

THE UNIVERSITY OF MICHIGAN
REGENTS COMMUNICATION

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Regents
November 21, 2013

ITEM FOR INFORMATION

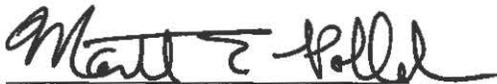
Subject: UM – Ann Arbor Response to the Fiscal Year 2015 Budget
Development Letter from the Michigan State Budget Office

Background:

As in recent years, the State Budget Office has made invitation to universities to respond in a letter to questions that would enable them to better understand the strategic challenges and opportunities facing Michigan's public universities. The office requested specific input related to the university's progress on the state's funding formula metrics, on the current achievements and future plans for cost containment, on outreach to U.S. Armed Forces veterans on campus, on strategic plans for the mission of the university and future enrollment in light of the State's declining K-12 enrollments and workforce transformation.

As this year's request was not in the form of a substantive budget request, and confirms the strategic direction that has been established with the Board of Regents, we responded with a letter on November 1, 2013, as requested, and provide herein as an item for information.

Respectfully submitted,



Martha E. Pollack
Provost and Executive Vice President
for Academic Affairs

November 21, 2013

Attachment

MARY SUE COLEMAN
PRESIDENT



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ANN ARBOR, MI 48109-1340
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November 1, 2013

Mr. John E. Nixon
State Budget Director
State of Michigan
111 South Capital
Post Office Box 30026
Lansing, Michigan 48909

Dear Mr. Nixon:

I am responding to your invitation to provide information to the state in support of the fiscal year 2015 budget development process for the University of Michigan–Ann Arbor. In this letter you will find information on the steps we are taking to improve performance under the state’s current higher-education funding model. We will provide an update to the details of our on-going efforts to contain costs and an explanation of our strategic plans regarding future enrollment in our key programs. Finally, we will describe the activities we are taking to welcome and support veterans of the U.S. Armed Services to our campus.

We continue to strive for a budget that strongly supports our commitments to academic excellence as well as affordability, including our longstanding policy to meet the full demonstrated financial need of all Michigan resident undergraduate students. As careful stewards of public resources, we remain focused on and dedicated to prudent and responsible financial planning.

The University of Michigan–Ann Arbor operates in an extremely competitive environment for faculty, students, staff and research dollars. We recognize the significant efforts the state has made in dealing with uncertain economic circumstances that require hard decisions and thoughtful prioritization of resources. We appreciate the recent modest increase in our state appropriation for fiscal year 2014, and want to stress how important it will be to retain this increase as base funding for fiscal year 2015. Also essential is additional base increases aimed at achieving the Business Leaders for Michigan’s (BLM) long-term goal of once again becoming a top-ten state in higher education funding. Like the BLM, we believe that strategic investment in higher education is essential to the future viability of the state and its economy.

Funding Formula Progress

The University of Michigan-Ann Arbor scores well on the performance funding measures developed by the state. We are committed to maintaining and, where possible, improving our success on these metrics. In the following passages we briefly describe some of the initiatives and efforts that are contributing to this progress.

Critical Skills Fields

The University of Michigan's enrollment has been growing slowly with an 11 percent increase overall in the past five years. While enrollment increases have varied across campus, we had seen some of the largest increases in Critical Skills areas like Engineering (18 percent), Business (13 percent), Nursing (11 percent) and Medicine (16 percent).

We are developing, or have developed, accelerated degree programs for students who may complete both a bachelor's and a master's degree in just five years, providing them with important professional credentials in fields where such a degree is highly desirable. Examples of these programs include Biophysics, Earth and Environmental Sciences, and Chemistry within the College of Literature, Science and the Arts, and Health Behavior and Health Education, Epidemiology, and Environmental Health Sciences within the School of Public Health.

The university also administers numerous outreach programs designed to foster interest among K-12 students in critical skills areas such as computer science, robotics, math, engineering, architecture and other STEM fields. We aim to bolster achievement and preparation for college work in these areas, providing research opportunities, mentoring, and access to U-M's world-class faculty.

Research & Development

With \$1.33 billion in research expenditures the University of Michigan is ranked No. #1 among public institutions nationwide, and No. #2 overall. We have a robust and diverse research portfolio and are proud of our world-renowned leadership in advancing knowledge in a wide range of fields. Our research and development activity contributes to the state's innovation agenda, creates jobs and draws talent to the region. A cornerstone of our research enterprise is the funding we receive from federal agencies, which is more than 60 percent of our total activity. However, we are keenly aware that growth in federal research spending is slowing and may even be reversed in the future. Institutional competition for research dollars surely will intensify. We are positioning the university to continue its leadership despite this environment by making strategic investments in growth areas and emerging research fields. We also continue to diversify our research funding sources with increased sponsorship from private industry and foundations. In fiscal year 2013 expenditures on research grants and contracts from industry reached nearly \$73 million, a 14 percent increase over the previous year. This is a significant increase, attributed to our continued value to the private sector. This level of funding corresponds to 8 percent of our total research volume from external sources, compared with the National Science Foundation estimate average of 5 percent for research-intensive universities.

This large proportion of external funding for U-M is particularly noteworthy given the breadth of disciplines pursued, as well as the extraordinarily large base funding of \$1.33 billion.

Six-Year Graduation Rate

Our six-year graduation rate is 91 percent, which places U-M in the upper echelon of institutions nationally. To maintain and further improve our students' high rate of success, we are enhancing our advising function on campus, including adding analytic tools that help monitor student progress and identify issues that are barriers to success and degree completion. Another critical piece to student success is our effort to increase opportunities for active and engaged learning experiences. Research opportunities, internships, field study and service learning programs help students make meaningful connections between their college experiences and their future endeavors. We also regularly solicit student feedback with the aim of improving the student experience.

Another key component to student success is our financial aid. For fiscal year 2014, we increased the general fund financial aid budget by \$16.4 million, a 13.7 percent increase for undergraduates, which meant that for the fifth straight year there was no increase in the net cost of a U-M education for resident undergraduate students with need. For many in-state undergraduate students with need, the total cost of attendance actually decreased, resulting in lower packaged loan amounts. Beyond our long-standing policy of meeting the full demonstrated need of Michigan students, we maximize the amount of grants and scholarships (aid that does not need to be repaid) and work hard to lower student loan burdens. This ensures that residents are well supported, significantly reducing the chance that they will interrupt their studies for a term or put their academic progress at risk by working long hours while enrolled. More than 70 percent of Michigan resident students report that they spend ten hours or less each week working for pay during the term. In fact, most of those students (41 percent overall) do not work at all during the academic year.

Total Degree Completions

The enrollment growth we have described, and incremental improvements in our retention and graduation rates, have helped to increase the number of degrees U-M awards at the undergraduate level by 8 percent over the past five years. Graduate and professional degrees have seen an even more significant increase over that same period, rising by 23 percent. This increase is the result of keen attention to factors that can increase graduate success. In recent years, we have worked to enhance the financial aid we provide graduate students, ensuring students are supported for the duration of their degree programs. We have initiated policies that encourage continuous progress toward degree, and bolstered the important mentoring relationships that are a crucial part of graduate education.

Because financial aid plays such an important role in successful degree completion at all levels, financial aid funding will be a top priority in the major fundraising campaign that the university will launch next week.

Institutional Support as a Percent of Core Expenditures

Cost containment has been a high priority on UM's campus for the past decade, and we seek cuts that do no harm to the academic mission of the university. Our current goal is to cut another \$120 million in recurring costs over the next five years. Recent efforts to meet that goal have included creating two campus-wide shared services organizations - for desktop support and for transactional finance and human resources processes. Both of these efforts allow us to operate more efficiently and, over time, reallocate resources to academic programs.

The university remains committed to continuous improvement, and we are well positioned to make progress on performance funding measures. However, some gains may appear modest because the university is starting from a position of high performance.

Cost Containment

The university continues on a stable financial path because of a disciplined approach to fiscal management that emphasizes multi-year budget planning, on-going cost containment, and continual reallocation of resources toward our highest priorities. This long-term focus has allowed us to minimize the negative impact of the global economic forces that continue to constrain financial resources so that we may continue to pursue our strategic investments in:

- Keeping a U-M education affordable by investing in student financial aid.
- Maintaining excellence by recruiting and retaining top faculty.
- Enhancing the student learning experience with new and innovative academic programming and experiential learning that are responsive to the current needs of our students.

Improvements in operating efficiency have enabled the university to increase central undergraduate financial aid budget by more than 10 percent in seven of the last eight years, even while support from the state has been declining (after adjusting for inflation). This extraordinary support has reduced the net cost for middle- and low-income Michigan families to a level that is actually lower today than it was in 2004.

We remain steadfast in our strategic approach to protect and strengthen the academic mission. The labor-intensive nature of teaching, the need to ensure affordable access, the obligation to preserve, archive, and invest in new technology, and the competition for the best faculty are powerful forces that drive up costs. In seeking efficiencies, we have adopted the following principles:

- Protect and invest in our core educational and research missions.
- Remain competitive for the best faculty, staff and students.
- Leverage our size and scale.
- Maintain high-quality essential services.
- Eliminate duplicate and lower priority activities.

- Shift costs from the general fund to other funding sources, where appropriate.
- Avoid short-term reductions that will raise costs or undercut quality in the long-term.
- Introduce centralization and greater sharing of resources in cases where this will result in higher quality services and/or more effective use of high quality facilities.
- Consider insourcing and outsourcing, when that leads to improvements in service at the same or lower costs.
- Take advantage of advanced technologies to achieve efficiency of operations.

Since fiscal year 2003, the university has set firm targets for cost containment. The first two phases of this work achieved \$245 million in annual recurring general fund cost reductions and cost avoidance. We are now on track to reduce another \$120 million between fiscal years 2013 and 2017.

Cost containment has been focused in the following areas:

- Unit reductions and/or reallocations to higher priorities.
- Strategic procurement.
- Health benefit restructuring.
- Energy initiatives.
- More efficient utilization of space and facilities.
- Greater productivity of staff.

For many years, we have incorporated an assumed level of reduction and reallocation, typically 1.5 percent to 2.0 percent of the budget, in each year's general fund budget proposal.

Key accomplishments during the first two phases of strategic sourcing include negotiating contracts on commodities such as computers, peripherals, office and medical supplies, furniture, travel, and maintenance on hardware and software. We also established annual processes to review purchasing patterns and explore opportunities to find additional savings.

Initiatives for energy conservation and sustainability include a university-wide program (Planet Blue), which has led to investments in sensors for electronic equipment, water fixtures, and building machinery designed to reduce energy and water use. During this time period, the university also was able to take advantage of significant savings due to an advanced investment in energy, LEED certified buildings, and regional chillers, all of which reduced recurring energy and utilities costs. In fiscal year 2013, energy conservation applied in 137 general fund buildings resulted in an 8.4 percent reduction in energy use and an avoidance of \$4 million in utility costs.

In the area of benefits, the health care plan was redesigned to share a greater portion of the cost with employees, to implement a waiting period for the retirement savings plan, to switch to

lower-cost vendors, to negotiate lower administrative fees, and to realize savings on an increase in the amount of generic drug dispensing.

Staff efficiencies were gained in facilities and maintenance operations by restructuring their work to align with geographic zones, implementing automated workflow processes in human resources, and an across-the-board move toward more employee self-service. A fund for on-going and major capital renewal was established by reallocating funds from lower priorities.

Similarly, a consolidation of the information technology resources eliminated redundant services and overhead.

We now are in the process of executing longer-term plans to achieve additional operational efficiencies and enhanced revenues in Phase III (2013 – 2017) worth \$120 million. These savings will again have a similar focus as the prior years, but will have a broader impact, as we attempt to integrate administrative efficiencies across the campus community.

A combination of unit reductions and reallocations, consolidation of administrative activities and staffing reductions allowed us to achieve more than \$30 million in savings during fiscal year 2013.

We are moving forward in fiscal year 2014 on the implementation of two major re-engineering projects. The first is in the area of technology, which is capable of reducing costs through automation and process efficiencies. The goal of the IT Rationalization project is to improve IT service delivery, reduce costs and upgrade the university's infrastructure for our office computing environment as well as our high-end research computing resources. Specific projects will target virtualizing servers across campus to reduce the amount of staff time, energy and hardware, while creating a net increase in computing efficiency; creating more efficient and consistent support systems for end-user computing; improving data storage offerings while reducing costs; and increasing the number of collaboration tools available to faculty, students and staff. Anticipated annual recurring savings will exceed \$8 million on general funds or \$13 million on all funds.

The other major project is the opening of a Shared Services Center. At this new facility, up to 300 existing employees will form a new team to perform transaction processing in the areas of finance and human resources. The goals are to increase operating efficiencies and to improve customer service. This will be achieved through standardizing business processes, eliminating non-valued added work, reorganizing and co-locating the workforce for finance and human resource activities, using enabling technology to streamline business processes and increasing the managerial span of control.

Efforts continue to reduce the total cost of benefits by reviewing and negotiating lower rates on vendor contracts, providing incentives for pharmaceutical mail-order use, switching to lower cost plans for major medical, and increasing medical and pharmacy co-pays.

Strategic sourcing continues with a four-year rolling cycle to review commodity contracts. The continued implementation of the managed-copier program across campus optimizes the total number of multi-functional devices serving units, and standardizes the type of printers and peripheral supplies (e.g., toner, paper, etc.). The anticipated annual recurring savings target is to reduce \$5 million on general funds and \$22 million on all funds by 2017.

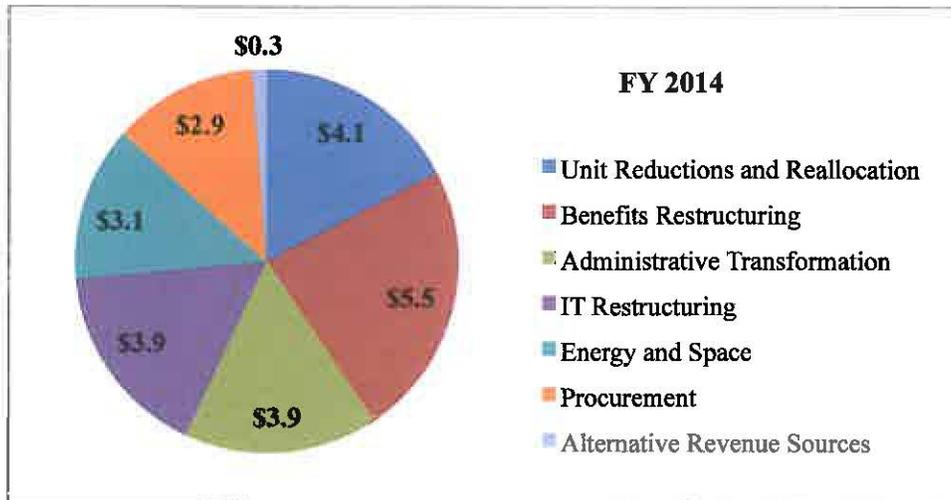


Figure 1: Phase 3 (fiscal year 2014) General Fund Reduction Plan

Additional savings of approximately \$27.1 million will be generated in fiscal year 2015 based on the programs being executed now.

Working to realize this level of cost containment has become more difficult, and in turn, it has been disruptive, but necessary. We are committed to exploring all possible ways to be more efficient in order to manage cost increases and enable investments in financial aid, faculty recruitment and retention and academic programs. But, there is a risk that consistently cutting and reallocating at a level higher than our rate of new investment will have a negative impact on the quality of the institution. Even with modest increases in state support, it will become increasingly challenging to continue to provide the same level of financial aid to our students, to attract and retain world-class faculty on the Ann Arbor campus, and to provide the range of innovative educational programs that we do today.

Although we are buoyed by our progress, we recognize that the fiscal environment remains challenging. These disciplined and strategic efforts around cost containment and revenue enhancement have been key to our success during this difficult financial period, and will help to position us for a stable future. A renewed effort to improve support from the state of Michigan has never been more important for a sustainable future.

Details of our cost containment activities may be found at <http://www.vpcomm.umih.edu/pa/key/budget/>

Strategic Planning

Enrollment on the Ann Arbor campus has been increasing steadily to an overall total of 43,426 as of fall 2012. Average annualized growth in enrollment over the past five years has been 2.3 percent signaling enduring interest in the degree programs offered by the institution.

Undergraduate enrollment was 27,956, and graduate enrollment was 15,470. Average annualized growth over the period has been 1.8 percent and 3.3 percent respectively.

Freshmen and transfer students are admitted to specific schools and colleges and for our largest, the College of Literature, Science and the Arts, undergraduate students are not required to initially select a major. In fall 2012 9,070 LS&A undergraduate students were “Undeclared.” After LS&A, the top five undergraduate programs by enrollment for fall 2012 were Engineering (5,757), Business (1,333), Kinesiology (883), Music, Theatre & Dance (792), and Nursing (641). While enrollments may vary somewhat over the next five years, we have no plan to change the overall enrollment.

The university believes strongly that the preparation of future leaders includes a strong general education base complemented by tangible applied skills. To this end, we are strengthening links between our undergraduate and graduate professional programs. Our graduate and professional schools of law, public health, social work, and information have each increased opportunities for undergraduate students to explore these fields and gain knowledge and skills that enhance their undergraduate studies. In some schools, undergraduate students can explore future professional interests; in others they may be able to take sufficient courses to earn a professional credential such as a major or minor. In programs like pharmacy and architecture, undergraduates may transition to graduate study before the bachelor degree is completed, earning both graduate and undergraduate degrees concurrently or sequentially.

Within the state of Michigan, the number of high school graduates is in a steep decline, a trend that is projected to continue through this decade. Nonetheless, U-M continues to be a strong draw for Michigan students who believe they can succeed here. The university presents an opportunity for Michigan’s top high school graduates to attain a truly world-class education within the borders of their home state and at an affordable cost. We continue to place access and affordability for these students as one of our very highest priorities.

Veteran Outreach

The University of Michigan-Ann Arbor remains committed to providing the highest level of support and educational opportunities for our service members, veterans, spouses and dependents.

Activities designed to welcome veterans and military students

The Veteran and Military Services Program (VMS) provides a comprehensive program of support and guidance to student veterans and service members. The program serves as their single point of contact to streamline services, support, and access to such offices as admissions,

advising, financial aid, counseling, and disability services. VMS provides assistance with deployment and return, supports a peer mentoring program, advises veteran/military student organizations, plans educational workshops and orientations, and hosts the annual Veteran and Military Symposium to increase the breadth and depth of campus awareness of needs and issues facing student veterans and service members.

Our commitment to support students with military experience

In July 2013, the Board of Regents approved a change to the in-state tuition guidelines, effective January 2014, to provide in-state tuition for all veterans, reservists, active-duty military and spouses and dependents of active duty military members.

U-M continues to assure that students with military backgrounds can afford a Michigan education by participating fully in the Yellow Ribbon program. The Yellow Ribbon program allows U-M to enter into an agreement with the Veteran's Administration (VA) to cover unmet tuition charges a student veteran may have after their GI Bill benefits have been applied to their tuition costs. Additionally, when the VA reported delays in processing student benefits, U-M was one of the first universities to implement a special process to ensure that all Post 9/11 GI Bill tuition was paid immediately after certification so students were not negatively affected.

In the spring of 2013, the university approved priority registration for student veterans, active duty military and National Guard and reserve members to facilitate the fulfillment of degree requirements mandated by the Post 9/11 GI bill.

U-M regularly commits to federal guidelines and initiatives related to veterans education, including Executive Order 13607 "Principles of Excellence for Military and Tuition Assistance and Veterans Education Benefits Program" (2012); the Department of Defense Voluntary Educational Partnership Memorandum of Understanding (2012); and the White House's "8 Keys to Success" (2013).

U-M partners with the VA to facilitate student veteran access to VA healthcare and benefits. We are a Vet Success Campus—hosting a Vocational Rehabilitation counselor from the VA on campus one day a week. U-M also is designated a Veterans Integration to Academic Leadership (VITAL) campus and brings a VA Healthcare representative to our major campus events and Student Veterans of America (SVA) meetings.

The university is a founding member of the Consortium of Michigan Veteran Educators; the primary mission of this organization is to increase student veteran awareness and advocacy statewide.

U-M is a founding member of the SVA, a national organization with more than 400 institutions now participating. Our vibrant SVA chapter is involved with an annual benefit dinner, veteran's week activities, and many other social and charitable events.

Economic Impact

U-M values its important role in economic development for the state. We regard it an essential part of our mission as a public university. We maintain a top academic enterprise so that our campus remains an economic development engine. Here, world-class talent, state-of-the-art facilities, and essential supporting infrastructure come together to create an environment where ideas and innovation flourish. The resulting benefits extend well beyond our campus.

A key element to the university's success in economic development is establishing strong relationships between our campus and both private industry and government. These efforts are demonstrated in our commitment to technology transfer, business engagement, partnerships with industry, student internships, community assistance, and a burgeoning campus entrepreneurial culture. Many of our efforts are ongoing, building upon years and a decade prior success. Other initiatives are new this year.

This year the university launched several new "acceleration" programs. In March, UM announced the Michigan Translational Research and Commercialization (M-TRAC) for Life Sciences. A new \$7.5 million fund – including a \$2.4 million grant from the Michigan Economic Development Corp.'s 21st Century Jobs Fund – will help U-M medical discoveries make the leap from the laboratory to the market, accelerating the potential of promising research projects to reach commercial success and help patients.

Building on the state's rich history in the automotive industry, two programs recently launched have the potential to revolutionize mobility and transportation. The Michigan Mobility Transformation Center is a partnership with the U-M Transportation Research Institute (UMTRI), the government, and industry to dramatically improve the safety, sustainability and accessibility of ways that people and goods move from place to place. Researchers will be able to test emerging concepts in connected and automated vehicles and vehicle systems. Similarly, M-TRAC Transportation was co-launched by UMTRI and the College of Engineering and is jointly funded by the university and the Michigan Economic Development Corp. Both of these projects have the potential to bring significant economic growth and innovation to the state in the area of transportation.

The success of the Business Engagement Center (BEC) continues into its sixth year. The BEC was founded to be a "front door" for companies seeking access to the university's expertise and other resources. The BEC now maintains relationships with more than 1,000 companies. The BEC partners with numerous other state and regional organizations such as the Small Business Association of Michigan, Ann Arbor SPARK, Pure Michigan, and chambers of commerce across the state.

Commercialization of university research is creating jobs and improving the quality of life for the residents of Michigan and beyond. U-M Tech Transfer recorded 108 licenses and options with existing and new businesses in fiscal year 2013. U-M researchers reported 421 new inventions, a record. Nine new startup ventures were launched in fiscal year 2013 with the

guidance and resources of Tech Transfer's Venture Center. The Venture Center is a one-stop hub for entrepreneurs and investors looking for startup opportunities based on U-M research. The pace of innovation is accelerating; it has launched an average of one new company every five weeks. The university also reported that 128 U.S. patents were issued in fiscal year 2013, up from 101 in fiscal year 2012. Licensing revenues increased from \$13.8 million to \$14.4 million, providing funds for the university to reinvest in research and innovation.

Student enthusiasm for entrepreneurship flourishes on our campus. We offer several courses, certificates, and degree programs for undergraduate, graduate, and professional students. The role of entrepreneurship extends beyond our Engineering and Business schools, however, and a two-year pilot initiative will implement a new curricular program "Be the Difference," which will coordinate and grow both curricular and co-curricular activities and communicate the importance of this area of interest more broadly across campus. Academic programs position U-M students to become leaders in innovation. They need not wait until graduation to get started, however. Through our Center for Entrepreneurship, the Zell Lurie Institute for Entrepreneurship, and student organizations like M-Powered and the Entrepreneur & Venture Club, our students can secure funding, obtain mentoring, find legal advice, access prototyping facilities, gather leads for outside investing, and receive other support critical to turning their innovative ideas into successful ventures.

The University Research Corridor is another way the university leverages its economic development muscle. Since 2006 the URC has allowed U-M, Wayne State University, and Michigan State University to collaborate and strengthen the role we play in transforming the state's economy. Another critical consortium role for the University is the Michigan Initiative for Innovation and Entrepreneurship (MIIE). The MIIE partners industry and philanthropic funding with university resources to help strengthen ties between small business, industry, and academia across the entire state. With a goal of funding 200 startups in a decade, the MIIE deploys resources to speed commercialization of university research and encourage innovation and entrepreneurial risk-taking.

The university's substantial research portfolio is the foundation of our economic impact in Michigan. In fiscal year 2013, the university had a record \$1.33 billion in research expenditures. Federal sponsorship represented almost 62 percent of this total, meaning the university's research activity attracted \$800 million in federal funds to the state. The research we conduct helps us develop the people and the ideas that drive the creation of new products and services, new companies, and entirely new industries.

Conclusion

To achieve our mission and to advance the excellence of the institution, we must maintain a focus on the future. Despite funding challenges, we must continually innovate so that the topics we study, and the methods we use to create knowledge, remain at the cutting edge.

Over the past several years, we have relied heavily on internal reallocation and cost containment to mitigate the effects of rising costs and simultaneous reductions in state support. We must continue these efforts – but there are risks to the institution if even modest relief does not materialize. Our costs continue to rise, the national faculty environment remains fiercely competitive, the needs of our student body continue to grow, and we must continue to ensure that qualified students of all economic backgrounds are able to attend the university.

As you are aware, the university has been appreciative of the advocacy of the Business Leaders for Michigan, who agree that as the state's recovery continues, support for higher education also should increase. BLM has advanced a public goal of adding \$100 million annually to higher education in our state over the next ten years. We are very supportive of this and acknowledge that the increases to higher education over the last two years have been steps in the right direction to achieve that goal. We respectfully ask that thoughtful consideration be given to making further progress in reaching the annual goal in the coming year.

For our state to be prosperous and successful, higher education must flourish. As one of the world's leading educational and research institutions, the University of Michigan is a key resource that can help stabilize and revitalize the Michigan economy. We are managing our resources strategically so that we can maintain the ability of the university to contribute to the vitality of our region, and the nation. The state's continued and expanded investment in our success is central to our collective future.

Sincerely,

A handwritten signature in black ink, reading "Mary Sue Coleman". The signature is fluid and cursive, with a long horizontal flourish extending to the left.

Mary Sue Coleman
President