BUDGET REVIEW WORK GROUP REPORT
Addendum to August 15, 2006 Report

March 23, 2007
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I. EXECUTIVE SUMMARY

In light of significant changes in the context within which campus budgetary decisions are made, Chancellor Fox requested that a campus work group be established and serve in an advisory role to the 2006/07 Campus Budget Committee. In February 2006, this campus Budget Review Work Group (BRWG) was charged with reviewing current allocation methodologies and presenting recommendations for the Committee’s consideration. The group met for five months and delivered a report to the Budget Committee on August 15, 2006 focused on recommendations pertinent to the 2006/07 budget process.

In summary, the BRWG reconfirmed its support for the principles that guide budget deliberations, and reaffirmed most current allocation methodologies. No changes were proposed for the 2006/07 budget year. The BRWG further recommended that it continue discussions on the following three key allocation components:

- Indirect Cost Recovery (ICR) funds,
- Deferred Maintenance budget, and possibly
- Enrollment Workload funds.

Over a period of three months, between October and December, representatives from the BRWG held five additional meetings focused primarily on ICR and deferred maintenance. Additional funding requested by the Academic Senate to help support recent increases in research grant funding requests was considered within the ICR discussions, as was the Next Generation Network (NGN) subsidy now provided from ICR funds. The group did not consider it necessary to further discuss enrollment workload funds allocation.

The recommendations that follow reflect the final outcome of these discussions and are proposed for implementation in the 2007/08 budget year.

Indirect Cost Recovery (ICR)

The changes recommended for ICR funds allocation attempt to simplify the current method of allocation, address research funding needs of the Academic Senate, and phase-out the ICR funds subsidy currently provided for NGN. Specific changes are as follows:

- Remove the Budget Committee’s specific allocations of ICR funds for Research, Animal Care, Effort Reporting System, AVC Research, and NGN from the current model, and fund separately. NGN is proposed to be phased-out from the ICR model starting in 2007/08. More specific detail is in the body of this report.
- Allocate the UC General Funds to both the Academic and Administrative units;
- Allocate available ICR funds on a 60% / 40% split to Academic /Administrative units.
• Include State research recovery in determining the fractional allocation amongst the Academic units;
• Fund the Libraries and Academic Senate as fixed proportions of the Academic units’ allocation, set at 8% and 3% respectively.
  o With regard to the Academic Senate, that campuswide continue to provide some one-time funds to help with the recent increase in research grant funding requests. These one-time funds would be phased out as permanent ICR funds are increased from within the ICR model. More specific detail is in the body of this report.

Deferred Maintenance (DM)

The BRWG recommends that the Budget Committee allocate $3 million to establish an annual deferred maintenance budget to reduce the multi-million dollar campus backlog, now conservatively estimated to be at least $245 million. Of this total, $36 million has been identified as ‘mission critical’ projects. To more effectively address this critical problem, the work group recommends that the campus borrow $10 million over a two-year period, beginning in 2007/08. It further recommends that a portion of the proposed $3 million annual budget, approximately $1 million per year, be used to pay down the debt service, with the remainder used to fund other projects on the critical and priority projects list.

The $3 million budget would be funded with Vice Chancellor unit assessments based on a share of the weighted State-supportable square feet. A process to determine priority and to update the long-term plan for deferred maintenance projects could be made in consultation with the Capital Outlay and Space Advisory Committee (COSAC), which already includes broad and regular campus consultation.

A more extensive summary of the main discussion and recommendations for each of these components is contained in the body of this report addendum.
II. INTRODUCTION AND REPORT ORGANIZATION

The environmental context in which budget decisions are made has changed significantly. State general support has declined and been partially replaced by tuition and fee revenue generated from student fee increases. Student enrollment growth is expected to continue, but at lower growth rates than in the last seven years and more focused on graduate enrollment. Additionally, growth on federal research funding is slowing and expected to remain low over the next few years. In light of these changes, Chancellor Fox requested that a campus work group be formed and charged with reviewing current allocation methodologies and presenting recommendations for the Campus Budget Committee’s consideration.

The initial report of the workgroup was delivered on August 15, 2006 and focused on recommendations pertinent to the 2006/07 budget process. In summary, the workgroup reaffirmed most current allocation methodologies, and proposed no changes for the 2006/07 budget year. It further recommended that it continue discussions on the allocation of Indirect Cost Recovery (ICR) funds, campus funding needs for Deferred Maintenance, and possibly how enrollment workload funds are allocated.

Below is a summary of funding principles reconfirmed and used by the workgroup to guide their deliberations.

- Priority is given to Academic Programs.
- Administrative functions must receive sufficient support to meet organizational goals of accountability, efficiency, and effective stewardship.
- Vice Chancellors are delegated maximum discretion to allocate funds within their areas, along with the accountability to follow all applicable policies.
- Allocation methodologies should:
  - Be clear, logical and consistent from year-to-year to facilitate long term planning by the Vice Chancellors.
  - Consider performance incentives where appropriate.
  - Consider mitigation of significant negative fluctuations on a single-unit and avoid unintended consequences.
  - Provide for permanent solutions to permanent problems.
- The budget review process and resulting resource allocations should be open.
- Every effort should be made to reach allocation decisions by consensus.

This addendum is intended to build on background provided in the initial report of August 15, 2006, and to provide a summary of key discussion of ICR and deferred maintenance issues, alternatives considered and the work group recommendations.
II. KEY COMPONENTS OF CAMPUS ALLOCATIONS

The workgroup continued its deliberation on select allocation components by summarizing prior work group discussions, then proceeding with a more detailed review of issues, concerns and possible allocation alternatives.

A. Indirect Cost Recovery (ICR)

1. Key Discussion: As described in the original report, the current campus ICR model allocates net available recovery funds from Federal, Private and Local recovery generated by the campus, after predetermined deductions and distributions are made per University policies and campus agreements which give ‘off-the-top’ priority to Garamendi Project funding, and Garamendi-type Campus Arrangements. The workgroup’s efforts at revising the current allocation model focused on reducing complexity while minimizing the impact of proposed changes on any one campus unit. In addition, the workgroup considered research funding needs of the Academic Senate and phase-out of the ICR funds subsidy now provided for NGN. The key areas of discussion included:

- **Impact of off-the-top adjustments:** Current allocation method gives priority to Garamendi Projects and Garamendi-type Campus Arrangements, prior to allocating remaining discretionary funds amongst Vice Chancellor (VC) units. These allocation adjustments were determined to be investments in the long-term interest of the campus.

- **Review of specific allocation elements:**
  - The Budget Committee’s specific allocations of ICR funds for Research, Animal Care, Effort Reporting System, Assistant VC Research, and Next Generation Network (NGN) have been in place for a number of years. These components add an unnecessary level of complexity to the current allocation model. Furthermore, initial discussions recommended that NGN funding be reviewed with the objective of reducing the ICR subsidy over time and that each units’ financial contribution be more reflective of usage.
  - A portion of UC General Funds has been returned to campus since 2000/01 with the allocation benefiting only the Academic units. These funds recently declined and had a significant negative effect on the net allocation to the Academic units.
  - The use of ICR rate components for allocation between Academic and Administrative segments may lack the logic it once had and therefore is no longer valid for future allocations.
  - Pro-rata allocations between the Academic VC’s:
    - The 2-year averaging pro-rata % has a negative impact on units that are growing at consistently higher growth rates, and offers protection to units growing at slower rates.
    - Consideration given to State research recovery in determining the Academic unit pro-rata distribution recognizes units that are heavily funded by State research funding.
  - The Library’s allocation has been funded at its ‘grandfathered rate’ of 3.0 points of the campus ICR average rate, and funded from the academic component of the allocation.
The Academic Senate’s allocation for Committee on Research (COR) grant funding from ICR has been fixed at $900,000 since 1995/96. In 2005/06, COR received an additional one-time $500,000 from campuswide resources. Because Senate membership has increased by approximately 30% since 1995/96, the Academic Senate requested its base funding be increased to $2 million per year, and future funding being adjusted relative to ICR growth.

2. **Recommendations:** After detailed review and impact assessment of each of the allocation elements noted above, the workgroup recommends implementing the following changes:

- Remove the Budget Committee’s specific allocations of ICR funds for Research, Animal Care, Effort Reporting System, AVC Research, and NGN from the current model and fund separately.
  - Phase out NGN subsidy from the ICR model in $200,000 increments each year starting in 2007/08, thus eliminating the subsidy by 2011/12. This would be offset with an equivalent increase in Vice Chancellor unit contributions using the NGN model which is more reflective of actual network usage.
  - Unit contributions to NGN to eventually be replaced entirely with higher communication user fees. It is recommended that user fees be adjusted beginning in 2009/10 thru 2011/12 to eliminate Vice Chancellor unit contributions. Specific changes to the user fee schedule should be made in consultation with the NGN advisory committee.
  - Other remaining Budget Committee allocations would be funded with a permanent assessment to each unit using the effective cost within the current 2006/07 model.

- Treat federal, state, private, and local recovery equally in the model.
  - Discontinue allocating UC General Funds exclusively to Academic units.
  - Include State research recovery in determining Academic pro-rata shares.

- Allocate all ICR funds based on a fixed 60% / 40% distribution between the Academic / Administrative units.

- Fund the Library allocation at 8% of the Academic unit total allocation.

- Increase Academic Senate COR funding and fix its allocation at 3% of the total Academic units’ allocation with a minimum allocation base of $1.4 million. The Academic Senate’s minimum base allocation from ICR funds will increase from the current $900,000 to $1.4 million over a five year period by simultaneously:
  - Continuing support of one-time funds from campuswide resources, decreasing from the current level of $500,000 by $100,000 per year; and
  - Increasing the permanent ICR funds by $100,000 per year over this same period.

In addition, the workgroup reaffirms no change to the following two allocation elements:

- Continue to use 2-year averaging to determine Academic unit pro-rata shares. This helps mitigate the impact of significant fluctuations in recovery within any one single-unit.
- Continue to make off-the-top deductions for Garamendi Project funding and Garamendi-type Campus Arrangements. These allocation adjustments were determined to be investments in the long-term interest of the campus.
Collectively, the changes recommended above reduce the complexity of the ICR model while minimizing the impact on any one particular campus unit.

**B. Deferred Maintenance (DM)**

Currently, the Campus does not have an ongoing budget for DM for State supportable space. The DM backlog for State supportable space is now estimated by Facilities Management to be at least $245 million, and growing. Of this amount, $36.4 million has been identified by a campus Deferred Maintenance Work Group as “mission critical” projects.

1. **Key Discussion:** No State or University funding has been provided since 2001/02. The situation is worsened by the under-funding of the Operations and Maintenance, Plant (O&MP) budget and the lack of funding for new research space coming on-line. There was consensus among the workgroup that ongoing funding needed to be provided for this growing campus need. The workgroup’s efforts focused on possible funding alternatives including:

   - **•** Borrow $20 million to help address the most immediate DM needs. Using the current planning rate of 5.75% over 15 years, would require annual funding of approximately $2 million per year for the next 15 years, but would not allow for new or other critical projects.
   - **•** Establish a base level of DM funding of $20 million to be funded over a four year period.
   - **•** A hybrid model that blends the above concepts. Establish an ongoing $3 million permanent budget and borrow $10 million in debt. Annual budget would be used partially to fund debt service, approximately $1 million per year for 15 years, and the remainder for other critical DM projects.
   - **•** Significant campus DM funding levels would require VC unit assessments. The allocation basis might be based on share of the total State-supportable space or Core Funds Budget.

2. **Recommendations:** The BRWG recommends that the Budget Committee adopt a funding plan, to begin in 2007/08, to allocate $3 million per year for DM projects. In addition, it recommends that approximately $10 million be borrowed over the course of the next two years to immediately address the most pressing critical projects. Approximately $1 million of the $3 million annual budget would be used to pay down debt service and the remainder would fund additional DM projects on the critical list.

   Vice Chancellor units would be assessed a share of the funding based on weighted State-supportable square feet. It is further proposed that Facilities Management look into developing weighting factors that take into account the varying construction and maintenance costs of research, classroom, office and other space. These weights would then be considered for use as a basis in determining unit assessments for deferred maintenance funding. Until these weights are available and reviewed, the current campus utility weights would be used.

   A process to determine priority and to update the long-term plan for deferred maintenance projects would be made in consultation with the Capital Outlay and Space Advisory Committee (COSAC), which already includes broad and regular campus consultation.
IV. IMPACT OF RECOMMENDATIONS

A. Implementation in 2006/07

There is no impact to the current campus allocation methodologies for the 2006/07 resource allocation process.

B. Implementation in 2007/08 and Future Years

It is proposed that recommendations contained in this BRWG report addendum be implemented beginning with the 2007/08 budget year. Changes recommended to the Academic Senate allocation and to the NGN subsidy within the model would be phased in over 5 years.

Recommendations impacting the 2007/08 and future budget years that require ongoing planning and consultation include:

- Changes to NGN communication user fees to replace the ICR subsidy should be made following consultation with the NGN advisory committee. The consultation is already underway.
- Deferred maintenance recommendations, require seeking the University of California, Office of the President’s approval for the $10 million in debt so that this funding is available beginning in 2007/08. In addition, a well-coordinated process to determine priority and to update the long-term plan for deferred maintenance projects in consultation with the Capital Outlay and Space Advisory Committee (COSAC), which already includes broad and regular campus consultation, is currently underway.

Lastly, given the complexity and constantly changing budgetary context, it is important to emphasize that a comprehensive review be conducted every 5-7 years, and that ad-hoc reviews be conducted of specific allocation components as deemed necessary by the campus.