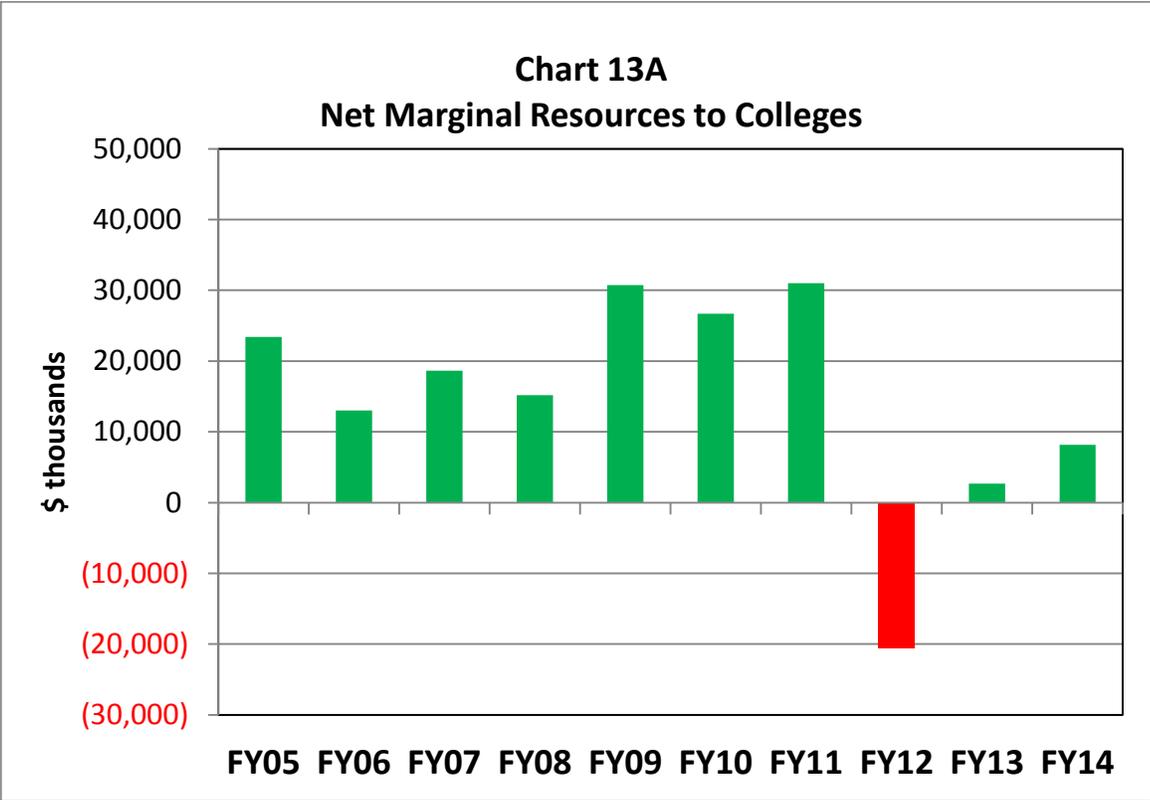


Chart 14 is a subset of Chart 13 that focuses just on the undergraduate marginal revenue and tax and assessments since FY2009. This is the time period when both SSI was constrained and undergraduate tuition rates were frozen 3 out of 7 years plus the funding for the undergraduate enrollment plan began. Again, FY2012 was particularly challenging as the tax and assessments exceeded the revenue. And in FY2013 and FY2014, the difference between the undergraduate revenue and allocations is very small. It should be noted that college specific fees such as program, technology and course fees are not included in the revenue.

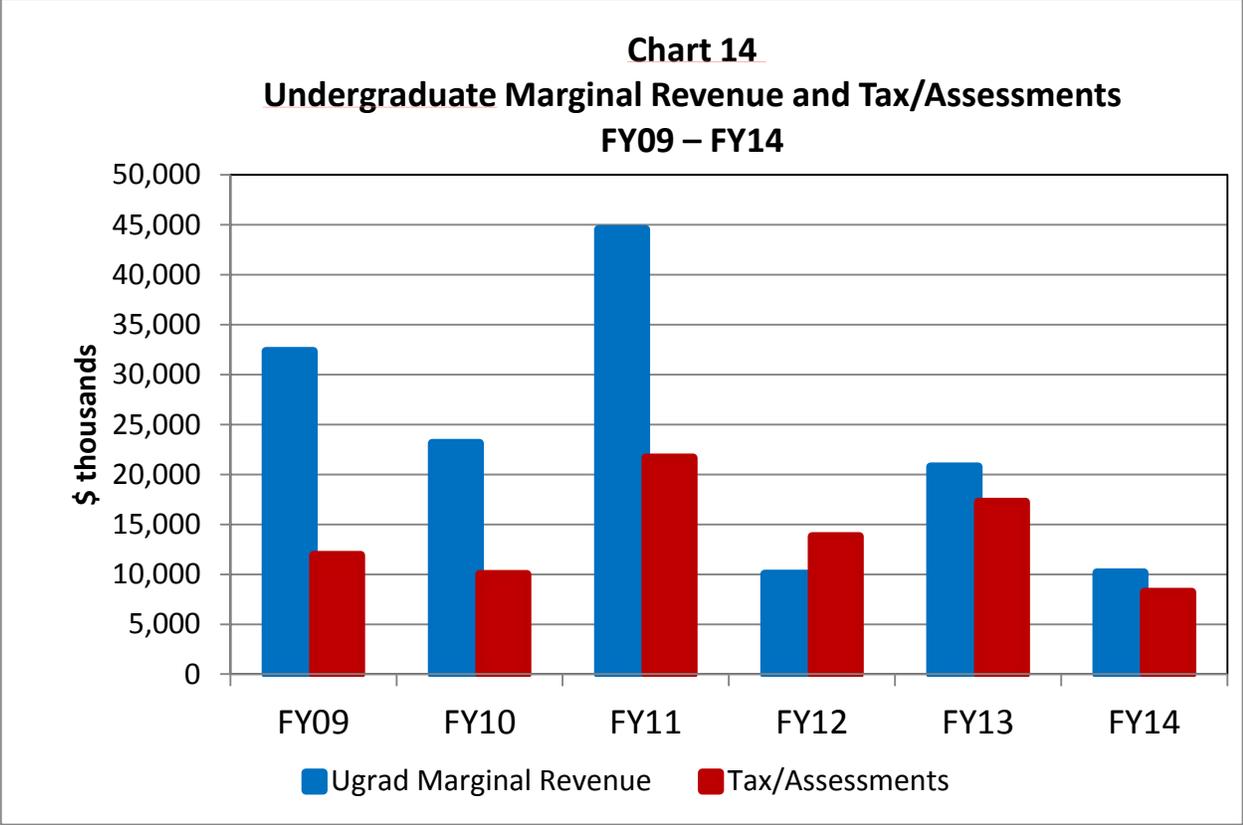
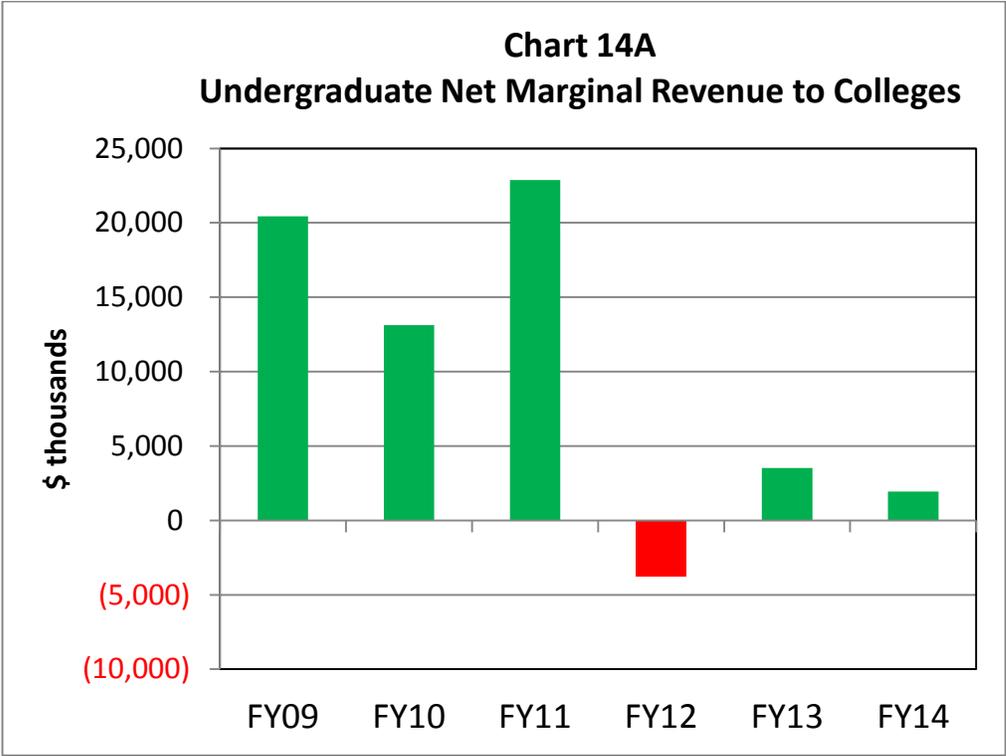


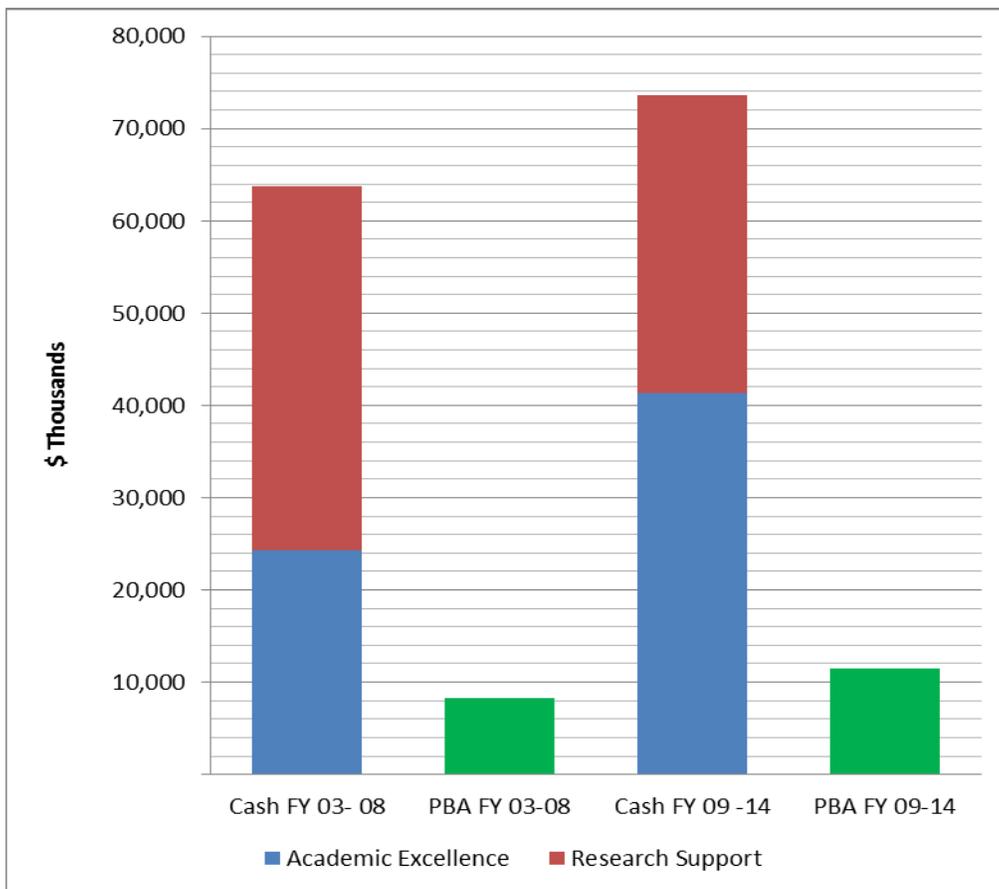
Chart 14A displays the undergraduate NMR for FY2009 to FY2014 for all colleges combined. This chart represents the difference between the two bars in chart 14. The continuing constraints are particularly dramatic with only \$3.5M and \$1.9M in undergraduate NMR distributed in total to all colleges in FY 2013 and FY2014 respectively.



What are the central resources available to the president and provost for strategic investment? The committee also examined the central resources available to the president and provost that comprise the strategic component of the university budget system. The reserves are grouped into four areas. The *president's reserves* are controlled by the president and are primarily funded by the 3% PBA reallocation in FY11 – 13 from support units. The *provost's reserves* are controlled by the provost and are primarily funded by the 3% PBA reallocation in FY11-13, the 5% tax, and a portion of the 19% central tax. The 19% central tax includes a \$2M incremental increase annually in PBA allocated to the provost for strategic investment. The *president/provost/CFO Reserve* is administered by those leaders and is primarily funded by income generated from the university's long-term investment pool. *Other reserves* include the parking endowment, which is currently distributed in accordance with the terms of the endowment, and the various affinity agreements, which are governed by the guidelines as approved by the president and provost.

Chart 15 displays the strategic investments from the reserves into academic excellence and research support. For FY2003-2008, of the total strategic investment, 72% of the cash and 36% of the PBA went directly to support academic excellence and research. In FY2009-FY2014, 70% of the cash and 67% of the PBA supported academic excellence and research.

Chart 15
Strategic Investments in Academic Excellence and Research Support



■ SECTION 5 - CONSULTATION AND SURVEY OF DEANS, SENIOR FISCAL OFFICERS AND DEPARTMENT CHAIRS

As part of its evaluation, and as the BSAC did in 2008, three members of the ad hoc committee met with the deans of the professional colleges, the College of Arts and Sciences, and the health sciences colleges. The committee also sought the input from the 128 department chairs by means of an electronic survey.

Meetings with Deans

Four questions were discussed during the meetings with the deans:

1. What aspects of the budget system most concern you?
2. Please provide examples of where the budget system has impeded your programs and/or services?
3. What aspects of the budget system has been the most helpful to you?
4. Please provide examples where the budget system has aided programs and/or services.

Perceptions of the Budget Model

The discussions were wide-ranging and did not focus exclusively on the questions above. The deans discussed their perceptions of the budget model. The following comments partially summarize the perceptions of the deans. Understandably, while some perceptions are consistent with budget realities, others are indicative that the budget structure and processes are not always fully appreciated. The deans' concerns guide some of our recommendations regarding training and transparency addressed in Section 8 – Recommendations.

- In general, it was understood that the budget model is based on enrollment and research change and that growth and declines in enrollment are buffered.
- The budget model allows for some degree of strategic planning, and colleges can focus on the revenue streams that they can control.
- Larger colleges felt it was advantageous that the college is the unit of budgeting, rather than departments, understanding that high enrollment, low cost programs can balance out low enrollment, high cost programs that are strategically important.
- Concern was expressed about the budget results in FY2012 due to unexpected external events and that the model was not designed to respond immediately to environmental impacts. *(Note: strategic allocations via the budget system have been used to buffer some impacts on colleges.)*
- Differing viewpoints were expressed, including that the model treats all colleges equally, the model favors undergraduate programs, and much of the university budget is outside the model. These perceptions appear to be based on individual colleges' perceptions.
- Deans expressed the desire for multi-year projections of central expenditures and revenues to facilitate strategic planning along with the need for a review of the central taxes and assessments and more transparency of the use of those taxes and assessments.

Survey of Deans and Senior Fiscal Officers

The committee also requested, from the deans and their senior fiscal officers, specific information about the budgeting process in their colleges. Of the 14 colleges, 5 colleges responded for a response rate of 36%. The questions and summary of responses are below:

1. Does your college communicate the structure and process of the budget model to the department level?
2. Does your college disseminate college budget model data to the departments?

3. Does your college have a financial advisory committee or group to discuss financial decisions and practices of your college?
4. Can you briefly describe the financial/budgeting process in your college?
5. How do you allocate funds to the departments?
6. What process is used in determining departmental allocations?
7. Who is involved in making budgetary decisions regarding departmental allocations?

Summary of College Responses

All respondents confirmed that their college shares some information about the budget model with departments and provides departments with data, although we did not request specifics of the data provided. Four of the five colleges have some type of financial advisory committee such as their executive committee, leadership team or budget committee. Generally, the departments present their college with requests (faculty lines, enrollment support, capital requests) that are then discussed at the college level. The department allocations are decided by college leadership. In all cases, the marginal funds received from the university's budget model are first used to fund compensation increases including AMCP and benefits. The remaining revenue is allocated according to strategic plans.

Survey of Department Chairs

The survey sent out to the department chairs included six questions:

1. Does your college communicate the structure and process of the budget model to the department level?
2. Does your college disseminate college budget model data to your department?
3. Does your department have a financial advisory committee or group to discuss financial decisions and practices of the college and of your department?
4. Are you or is your department somehow involved in financial decision making at the college level?
5. Can you briefly describe the financial/budgeting process in your department?
6. What improvements would you like to see with regard to the structure and process of the budget model?

Summary of Department Responses

The response rate was very low for the department survey (15/128 for 12% response rate). It is difficult to provide generalized statements about the responses due to the low response rate, and it is not possible to determine why the response rate was so low. Ten out of 15 department chairs indicated that their college provided information about the structure and process of the budget model. However, three of these qualified this response by mentioning that information was provided "to some degree." One department chair observed that information about the structure of the budget model was provided, but little with regard to the process. Seven out of 15 department chairs agreed that their college provided budget model data. Only three department chairs indicated that they have a financial advisory committee, and only two indicated involvement in financial decision making at the college level. In most cases, the department chair and the department financial manager made the department's budget decisions. With regard to the last question, the department chairs mentioned the desire for more transparency about how the budget model operates at the university level, translates into the college level, and how they can budget in the face of external uncertainties (e.g., decreasing SSI; decreasing external funding from NIH, NSF, etc.; unclear expectations regarding POM and other 'central' needs).

■ SECTION 6 - EVALUATION OF RECOMMENDATIONS FROM 2008 BSAC REPORT

The BSAC report from 2008 made six recommendations. The Ad Hoc Budget Committee reviewed each recommendation to determine if it had been implemented and evaluated the outcome. The results are discussed below.

BSAC Recommendation 1 – All university resources should be used to promote academic and research excellence.

Recommendation 1 focuses on strategic planning across and within all units of the university and emphasizes that those decisions should be strategic in nature rather than strictly determined by the budget model. Over the last five years, the university has focused on an annual strategic planning process. As the strategic planning process is refocused with the changes in university leadership, it is critical that emphasis continue on transparency and inclusion at all levels, from departments, across colleges and up to university leadership.

BSAC Recommendation 2 – Resources and responsibility for achieving the goals set forth in the Academic Plan must be shared by all offices of the university, both vertically and horizontally.

Recommendation 2 focuses on ensuring that critical colleges and departments receive the resources to achieve the goals of the Academic Plan even if the resources generated through the budget model are not sufficient. We were not able to assess the extent to which this is occurring.

On the positive side, significant strategic investments have been made, particularly in academic and research excellence. Chart 15 in section 4 displays the strategic investments in colleges to promote academic and research excellence, totaling \$74M in cash and \$12M in PBA for FY2009 - FY2014. This support significantly increased from FY2003 – FY2008, when \$64M in cash and \$8M in PBA was distributed. Looking forward, significant investments will continue with the Discovery Themes program. It will become increasingly important to assess the success of these investments.

However, even with the strategic investments, the colleges were fiscally challenged in the last five years, especially since FY2012. Charts 13 and 14 specifically illustrate the negative impact of declining marginal resources and high marginal assessments.

BSAC Recommendation 3 – The entire budget of the university should be exploited to secure new strategic investment funds of at least \$10M annually of cash to drive further quality improvements.

The university has developed new strategic investment funds, including the provost's and president's reserves that increased by the 3% PBA reallocation generating \$27.8M in total, \$19.7M and \$8.1M respectively, for the provost's and president's reserves. The asset monetization of parking generates \$23M annually, with over \$9M annually to be directed to discovery themes. The affinity agreements generate \$14M annually, and all follow a proscribed funding model for distribution of the revenue streams. These new revenue streams far exceed the \$10M annually of cash in the BSAC recommendation. These funds will allow the university to move forward with investments in discovery themes, faculty initiatives, student scholarship support, and other academic and research initiatives that would not have been possible if the affinity agreements and asset monetization had not occurred.

BSAC Recommendation 4 – Deans should work with department chairs, with each other, and with the Provost to develop strategies to reward academic quality and to promote trans-institutional interdisciplinary research.

This BSAC recommendation emphasized the importance of interdisciplinary research and programs to the success of the university in obtaining research funding and attracting both new faculty and

graduate students. It was noted that a decentralized budget model could hinder these efforts. The discovery themes initiative is designed to foster interdisciplinary research and academic programs, particularly with the hiring of new faculty. The leadership of the discovery themes crosses colleges, Office of Research and Office of Academic Affairs. As the discovery themes move forward, transparency, particularly with financial and budget data, will be critical and should be shared throughout the university.

BSAC Recommendation 5 – Systematically review on a regular basis the efficiency of central administration offices, as well as centers, programs and institutes that fall within their jurisdiction.

The university has implemented a review process for central administration offices; however, reviews of centers, programs and institutes have not occurred. The Central Services Subcommittee (CSS) of Senate Fiscal Committee (SFC) conducts these cyclical reviews. Because the committee focused efforts on restructuring the review process in FY2011, no review took place. To date, CSS has completed five reviews and a sixth is in progress. In chronological order, they are:

FY 08 & FY 09	Office of Research
FY 10	Department of Public Safety
FY 11	Process under review; no reviews scheduled
FY 12	University Libraries
FY 13	Office of the Chief Information Officer (OCIO) and Office of Student Life
FY 14	Facilities Operations and Development (FOD)

CSS recommendations focus on operational efficiencies, communication strategies, financial planning, enterprise risk review, resource allocation, generation of alternate revenue streams, debt management and human resource planning.

BSAC Recommendation 6 – The Provost should use current committees or establish working groups to develop processes whereby we can gather information on the effectiveness of our GEC instruction, the effectiveness of our majors and minors, and on student outcomes.

The Council on Academic Affairs (CAA) established a university level advisory committee for the general education curriculum. The committee evaluates the general education program annually, including analyzing trends, monitoring new courses, and assessing the outcomes. The Office of Academic Affairs also conducts academic program reviews, including a self-study developed by the unit and a review by an external review team. Detailed information can be found at <http://oaa.osu.edu/programreview.html>.

Funding Possibilities - In addition to the six recommendations, the BSAC also presented funding options to generate additional resources. The options for revenue generation within the budget model were:

- Differential tuition
- Program, lab and learning technology fees
- Charge for credit hours over a maximal threshold, such as 18 or 20 hours

All three of these options have been implemented. Differential tuition has been used to generate additional revenue for colleges with professional graduate programs. These colleges are able to charge tuition based on external market conditions. Program, lab and learning technology fees have all increased significantly, since FY2008, as illustrated in Chart 9. We support the work of SFC to review these fees to ensure the fees are invested appropriately in academic programs. It is critical to strike the right balance between implementing these fees to support additional costs not funded from tuition or SSI and using

these fees to circumvent the low undergraduate tuition increases. Beginning FY2013, students enrolled in more than 18 credit hours per semester are assessed for those additional credits. And also beginning in FY2013, international undergraduate students are assessed an additional \$500 per semester to fund additional resources for those students.

Options presented for revenue generation outside the budget model were:

- Assessment on athletic revenues
- Assessment on clinical revenues
- Raise the payout on endowment revenues; increase the amount of unrestricted endowment funds

Athletics already provides significant revenues to the university, and is only 1 of a few college athletic programs in the country that is self-supporting. For example, Athletics funds grant-in-aid for student athletes, overhead for university services provided to Athletics, and student support services. Of particular note is the funding for the renovation of Thompson Library with Athletics committing \$9M over 9 years toward the renovation.

Although the payout on endowment revenues has remained relatively constant over time at a conservative level of 4 – 4.5%, the university has a revenue stream from earnings on the long term investment pool called the “Academic Strategic Venture Capital fund”. It generates \$55M annually in cash for strategic investment, assuming an 8% annual return on investment.

In addition, the BSAC stated “finally, only after all other options have been exhausted should taxes be raised on colleges”.

As illustrated in Chart 12, the overall tax and assessment rate has increased dramatically since FY2008. Also, the total tax and assessment rate is not entirely transparent. It is widely known that the central tax rate is 24% and has not changed over time; however, it is much less widely known what the overall tax and assessment rate is and that it fluctuates annually. Given that the assessments fluctuate annually, and are not reviewed comprehensively, a series of isolated decisions have led to a high assessment rate.

■ SECTION 7 – OBSERVATIONS, RISKS, AND OPPORTUNITIES

Observations

The committee discussed extensively the guiding principles and validity of the current model. In summary, the committee believes the current budget model is fundamentally sound. The revenues flow appropriately, and it is appropriate that taxes/allocations pay for centrally-provided services. However, over the last several years, unintended consequences have resulted in a commonly held viewpoint that the model is flawed. Rather than the model being flawed, the committee believes that a lack of transparency, insufficient long-term projections and modeling, and decisions being made without sufficient holistic data analysis of the impact on colleges all contributed to a perception that the budget model does not work.

The committee also discussed the appropriate unit for budgetary responsibility, specifically the college or department. The committee came to a consensus that the college should remain the unit for budgetary responsibility; however, it is critical to have budget information disseminated to the department level as department chairs should be routinely informed and engaged in discussions about the budget process.

The committee agreed that the totality of all assessments is not easily transparent. In addition to the assessments in the model, colleges have had a number of assessments outside of the model, including

assessments for OSU Buckeye Box and SIS implementation. Additional charges have been implemented for the recentralization of services, including background checks and FMLA (Family Medical Leave Act). All of these assessments combined negatively to impact the colleges' budgets.

Because the budget of regional campuses is through a separate funding mechanism than the budget model, regional campuses budgets are not addressed in this report. The OBOR subsidy funding for regional campuses is changing, and the funding of regional campuses is currently under review by SFC.

Risks

State Funding - The OBOR SSI allocation model changes pose a risk to the university. The current model developed by OBOR emphasizes at-risk and non-traditional students. The university cannot react quickly to the changing priorities from the state, and the priorities may not converge with the priorities of the university. Recently, we have seen that funding can shift quite dramatically annually among universities. The changes to the model were intended to create incentives and reward quality. We believe there are unintended consequences to the OBOR model that have and will continue to have a negative impact on the university. For example, when an institution increases quality in the form of improved graduation rates, they receive additional funds through the model. This was the intended outcome. However, given that the revenue available to higher education is a fixed amount, the revenue flowing to institutions with already strong graduation rates is reduced. So, universities such as OSU and Miami of Ohio are negatively impacted. Also, the OBOR model now rewards on-line learning programs. The university is investing in e-learning opportunities, but other universities, such as Ohio University, have increased their enrollment in on-line programs significantly.

Capital Investment - The university is near maximum debt capacity with the capital investment in the new hospital and the north campus residential housing, limiting the ability to fund the construction of new academic buildings and renovation of current academic buildings. The ability to recover the cost of the North Residential District is a risk. To fully fund the bond payments using revenue generated through housing fees and based on current operating expense levels, the room rates are projected to increase 6% annually for the next 10 years. Increasing housing rates at this level limits the ability to increase tuition which in turn limits resources flowing to the colleges via the budget model.

Second Year Transformational Experience Program (STEP) – STEP is currently funded on cash rather than PBA with an estimated ongoing cost when fully implemented of \$15M.

Wexner Medical Center and Healthcare Reform - An even greater risk to the university is associated with the medical center. Because approximately half of the university revenues are generated by the medical center, if the medical center were to experience financial difficulties for any reason, including external forces such as healthcare reform or Medicaid changes, the university would be negatively impacted. For example, the health sciences colleges rely on the transfer of operating and capital funds from the medical center to fund a portion of their academic programs. The transfer grew from \$87M in FY2011 to \$124M in FY2013. The majority of the support goes to the College of Medicine with a small portion of the funding, less than \$3M, distributed among the other health sciences colleges. Plans are being developed now to significantly reduce the hospital transfer over a period of a few years.

Changing Demographics - The changing demographics of the faculty is a risk. Over 40% of the faculty are retirement eligible in the next five years, and STRS retirement changes slated to take place in summer 2015 could result in a large number of faculty retirements.

Federal Research Funding – As discussed and illustrated in Section 3, federal research funding has been relatively flat in the last five years excluding the one-time infusion of ARRA funding. This is expected to continue with the constraints on the federal budget.

Unfunded pension liabilities – The Governmental Accounting Standards Board (GASB) has issued a new accounting standard that will require the university to recognize a pro-rata share of the unfunded pension liabilities of OPERS and STRS-Ohio in the university's financial reports, starting in FY2015. In addition, the debt rating agencies have incorporated these unfunded pension liabilities into their credit analyses of the university. Although these pension liabilities do not represent legal claims on the university's resources, they will negatively impact key university financial ratios and will need to be clearly explained to our stakeholders.

Long Term Planning – Decisions have been made with an insufficient comprehensive analysis of the long-term effects on the colleges.

Opportunities

Enrollment Plan - The enrollment plan presents the university with a tremendous opportunity to invest in recruiting and retaining the highest quality students and providing significant scholarship support to those students. However, the investment has not been without risk. The cost of the enrollment plan has been borne predominantly by colleges via the student services assessment during a time of declining SSI and low tuition growth.

Alternative Revenue Streams - Even with the challenges of the economic recession, the university has developed alternative revenue streams that it did not have previously which will result in significant investment in academic and research excellence.

SECTION 8 - RECOMMENDATIONS

Overarching Recommendation

1. *The guiding principles and design of the university budget model are fundamentally sound. The committee recommends the budget model should be retained. To fully take advantage of the budget model, central university decisions (e.g., about tuition increases and AMCP) must be made in a coordinated, holistic, transparent manner with the impact of decisions on colleges and support units modeled prior to the decisions being finalized.*

The remaining recommendations address three areas: the annual planning and review process, the budget model, and management reporting and training.

Annual Planning and Review Process

2. *The Senate Fiscal Committee (SFC) should comprehensively review annually the tax and all assessments in the budget model (for example, student services, research administration, and physical plant assessments) and other assessments outside of the model, both cash and PBA based. Multi-year investment decisions (i.e. five year enrollment plan) should also be evaluated annually to determine if adjustments should be made. SFC should be given sufficient time to conduct an in-depth analysis and review including assessing unintended consequences.*
3. *A robust multi-year projection model should be developed that can be used by colleges to model budget scenarios based on a variety of inputs. A projection model will greatly aid units in multi-year strategic planning.*

4. *The review process for central administration offices should be supplemented by a follow-up review.* The Central Services Subcommittee (CSS) of Senate Fiscal Committee has invested significant time in these reviews which resulted in robust recommendations. A follow-up report should be completed annually on the outcomes of the recommendations specifically examining if the recommendations were implemented and if not, why?
5. *Three institutional risks should be carefully evaluated and monitored to ensure their impact is understood, and strategic decisions should be made to minimize negative effects on the budget.* The university risk management program has identified a number of key risks. The committee has focused on identifying three financial risks which could impact the model because they could divert funding from other initiatives or potentially be included in an assessment. Strategic decisions need to be made to ensure the risks are minimized for the budget model. The risks in priority order are: 1) OSU Wexner Medical Center and the changing healthcare environment, 2) the cost of the north residential housing, and 3) the ongoing cost of STEP.

Budget Model

6. *Re-evaluate the subsidy allocation methodology when the OBOR methodology is finalized.* The committee recommends not considering the OBOR methodology until all changes are clearly understood. It is critical that the impacts of changes in the OBOR methodology are understood and modeled by the university. The university should also work proactively and collaboratively with the OBOR to develop and evaluate new SSI allocation methodologies to avoid unintended consequences (e.g. graduation of lesser prepared students) and possible gaming of the system.
7. *Limit the assessments outside of the budget model.* All assessments, whether one-time or on-going, should be evaluated for their financial impact on units prior to finalizing the assessment, including the impact of multiple changes occurring concurrently. A process should be developed and implemented to compile and review all assessments, both inside and outside the budget model and including both cash and PBA assessments.
8. *A “re-basing” analysis should be completed for all colleges.* The analysis and financial modeling should be done to determine if multi-year rebasing of colleges is indicated. The financial analysis should examine the history and projections for all colleges and include a comprehensive examination of all sources and uses in colleges, not just those in the budget model.

Management Reporting and Training

9. *Colleges should have a college level committee for fiscal and budget issues with adequate department level faculty and staff representation.* This could be a committee(s) that is already in place serving multiple purposes, such as an executive committee, or a specific budget committee entirely focused on the budget for the college. The committee can assist the college administration in planning by providing grassroots information, transmitting timely concerns, and conveying feedback. The presence of a committee may also help provide continuity in event of senior administrative turnover in a unit.
10. *To increase transparency, fiscal presentations by college leadership, such as the dean and senior fiscal officer, to faculty and staff are desirable and expected.* The committee recognizes and stresses the need for simple and transparent financial disclosures. At the same time, it is cognizant that arrangements to achieve this goal can vary across colleges given their different sizes and structures. Colleges should provide comprehensive annual and intertemporal fiscal data at both the college and department level to faculty and staff. The quantitative data can be complemented by an accompanying qualitative dean’s

report made available to all faculty and staff. Such a report must link the college's fiscal resources and use of net marginal resources, whether increasing or decreasing, with planned strategic initiatives.

11. *Financial training for unit leaders, including deans, associate deans, department chairs, and senior fiscal officers, should be implemented.* Understanding the university budget model, modeling tools and financial reports available is critical to effectively lead a unit. Given changes in leadership in colleges over time, ongoing training is critical. This recommendation is based on the surveys and discussions with deans, department chairs and senior fiscal officers.
12. *Develop and maintain centralized financial reports that are easily accessible and provide multi-year data by college and department.* Current examples are University Profiles, Sources and Uses, and the budget restructuring database. Reports should be at both the college and department level, include comparisons across colleges, include NMR at the department level, and include both historical trends and projections. Training and documentation on the use and interpretation of these reports is also critical.
13. *The Senate Fiscal Committee should review the recommendations above in early FY2016 to determine the status of the implementation of the recommendations.* The progress should be monitored and be ongoing to ensure these recommendations are implemented well before the next five year review of the budget.