Finance Reform

A new metrics-informed financial model designed to improve transparency, align incentives with campus goals, and simplify our planning and management environment

http://budget.berkeley.edu/financereform

Speaker Series
March 10 20165
Today’s objectives

• Introduce our new Strategic Initiative to design a new financial model for the campus

• To share our current state analysis and early elements of the new campus financial model

• To start an ongoing dialogue with you as we prepare to begin the design phase

• To clarify what the Project “is” and “is not”!
What is a financial model?

UC Berkeley is positioning itself to redesign our hybrid model.
Our work to date
UCB’s Case for Change

- Untenable revenue performance over the last decade
- We cannot resolve our financial sustainability issues at the center
- Campus is eager for change
- There is a desire to adopt allocation practices which support the strategic goals of the institution.
- Practices need to be simple, rational, incentivize revenue generation and cost containment
- The yearly budget review meeting remains a key leverage point.
- Shared collaboration is key to improve and optimize our resource allocation methodology

Feedback from the Education Advisory Board:

Growing Concerns About the Financial Sustainability of Higher Education

34% of University Presidents surveyed in 2014 are not confident in the sustainability of their institution’s financial model.

Revenues Under Pressure As Costs Continue to Grow

- State Budget Pressures
- Federal Budget Cuts
- Declining Median Incomes

- Employee Benefits
- Deferred Maintenance
- Rising Compliance Costs
- Legacy Programs

No Institution Is Immune – Elite Public Research University

- Multiple rounds of state budget cuts reduce strategic investment funds
- Major consulting engagement cut costs by 3% but didn’t slow cost growth
- Faculty resistance to shared services limits further cost savings
- State limits on tuition increases and growing financial need slowing revenue growth
- Declining federal research funding exposes dependence on indirect cost recovery funds

(Source: Education Advisory Board)
Project goals

• Sustain and enhance the academic preeminence of UC Berkeley, underpinned by a sustainable financial model

• Strengthen units’ abilities to influence revenue growth

• Simplify allocation decisions and processes

• Better allocate funding in line with campus priorities and workload

• Ensure provision of adequate strategic funding

• Allow campus leaders at every level to be nimble in allocating resources

• Encourage more horizontal collaboration
Early stages will focus on Academic units
The initiative will also simplify the funding of central services

- Simplifying UC Berkeley’s financial model impacts all units.

- We need to think about the best way to fund central services, e.g. simplify current recharge activity and re-examine carry forward policies

- This will be a complex exercise given the heterogeneous nature of these activities
Current State
UC Berkeley’s current financial model is extremely complex
There are many different processes, determined at different times, by different people, that make up one unit’s financial relationship to campus.
Low-value transactions occupy time, add cost, and make it difficult to forecast.

There were 150,000 manually generated budget journal lines in 2010-11. Of these, at least 65% (shown here) are immaterial to our $2 billion budget.

- 65% of budget journal lines are <$10,000
- 18% of budget journal lines are <$100
- 7% of budget journal lines are <$10

*Actual Dollars – Not in Thousands!*
Early Thinking:
Berkeley’s New Financial Model
The starting point

**Analysis:** after review, we know there is some equity and logic that has built a great university

**Findings:** allocations show a strong correlation between various metrics. A simple model using just three such metrics can explain more than 92% of current budget allocations…

**Next Steps:** build upon the findings to design a model that is more transparent and responsive to changes in workload
Outcomes from applying metrics to campus support

The best statistical equation to explain the distribution of current campus support to instructional units involved SCH, Grad Academic headcount, and Grad Professional headcount.

<table>
<thead>
<tr>
<th></th>
<th>SCH</th>
<th>Grad Acad HC</th>
<th>Grad Prof HC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value per Unit (coefficient)</td>
<td>$313</td>
<td>$30,508</td>
<td>$15,142</td>
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<tr>
<td>Confidence Level</td>
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<td>1.0000</td>
<td>.9961</td>
</tr>
<tr>
<td>Explanatory value ($r^2$)</td>
<td>0.922</td>
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Outcomes from applying metrics to campus support

SCH and Grad Academic Headcount have the strongest singular relationships to campus support as evidenced by high $r^2$ values (closer to 1.00 is a perfect relationship)

**SCH**

- $R^2 = 0.89$

**Grad Acad HC**

- $R^2 = 0.82$
Outcomes from applying metrics to campus support

Undergraduate Majors Headcount and Degrees Awarded are good but less related…

UG Majors Headcount

UG Degrees Awarded
The emerging new model

Central Campus Revenue Sources
Approximately $1.2B

Tuition and Fees
- Tuition
- Non-Resident Tuition
- Other Fees

State Appropriations
- State Appropriations

Other Income
- Indirect Cost Recovery
- Investment Income
- Gifts to Campus
- Sales and Services (AFC)
- Campus Reserves

Core Operating Budget
- Profit/Gain Sharing
- Informed by performance standards and based on approved budgets and Strategic Allocations

Metric informed Allocations
- Strategically Directed Funding

Schools and Colleges
- Various revenues flowing directly to units
- Capital Projects

Other Units
- Various revenues flowing directly to units

Capital Projects

Profit/Gain Sharing (year end balance)
Key metrics will inform resource distributions

**Hypothetical** Resource Distributions to Schools and Colleges

**What are the right metrics and values for our new financial model?**
Metrics-Informed Allocations – The Two Pronged Approach

1) Revenue Profile

- Strategically Directed Funding
- Professional Degrees & Programs
- Gifts & Endowments
- Research Funding
- Tuition & Fees

2) Cost Profile

- Support Budget
- Supplies & Expenses Budget
- Research Budget
- Instructional Budget

UNIT PROFILE
How should we collaborate going forward?

FY16
Design
Develop methodology
Gather Data
Design prototype
Communications
Stakeholder engagement
Review cost allocations

FY17
Test
Test prototype
Rollout interim TAS model
Build capacity
Establish incentives and policies
Prepare systems and reports

FY18
Implement
Roll out the new metrics-informed revenue model
Combine instruction budgets
Update carry-forward policies
Reform cost allocations

FY19
Make adjustments
Review to match experience and update methodology

Future Phases
Consider transition to a more autonomous model
Utilize performance/curriculum metrics