

UNIVERSITY OF MASSACHUSETTS AT AMHERST
OFFICE OF THE FACULTY SENATE

From the 640th meeting of the Faculty Senate held on April 7, 2005.

ADDRESS BY JOYCE HATCH, VICE CHANCELLOR FOR ADMINISTRATION AND FINANCE
(please see attached Power Point presentation)

Thank you, I am glad to be here. Ernie May suggested quite awhile ago that I attend a Faculty Senate meeting to help further explain the budget web site and the information on that site. Also, over the last few months, as we talked more and more about the Capital Plan and all the facility work going on, I get many questions that relate to: how are we paying for this? Jim Cahill addressed this group earlier and talked a lot about the Capital Plan from the Facilities point of view, so I will get to the funding side of it.

First, trends in the Campus General Fund. Some of the questions that I do not hear as frequently now, but I used to hear, “If we are raising student fees so much, where is all that money going? Isn’t that enough to cover the budget cuts of the last two years?” That is one piece. Some other questions have to do with where are we going, where are we putting our money, what are our strategic goals and how does the budget reflect that? There are also questions around the funding of the Capital Plan. Hopefully I will be able to answer those, and, at each point in the presentation, I will ask for questions.

The good news is that right now, this year, the dust has settled. We are very stable, actually. That may still not make a lot of people happy. We still have many needs; a lot of things are unfunded, but the free fall of budget cuts for *three years* has stopped. We had a budget cut in 2002, 2003, and 2004. The most infamous one was in 2004 and I will talk a little bit about what we did then.

First of all, I thought that I would give a little background, because the Campus Budget is broader than the state appropriation and it is broader than something we call the General Fund. The General Fund is a group of funds, including the biggest one, which used to be the state appropriation, but now it consists of the curriculum fee, infrastructure fee, the RTF, and the indirect cost recovery. This is the group of funds that is used to fund the main mission of the campus: all the instruction, academic departments, the administrative support. When we talk about budget cuts, it is to this group of funds. There are other funds on campus however, some of which can be used to fund the main mission. We have other unrestricted funds: Continuing Education, some sales and services, other student fees—the biggest being auxiliary operations. We run, particularly the auxiliary operations, as stand-alone financial entities. We fully cost them. We charge them for their utilities, for a lot of overhead—they are charged an overhead rate in addition to utility costs. Examples would be housing, dining services, and the Campus Center runs fully costed, almost entirely.

The other group of funds that you are more familiar with would be Grants and Contracts Restricted, and, even though we talk often about how grants and contracts do not help the General Fund, do not help support the rest of the campus, indirectly we know they do. We know that researchers are able to hire graduate students and do a lot of work and accomplish many research objectives through these funds. As those funds grow, in fact, the academic departments are helped.

The other ones with which department heads and deans probably are more familiar would be gifts. If there is anything on this Campus that is an anomaly when I look at other financial statements for other universities, the one thing that would stand out to us would be the level of endowment earnings. That is no surprise. It is a function of the fact that our endowment is so far behind every other major state flagship in the country; and that is one of the initiatives underway—to try to address that. We will be talking about the General Fund for the rest of this presentation, but I wanted you to realize that, in fact, there are other funds, some of which academic departments have access to.

So, what has happened in the last two years? I usually group the two years together for a lot of reasons. It is comparing 2003 to 2005. We received the huge budget cut in 2004. It was over \$36 million, even though it looks like \$35 million here, and I will tell you why. We had a strategy over two years to address that. We implemented a student fee that annualized over two years, 2004 and 2005. We collected bargaining increases that kicked in over two years, 2004 and 2005 (halfway through). The best way to look at how we solved the problem is to look at the two years together. I have outlined the pinkish color as defining it as a problem. We took a cut of over \$36 million. It looks like \$35 million here because now we have tuition retention and the change between 2004 and 2005 in tuition retention for out-of-state students went up slightly. We are on the right curve with tuition retention. That did not exist in fiscal year 2003. We received bargaining increases and the other increases that are part of the solution are the fees. Students definitely helped to offset the budget cut. We have been saying that over and over and this shows that. We have slight increases in other overhead, on grants in particular.

What was the rest of our problem? Why was \$51 million not enough to solve the problem? If you look down under uses—I have categorized them and added them over two years—the collective bargaining salary at \$21.8 million, that is over a two year period, that is annualized. That was actually covered by the state, so that did not add to our problem. But the other cost

increases actually did. Other salaries, non-unit—anyone who is a department head, any non-unit member, including some of our classified staff—we covered those costs. The utility budget, no surprise, went up. This is a two-year amount, \$3.4 million over two years, both 2004 and 2005. Financial Aid and the Curriculum Fee, we look at those as inflationary, because if the fee is going up—and it went up 40%—the cost of financial aid goes up to cover the difference at the same rate and the curriculum fee waivers for all the graduate students go up also. Then some central costs in this year, fiscal year 2005, experienced increases. We had a huge assessment from the President's Office of a \$3.6 million increase. Last year, it went down a little and this year it went up, so that was part of our inflationary cost increases. It was a surprise that it was to that degree. We did ask a lot of questions. Some of it is related to the PeopleSoft infrastructure and that operation that is run centrally now. Those costs we used to pay one-time money for and now they are more institutionalized and permanent. Most of those—the unfunded, inflationary, mandatory—are not a discretionary item at all.

Then we get to the decision points, some of which actually the infrastructure started a few years ago. The infrastructure is in reaction to some of the debt that we borrowed a few years ago and now the debt payments are kicking in. One of the decision points was faculty hires. For two years, even in fiscal year 2004, when we were going through \$40 million of actual loss of state revenue, \$20 million dollars of budget cuts, the Campus still put in \$1.5 million each year in 2004 and 2005 for new faculty hires. Some of the others are just smaller amounts, but to summarize: We were faced with a loss of state funds and cost increases of almost \$38 million and we balanced the budget with student fees and the Campus budget cuts. That really sums up two years' worth.

[At this point Vice Chancellor Hatch asked if there were questions on this section of her presentation. Please see the minutes for those questions and answers.]

Ok, looking ahead. What I am going to show you is one of the scenarios that we are using to look ahead to see how much we can do new. One of the scenarios includes looking at level enrollments. This is important; this is the one that I am going to show you today. We are also making the assumption, because it is the conservative option, to look at the state appropriation increasing only to the extent that we receive collective bargaining money. The collective bargaining increase that we are using, right now, is the latest information that the Governor's Office is putting on the table of 2% a year. Should it be better than that, of course it will be reflected here, but at the moment that is the best information that we do have. We have committed to mandatory student fees not going up more than inflationary costs for the next few years. After a 40% increase for two years, we have to keep our commitment to keeping that down to 3%.

Again, this is starting at fiscal year 2005. We have small increases each year on the order of \$7 million to \$8 million a year. Two new things have happened. One is that the indirect cost rate was just renegotiated, so we have an indirect cost rate on grants and contracts. It was 50%. Starting next year it will be 56.5%, and then 57% for two years. That is good news. Our best projections are reflected here, as well as, for the first time beginning next year, the Campus will be receiving an overhead from Continuing Education operations. We have an agreement with them and they will be aiming to return some funds to benefit the whole campus. Under the Uses side—I will just go through fiscal year 2006, just to show some of the increases—again mandatory salary increases. Nothing too much unusual is happening, except under utilities. I just want to talk a little bit about utilities.

I have been here before talking about our energy conservation program. We are investing \$42 million. If we had not been investing \$42 million, to bring down our energy usage 20% and 25%—in two years we will be at that point—these costs would be much, much higher. The \$2.2 million in utility cost increases this year will rise about \$700,000 next year to \$2.9 million and so on. These are cumulative totals. In fiscal year 2008, the new heating plant goes online and we convert from coal to oil and gas, primarily gas, but oil as a back up. The good news is that we will be more efficient; we will be cleaner. The bad news is that we will be dropping coal, which is the cheapest form of energy anywhere and particularly in the Northeast. The cost increase would normally be about \$3 million, just when we turn on the new heating plant, but we are able to offset that with some of the energy savings and a few other things that we are doing.

Most of the other things here are just inflationary increases. The big item is, of course, infrastructure. The Capital Plan and again next year another \$1.5 million for faculty hires. I am sure that there is interest here, but if we have level enrollment, if we do not get anything beyond salary increases from the state, we will be able to add another \$1.5 million for faculty hires next year and then it stays level. This is contingent upon the assumptions we just went through. The academic initiatives include things that are already pretty much committed: something for the library and we have to do something with instructional technology. There really is not much leeway here for new programmatic things, even though that is how we are describing them.

[Vice Chancellor Hatch asked if there were questions on this section of her presentation. Please see the minutes for those questions and answers.]

I thought that I would go into the Capital Plan funding. If you notice here, this is under the infrastructure line, it shows the increases each year. This year we put in an additional \$5.1 million in our Capital Plan out of our Operating Budget. Next year it will go up about \$3 million to \$8.4 million and so on. In fiscal year 2005, the \$5 million is in addition to \$30 million that is already in our Operating Budget. It goes for debt and, actually, we call it a revolving repair and replacement pool for major, major projects. The interesting thing is that not only is the Campus General Fund picking up the new debt, but in addition, as we put on new housing, which is under Auxiliary Operations, we have a renovation of one of the dining commons, also a renovation of the Campus Center. Those operations are all under Auxiliary Operations. They will be picking up their own debt. The goal is to have all of those operations fully costed and as we borrow money—the most recent borrow included something for the new student housing—the payment does not really start to hit until 2007 (we were able to fund it that way) and then into 2008. These operations will be picking up their own debt.

One of the financial indicators that our Trustees look at, and actually I just had a discussion with Vice President Lenhardt yesterday, is we just had a new rating from Standard and Poors for our borrowing. We are rated as “A.” There are two main pieces of information they look at when they rate for borrowing purposes. One is your fund balance or your financial cushion and ours is not terrific compared to other institutions our size. The other thing they look at is the amount of debt that you currently have. We are under the amount that triggers any red flags as far as they are concerned. We still do have the capacity from an external view to borrow more money, but, of course, the constraint is the impact on the Operating Budget.

I’ll just go through a few things that we have gone over before and what we are doing. The total Capital Plan of \$544 million, as you can see, is over five years. What we are projecting is a state contribution of only 11%. Right now, unless the Legislature authorizes another capital bond authorization, we run out in two and a half years with the current authorization. The Governor has to approve it. We will not be able to spend beyond \$59 million. This is all that is authorized at the moment. To get anything beyond that there has to be an authorization bill and then the Governor has to give us a spending cap each year. We are pretty confident that we will get \$59 million, but you can see it is 11% of the plan. We have plans to raise money. We have some in hand from private funds. We have plans to continue doing that. Right now 87% of the plan is funded by this campus, either through borrowing—the energy project is a borrow—or the Campus revolving pool over five years.

If we were to look at other institutions, and we have not done a peer study—I know Ernie is going to ask me about that—we have not done one in quite a few years, but the President’s Office actually did one last year. Just to look at state contributions for capital. They found that for research institutions or systems, we were *way* behind what states are contributing to the capital plans of each of the other institutions. What are we doing? This is just to sum up. We have almost \$200 million dollars of new buildings, renovations, deferred maintenance (and I think Jim Cahill showed you all the individual projects); we have a whole map of the campus and every building has a condition color. Bright red is a red flag that means it should be demolished. We have a number of those (they are not red on the slide). We have a few buildings that are abandoned and they should be demolished. The Chapel, it’s abandoned, but it needs a lot of work before we can open that. You can see we have “In Use, Should Be Demolished” 3% of our space. Right now, before we invest in the Capital Plan, or before it is spent—we have a lot of the funds in hand—only 34% of our buildings are categorized in “Good Condition.” After we spend half a billion dollars, that goes up to 40% good or new. Some of our buildings that should be demolished will be demolished but, depending on what department you are in, I am sure you know, much of this space—including this building—needs systems upgrades, other deferred maintenance. It is actually to show that we need to be doing this, but we still have a *long* way to go before we really fix the campus.