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UNIVERSITY OF MINNESOTA

Budget and Finance

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March 12, 2010

The Honorable Sandra L. Pappas, Chair
Higher Education Budget & Policy Division
Minnesota Senate
75 Rev Dr Martin Luther King Jr Blvd Rm 120
St Paul MN 55155-1606

The Honorable Tom Rukavina, Chair
Higher Education & Workforce
Development, Finance & Policy Division
Minnesota House of Representatives
State Office Bldg Rm 477
100 Rev Dr Martin Luther King Jr Blvd
St Paul MN 55155

Dear Senator Pappas and Representative Rukavina:

Minnesota Session Law 2009, Chapter 95, Article 1, Section 5, Subdivision 2(b) requires that the Board of Regents submit an expenditure reduction plan by March 15, 2010 to achieve the 2012-2013 base established in Minnesota Session Law 2009, Chapter 95, Article 1, Section 5, Subdivision 2(h) which states for fiscal years 2012 and 2013, the base for operations and maintenance is $596,930,000 each year. This figure in combination with the base rolled forward for state specials resulted in an overall fiscal years 2012 and 2013 base of $670,002,000 for each year.

Since enactment of Minnesota Session Law 2009, Chapter 95 the Governor took action to reduce the University's enacted fiscal year 2010–2011 appropriations. In particular, the Governor reduced the enacted fiscal year 2011 appropriation by $50,000,000. This resulted in a revised fiscal year 2011 authorized appropriation amount of $627,311,000. Table 1 below outlines the fiscal year 2010 and 2011 appropriations compared to the fiscal year 2012 and 2013 base funding level enacted by Minnesota Session Law 2009, Chapter 95.

Table 1
University of Minnesota Appropriations
Operations & Maintenance/State Specials

	2010	2011	2012	2013
Enacted Funding	$623.7	$677.2	$670.0	$670.0
Governor's Unallotment	0.0	50.0	0.0	0.0
Revised Funding	$623.7	$627.2	$670.0	$670.0

As Table 1 indicates, the Governor's unallotment did not impact fiscal year 2012 or 2013 base funding levels enacted by Minnesota Session Law 2009, Chapter 95. At the present time the Governor has recommended further reduction to the University's FY2011 appropriation. The Governor's recommendation reduces the University's fiscal year 2011 appropriation by an additional $36,120,000. The Governor has also recommended an adjustment to Minnesota Session Law 2009, Chapter 95 so that the University's base funding level for fiscal years 2012 and 2013 are also reduced.

Table 2 below outlines the impact of the Governor's budget recommendation on the University's appropriation levels for fiscal years 2010 and 2011 as well as recommended changes to the University's appropriation base funding level for fiscal years 2012 and 2013.

Table 2
University of Minnesota Appropriations
Operations & Maintenance/State Specials

	2010	2011	2012	2013
Enacted Funding	$623.7	$677.2	$670.0	$670.0
Governor's Unallotment	0.0	(50.0)	0.0	0.0
Revised Funding #1	$623.7	$627.2	$670.0	$670.0
Governor's Budget Rec.	0.0	(36.1)	(78.9)	(78.9)
Revised Funding #2	$623.7	$591.1	$591.1	$591.1

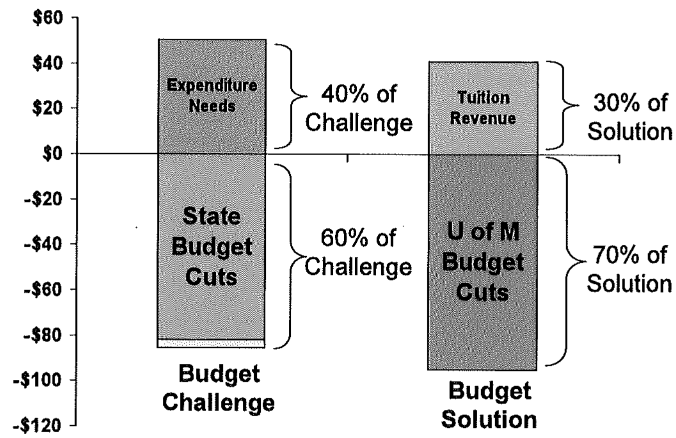
The Governor's proposed budget cut for fiscal year 2011 reflects the maintenance of effort funding requirement contained in the American Recovery and Reinvestment Act. As such the University's state appropriation for fiscal year 2011 was reduced by the Governor to the fiscal year 2006 funding level. In addition, the Governor has proposed to set the University's funding base for fiscal years 2012 and 2013 at that same fiscal year 2006 level.

In determining how to respond to the requirement contained in Minnesota Session Law 2009, Chapter 95, Article 1, Section 5, Subdivision 2(b), the University took into consideration the continuing decline in state revenues during the current biennium, the potential outcome of the 2010 Legislative Session, and the projected state revenue shortfall for fiscal years 2012 and 2013. The University has decided to respond assuming a base funding level of $591.1 million as opposed to the $670.0 million funding level identified in Minnesota Session Law 2009, Chapter 95. The remainder of this document describes the University's actions in both FY2010 and FY2011 to meet a base funding level of $591.1 million for fiscal years 2012 and 2013.

As Table 2 above indicates, the University's fiscal year 2010 appropriation level authorized by Minnesota Session Law 2009, Chapter 95 was $623.7 million. The $623.7 million fiscal year 2010 funding level represented a reduction of $78.9 million from the actual 2009 level. The President's recommended fiscal year 2010 operating budget addressed this reduction in conjunction with additional budget challenges facing the University for balancing its fiscal year

2010 operating budget. Chart 1 below outlines both the budget challenge and the budget solution implemented for fiscal year 2010.

Chart 1
President's Recommended Operating Budget FY2010
$135.9 Million Budget Challenge



As Chart 1 indicates, 60% of the budget challenge faced by the University in fiscal year 2010 was the result of the steep reduction in state appropriations totaling $78.9 million in the first year of the biennium. The total budget challenge amounted to $135.9 million for fiscal year 2010. Roughly $95.1 million or about 70% of the budget solution was resolved through operating budget cuts while 30% of the solution came in the form of increased tuition revenue. Budget reductions implemented for fiscal year 2010 were recurring reductions designed to ensure that the University's ongoing operating budgets did not exceed the authorized $623.7 million funding level contained in Minnesota Session Law 2009, Chapter 95. Reducing operating budgets to the authorized $623.7 million funding level also had the benefit of closely matching the revised funding level of $627.4 million resulting from the Governor's unallotment actions in 2009. Budget actions by the University in fiscal year 2010 ensured a structurally balanced budget beginning in fiscal year 2011 prior to any additional budget reduction actions by either the Governor or the Minnesota Legislature in 2010.

To balance the University's fiscal year 2010 operating budget, over $70 million of reductions were implemented in academic units and approximately $18 million of reductions were taken in support units. Highlights/examples of actions taken include:

- Elimination of faculty, staff and student positions within units through lay-offs, retirements and elimination of open positions (this by far results in the largest savings–estimated at over

80% of the total and over 1,000 positions) reduction in general expenses including printing, travel, supplies, professional development;

- Restructuring of instructional delivery–increased teaching loads, increased course section sizes, reduced numbers of sections, altered Teaching Assistant allocation, etc.;
- Selective reductions in program funding; and
- Implementation of an early retirement incentive option to assist units in reducing compensation costs.

Specific examples of reductions taken in fiscal year 2010 in support units include:

- Reductions in office cleaning from five days per week to one, and lab cleaning from three days per week to one;
- Reduced preventive maintenance frequency/tasks and overtime costs;
- Reconfigured and reduced the number of service points in libraries (Wilson Library from 13 to seven service points);
- Cancel/delay in classroom upgrades, repairs and replacements;
- Eliminated some software maintenance and support (CUFS); and
- Implemented a hiring freeze in the Office of Information Technology resulting in the elimination of 34.5 FTE.

Below you will find examples of the impact of the budget actions taken in the College of Liberal Arts and the Institute of Technology. The budget reductions taken for fiscal year 2010 were deep for nearly all segments of the University and these two units are provided as examples of necessary actions due to reductions in state appropriations.

FY2010 College of Liberal Arts (CLA)

Category	Amount
Retrenchment of open faculty lines (52)	$5,817,000
Reductions to instructional staff	$2,536,000
Reductions to non-instructional staff (22)	$1,897,000
Eliminating tuition reserve budget	$947,000
Reduction to SEE budgets	$783,000

Specific examples of actions taken to reduce costs:

1) Cost savings in CLA Administration.

a) The college created a chief of staff position to oversee work in the Dean's Office, CLA Human Resources, and CLA Media and Public Relations, as well as coordinating work among the college's leadership team. This reorganization eliminated three positions and has led to new efficiencies and improved coordination.

b) Both administrative and development officer staff reductions were achieved in CLA External Relations.

c) Staff reductions in Fiscal Administration: The number of service teams within CLA was reduced to provide greater depth on each team, and to cover turnover, vacations, and leaves. Savings were achieved by reducing one team lead. CLA Student Services achieved cost savings through eliminating vacant positions, and redistributing responsibilities of advisors and other office staff.

2) Eliminate/reduce staff positions in academic units. Several vacant staff positions were unfilled this past year and administrative work was redistributed among current staff. Some positions were reduced as a result of implementing shared service models across academic units.

3) CLA has achieved utility cost savings through Facilities Management's building recommissioning initiative. The most dramatic example of savings comes from the Regis Center for Art, where annual utility costs dropped 32%. CLA is exploring software solutions to keep machines powered off during periods of non activity, as well as virtualizing servers, which could lead to substantial energy cost savings.

FY2010 Institute of Technology (IT)

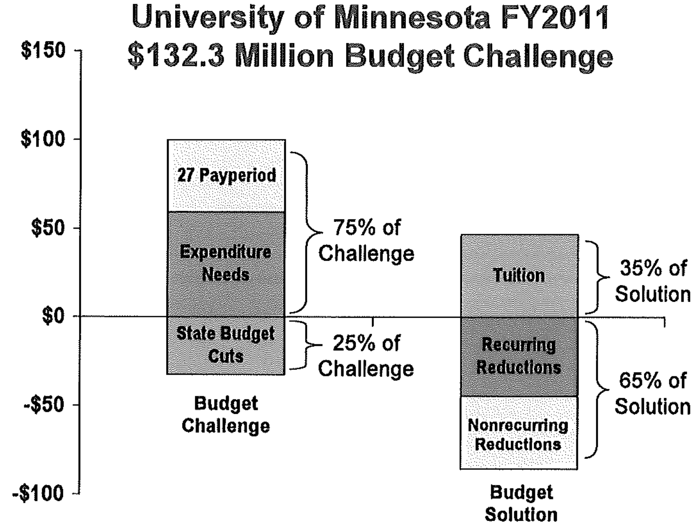
- A cut of approximately $300k was taken in the Dean's office budget ranging from communications and development to student services.
- Seventeen faculty positions were not filled, saving approximately $2M.
- Approximately 20 staff positions in departments were eliminated, saving roughly $1.2M.
- Approximately $1.4M was cut from the TA budget with obvious consequences, particularly in the face of a significant increase in student credit hours. The supplement provided by stimulus funds for additional TAs in FY2010 was critical to offset this cut for one additional year.
- Approximately $1.0 M was cut in instructional equipment and computing.
- Approximately $400k was cut from IT funds for repairs and betterment of programs.

- A cut of approximately $1.0M was taken from Centers (Digital Technology Center, UNITE, Nanofabrication Center, Minnesota Geological Survey, Institute of Technology Center for Educational Programs, Charles Babbage Institute, Medical Device Center and Center for Nanostructure Applications). IT Center for Educational Programs (ITCEP) became a unit of the Mathematics Department in the form of MathCEP.

The recurring savings from budget reduction steps taken across the University may be realized over a period of time as the process for position elimination often requires notice periods and implementation of program or service reductions needs to be phased-in. A portion of the State Fiscal Stabilization Funds appropriated to the University has been used as a nonrecurring bridge to allow for this to happen. Pursuant to the requirements outlined in Minnesota Session Law 2009, Chapter 95, the University of Minnesota also used State Fiscal Stabilization Funds to hold the tuition rate increase for Minnesota resident undergraduates to 3.1% in fiscal year 2010.

Assuming that the Governor's recommended budget reduction of $36.1 million for fiscal year 2011 is implemented, the University operating budget planning framework is outlined in Chart 2 below.

Chart 2
University of Minnesota FY2011
$132.3 Million Budget Challenge



As Chart 2 indicates, the budget challenge facing the University in fiscal year 2011 totals approximately $132.3 million. Due to efforts taken in fiscal year 2010 to ensure that the University budget was firmly set at the authorized funding level of $623.7 million in fiscal year 2010, the new state funding challenge for fiscal year 2011 of $32.3 million reflecting the Governor's recommended budget reduction (reducing the University's base funding level to $591.1 million) represents roughly 25% of the total budget challenge facing the University.

Roughly $100.0 million of the remaining challenge is a consequence of expenditure requirements and investment needs in fiscal year 2011. This figure includes the need to meet an extraordinary payroll requirement stemming from a biweekly payroll system.

- 44% ($59 million) of this shortfall is increased annual costs including:
  - $32 million to address compensation, including a 2% compensation pool increase, and payments to the fringe pool
  - $27 million to support financial aid and scholarship commitments, academic investments, facilities costs, and other essential expenditures
- 31% ($41 million) is a one-time 27th pay period necessitated by the payroll calendar
- 25% ($32.2 million) is the governor's proposed budget cut.

The University will address the budget challenge of fiscal year 2011 primarily through budget reductions. Approximately 65% of the solution will be met with budget reductions and 35% will be met through increased tuition revenue.

Compensation Planning

Human capital is our most important resource. Our goal is to address all of our budget challenges in a way that is as fair and equitable as possible, while positioning our employees well in terms of future employment and compensation.

As a result, the leadership of the University has spent the past several months discussing and modeling a number of solutions to our challenges related to compensating our employees. The proposed plan currently under consideration includes:

- An increased compensation pool, which delivers a 2% salary increase for all labor represented employees and all civil service employees beginning with the new pay year this summer, and provides for merit increases determined at the collegiate/unit level for faculty and academic professional and administrative employees, effective January 2011.
- Mandatory furlough days for civil service and bargaining unit employees. These furlough days are proposed to be taken during the last week of December 2010 (except for essential employees, who will have staggered scheduling). This also enables us to close our campuses during the winter holidays.
- Mandatory onetime salary reductions for faculty and all academic professional & administrative staff.
- Additional onetime salary reductions for all executive-level employees (including deans, associate and assistant vice presidents, vice provosts, etc.), bringing the total mandatory furlough for these employees to six days.

- Additional voluntary furlough days available to all employees (not to exceed 10 furlough days total, e.g., three mandatory civil service and bargaining unit employees plus seven voluntary).

This approach best enables us to compensate, support, and retain talented faculty and staff and to reduce the immediate impact of substantial state budget reductions on our employees, our quality, and our competitiveness—while addressing the need for real and immediate savings. It also requires that everyone participate at some level in addressing these financial challenges. Finally, making a 2% compensation pool available to all employees (not just those with contractually obligated increases) avoids future inequity issues resulting from salary freezes/necessary retentions/new hires and is a positive move in terms of future earnings, fairness, and morale for all employees.

Budget Reductions

The University's approach to budget reductions for fiscal year 2011 will involve a process similar to FY2010. Each unit across the University has been asked to prepare a plan for implementing a 2.75% reduction on their FY2010 state appropriation and tuition allocation base (adjusted for the removal of certain categories of spending such as student financial aid, utilities, lease obligations and so forth). The annual budget process, then, involves a discussion between senior management and each unit about the unit's goals, priorities, progress and financial concerns, and part of that conversation has focused on the prepared reallocation plans and the associated impacts on staffing levels, service provision and instructional and research activities. Based on those conversations, senior management will recommend differing levels of reallocation, which will be included in the President's Recommended Operating Budget to the Board of Regents in June 2010. The reductions will not be made across the board. For example, student financial aid programs will not be reduced.

As a result of actions taken in both fiscal year 2010 and 2011, the University will have established a recurring budget level based upon a state appropriation base of $591.1 million for FY2012. This base will be roughly $79 million below the level originally authorized in Minnesota Session Law 2009, Chapter 95. In light of the state's spending budget challenges the University considers taking the steps highlighted above for both fiscal years 2010 and 2011 to be the prudent and responsible course of action.

If you have any additional questions regarding the information outlined above please don't hesitate to contact to me.

Sincerely,

Richard H. Pfutzenreuter III
Vice President and Chief Financial Officer