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Faculty Budget Priority Committee Annual Report 2012

Faculty Budget Priority Committee

Faculty Budget Priorities Committee Year-end Report

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The Faculty Budget Priority Committee is charged examining all fiscal affairs of the University and recommending fiscal priorities to the Faculty Senate and University administration. During the course of the 2011-2012 academic year the committee met regularly (usually twice a month) to review and comment on the University's new budget model (Mission Driven Allocation, MDA) as it was being developed. The committee also reviewed the University's current budget. This report is intended to primarily be a summary of committee's discussions and recommendations regarding the University's new budget model.

In brief, the MDA budget model should be a significant improvement over the University's current budget model in terms of its transparency at all levels. The manner in which funds are distributed (and collected) in the model in its current state is more closely linked to promoting efficiency than effectiveness. The committee has identified a number of features of the MDA model that may incentivize undesired behaviors. MDA in its current state will rely heavily upon an expectation of good leadership both on the part of the central administration, the MDA's governing committees and the Faculty Senate. Administrators must be committed to the University's stated mission and the success of our students. Four committees that will oversee the budget, evaluate funding proposals and the operation of cost centers, and resolve budget disputes must have strong faculty representation. The Faculty Senate must be vigilant in its role as guardian of the curriculum and discourage colleges from creating courses for their majors that would be better taught by content-experts in other colleges.

What follows is a summary of the committee's discussions and observations during the course of its deliberations.

<u>MDA Goals</u>

- Increase budgeting transparency
- Expect revenue to exceed cost where possible (in "responsibility centers") – by as much as reasonably possible
  - Increase efficiency in colleges
  - Increase entrepreneurial activity in colleges
  - Generate strategic initiative funds
- Increase independence of colleges
- Increase efficiency in non-academic units

Primary Question and Comments from the Committee:

- How do academic quality and other mission specific goals dovetail with this model?
- MDA has the potential to achieve its stated goals, but an excessive focus on profit could cause it to work against the University's mission as in the following examples:
  - Over-incentivized cost cutting could lead to reduced quality (over reliance upon adjunct faculty, larger class sizes, etc.)
  - Over-incentivized revenue enhancement could hurt affordability or increase the use of resources on non-academic (or barely-academic) activities that generate profit.
  - Over-incentivized short-term financial result could reduce long-term sustainability (ex. – will failing students be given passing grades to prevent the elimination of a program, which then harms the University's reputation and long-term ability to attract high quality students, or students in general, in later years?).
- The committee emphasized throughout its discussions with the administration that the budget model needed to be closely tied to the University's mission. The change in the model's name (from "Responsibility Centered Management" to "Mission Driven Allocation") is an acknowledgement of that need but tangible changes to the parameters of the model itself have not yet been made (though a few are being explored by a work group).

Key Specific issues:

- Although MDA can't be implemented without budget transparency, MDA is not the only budget model that would provide budget transparency. The University's current budget model (a traditional base budget model) does not lend itself to transparency except at the very highest and very lowest levels.

- The high strategic initiatives contribution (16% of instructional revenue) could interfere with the colleges' pursuit one of the stated advantages of MDA: to be able to invest in new initiatives/entrepreneurial activities on their own (increased college independence). They will effectively need approval from the Provost for these activities via subvention negotiations in that colleges should expect to be in a deficit each year that will be reconciled by the use of subvention funds. A substantial majority of the subvention funds (as much as 13 to 14% of the University's budget) will be used in such a way.
- Some colleges are simply in a better position (e.g. CEHS and CoLA) to generate net revenue than others (e.g. CECS and SoPP). Thus, the percent of each college's revenues that can be contributed to the strategic initiatives fund is bound to differ in the long run. The central administration should consider setting realistic differential strategic initiatives contribution rates for the colleges.
- The higher the percentage of instructional revenue that needs to go to the strategic initiatives fund, the greater the likelihood that undesirable outcomes will occur. The search for further profits could elicit the kinds of mission incompatible problems alluded to above, such as:
    - Excessive use of adjunct faculty simply to reduce costs
    - Development of low quality – high revenue academic programs that increase profit in the short-run but decrease profit in the long-run by diminishing WSU's reputation
    - Excessive competition between colleges in the form of colleges teaching courses outside their areas of expertise primarily for the associated revenue stream or the expenditure of college funds to draw students who are already at WSU away from one college to another
    - Excessive growth of class sizes
- MDA diverts instructional revenues from the colleges earning them to subsidize activities conducted at other colleges (such as funded research). While this may have the benefit of encouraging desired outcomes (such as more funded research), the administration needs to keep track of the budgetary distortions created by these revenue diversions in order to understand which departments might actually be covering their costs before some of their funds are diverted.
- The diversion of 25% of tuition from the college teaching a course to the college of each student's major may encourage excessive use of adjuncts to teach classes predominantly serving other college's students
- The diversion of 40% of SSI funding from colleges that don't generate much funded research to colleges that do will encourage more effort to get research grants, but will just hurt colleges with little funding opportunities.
- The faculty of each college should consider either setting up a committee similar to the Faculty Budget Priority Committee to review MDA budgets at the college level or include those duties in the charge of an existing committee as colleges review their bylaws. The chair of such a college-level committee would be an excellent representative of their college to the Faculty Budget Priority Committee.

The Committee's Questions and Comments on Each of the Major Features of the MDA Budget Model

Strategic Initiatives Fund

- Creates a pool of resources to support academic initiatives (currently proposed to be 16% of the instructional budget – roughly $48 Million)
- By creating a cost/responsibility that most colleges can't meet with their current budgets, an incentive is created for colleges to generate more profit.
    - Colleges may increase cost efficiency (cost reductions that don't impact quality or quantity served)
    - Colleges may expand existing programs or pursue new programs that increase revenue net of cost

Questions/Issues

- This may be the most important part of MDA because it appears to have the most potential to induce desired or undesired activity
- The current plan is to have colleges face a tax (strategic initiative contribution) they can't afford – at least not in the first few years – then negotiate with the provost to receive the as much of the shortfall back as possible (subvention). On its surface, this does not appear to allow the colleges to pursue one of the stated advantages of MDA: to be able to invest in new initiatives/entrepreneurial activities on their own. They will effectively need approval from the Provost for these activities via the subvention negotiations in a way that is not very different from the current budgeting process.
- It appears that in practice, colleges will not be put in a deep financial hole for a few years as MDA is first implemented because many of the shortfalls will be forgiven through subvention. What about after that if a

- Will the strategic initiatives fund be used to support non-academic initiatives?
- Will MDA incentivize that costs be cut in a manner that reduces quality such as:
  - Excessive use of non-research faculty and adjuncts
  - Class size increases that harm instructional quality
  - Reduced research support funding by college deans?
- Will low-quality low-cost programs be developed just to enhance profit for a college?
- Will college level academic resources be allocated to non-academic activities just to turn a profit for the strategic initiatives pool?
- Is 16% ($48 Million) the right level for this contribution? Of that approximately $48M all but $2 to $4M will be returned to colleges as subvention leaving a relatively small amount for strategic initiatives.
- What about programs or expansions that cover all costs but not all of the strategic initiatives contribution. In other words, these increase profit (net revenue) to the university, but decrease profit to their college because they cover all costs except a portion of the 16% tax? Eliminating these programs would paradoxically reduce the university's net revenue.
- What about programs that increase profit to the university but not to their college because 40% of the associated SSI funds are redirected to colleges that do more grant supported research? Again, eliminating these programs would paradoxically reduce the university's net revenue.
- Will MDA encourage excessive silo behavior so colleges or departments can maximize their profit, or will it encourage more collaboration?

Possible Alternatives:

- Make the tax smaller than 16%
- Tax the profit rather than the revenue and reduce the tax rate as profit grows or find some other way to share the profit with the colleges before the 16% threshold is met
- Set tax rates for each college based on reasonable expectations for each college. Some colleges just face higher costs and their revenue options are constrained by the tuition policies.
- Rather than starting with the full tax which most colleges will request back in subvention negotiations, start with a manageable tax that is increased from year to year based on reasonable expectations
- Reduce the tax in response to satisfaction of effectiveness/quality goals. The committee has worked on finding a way to hardwire this in to the budget model but has not been able to find an approach that did not also have a potential to incentivize undesired behaviors.

All of the above could reduce the likelihood that colleges would pursue activities that hamper our ability to meet the University's mission in order to satisfy arbitrary financial goals. It is important to remember that economic principles point out that each incremental 1% increase in the strategic initiatives fund contribution requirement will be progressively less beneficial to the University and become increasingly costly to individual colleges in terms of forgone opportunities and/or reduced program quality.

- Can we identify useful ways for colleges to be rewarded for effectiveness/quality?

<u>75%/25% split of tuition (75% to college teaching a given student and 25% to college of student's major)</u>

- Encourages colleges to accept and advise students at an earlier point in their college careers
- Helps cover the overhead costs of advising students
- Are there any other justifications?

Questions/Issues:

- Justification seems weak (not worth the benefits) to some faculty in the college of business
- Will this result in excessive use of adjunct faculty for courses taught to students of other colleges?
- Will this encourage excessive recruiting of students to colleges before they are ready to commit to a college?
- Will this encourage colleges to develop required courses that really should be taught by subject matter experts in other colleges? (note that the strategic initiatives tax probably also creates/amplifies this same incentive)

Possible Alternatives:

- 10%/90% (or similar) split if a course is taught by an adjunct
  - Discourages colleges from using adjuncts to teach courses taken by large numbers of other colleges' students (it's effect on classes taken by large numbers of a college's own students is neutral)
  - Might this over-incentivize too little adjunct faculty usage (what is the optimal split)?
- Mitigate the adjunct incentive. In the absence of an adjustment of the 75%/25% proposed above, specifically redirect the financial gain of adjunct use by the University charging the College (after the fact) for each course

- Exclude the split for freshman or courses taken predominantly by freshman
    - Discourages excessive efforts to get students to declare a major too early

<u>60%/40% split of state subsidy funds (60% to college teaching a given student and 40% to colleges based on funded research)</u>

- Encourages funded research activity by allocating funds to colleges that are successful at acquiring those funds
- This split might incentivize colleges to employee full-time faculty who are more likely to participate in research activities than part-time faculty/adjuncts
- Any other justifications for this split?

Questions/issues:

- State Share of Instruction is still a significant part of the budget (approximately 30%), so this split matters – but with rapidly decreasing subsidy support, one has to wonder how long it will matter
- Note the above comment about revenues leaking from their source to sources of funded research. This could cause bad decisions if a college decides to kill a program that is profitable to the University but not to its college simply because of the revenue redirect.
- The committee has not discussed this issue very much relative to the others. We may have overlooked some important impacts.

<u>Service Unit Costs</u>

Service units will be evaluated regularly by a large committee that will include employees from multiple parts of the University

- Provides the University with an opportunity to regularly evaluate whether these units provide the services asked of them
- Provides the University with an opportunity to regularly evaluate the efficiency with which these units operate
- Many different types of University employees will be represented on the committee

Questions/Issues:

- While many different groups will be represented on the committee, will they have sufficient expertise to make decisions about the service units' performance?
- It seems to charge colleges for these units based on average total cost, but going forward the only added costs these units face will be variable costs. Failing to account for this will give more funds to service units than necessary and will discourage innovation by overcharging for it.
- MDA isn't really needed in order to use this procedure

<u>Other Issues</u>

How to appropriately reimburse departments or colleges for activities that are part of the mission but have higher costs?

- Honors courses and Honors program
- Matrix departments
- Writing Intensive courses in the WSU core
- Interdisciplinary programs across colleges
- Clearly some courses (those with labs and those at advanced-levels) are more expensive to offer, yet this is nowhere reflected in the WSU-MDA. Why has the OBR credit-hour weight system (which is now in use and would help compensate for some of these issues) not incorporated at least in part?