



**Budget Model Redesign Initiative**  
**Stakeholder Discussions**

February 18, 2014

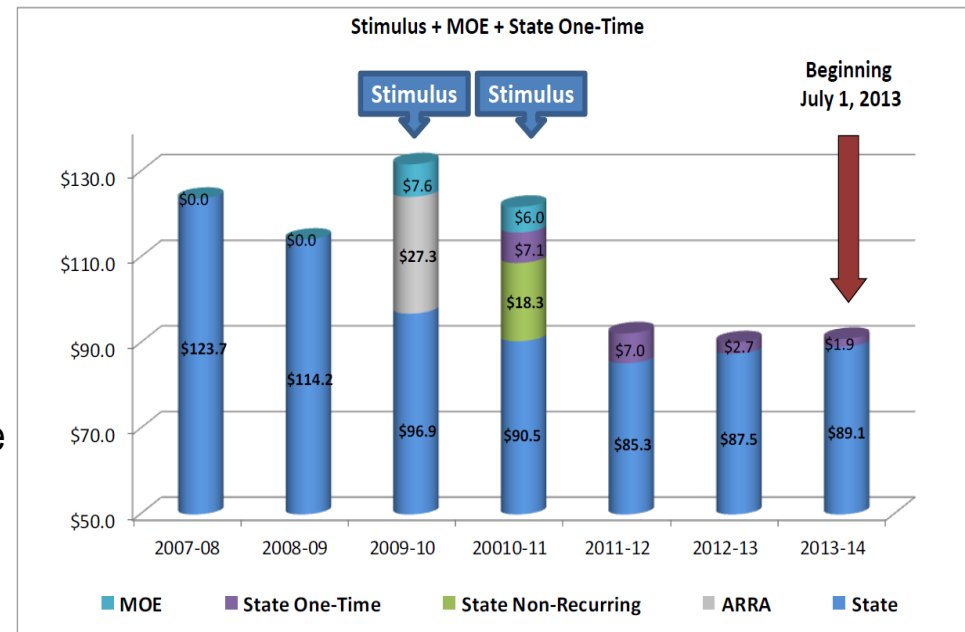
Why should the University of Memphis Explore a budget model redesign?

## Financial Challenges

- Decline in Enrollment
- Loss of \$44M in State Appropriates over 6 years
- Loss of Central Stimulus dollars and surplus cash fund to bridge funding gap

## Initiative Goals

- Change our budgeting model to be more responsive and responsible
- Connect expense decisions to revenue
- Maintain the ability to support University values and initiatives.



# Project Timeline

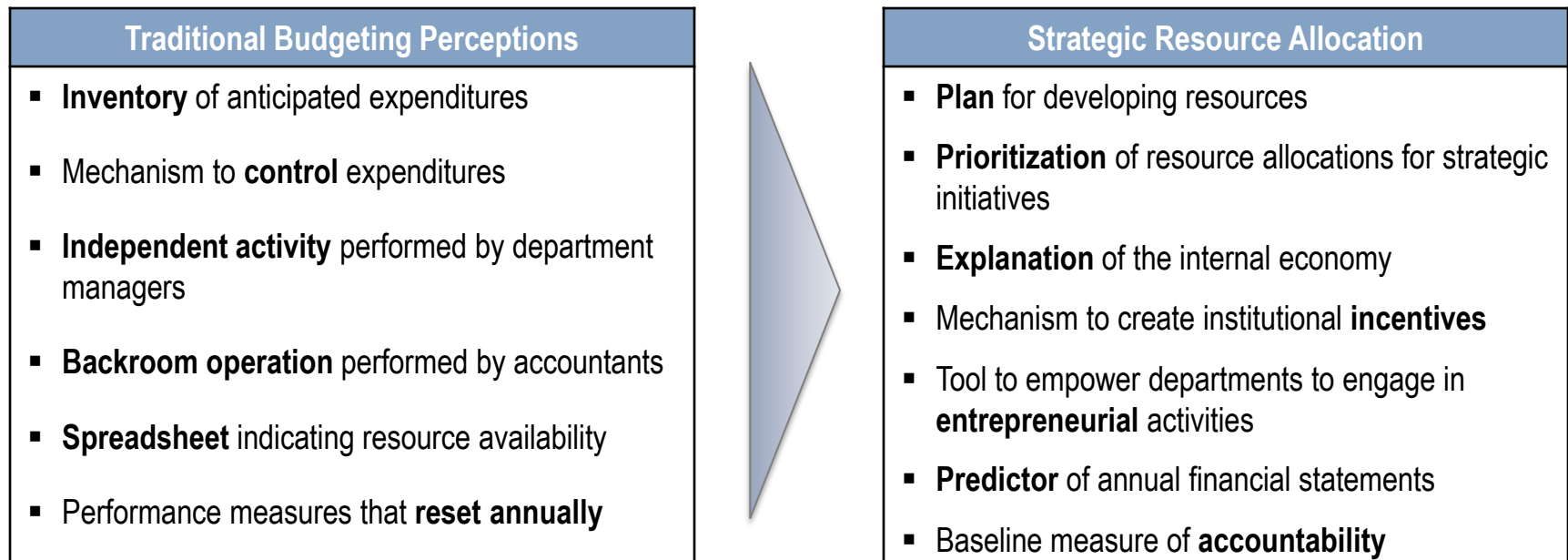
A sixteen person Steering Committee has been charged with overseeing UM's evaluation of a new budget model, a process which is expected to last through the spring.

	2013		2014					
	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	Jun.
<b>Plan</b>	◆							
Budget Working Group Orientation							■	
Project Plan								
Kick-off Meeting						◆		
<b>Discover</b>		■						
Data Identification and Collection								
Data Analysis and Review								
<b>Design</b>		■	■					
Categorize Units (i.e., Revenue, Support, Hybrid)								
Group Funds (i.e., Unrestricted, Restricted, Lambuth, Other)								
Memphis Model P&L Framework & Structure								
<b>Develop – Cost Allocations</b>			◆	■				
Define Administrative & Support Cost Pools								
Identify Allocation Drivers								
Align Drivers and Cost Pools with Economic Reality								
<b>Develop – Revenue Allocations</b>				■	◆			
Tuition Revenue Allocation Algorithm								
State Appropriations Revenue Allocation Algorithm								
<b>Present – Memphis Model Recommendations</b>							◆	■
Present Revenue + Cost Allocations Using FY13 Actuals								

**Huron Consulting Group is assisting the University and Steering Committee with the facilitation of the above work plan and model development.**

# Resource Allocation (e.g. “budgeting”)

Broadly speaking, budget redesign initiatives typically attempt to highlighting the strategic importance of resource allocation and change an institution’s culture of decision making.



As we discuss market trends and approaches to resource allocation, our hope is that participants will consider the broad definition of budgeting, as described in the rightmost box above.

# Overview of Budgeting Alternatives

Incremental budgeting is the most common approach to institutional budgeting, though an array of alternative and hybrid models exists.

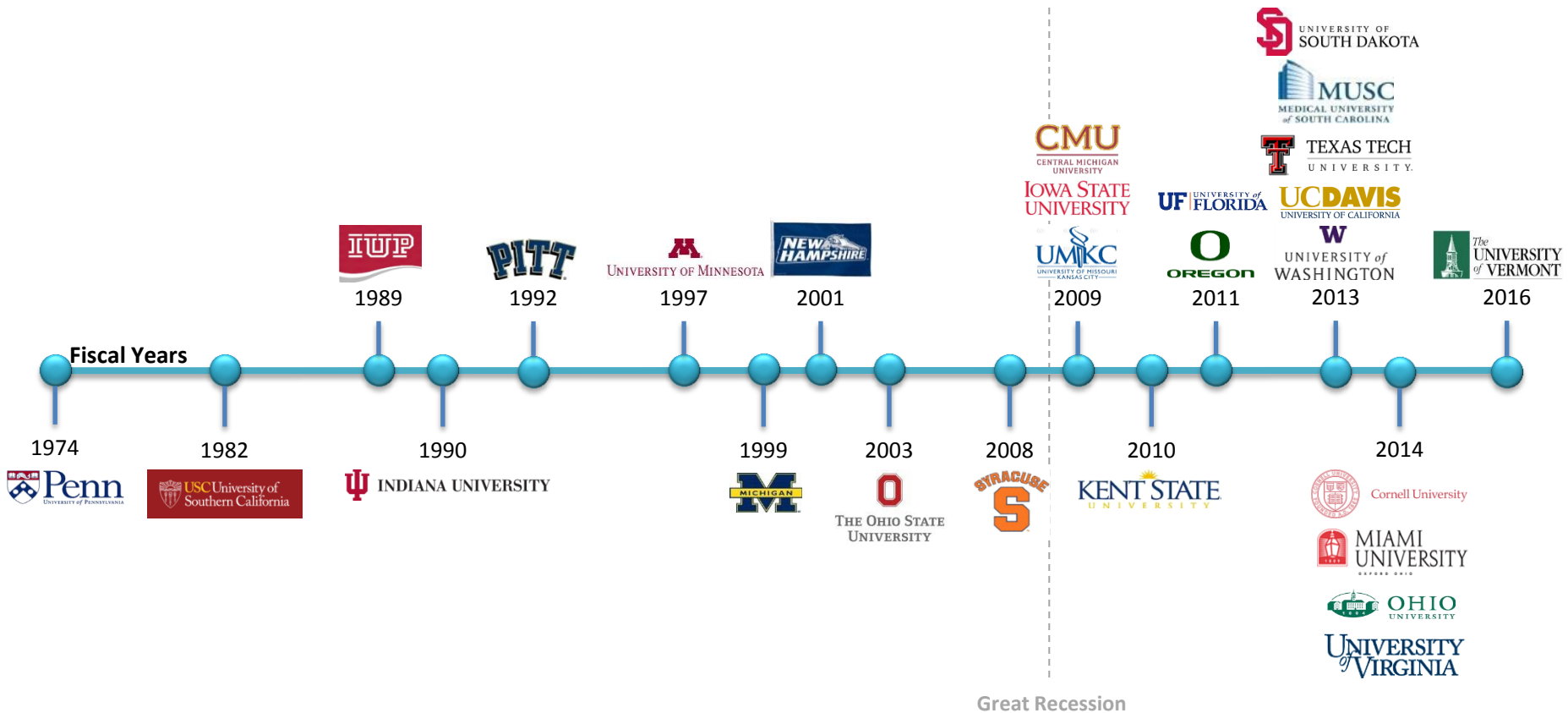
Common Budgeting Models <sup>1</sup>			
<p style="text-align: center;"><b>Incremental Budgeting</b></p> <ul style="list-style-type: none"> <li>▪ Centrally driven</li> <li>▪ Current budget acts as “base”</li> <li>▪ Each year’s budget increments (decrements) adjust the base</li> <li>▪ Focus is typically placed on expenses</li> <li>▪ Common Modifications:                             <ul style="list-style-type: none"> <li>– Block-grant versions bucket line-items together to promote local control</li> <li>– Revenue incentives may be incorporated for the allocation of resources above-and-beyond the base</li> </ul> </li> <li>▪ Approximately 60% of institutions and 79% of public doctoral institutions report using incremental budgeting</li> </ul>	<p style="text-align: center;"><b>Formula Funding</b></p> <ul style="list-style-type: none"> <li>▪ Unit-based model focused on providing equitable funding</li> <li>▪ Unit rates are input based and commonly agreed upon</li> <li>▪ Annual fluctuations are driven primarily by the quantity of production and not from changes to rates</li> <li>▪ Common Modifications:                             <ul style="list-style-type: none"> <li>– Weighting schemes to control for local cost structures</li> <li>– Used only for select activities (e.g. instruction)</li> </ul> </li> <li>▪ Approximately 26% of institutions and 45% of public doctoral institutions utilize a formula funding model</li> </ul>	<p style="text-align: center;"><b>Performance Funding</b></p> <ul style="list-style-type: none"> <li>▪ Unit-based model focused on rewarding mission delivery</li> <li>▪ Unit rates are output based and commonly agree upon</li> <li>▪ Annual fluctuations are driven primarily by changing production and not from changes to rates</li> <li>▪ Common Modifications:                             <ul style="list-style-type: none"> <li>– Weighting schemes to control for local unit mission</li> <li>– Used only for small portions of overall resources (as little as 1% - 5%)</li> </ul> </li> <li>▪ Approximately 20% of institutions and 26% of public doctoral institutions utilize a performance funding model</li> </ul>	<p style="text-align: center;"><b>Incentive-Based Models (RCM)</b></p> <ul style="list-style-type: none"> <li>▪ Focus on academic units</li> <li>▪ Incorporates a devolution of revenue ownership to local units, as generated</li> <li>▪ Allocates costs to revenue generating units</li> <li>▪ Utilizes a centrally managed “subvention pool” to address strategic priorities</li> <li>▪ Common Modifications:                             <ul style="list-style-type: none"> <li>– Revenue allocation rules</li> <li>– Number of cost pools</li> <li>– Participation fee (tax rate)</li> </ul> </li> <li>▪ Approximately 14% of all institutions and 21% of public doctoral institutions use an incentive or RCM based model</li> </ul>

(1) Adoption rates from the 2011 Inside Higher Education Survey of College and University Business Officers; Percentages do not add to 100% due to hybrid budgeting models.

**It is very common to find institutions that are utilizing multiple budget models simultaneously, either as hybrid models or models to facilitate various university missions.**

# Budget Redesign Initiatives

The negative effects of the struggling economy have considerably increased the frequency with which universities are undertaking comprehensive budget redesign initiatives.







# Recent Budget Redesign Initiatives

Unique contexts have led to a number of recent budget redesigns, but a review of redesign rationales shows common themes behind many redesign initiatives.

## Common budget redesign rationales:

- Change nature of decision making
- Move to a more methodical approach
- Grow revenue
- Promote incentives
- Increase transparency

Institution	Reasons for Redesign	Implementation Date
	<ul style="list-style-type: none"> <li>• Promote academic excellence and financial sustainability at all levels of the university</li> <li>• Encourage innovation and entrepreneurship</li> <li>• Improve transparency, clarity and predictability of budgeting</li> </ul>	In Progress (Projected FY2016)
	<ul style="list-style-type: none"> <li>• Align revenue streams to the colleges in support of their instructional mission</li> <li>• Direct tuition to colleges based on their teaching activities</li> <li>• Implement a cost pool system that assigns colleges the costs for support services</li> </ul>	In Progress (Projected FY2015)
	<ul style="list-style-type: none"> <li>• Distribute revenues and address costs in ways that are consistent, coherent, and transparent across colleges and units</li> <li>• Allow the university to think and make decisions collectively</li> <li>• Bring clear understanding of the university's finances and expenses</li> </ul>	In Progress (Projected FY2014)
	<ul style="list-style-type: none"> <li>• Identify sources of new revenue</li> <li>• Improve the allocation of resources</li> <li>• Achieve greater operating efficiencies</li> <li>• Provide better information for decision making</li> </ul>	In Progress (Projected FY2014)

# Critical Budget Redesign Decision Points

As the University proceeds with the design of a new budget model, the leadership team and stakeholders must consider how the model should promote University goals and drive continuous improvement.

- What degree of centralization/localization would allow the University to optimize decision making and resource allocation?
- How should incentives be incorporated into resource allocation?
  - How can the University incentivize recruitment and instruction?
  - How can the University incentive research?
- What steps should be taken to ensure resource allocations are aligned with strategic priorities?
- How can the University's model enhance coordination and efficiency among administrative units?
- How should the University's resource allocation model be governed?



As with any change management initiative, anxieties are likely to run high when consideration is given to changing institutional funds flows.

## Common Criticisms/Challenges

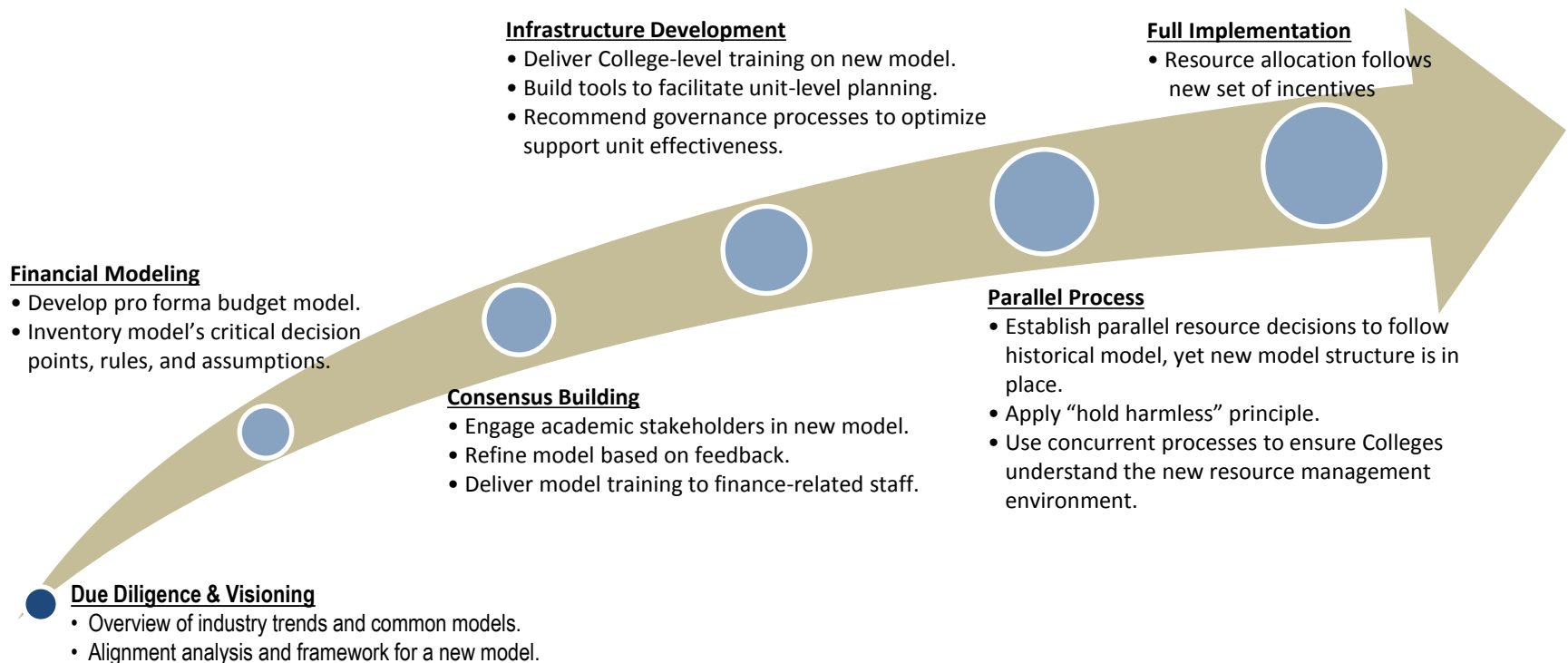
1. New budget models do not create new resources; therefore, modifications are zero-sum games
2. Illustrative funding models almost always create an impression that the grass is greener
3. Proposals will undoubtedly be made for special considerations for unique business models
4. Model adaptations for special considerations result in excess model complexity (model can collapse under it's own weight)
5. Constituents often prefer the “devil they know”

**Diligent project management, frequent communication and data-driven recommendations can help alleviate these challenges and lead to successful implementation.**

When effective, resource management and allocation models have the ability to materially transform institutions over a five to ten-year period as they can change the culture of decision making.

- **President's Cabinet:** removes the luxury of “all things to all people” by forcing difficult decisions.
  - Institutions understand how Colleges and Schools are creating and using resources.
  - Allocations reflect the Institution's mission and act as “value judgments” for institutional units.
  
- **President, Provost, and CFO:** force clarity regarding priorities and strategic initiatives.
  - Through the design of incentives, priorities have meaning and produce funding for local units.
  - Full transparency in how resources are used to promote strategic initiatives.
  
- **Deans:** understand the full cost of activities (academic programs, research, etc.) and prioritize them through cross-subsidies between their revenue generating activities and their mission-driven activities.
  - Program growth is no longer a question of simply “doing more with less”.
  - Promotes understanding that research activities lose money and must be subsidized.
  
- **Support Units:** connect service levels and resource levels.
  - Support unit budgets must be justified and paid for by revenue producing units, which introduces enhanced accountability and perhaps competition.
  
- **Department Chairs and Faculty Members:** see how activities drive funding for their respective units.
  - Incentivize innovation in the classroom, much like incentives for innovation in research.

Budget redesign initiatives typically take 18-24 months, beginning with a due diligence and visioning phase and culminating in a one-year parallel process.



**The University is currently working on the due diligence and financial model steps. Immediate next steps include incorporating feedback from stakeholder meetings and vetting options with the Steering Committee.**