University of Connecticut
Office of the President

Michael J. Hogan
President

DATE: June 24, 2008

TO: Members of the Board of Trustees
FROM: Michael J. Hogan

I'm pleased to submit the University of Connecticut's FY2009 spending plan to the Board of Trustees. The plan highlights the strategic and innovative thinking of the University's senior administrators in a challenging fiscal environment. As the plan reveals, even in a difficult context, we can deploy our resources toward strategic priorities, which will continue to move and even accelerate the University along its upward trajectory of excellence.

The spending plan recognizes the realities of the current fiscal environment confronting the State of Connecticut and the University. The revenue and expense plans reflect only incremental shifts over the prior year. While this creates enormous challenges in taking UConn to the next level of excellence, if approached systematically and deliberately, these budget challenges can become opportunities for the University to become more efficient, more nimble, and more focused.

Indeed, if there is a word to capture the document, it is "strategic." We are now completing UConn's Academic Plan, which we previewed for you at the April 2008 Board meeting and will bring to you for further review and consideration in September. The Academic Plan highlights strategic goals in research, teaching, outreach, and diversity that will move UConn to the next level as a destination university of excellence. These goals reflect our strategic priorities and it is those priorities that drive our spending plan. In addition, the Academic Plan articulates budgetary strategies that emphasize reallocation and the pursuit of additional revenues (e.g., through effective and full use of endowments; recouping, to the full extent possible, all allowable costs on extramural grants and contracts). These budgetary measures will allow us to secure new resources for and direct limited resources toward our strategic priorities.

We have also undertaken key steps, articulated in the Academic Plan, to prepare our organizational infrastructure to be more nimble and effective at reaching our strategic goals. Most notably, we have:

- Established the position of Vice President for Research, overseeing the research enterprise of the entire university, including the Health Center;
- Realigned the Schools of Medicine and Dental Medicine with other colleges and schools at UConn reporting to the Executive Vice President and Provost.

The former will poise us to foster new levels of research collaboration across and beyond our campuses and to more effectively share and deploy research-related assets and expertise throughout the University. The latter will provide new opportunities for academic partnerships across all of our health science schools and programs. Both of these outcomes speak directly to our aims to grow our research enterprise and enhance the quality of our academic and outreach programs.

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In addition to these infrastructural enhancements already in place, our Academic Plan calls for reorganizing and aligning our diversity-related programs across the University to leverage the expertise and resources that exist in these offices and channel them toward the strategic goal of improving diversity among faculty, staff, and students, as well as creating a climate that welcomes different perspectives.

Also, we will broaden the scope of our Enrollment Management Office and bring the Office of Institutional Research under its oversight, with the expanded operation led by a Vice President for Enrollment Management. Much of our success as the top-ranked public university in New England reflects careful work by Enrollment Management in tracking demographic trends, analyzing areas of high student demand, understanding economic development needs and opportunities, and assessing shifts in state and federal policies that govern research and education. As we focus on the strategic goals of our Academic Plan, particularly those related to enhancing research and graduate education, we need analyses to support decision-making in our graduate and research programs. The broadened scope of Enrollment Management will provide this key analytic and support function.

With regard to capital planning, our Academic Plan has helped us reassess UCONN 2000 Phase III (21st Century UConn). The Plan identifies priority research and academic areas, such as Health and Human Behavior; Arts, Culture, & Society; and the Environment. Thus, we have used these priorities, alongside our ever-present priority to maintain the safety and efficiency of our facilities to guide the scheduling and capital plan for named projects in UCONN 2000 Phase III.

Likewise, we are taking strategic measures related to the UConn Health Center (UCHC). As the budget indicates, UCHC continues to confront the chronic deficit situation that it has faced in prior years. This is a situation that reflects a complex convergence of challenges, including the demand for services for which revenues do not keep pace with costs (e.g., services needed by the under- and un-insured); the increasing costs of training the next generation of doctors, dentists, and healthcare professionals as the State's academic medical and dental medicine school; and the relatively small size of our hospital.

Again, however, while these are challenges, they also force us to think strategically and to seek new opportunities for revenue enhancements and cost savings. And, we've done just that. We are nearing completion of an engagement with PricewaterhouseCoopers to identify ways to streamline operations and are now poised to implement the recommendations that emerged from that engagement.

In addition, through a series of very positive and very fruitful discussions with the hospitals affiliated with UCHC and our Schools of Medicine and Dental Medicine, as well as legislators and policymakers, we are now in an unprecedented position to embark on new collaborations with these hospitals. The State commissioned the Connecticut Academy of Science & Engineering (CASE) to conduct a needs-based analysis of UCHC, with a focus on its need for additional hospital beds. As CASE noted in its report, "all parties agree on the paramount need for UCHC to achieve excellence in the schools of medicine and dental medicine." The report recognizes the critical economic impact of UCHC and recommends the development of collaborative relationships with one or more regional hospitals. CASE is now monitoring the process through which we will seek such collaboration(s).

In summary, there is no doubt that we will confront challenges; but our strategic approach has and will continue to frame these challenges as opportunities and we will remain undeterred in our resolve to move the University of Connecticut to the next level of excellence. At our annual Budget Workshop, we will highlight these fiscal challenges, as well as our strategic approach to addressing them. It's an approach that reflects the creativity and persistence of leaders in the senior administration, including Vice President & Chief Financial Officer, Lori Aronson; Vice President & Chief Operating Officer Barry Feldman; Executive Vice President & Provost Peter Nicholls; and Executive Vice President & Dean of the School of Medicine, Peter Deckers. I am appreciative of their help and creative energy in preparing this budget.

Highlights
Fiscal Year 2009
University Spending Plan

BUDGET PROCESS

For even-numbered fiscal years, the University prepares a single fiscal year spending plan; for odd-numbered years, the University also prepares a "current services" budget for the upcoming biennium for submission to the Office of Policy and Management (the Governor's budget agency), as well as to the State Department of Higher Education. ("Current services" refers to the cost of continuing current programs and services, updated for inflation. The "current services" budget forms the basis of the Governor's recommendations to the legislature.) The June 24 budget workshop will focus on the spending plan for Fiscal Year 2009, but the Board will also be asked to act on the biennial "current services" request for Fiscal Years 2010 and 2011. The tuition and fee charges for Fiscal Year 2009 were set in November 2006 by the Board. The proposed charge structure for the coming biennium will be presented to the Board at the November 18, 2008 meeting.

BUDGET GOALS

For the past couple of years the University has been shifting into a minimal growth mode with respect to enrollment at Storrs. Our budget goals at Storrs have changed with the changing times, from managing dramatic growth to growing quality. However, the current state of the economy is such that UConn's excellent value may be affecting the marketplace more than expected, as evidenced by increases not just in applications, but in paid deposits. It appears that the UConn equation (quality + price = value) is driving demand among talented students as never before. As a result, although we had originally planned only a very small increase in the Storrs freshman class for Fall 08, we have made the conscious decision to increase the class size to approximately 325 more students than in last year's class. This decision to offer the Storrs opportunity to more students will have an effect on this year's budget. For Fiscal Year 2009, faculty hiring (which translates into course coverage, improved student faculty ratio and research productivity) remains the focal point in the proposed spending plan for the Storrs-based program.

At the Health Center, our immediate goal, simply put, is fiscal survival. For a second year, we have had to ask the state for deficit assistance, and the extremely constrained financial environment remains the overarching reality. The structural problems at the hospital will persist until a structural solution is found. Expense reduction efforts have intensified, with a focus on PricewaterhouseCoopers recommendations, and the budget under development includes very limited investment, largely restricted to revenue-generating services. As of this writing, it appeared likely that a full Health Center budget would not be ready in time for mailing with the workshop materials. On June 2, the Finance Subcommittee of the Health Center Board of Directors reviewed a proposed FY 09 budget and asked for major revisions. As a result, the June 9 meeting of the Board of Directors did not include the operating budget as an action item. A meeting of the Finance Subcommittee has been tentatively scheduled for June 19. While the goal is to have a budget adopted by the Board of Directors in time for a Trustee discussion on June 24, this material does not include detail on the Health Center spending plan for FY 09.

THE STATE BUDGET

Because the legislature this year decided to leave the FY 08 and 09 budget untouched, the state's appropriation reflects the fiscal environment of one year ago. There is, as a result, a significant disconnect between the state budget for FY 09 as adopted and the reality of today's FY 09 revenue outlook. We do not know what the next few months may bring in terms of Executive Branch budget adjustments. In the meantime, the state's appropriated budget support for the University is as follows.

The effect of the General Assembly's decision not to pursue a revised FY 09 state budget is that the original FY 09 budget— the second year of the biennial budget enacted last year— remains intact. This leaves Storrs with a FY 09 appropriation of $229,416,160 and the Health Center with $101,963,598. These amounts represent a stable current services budget level for the Storrs-based program and the academic program at the Health Center. The Health Center appropriation includes the second, and final, piece of the funding for the Academic Gap. (The $20 million gap was closed with $13.5 million in FY 08 and $6.5 million in FY 09.)   In addition, the FY 09 appropriation to the State Comptroller includes the authorization for her to pay up to $3.6 million in fringe benefit costs for John Dempsey Hospital employees. This is the first time the state has provided any funds to support fringe benefit costs at John Dempsey Hospital; the $3.6 million represents approximately one-third of John Dempsey Hospital's total fringe benefit differential. The fringe benefit differential is the estimated annual dollar value difference between the John Dempsey Hospital fringe rate and the Connecticut Hospital Association member average.

From the Storrs perspective, the biggest disappointment is that the $1 million approved by the Appropriations Committee for new faculty will now not materialize. However, the $1 million in FY 08 faculty hiring funding <u>is</u> rolled forward into the FY 09 appropriation (in other words, state support for that hiring cohort continues), and the Eminent Faculty Program and the Center for Entrepreneurship remain funded at $2 million each for FY 09.

In special session, in the early hours of June 12, the General Assembly enacted a deficiency bill containing $21.9 million to address the Health Center's FY 08 shortfall. (Deficiency bills are the state's mechanism to address shortfalls in current year agency budgets.) At present, we project a year-end deficit of approximately $22 million, more than $20 million of which is attributable to the hospital. (The final number will not be available until we have completed FY 08 closeout.) We are in an extremely tight cash position at the Health Center, and the General Assembly's action was critical to our financial viability. We are hopeful that the Governor will sign the bill soon. In an unusual procedural twist, the Department of Correction deficiency (which includes $6.5 million slated for "inmate medical services" provided by the Health Center's Correctional Managed Health Care program) was addressed through the Finance Advisory Committee process. Procedural abnormalities aside, the bottom line is that we have been assured that funding is now available to cover current year needs. The $6.5 million shortfall was driven in part by the big increase in the inmate population last summer and fall, but the funding was also intended to meet the actual cost of inmate services at John Dempsey Hospital.

One proposal that saw favorable action during the regular legislative session is the bill endorsing the work of the Connecticut Academy of Science and Engineering (CASE) concerning the future of the Health Center's academic/research enterprise and the John Dempsey Hospital. The bill sets out a process and a timetable for the development of a plan to ensure that the Health Center "flourish as a comprehensive academic health center of excellence" (to quote CASE) and assigns to CASE responsibility for 1) monitoring the process of regional deliberations on possible collaboration and 2) reporting to the General Assembly in preparation for the coming legislative session.

Fringe benefit support from the state for Storrs is estimated at $95.7 million for FY 09. The state share of the Storrs-based operating budget, which stood at 50% in FY 91 and 35.4% in FY 06, is projected to be 36% for FY 09.

SPENDING REDUCTIONS AND CONTROLS

State tax receipts have plummeted, and a state budget that started the current (FY 08) year in surplus has ended in deficit. In the course of the last few weeks, Governor Rell has issued a number of directives to reduce state spending as an immediate response to revised revenue projections. The University has instituted, for both the Storrs-based program and the Health Center, new review and approval procedures in keeping with the Governor's specifications. This includes serious constraints on the hiring of personnel, now limited to essential University operations: health and safety, and our top instructional priority: course coverage.

We continue to seek efficiencies where possible, both immediate and long-term. At Storrs, the most significant undertaking remains in the area of energy efficiency, with the new cogeneration plant as the foundation, but also with a greater focus on taking advantage of the opportunity for savings in the renovation of older buildings. UCONN 2000 (augmented by auxiliary funds for projects like dormitory window replacement) is making a significant contribution to conservation efforts, and the FY 09 capital budget has more renovation and deferred maintenance projects than originally contemplated.

At the Health Center, approximately $78 million in operational efficiencies were achieved from FY 00 through FY 08. The “value analysis” project, a systematic look at ways to reduce costs and enhance operations, continues to produce savings in such areas as product standardization and scheduling improvements. The current year PricewaterhouseCoopers engagement is also producing efficiencies, most immediately in revenue cycle and supply chain improvements. As with the other campuses, the Health Center is benefiting from UCONN 2000 in energy conservation efforts. Two major deferred maintenance projects (cooling coil and heating coil) are converting the original electric heat system to more energy efficient steam and hot water systems. The main cooling tower replacement is complete, and we continue to replace boilers and chillers with up-to-date energy efficient equipment.

BUDGET PLAN AND PRIORITIES

By way of background, although we have not yet completed year-end closeout, our very preliminary estimates indicate that the Storrs-based program is forecasted to close FY 08 with a net gain of $6.5 million. $1.0 million of the net gain represents a reserve repayment for the November 2001 drawdown of $11.5 million for Towers Dining Center and the Student Union. $2 million of the net gain represents unspent state appropriation funds for the Eminent Faculty program. (You will recall that the legislation creating the program requires a private industry match, and the program needed lead time for recruitment.) The unspent funds will carry forward to Fiscal Year 2009 and be designated for this program’s support. In addition, we forecast savings in University funds in the energy account ($2.6 million) and in Financial Aid ($1.9 million replaced by additional state/federal funds).

This proposed spending plan for FY 09 projects a $0.9 million net loss for the Storrs-based program. (This is because expenditures for the Eminent Faculty program are budgeted in FY 09 but will be funded by carry-forward funds.) FY 08 and FY 09 budget totals are displayed below. (Percentages represent increases over the prior year.)

	FY 08	FY 09
Storrs-based	$ 901.1 million (5.6%)	$954.2 million (5.9%)

(Please note: detailed charts for the current funds budgets, and their revenue/expenditure components, are found in Tab 4 and 5 of the budget materials.)

This budget reflects the following:

- The state appropriation and estimates of state fringe benefit support
- Efficiencies, cost-reductions and reallocations rolled out permanently into the base budget
- Revenue enhancement/implementation of charges previously approved by the Board
- Expenditures for quality: the faculty hiring plan, course coverage and an enriched educational experience
- Expenditures for equity: increased financial aid

STORRS AND THE REGIONAL CAMPUSES

Our strategic budgetary focus remains the faculty hiring plan, which is the key to realizing the Academic Plan's three interrelated objectives: improving undergraduate instruction, growing research productivity and enhancing the University's reputation as a center for scholarly endeavor. The University's plan to increase full-time faculty is designed to: enhance the quality of the student experience, further the state's economic growth through research and workforce development, solidify the University's growing national reputation, and maximize the investment of parents and all taxpayers by ensuring that students can graduate in four years.

In FY 06, we began the academic year with 51 net new faculty members. In FY 07, we added 13 faculty to that number. Starting in FY 08, the effort to recruit more faculty was organized into a comprehensive five-year plan. The plan provides for hires in areas that respond to student demand, offer greatest research opportunity and tie to the state's economic development. Many of the initial positions are in the fields of the state's workforce needs, namely science, technology and financial services. The faculty hiring plan has as its five year goal the addition of 175 net new faculty active in both instruction and research by FY 12. Although we had sought state support for the effort in past years, until FY 08 our additional hiring was funded through reallocation of resources.

In FY 08, $2 million in reallocated funds were significantly enhanced with an important infusion of $1 million in new, targeted state aid for the hiring of additional faculty. (The biennial budget includes $1 million— not additive— for FY 09 as well.) The funding of the FY 08 component of the plan resulted in a net increase of 30 faculty members.

The FY 09 phase of the plan, all funded through reallocation, will support yet another addition of 30 faculty. Ten of these faculty are in high priority workforce development areas and include Engineering, Biological Sciences, Chemistry, and Nursing. Three hires will be in the School of Business and three will be involved in Urban Education and teacher preparation in the Neag School of Education.

Two new hires will augment our environmental focus: one in atmospheric studies and one in GIS/conservation. Additionally, 12 faculty hires will meet the educational needs of Undergraduate Education, Humanities and Social Sciences.

This fall will see not just new faculty, but also new academic leadership. Last year brought us four new deans, and FY 09 does the same— this time, in Social Work, Liberal Arts and Sciences, Agriculture and Natural Resources and the School of Medicine.

Revenue

The University relies heavily on its non-state revenue streams for fiscal stability, particularly in times when the state budget is under stress. These sources include tuition/room/board/fees at Storrs and the regional campuses, as well as private support and research funding.

The proposed budget incorporates the implementation of increases approved in November 2006 for tuition, room, board and fees. Detailed breakouts are in Tab 5 of these materials. Please note that for an in-state student, tuition covers only about one-third of the cost of academic services; all charges combined (tuition, room, board and fees) cover only one-half of total costs.

For FY 09 the total in-state undergraduate charge will be $18,638, an annualized increase of 6.44% over FY 08. Out-of-state undergraduate charges would rise at approximately the same percentages, for a total charge of $33,350 in FY 09. As described below, additional financial aid is budgeted to offset the impact of increased charges on financially needy students and families. The unexpected increase in the number of deposits from accepted students this year is another indication that UConn remains a tremendous value in comparison to our competitors—but it is a value only if the high quality of education remains high.

Tuition revenue growth—the combined effect of enrollment and tuition charges—is projected at 6.7% for FY 09 over FY 08. (Please see Tab 5 Current Funds chart.) Changes in room and board (in Auxiliary Enterprises) and fees drive an increase of 4.8% for FY 09 over FY 08 revenue. Please note that growth in these revenue streams is now mostly a function of rate changes. Another major source of revenue for FY 09 is state support of $343.5 million (a 5.6% increase over FY 08).

Expenditure Highlights

- Current Services Needs

  This budget respects the constraints of the current economic environment. The lion’s share of the increase in the budget is to support inflationary growth in ongoing activity: collective bargaining increases, fringe benefit costs, utility demands, and service and commodities contracts. The two areas of expansion that serve as the exceptions to this general rule are undergraduate education and financial aid, described below.

- Undergraduate Education Enrichment

  If we are to continue expanding the ranks of highly talented students, we must enrich the educational experience. In FY 09, the budget devotes an additional $255,000 to the expansion of the Honors Program, $100,000 to enhance Living & Learning communities, and $250,000 to support engagement with the Study Abroad program. In addition, we are working to expand opportunities for service learning and research experiences with faculty.

- Undergraduate Course Offerings

  One measure of the enrollment surge is the increase in undergraduate credit hours, which jumped from 360,191 hours in FY 96 (Fall of 1995) to 564,086 in FY 08 (Fall of 2007). This is a 57% increase over that period at all campuses and 55% at the Storrs campus alone. We have tried to respond to demand with a flexible mix of instructional capacity, including full-time faculty, in-residence faculty (3 year appointments) and adjunct faculty. This flexibility has been an essential element in managing instructional demand because of shifts in student course-taking behavior by content area, as well as financial realities. We had thought we were reaching a point of equilibrium, but now, for FY 09, we are faced with the potential need to provide additional course coverage to meet the needs of a Storrs freshman class with approximately 325 more students than last year. This may require a commitment of $0.6 million in additional course coverage/extra sections. From FY 00 to FY 08, the University has devoted $9.6 million in new dollars to meet course demands of increased enrollment, with much of the increase in CLAS. Our largest increases in enrollment have been in nursing, pharmacy, biological sciences, physical sciences, accounting and engineering. Two related points: 1) these are disciplines that address critical workforce shortage areas and 2) all of these students take courses in CLAS.

- Financial Aid

  Financial aid represents an expenditure that, while to some extent discretionary, is inextricably intertwined with the mission of the University and is therefore treated as a “must do” in our budgets. When we develop our budget, each increase in student costs is matched by increased financial aid to ensure that no student’s UConn education is denied or hampered based on financial need. For FY 09, the University will earmark $287.2 million for all forms of financial aid, and $96.1 million (including tuition waivers) of that amount will be funded with tuition revenue. In other words, a remarkable 38.9% of this University's tuition revenue is dedicated to financial aid; 17.5% is dedicated to need-based aid. In fact, 77% of UConn's students received some form of assistance last year. This budget represents an increase of $19.7 million over FY 08 total financial aid expenditures.

HEALTH CENTER

The Health Center budget is currently under development. Depending upon the schedule set by the Health Center Board of Directors, materials will be sent under separate cover or distributed at the June 24 meeting.

FUND BALANCE

For the Storrs-based program, the FY08 year-end Unrestricted Fund Balance is projected to be $60.7 million. However, $2 million of this amount is a temporary increase representing unspent state appropriation funds for the Eminent Faculty program. Excluding this one-time carry forward funding, the Unrestricted Fund Balance represents 7.3% of the FY 08 unrestricted budget ($802.3 million) or, alternatively stated, 27 days' worth of operations.

The $60.7 million fund balance represents the funds and inventory remaining in these accounts: the Research Fund (designated for research); the Auxiliary Operations (residential, dining, health, student activities and recreational services); Departmental Generated (self-supporting fee-based instructional programs such as Continuing Studies and MBA); and a liability for compensated absences (vacation/sick leave), which is an accounting requirement.

It is important to remember that the fund balance, while not all technically encumbered, may be committed in a more generic sense. First of all, funds may be held in a departmental account in anticipation of an expenditure (such as start-up costs for a new researcher). Second, under the provisions of UCONN 2000, the University is required to maintain a Renewal and Replacement Fund to keep projects in sound operating condition; the fund balance serves this purpose under the Master Indenture. Third, these amounts include inventory.

The fund balance is our operating capital and reserve for programs and activities that generate revenue and are not supported by state appropriation or tuition funds. We borrow from the fund balance to pay our bills when necessary. For example, in FY 04, the University didn't receive $13.4 million in state fringe benefit support until June—the very end of the fiscal year. In FY 05, the first quarter allotment of our entire appropriation did not arrive until September 28th—two days before the close of the fiscal quarter. Another example: the state generally informs us of changes in fringe benefit rates after the fiscal year has started, and frequently the increases have a significant fiscal impact. The fund balance allows us to manage these dislocations without disrupting the University's operations.

At year end, when funds are available, we also set aside dollars in accounts for planned one-time expenditures, mostly capital. These accounts comprise our plant funds. A good example of this is the $10 million we set aside for our technology infrastructure upgrade plan. Plant funds also include specific repair projects and furniture/equipment replacement for Residential Life/Dining Services.

For Storrs, then, our projected unrestricted net assets of $128.7 million are made up of the $60.7 million current fund balance, an estimated $32 million in unexpended plant funds and a third component: $36 million in funds that are internally restricted for the retirement of indebtedness. We have traditionally been very conservative with regard to savings for debt obligations, maintaining funds at a level of approximately 1.6 times our annual debt payments. We believe that this policy has served us well. Please note that the $32 million in plant funds includes $15 million in FY 08 recoveries from construction contractors. The recovered funds were used to replenish accounts for projects that were put on hold during the code correction activity at certain residential complexes. The plant funds also reflect remaining balances for Board-approved projects (like dormitory window replacements) and unforeseen expenditures (like the Stamford campus carpet replacement).