

Following is a condensation of the budget report presented by Glen R. Stine, director of Budget Analysis, to the Trustees in June as they adopted the 1984-85 budget. The chief alterations are the elimination of technical discussion of revenues as noted below under "Key Trends and Indicators," and of figures more detailed than in the overall budget shown on page IV.

Budget for The University of Pennsylvania Fiscal Year 1984-85

June 22, 1984

Executive Summary

The University of Pennsylvania's total outline budget for fiscal year 1985, including the health services and restricted components of the budget, totals \$748.4 million. The balance of the budget is achieved only after each of the schools, resource centers, auxiliary enterprises and administrative service centers achieve balance. In setting this outline budget, the University followed the President's planning priorities stated in "Choosing Penn's Future" and worked closely with the Deans and Academic Planning and Budget Committee in establishing numerous important academic and fiscal objectives.

- To provide real growth in faculty salaries.
- To maintain and enhance the quality and diversity of its student body by holding total increases for undergraduate and graduate students for 1985 to 7.6%—including increases of 8% for tuition, 7% for residences and 6% for dining.
- To stabilize its graduate Ph.D. enrollments and improve the quality of its Ph.D. students through a major increase in University graduate fellowships and new support for graduate research assistants.
- To help ensure that admitted students and families can meet the cost of a Penn education, the University has implemented the Penn Plan and will continue to meet its commitment to need-blind admissions.
- To continue to meet deferred maintenance problems, the University has provided funds for 1985 to pay for a number of important amortizations of renovations and has increased its funded deferred maintenance program.
- To support the Library's special requirements for maintaining its collections.

In "Choosing Penn's Future" the President emphasized that "we will succeed best by being careful in husbanding our resources in order that we may boldly invest in our own future." Therefore, in order to accomplish these academic and fiscal objectives, a series of extremely difficult management decisions were necessary. Most important of which was limiting controllable administrative cost increases to 2% except for the area of development where the University will be spending more to gain more. Among many other examples, continued implementation of energy conservation has allowed the University to reduce its estimates of consumption by 3% for 1985. To continue to improve the financial health of the institution the fiscal year 1985 budget calls for the University to drop the sending rule .2%—6.4% to 6.2%.

Other assumptions and indicators used in the preparation of the budget include:

- Stable undergraduate enrollments even with increased applications.
- Strong and stable enrollments in the School of Medicine, Veterinary Medicine, and Law and Wharton.
- An aggressive development effort yielding another record fund raising year.

- A.I.F. spendable income increasing by 10.9%
- Continued competitive position in federal research grant and contract awards with marginal increases in indirect cost recoveries.
- The requirement of meeting extraordinary employee benefit increases.

Finally, the University must be seriously concerned about potential problems in uncontrollable expense areas. Possible major electrical increases, telephone line charges, and interest rate increases would all have serious implications for the University and heavy impact on the budget.

Outline FY 1984-85 Budget Document

The University of Pennsylvania's budget outline for fiscal year 1985 will total \$748.4 million. This total can be divided into three major components with the University portion of the unrestricted budget totalling \$301.5 million, the Health Services component totalling \$300.0 million, and the projection of restricted expenditures being \$146.9 million. The budget outline presented here represents a total increase in both revenues and expenditures of 8.6% above the comparable budget figures for the current year. The budget is in balance, with the largest growth of 9.4% occurring in the Health Services component.

Key Trends and Indicators

Revenues

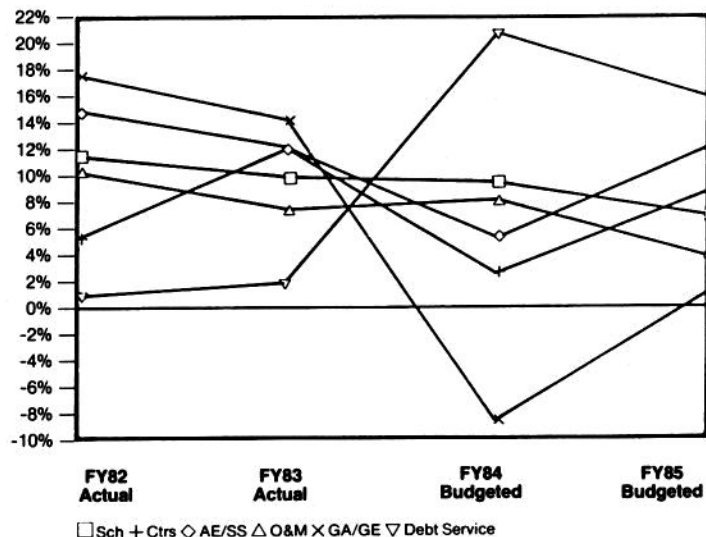
The University's revenues are affected by an array of factors characteristic of large research universities. The six key indicators of change are enrollments, research activity, fund raising, investment activity, sales of services, and external appropriations. Since our budget system distributes these revenues to the various parts of the University, any major financial shifts in any school can also have an impact on the entire budget.

Enrollment-driven revenues are key. They have an important effect on student services revenues, and link directly to revenues for auxiliary enterprises such as the residence halls, dining service, and bookstore. Since most of these services follow our regular academic year enrollments, it is vital that we monitor them closely.

[At this point in the full report, a series of annotated graphs shows multi-year trends for many of the key revenue indicators. Some will appear in longer progress reports being readied for *Almanac* by those in charge of investments, research grants and overhead, etc. An overview of "Financial Health Indicators" is retained in this document (page III).—Ed.]

Percent Change in Expenditures By Purpose, FY82 to FY85

Percent Change



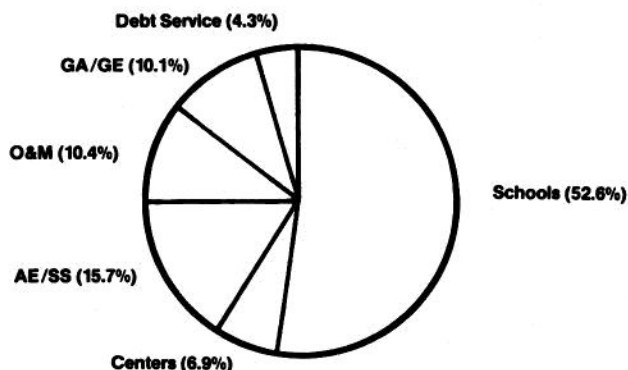
Expenditures

A number of factors affect the University's expenses. Inflation, amounts of service provided, and changes in both the knowledge base and technology are all key. The University must particularly watch the balance among major areas of expenditures. Instruction and research are the purposes of Penn's existence, and it is essential to maximize the percentage of the budget allocated to these purposes.

Above are the year-to-year percentage changes in major expenditure categories. The graph indicates a relative stable annual growth in the indirect expenditures of schools, between 11.5% and 8.0% while the resource centers and auxiliary enterprises show more sporadic, but general growth throughout the period. Debt service has been also steady in recent years with some growth planned for FY1985 due to renovations to the Quad and the stadium.

Of particular importance, the expenses of the University's central administration, as the result of several important efforts, has been growing much more slowly in recent years. This can be seen in both General Administration/General Expense (GA/GE) lines and the plant operations and maintenance lines. Shown below are the relative expenditure percentages planned for the FY1985 budget.

FY85 Unrestricted Budgeted Expense By Purpose



Managerial Objectives and Accomplishments

The University's budget planning process for FY1985 started early last summer (1983) by reviewing directions and trends with each school and center. The formulation of the budget goals, however, began much earlier. During 1982 the Council of Deans prepared six working papers on important issues facing the University. With the help of the Academic Planning and Budget Committee, these papers were widely discussed throughout the campus. The papers and the reactions they produced helped the President shape the University's strategic plan, "Choosing Penn's Future." These documents, discussions within the Academic Planning and Budget Committee, the Council of Deans and the Board of Trustees, formed the essential guidelines for starting the budget planning process. They established a number of important objectives—both academic and fiscal.

We began with the fundamental premise that the University budget must be balanced. This premise in turn requires balanced budgets for the twelve schools, five resource centers, and four auxiliary enterprises. We also recognized the tendency in some parts of the University to overproject income, particularly from graduate enrollments, and we knew we would have little or no new subvention funds to provide for the schools. Nevertheless, we believe that realistic balanced budgets have been accomplished.

"Choosing Penn's Future" established a second key aim: real growth annually and over a sustained period in faculty salaries. The University has accomplished this aim since 1981, after a period when faculty salary increases were less than the growth in the cost of living. The 5% salary pool increase plus a special central salary reserve for market adjustment and special merit will allow the University to continue to meet this objective again in FY1985. Continued high increases in our employee benefit costs mean, however, that overall compensation is increasing at a substantially faster rate than the salary increase.

A third objective was to bring down the rate of tuition increase to a level more nearly reflecting the rate of inflation and growth in family incomes. Even with the implementation of the Penn Plan, the pressures of financing a University education required this step. It is essential to maintain our competitive position vis-a-vis other schools and to keep our student body diverse. The projected 7.6% increase in total costs and 8% increase in tuition are higher than the inflation rate, but they represent a major reduction from the tuition increases of recent years. (In the 1983-84 budget, the increases were 9.9% and 11% respectively.)

A fourth critical set of objectives was to meet vital emerging academic priorities. With the assistance of external support, we are launching two major new academic program efforts—the Joseph H. Lauder Institute for Management and International Affairs and a new Plant Science Institute.

With allocations of scarce unrestricted funds, we are working to stabilize our graduate Ph.D. enrollments and improve the quality of our Ph.D. students through an \$800,000 (47%) increase in University graduate fellowships, and a new fund that will support one-half of a graduate student's tuition when the other half is supported by a research grant or contract. This fund will also assist in making our research grants more competitive.

Implementation of the University's new academic computing plan is also a key objective that is partially funded in this budget, though we recognize that the implications of the plan will continue to have major cost implications for many years to come. Steps are also underway to upgrade our administrative information systems, and with the hiring of a new Vice Provost for Computing, we expect to make significant progress in both areas next year.

Among schools, many important steps are underway. Of particular importance, the Dental School has developed its budget in a way that should accomplish a major revamping of its programs and improve quality, while reducing the number of students in the entering class from 108 in FY1984 to 75 in FY1985.

A fifth area of concern has been meeting deferred maintenance problems. This operating budget provides essential funding for sustaining a

(continued past insert)

number of efforts. The Residence Hall budget provides amortization costs for continued renovation of the Quad dormitories including a major utility project to be completed this summer and allows us to move into completion of the rest of the renovations in the next 5 years. An 8% increase in planned maintenance and showcasing is also in the residence budget. Funds are available to pay for amortizations of the renovations in Franklin Field, the Evans Building, New Bolton Center and for the acquisition of Blockley Hall. Finally, a funded deferred maintenance program will be increased 20% and the utility budget has additional funds for renovation of its key chiller capacities in the chemistry area. We also hope that fund raising efforts will be successful in providing funds for other efforts.

These important objectives could not have been accomplished without a series of extremely difficult management actions. Most important, the President, in early October of 1983, sent to his major administrative officers a memorandum limiting controllable administrative cost increases to 2%. Except for the area of development where we are spending more to gain more, that goal was substantially met. The administrative areas have been charged to again meet that goal for FY1986. Among many other examples of managerial actions, continued implementation of energy conservation has allowed us to reduce our estimates of consumption by 3% for next year.

Financial Health Indicators

The complexity of the University of Pennsylvania's budget means that many factors contribute to its financial health. Important elements like the University's ability to plan and adapt to its changing external environment are difficult to quantify. Several indicators suggest, however, that the University's financial position is sound though subject to many uncertainties.

First, the University is enjoying another increase in applicants to its undergraduate programs. This is particularly significant given the decline in the number of 18 year olds who make up the applicant pool. Using the Penn Plan as a primary vehicle for marketing the University's ability to assist students with financing our education, we also hope over the next several years to see an improvement in our yield rate.

Second, strong admission pools remain in the Schools of Medicine, Veterinary Medicine, Law, and Wharton. Improvements in applicants and enrollments were seen in FY1984 in architecture, social work, and education; continued improvement is needed if the University is to remain healthy. Even in the Dental School where applications have fallen, the implementation of a plan for major restructuring shows both vitality and adaptability.

The document "Building Penn's Future" sets forth an aggressive development effort. Campaigns have been established for a number of schools and centers. We cannot yet measure the yield of these efforts, but a record year for fund raising is expected in FY1984 and school budgets reflect expectations of continued growth. Preliminary results of the efforts can be seen in our restricted gift accounts. The table below shows the statistics.

*Comparison of Restricted Gift Revenues, Expenditures
and Balances Available
Eleven Months Ended May 31, 1984 and 1983
(in thousands of dollars)*

| | Balance July 1 | Current Revenue | Current Expense | Net Current Year | Balance May 31 |
|---------------|-------------------|--------------------|--------------------|------------------------|-------------------|
| FY1984 | \$23,790 | \$17,673 | \$14,508 | \$3,165 | \$26,955 |
| FY1983 | 22,196 | 16,038 | 14,186 | 1,852 | 24,048 |
| Change Amount | \$1,594 | 1,635 | 322 | 1,313 | 2,907 |
| % | 7.2 | 10.2 | 2.3 | | 12.1 |

Increases in fund balances are being shown in a number of auxiliaries and restricted service centers as well. The University has also taken steps to address several problems in these areas.

Similar strength in restricted funding is also shown in our investment

income. Continuing accounts in the AIF will grow 10.9% in expendable income for FY1985. For the first time in three years, the available income will grow at a rate faster than the rate of overall budget growth. The success of John Neff and his colleagues is clearly the major reason behind this change. Also important has been the institution of a spending rule on the percentage of the A.I.F. that may be used annually. The income reinvested from the implementation of the spending rule now represents approximately one-third of the growth in spendable income. To further this approach and to recognize the strength of our investment strategy the fiscal year 1985 budget calls for the University to drop the spending rule .2%—from 6.4% to 6.2%. This effort will continue to improve the financial health of the institution.

Another key to the University's financial picture is strength in external research support during FY1984. It has been an excellent year, as the table below showing grant and contract awards shows. Most important these numbers suggest that the University seems to be increasingly competitive and able to attract a growing percentage of the federal dollars available. Another encouraging indicator is the increase in award dollar months available to 7.7 from 5.7 a year ago. The indirect cost recoveries in the FY1985 budget, however, raise troubling concerns about our ability to sustain continued increases. The indirect cost recovery rate has also dropped from 65% of modified total direct costs to 64%. This reduction in rate, however, is the result of a rate negotiation with the federal government which substantially reduces our potential past liabilities, and thus, we believe strengthens our long range financial health.

*Grant and Contract Award Summary
(in thousands of dollars)*

| | FY1982 | FY1983 | % Change | FY1984 | % Change |
|-------------|-----------|-----------|-------------|-----------|-------------|
| Medical | \$74,186 | \$73,260 | (1.2) | \$87,500 | 19.4 |
| Non-Medical | 39,045 | 39,746 | 1.8 | 48,200 | 21.3 |
| Total | \$113,231 | \$113,006 | (.2) | \$135,700 | 20.1 |

A financial statement is obviously not the primary measure of Penn's success, but it does indicate a sound financial structure. The recent AA bond rating for the Hospital's issue and the equipment financing issue is partly a reflection of the overall University's financial health.

Continuing Concerns

Though the University's financial picture is generally positive, a number of areas require continuing attention. The positive balances in University the over the last several years have been always less than 1% of the entire budget. Unexpected changes in our environment or an inability to address weak areas could lead us to a negative financial position. Even though modest contingency funding must and has been built into this budget, the University must also work to address its continuing problems.

Graduate (Ph.D.) enrollment remains a concern in spite of both a slight increase in enrollments this past fall, and the steps described earlier as part of an effort to stimulate enrollments. Substantial additional efforts are needed in future years. Even with the increases in graduate fellowships and the subsidy for research assistantships, our graduate support is considerably below a number of Penn's peers. The demographic changes and need for technological advancement suggests that increasing national attention will be focused on the need for superbly trained graduate students. The University of Pennsylvania must overcome its current problems to remain competitive in the face of short term enrollment problems.

Our deferred maintenance problems continue to be a primary concern. From an academic perspective, upgrading research labs and facilities takes highest priority. At stake is a \$130 million externally funded research base, national prominence, and the ability to attract quality faculty. Examples of planned efforts to meet this problem are

abundant—the development of a micro-fabrication laboratory in Engineering, chemistry and laser lab renovations, a Plant Sciences building in Arts and Sciences, considerable efforts in the School of Medicine, and the Nuclear Magnetic Resonator Facility at the Hospital. The upgrading of the computer facilities provides further examples. Nevertheless, we are not able to meet the needs. New Bolton Center faces considerable problems and many major research facilities like the Laboratory for Research on the Structure of Matter are in need of renovation. Technology changes alone probably require that the University invest funds in these efforts at a rate as high as 3% above inflation.

The University library is receiving additional subvention in FY1985 designed to allow it to maintain the current position of its collections. Yet over the last several years, extremely high rates of inflation in books and periodical costs have reduced the numbers that could be purchased. Furthermore, the library is poised on a new era of computerized informa-

tion retrieval in which it must have a major role. Each increase in library funding, however, must mainly come from central subvention since the library has no other source. Yet this funding pressure is seriously limiting our ability to accomplish other academic priorities. To meet the full library need would totally eliminate our ability to do anything else. Thus we have placed the library as a high priority in our development efforts next year.

Finally the University must be seriously concerned about potential problems in uncontrollable expense areas. Possible major electrical increases, telephone line charges, and interest rate increases would all have serious implications for the University and a heavy impact on the budget.

In short, the budget discussed here represents considerable planning and the efforts of many people. It is based on key managerial efforts to implement our academic objectives.

University Operating Budget by Center, Fiscal Year 1985

(in thousands of dollars)

| | REVENUES | | | | | | | EXPENDITURES | | | | |
|--|----------------|----------------|------------------------------|-----------------|----------------|-----------------|----------------|----------------|----------------|--------------------------------|----------------|----------------|
| | Direct | | General University Resources | | | | | Direct | | Allocated Costs | | |
| | Unrestricted | Restricted | Program Special | Program Regular | Financial Aid | University Bank | Total | Unrestricted | Restricted | Administrative Service Centers | Net Space | Total |
| Schools | | | | | | | | | | | | |
| Annenberg School | 828 | 5,742 | | 88 | 77 | 7 | 6,742 | 369 | 5,742 | 604 | 27 | 6,742 |
| Arts & Sciences | 58,292 | 27,038 | | 11,294 | 2,170 | (103) | 98,691 | 53,391 | 27,038 | 17,843 | 419 | 98,691 |
| Dental Medicine | 13,970 | 4,425 | 805 | 2,953 | 76 | (44) | 22,185 | 13,697 | 4,425 | 3,964 | 99 | 22,185 |
| Education | 3,650 | 809 | | 484 | 77 | (56) | 4,964 | 3,383 | 809 | 759 | 13 | 4,964 |
| Engineering | 11,571 | 9,216 | | 2,463 | 270 | (28) | 23,492 | 10,384 | 9,216 | 3,800 | 92 | 23,492 |
| Fine Arts | 5,120 | 801 | | 1,952 | 160 | (18) | 8,015 | 5,661 | 801 | 1,502 | 51 | 8,015 |
| Law | 6,946 | 524 | | 1,491 | 157 | 91 | 9,209 | 6,914 | 524 | 1,713 | 58 | 9,209 |
| Medicine | 24,347 | 58,266 | 3,467 | 1,144 | | 81 | 87,305 | 14,199 | 58,266 | 14,582 | 258 | 87,305 |
| Nursing | 4,392 | 2,007 | | 227 | 75 | 229 | 6,930 | 3,776 | 2,007 | 1,124 | 23 | 6,930 |
| Social Work | 1,274 | 296 | | 448 | 46 | (45) | 2,019 | 1,419 | 296 | 299 | 5 | 2,019 |
| Veterinary Medicine | 13,665 | 7,078 | 8,519 | 1,064 | | (172) | 30,154 | 17,590 | 7,078 | 5,367 | 119 | 30,154 |
| Wharton | 31,178 | 16,938 | | 1,662 | 676 | | 50,454 | 26,146 | 16,938 | 7,211 | 159 | 50,454 |
| TOTAL | 175,233 | 133,140 | 12,791 | 25,270 | 3,784 | (58) | 350,180 | 156,929 | 133,140 | 58,768 | 1,323 | 350,160 |
| Resource Centers | | | | | | | | | | | | |
| Annenberg Center | 1,272 | 96 | | 771 | | | 2,139 | 1,604 | 96 | 415 | 24 | 2,139 |
| Intercollegiate Athletics | 1,184 | 343 | | 3,995 | | | 5,522 | 3,698 | 343 | 1,410 | 71 | 5,522 |
| Interdisciplinary | 608 | 7,708 | | 2,946 | 14 | | 11,276 | 2,747 | 7,708 | 807 | 14 | 11,276 |
| Library | 1,877 | 490 | | 11,139 | | | 13,506 | 9,737 | 490 | 3,141 | 138 | 13,506 |
| Museum | 1,016 | 1,226 | 150 | 2,588 | | | 4,980 | 2,749 | 1,226 | 936 | 69 | 4,980 |
| TOTAL | 5,957 | 9,863 | 150 | 21,439 | 14 | | 37,423 | 20,535 | 9,863 | 6,709 | 316 | 37,423 |
| Administrative Service Ctrs. | | | | | | | | | | | | |
| Student Services | 11,263 | 1,311 | | | | | 12,574 | 11,263 | 1,311 | | | 12,574 |
| General Administration | 686 | 87 | | | | | 773 | 16,655 | 87 | (15,969) | | 773 |
| General Exp. | 783 | 791 | | | | | 1,574 | 22,134 | 791 | (21,351) | | 1,574 |
| Operation & Maintenance | | | | | | 0 | 30,990 | | (30,990) | | 0 | |
| Net Space | | | | | | | 0 | 2,022 | | | (2,022) | 0 |
| TOTAL | 12,732 | 2,189 | | | | | 14,921 | 83,064 | 2,189 | (68,310) | (2,022) | 14,921 |
| General University Resource | 69,407 | | (12,941) | 46,709 | (3,796) | 58 | 6,017 | 6,017 | | | | 6,017 |
| Aux. Enterprises | | | | | | | | | | | | |
| Residences | 19,838 | 1,725 | | | | | 21,563 | 19,481 | 1,725 | 147 | 210 | 21,563 |
| Dining | 8,997 | | | | | | 8,997 | 8,746 | | 209 | 42 | 8,997 |
| Bookstore | 6,938 | | | | | | 6,938 | 6,847 | | 84 | 7 | 6,938 |
| Parking | 2,402 | | | | | | 2,402 | 2,302 | | 60 | 40 | 2,402 |
| TOTAL | 36,175 | 1,725 | | | | | 39,900 | 37,376 | 1,725 | 500 | 299 | 39,900 |
| Total Unrestricted | 301,504 | | | | | | 301,504 | 303,921 | | (2,333) | (84) | 301,504 |
| Total Restricted | | 146,917 | | | | | 146,917 | | 146,917 | | | 146,917 |
| Health Services | | | | | | | | | | | | |
| Hospital of University of Pennsylvania | 222,739 | | | | | 222,739 | | 217,912 | 1,766 | 81 | 219,759 | |
| Clinical Practice | | 80,251 | | | | | 80,251 | | 79,681 | 567 | 3 | 80,251 |
| TOTAL | | 80,251 | | | | | 302,990 | | 297,593 | 2,333 | 84 | 300,010 |
| Total University | 301,504 | 227,168 | 0 | 0 | 0 | 0 | 751,411 | 303,921 | 444,510 | 0 | 0 | 748,431 |