The Fiscal Sustainability Journey at Minnesota State University Moorhead
August 23, 2011

Minnesota State University Moorhead (MSUM) now has a sustainable long-term budget plan. That means that we do not anticipate any major cuts as long as key planning elements remain within anticipated parameters. Our current sustainability reflects the hard work of many faculty and staff over the past three years.

The purpose of this document is to provide an overview of our budget plans and key elements of fiscal sustainability. To that end, we discuss our recent budget history, planning parameters and processes for fiscal sustainability, and long-term budget planning assumptions.

Recent Budget History
The following table shows MSUM’s recent budget history.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Structural Deficit</th>
<th>Decrease in State Allocation</th>
<th>State Allocation</th>
<th>Tuition Rate Increase From Previous Year</th>
<th>Total Tuition Revenue</th>
<th>Misc. Revenue</th>
<th>Total General Fund Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>09 (AY 08-09)</td>
<td>4.95M¹</td>
<td>$29.8M</td>
<td>3%</td>
<td>$32.9M</td>
<td>$.8M</td>
<td>$63.5M</td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>0</td>
<td>$3.3M</td>
<td>$26.6M</td>
<td>5%</td>
<td>$38M</td>
<td>$1.2M</td>
<td>$65.8</td>
</tr>
<tr>
<td>11</td>
<td>0</td>
<td>$.89M</td>
<td>$25.7M</td>
<td>5.13%</td>
<td>$39.4M</td>
<td>$1.4M</td>
<td>$66.5</td>
</tr>
<tr>
<td>12</td>
<td>0</td>
<td>$2.6M</td>
<td>$23.1M</td>
<td>5%</td>
<td>$41.8M</td>
<td>$1.8M</td>
<td>$66.7³</td>
</tr>
</tbody>
</table>

Notes
1. Prior to fiscal year 09, a structural deficit had gradually accumulated. It resulted from the combination of spending in excess of revenue and overly optimistic revenue projections. The total structural deficit of $4.95M was eliminated coming into the FY 10 and 11 biennium.
2. In FY 09, state appropriation comprised 48% of our general fund budget with tuition/fees comprising 52%. By FY 10, the state appropriation portion dropped to 41% and then to 39% in FY 11. Now, entering the FY12-13 biennium, it is 36% with the remaining 64% coming from tuition/fee revenue.
3. The general fund budget for the current biennium is projected at $66.7M. This is a conservative projection based on enrollment decreasing slightly. As you recall, we always underestimate revenue. Currently, we anticipate enrollment holding steady.
4. Note that federal stimulus money was used to decrease the actual tuition increase paid by the students during FY10 by 2% and FY11 by 2%.
5. Misc. revenue includes the auxiliary administrative fees and some differential tuition.

Planning Parameters and Key Elements for Fiscal Sustainability
As we know, to maintain a balanced budget, revenues must equal or exceed expenses. To maintain a sustainable budget that also invests in our future, projected increases in revenues must both exceed projected increases in expenses and provide additional funds for investment in quality improvement and in new growth areas that are consistent with our brand. For further discussion in this area see the discussion paper presented to the community in February 2011 at http://www.mnstate.edu/president/Speeches/fiscal/fsconceptpaper021011.pdf. In this section, we discuss the following key planning parameters and key elements for fiscal sustainability: revenue projections, expense projections, relationship of revenue projections to expense projections, return on investment and infrastructure funding, and campus processes that connect resource allocation to revenue generation and efficiency.

Revenue Projections
Like most public, comprehensive universities, our primary sources of revenue are tuition and state funding. Both are impacted by internal and external factors.

As we discussed in the February discussion draft, state funding is determined by the allocation from the state legislature and the MnSCU allocation framework, which takes into account enrollment, programmatic comparisons, and national spending levels. It is likely that MSUM’s state funding will continue to decrease for two reasons. First, we cannot assume state funding will remain at current levels. Fluctuation in state tax revenues, growth in other state funded programs (e.g., K-12, Human Services, Corrections), and the political process all influence MnSCU’s appropriation from the state. Second, even if enrollment grows at MSUM, our slice of the state appropriation pie is likely to decrease. Like the state’s demographic, enrollment is growing much faster in the metropolitan areas, thus increasing the number of students in the MnSCU system and decreasing the ratio of MSUM enrollment to total system enrollment.

Tuition revenue is influenced by structure, volume, and rate. Structure refers to how tuition is charged, including tuition banding and differential policies. Volume refers to enrollment numbers. Rate is the actual tuition rate charged. Interestingly, volume is influenced by rate. For example, if tuition increases are too steep or if the rate is too high in relationship to comparable institutions, enrollment tends to drop.

Currently, our tuition rate is very favorable compared to our peers. As reported in the System Board of Trustees material in June 2011, the fiscal year 2012 annual year tuition and fees for MSU-Moorhead are $6,937, and the comparable numbers for the other System residential universities are $7,300 at Bemidji State, $6,836 at MSU-Mankato, $6,846 at St. Cloud State, $7,424 at Southwest State, and $7,203 at Winona State. For our other competitors, comparable numbers are $13,060 for the University of Minnesota, $7,457 for NDSU, $12,350, for UM-Duluth, and $6,972 for UND.
Expense Projections
The largest portion of our increased expenses is likely to come from changes in personnel costs. Currently, personnel costs comprise 80% of our budget. Personnel costs are determined by negotiated compensation rates as well as by the number and composition of our workforce. Non-personnel or operating costs include such things as energy, materials, debt service for bonded projects, and contracted services. New building projects and major renovations are supported by separate state appropriations and are not included in this discussion of the budget.

Relationship of Revenue Projections to Expense Projections
We have a relatively closed system with just two major sources of revenue, tuition and state funding, and two major sources of expenses, personnel costs and operating expenses. Currently, tuition makes up 64% of projected revenue, and compensation accounts for 80% of projected expenses.

In order to maintain a balanced budget, increases in compensation expenses must be balanced by increases in tuition revenue from either tuition rate or student population increases. If tuition revenue increases do not keep pace with compensation increases, we must look to a decrease in expenses through budget cuts or increased productivity. Currently, a 1% compensation increase is approximately $500,000 and a 1% tuition revenue increase is $400,000. Thus, if we look only at increases in revenue and not at budget cuts, each 1% increase in compensation must be balanced by a 1.25% tuition revenue increase. Such an increase cannot come solely from an enrollment increase, because additional students imply additional personnel costs to maintain quality service. For the foreseeable future, the decision to replace departing personnel and to fund new positions must be evaluated in terms of its status as a strategic investment in the University.

Return on Investment and Infrastructure Funding
In addition to the direct costs of instruction (e.g., faculty), many indirect and infrastructure costs are necessary to maintain the university. Examples of those costs include energy, insurance, maintenance, technology, student and academic support personnel, admissions recruiters, and administration. Our current federal indirect rate is 44%, which reflects the percentage of estimated indirect costs as computed for federal grant purposes.

As we recall, tuition currently comprises 64% of our general fund budget with state funding comprising 34%. Thus, state funding is insufficient to maintain the infrastructure. This means that tuition revenue must not only cover direct instruction but also cover some infrastructure costs. Therefore, in order to remain fiscally sustainable, academic units cannot run a deficit. The overall return on investment (i.e., the ratio of tuition revenue to instructional and support costs) for the tuition dollar (i.e., the cost recovery rate) must be well above 100%. Fortunately, thanks to the hard work of our faculty and deans, our overall institutional cost recovery ratio has risen from 98% in FY09 to 126% in FY11. In order to us to remain sustainable and to have
some funds to invest in program improvement, innovation, or in new opportunities, we must maintain the overall cost recovery ratio above 120% while also improving program quality.

**Campus Processes that Connect Resource Allocation to Revenue Generation and Efficiency**

A number of campus processes help MSUM to stay on the path to fiscal sustainability by connecting resource allocation for personnel expenditures with revenue generation or efficiency. Two committees fill this role while also aiding in our efforts to foster transparency. Both the Academic Affairs Budget Advisory Committee (AABAC) and the Non-Instructional Budget Advisory Committee (NIBAC) review and recommend prioritization of long-term personnel expenditures. Both committees are comprised of Vice Presidents and/or Deans as well as appointees from relevant bargaining units. Both committees make recommendations to the president, who then weighs the recommended priorities along with revenue and expense projections before approving proposed hires.

The NIBAC focuses on efficiency of unit organization. When reviewing proposed positions, they review the unit organizational chart, may benchmark staffing against comparable units at other universities, consider potential consolidations or reorganizations for efficiency, and inquire about efficiencies through using LEAN process reorganization.

The AABAC has two major functions. First, it recommends prioritization of faculty hires based on cost recovery ratios, quality indicators including graduation rates, and other considerations, such as business plans for new or expanding programs. Second, it monitors cost recovery ratios and quality indicators for departments and programs, making recommendations for improvement where needed or potential consideration of program closure.

In addition to these committees, other campus processes aid sustainability. For example, the LEAN group has helped the campus to review and improve the efficiency of various processes (e.g., readmission, furniture orders). Similarly, energy monitoring and benchmarking has contributed to decreases in overall expenses.

**Long-Term Budget Plans**

We are making long-term budget projections using the following assumptions. First, as noted earlier, state funding is not certain and may decrease. Second, our goal is to gradually increase enrollment to a head count of 8,000 with some of the increase coming from residential students, some from online, some from the Twin Cities completer programs (e.g., the programs at North Hennepin Community College), and increased retention. It is hoped that some of the increased revenue from increased volume can offset some of the potential decrease in state funding.

Although compensation increases are negotiated at the MnSCU System and Minnesota Management & Budget (MMB) state levels, each campus must build plans for such increases into expense projections well in advance of the negotiations and potential settlements. This is because tuition increases, which are often constrained at the System level, cannot directly offset significant compensation increases. We have built a 5% compensation increase into the
budget plan for the 2012-13 biennium and plan to build in 3% each year thereafter. Funds that build up before we incur negotiated increases in compensation will be used for deferred maintenance as well as investments to increase revenue. Projected operating expense increases will continue to be tied to the consumer price index increases.

Tuition rate increases are subject to campus consultation with the Student Senate as well as approval by the MnSCU Board of Trustees. Given that caveat, we are modeling rate increases at 4 to 5% each year. As you recall, a 1.25% increase in tuition is needed to balance a 1% increase in compensation. When increases in tuition do not keep pace with compensation changes, sustainability requires reductions in personnel as a significant part of the solution. (You will recall that non-personnel costs are only 20% of the budget.)

In summary, at the present time our budget is balanced. This situation is thanks to the hard work of our dedicated faculty and staff as well as the understanding of our student leaders who supported needed tuition increases. As long as revenues and expenses remain within anticipated parameters, we expect that our budget will remain balanced for the foreseeable future.