

Response from Howard Bunsis (Treasurer, AAUP) and Gary Rhoades (General Secretary, AAUP) to comments of University Senates Conference memo of 2/10/2010

Response to University Senates Conference Comments in February 10, 2010 Letter

Comment 1: The UI system may have resources, but these resources can only be used for certain purposes. In addition, even though there is not a significant decline in the State appropriation, the real problem is due to cash flows from a delay in the State appropriation.

Resource Allocation Issue: The fungibility of funds

The UI system has over \$4 billion in total revenues, and less than \$700 million comes from the State of Illinois appropriation. Therefore, the state appropriation is only 16.8% of total revenues. This is a fact. The claim that certain revenues can only be used for certain purposes is a standard claim that overstates the case and misrepresents the fungibility of various funds (as we will later clarify). The fact is that administrators have access to a wide variety of revenue sources. In fact, it is not uncommon for there to be shifts in and out of various funds. The bottom line is that the UI administration has the ability to tap into various resources; they simply choose not to.

The 45% figure reported in the comments is incorrect. The 2010 budget reports that the State appropriation will be 40% of what the budget calls total operating revenues; once again, this formulation assumes an overly restrictive view of various revenue sources. Although it is obviously true that some monies are designated for some purposes (e.g., a gift designated for a building), university funds are more diverse and fungible than the faculty senators' comments suggest.

State Appropriation Issue: Will the monies owed by the state be paid

In addition, point #1 seems to imply that the State appropriation either will not be realized by the UI system, or that it will go down significantly. However, the best evidence that the UI system expects the State appropriation to be realized is in the UI system's own budget documents. The 2010 budget is at: (http://www.obfs.uillinois.edu/aboutobfs/documents/2010_BSO_Full.pdf)

This document was reported to the Board on November 12, 2009. *Please note that the University senators' response letter cited the 2009 budget, and therefore did not use the most current data (we offer are additional remarks about current information and transparency below).* And what does this budget document report:

- The 2010 State appropriation is projected in the budget to be exactly flat with 2009 levels. This is critically important. On November 12th, the State's cash flow problems were certainly known and very public. If the UI system administrators believed that the State was NEVER going to pay the appropriation, it would not have budgeted 2010 appropriations to be exactly the same as the 2009 appropriation. If the administrators did not have this belief it would have been imprudent and irresponsible of them to build that into the 2010 budget. The

university senators' belief that the appropriation will be lost forever is contradicted by the UI administration itself. The authors of the response letter are assuming a doomsday scenario that the UI administration does not share.

- Most importantly, the comments support the notion that the reduction in the State appropriation of 6% is not sufficiently large to merit furloughs. The rationale for furloughs is consistently made by the UI administrators and by the University Senates Conference on the assumption that the State of Illinois will never pay back the UI system the delayed payments from the appropriation. This is a doomsday scenario that will almost certainly not come to pass. The State will almost certainly pay back the UI system what is owed.
- Total revenues for 2010 will be 12% above 2009 levels, according to the UI administration's own predictions. Therefore, the 2010 budget predicts continued revenue strength going forward; furloughs are simply unnecessary, given the UI system's own projections.

If there is a short term cash flow problem due to the payment delay, furloughs *that will be repaid to faculty and staff* should be the last option. Below are the other options that we believe should be implemented before the hard-working employees of the UI system are asked to give back their salaries. Doomsday predictions are not a reasonable rationale for furloughs, particularly given the disproportionate growth of administrative costs in the UI system over several years. Instead, we ask that the following options be examined before non-refundable furloughs are implemented:

In making these suggestions, we are pleased that the university senates conference acknowledges that the last option should be considered. The value of an independent faculty voice is to trigger deliberations and put ideas on the table that otherwise would not have been addressed. That is what we sought to accomplish with our report.

- (a) Use existing reserves. As indicated in the report, the UI system has hundreds of millions of dollars of reserves, and contrary to the claim in the response letter, these reserves have not been "burned" up. That is almost certainly untrue (see below on reserves).
- (b) Any reduction in spending should not come from the employees, but from administrative costs and administrative spending. We will indicate below how administrative costs have outpaced educational costs at UI, and how the administration continues to forecast increases in administrative costs even as they propose non-refundable furloughs and further reduced shares of institutional monies spent on the core educational mission.
- (c) If the administration claims they have no cash reserves (a dubious claim), the UI can borrow short term money to guide them through this period. Borrowing money is not a long term solution to long term issues which certainly do exist, but the furloughs are, in the administration's own words, and in the words of the university senates conference, a

response to a short term cash flow problem. The UI system still has a very strong credit rating.

- (d) The reserves of the UI Foundation could and should be used to help with any short term cash flow problem. The UI Foundation has over \$1 billion in assets; any temporary shortfall can be borrowed from the Foundation, and then repaid when the State pays the appropriation. It is not advisable to use Foundation dollars, but since they will be repaid in a short time, it is a solution that is preferred to reducing the pay of current employees.
- (e) The last option, after the above three have been exhausted, would be to ask the UI system's employees to accept a temporary reduction in pay *that would later be refunded to them*. When the university gets the appropriation due from the State, as is almost certain to happen, then the pay reduction should be paid back to the employees, with interest. In comment #1, the university senates executive response, like the UI administration states that furloughs are designed to get the UI system through a short-term cash flow problem. However, once the system is repaid the money from the State, the employees should be given back any furloughs that were surrendered.

Again, we are pleased that the University Senates Executive agrees that the UI administration should consider this option. That is the function of an independent faculty voice, to weigh in on issues, to raise questions, and to put feasible options on the table. That is precisely what we have done.

Comment 2: Criticizes the statement in the report that administrators claim that "this" money can only be used for this, and "that" money can only be used for that. In addition, uses the 2009 budget as the basis for the comments.

The claim is made by the University Senates Executive that some funds are "restricted," and therefore can only be used for certain purposes. As noted above, that is a standard argument of administrators that overstates the case and is belied by their own movement of monies among funds. The percentage contribution of the different revenue sources are detailed in the original report (see table 4). An examination of this table reveals that there are seven different general revenue sources documented. That is certainly more than the one identified by the Faculty Senates Executive.

The second part of this comment is that the analysis in the Bunsis report is based on the 2009 budget. There are two problems with this:

- (i) The 2010 budget is available, as it was reported on the UI system website on November 12, 2009. By comparing the 2008, 2009, and 2010 budgets, we will be able to discern trends in spending (administrative versus academic)
- (ii) The biggest problem is that the University Senates Executive comments do not make any reference or examination of the actual financial statements. In fact, in criticizing the

Bunsis report, the University Senates Executive appears to confuse budgets with audited financial statements. Every year, the UI system properly creates a budget of what it expects to take in for revenues, and what it expects to spend. However, these plans generally do not play out entirely according to plan. Revenues and expenses are generally somewhat different than expected. The most important documentation to judge the financial condition of any university or system is the audited financial statements. The budget is not audited by an independent accounting firm; it is just a plan. The financial statements reflect the results of all operations, and results that have been authenticated by an independent outsider. It is highly problematic that furloughs have been implemented before the most recent financial results have been disseminated to the public. This issue is examined further below.

Good governance is based on all parties in the process having meaningful information to inform their decisions. It is time to open the books. Again, we are pleased that the University Senates Executive calls for a top to bottom review of the university's finances. Throughout the past year, in speaking to hard times in higher education, the national AAUP has repeatedly called for universities to provide fiscal transparency, for institutions to open their books. If our analysis contributes to that happening in the UI we will be very pleased.

Comment #3: The report is based on FY 2008 budget numbers, and the bond rating is the 3rd highest. In fact, the comments state that the numbers are outdated. In addition, Illinois is on its way to a junk rating, and the A rating being the 3rd highest is misleading. Lastly, the claim is made that a "junk" rating is near.

The above statements are simply incorrect.

First, the original report is based on three sources:

- I. The 2008 actual financial statements. As detailed above, a budget is not the same as actual financial statements. The University Senates Executive apparently has confused or mistakenly conflated the two different sources.
- II. The 2009 budget, the same budget that the authors of the response indicate they utilized
- III. The 2010 budget, which was reported on November 12, 2009.

Tables 11, 12, 13, 14, and Figure 5 of the original report are all based on the most recent budgets.

What is most troubling is that the audited financial statements for the year ended June 30, 2009 are not publicly available, as we indicated in the original report. The original report was created in January 2010, and the audited financial statements were not available at that time. As of drafting our response here (February 15, 2010), the audited financial statements for the year ended June 30, 2009 are still not available.

We reiterate, then, our pleasure at the University Senates Executive calling for a top to bottom review of the UI’s finances. Our report aimed to promote transparency, to provide an analysis that would raise questions about the current path of the UI, and to trigger a universitywide review of finances by faculty and administration. In order for such a review to be meaningful and comprehensive, it is essential for the faculty and staff to have access to the most recent financial statement.

Why are these audited financial statements so important? As stated above, these statements are authenticated by an independent outside agent. In addition, the University Senates Executive claim that the reserves have been “burned” through (more later on how unfounded that comment is). In order to judge the level of reserves, it is critical that the 2009 financial statements be revealed. Budgets do not report reserves; budgets report expected future revenues and expected future expenses. In fact, since the UI system budget for 2009 and 2010 predicted total revenues would exactly be matched by total expenses, reserves were not expected to change at all. However, as reality does not always follow predictions; we need the actual financial statements to judge the level of reserves. The lack of this information was made clear in our original report.

In order to get a sense of the current lack of transparency from the UI administration, below is a table detailing when the last five years of audited financial statements were revealed to the public.

Fiscal Year End	Date Financial Statements Were Available
June 30. 2008	December 30. 2008
June 30. 2007	February 8. 2008
June 30, 2006	October 4, 2006
June 30, 2005	September 28. 2005
June 30, 2004	October 15, 2004

Source: UI system financial statements. Dates are the ones reported in the letter signed by the Chief Financial Officer of the UI System, as well as a letter signed by the independent auditors (these dates are the same in each report).

This table makes clear that the June 30, 2009 financial statements will be disseminated at a date later than any time in the last five years. Last year’s financial statements were reported on December 30th; this year’s report will be at least one and ½ months later than that. That is problematic given that the university has made significant financial decisions that such audited data would bear directly on.

The AAUP, in its statement on furloughs and financial difficulties at <http://www.aaup.org/AAUP/Financial/Finance/> makes clear that transparency is a key element in ensuring that faculty has a voice in the financial decisions related to potential furloughs. What is

critical is that faculty has all the information necessary to make informed judgments. By implementing furloughs before the June 30, 2009 financial statements (and reserve information) is revealed, the UI system has compromised a basic principle of genuine shared governance. In our view, the faculty senates executive should not criticize our report for not using current data; rather, they should criticize the UI administration for not making all the relevant information publicly available in a more timely fashion, and *before* implementing furloughs.

Therefore, we call on the UI system to provide the following information, in the name of transparency and shared faculty governance:

I. The audited June 30, 2009 financial statements

II. The “crosswalk” or “mapping” from the budget to the audited financial statements. Specifically, the budgets that the university senates conference comments cite contain dozens and dozens of accounts. In order to ascertain the current financial situation and the extent to which the current pattern sufficiently supports and protects the core academic mission of the university, we need to know exactly what has been spent on the mission, and what has gone to other expenditures, such as on administration and athletics, for example. More specifically, the audited financial statements have an expense category named “Instruction.” The faculty and public need to know exactly what budgetary accounts comprise that instruction category.

III. The fund financial statements, which include the fund balance sheets, and the fund statements of Revenues, Expenses, and Changes in Fund Balances.

The comments claim that there are only certain funds that are available for spending on educational costs. However, these funds are reported in total in the budget, but the audited results of these funds, along with the reserve levels of these funds, are not reported in the audited financial statements. Nonetheless, these fund statements exist. The public needs to see them.

Notes on Bond Ratings

The comments claim that the 3rd highest rating comment is misleading.

Below are the ratings that Moody’s issues. A rating of A2 may be the 6th highest overall, but there are 24 possible ratings reported below. Stating that A2 is in the 3rd category out of 9 is comparable to stating that it is the 6th highest rating out of 24; indeed, in relative terms the latter calculation is slightly higher.

As to the State’s rating of A being a pit-stop on the way to junk, this is simply untrue; it makes no sense. The state would have to decline another 16 or 17 rating categories to get there. This is simply not going to happen. Yes, the State is not in great financial condition. But claims of junk status are so

grossly overstated that they indicate the university senate executive are posing another doomsday scenario that will almost certainly not occur.

Rating	Description	
Aaa	Issuers or issues rated Aaa demonstrate the strongest creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Aa	Issuers or issues rated Aa demonstrate very strong creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
A	Issuers or issues rated A present above-average creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Baa	Issuers or issues rated Baa represent average creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Ba	Issuers or issues rated Ba demonstrate below-average creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
B	Issuers or issues rated B demonstrate weak creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Caa	Issuers or issues rated Caa demonstrate very weak creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Ca	Issuers or issues rated Ca demonstrate extremely weak creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
C	Issuers or issues rated C demonstrate the weakest creditworthiness relative to other US municipal or tax-exempt issuers or issues.	
Modifiers for Municipal Ratings		
Moody's applies numerical modifiers 1 , 2 , and 3 in each generic rating classification from Aa through Caa .		
The modifier 1 indicates that the obligation ranks in the higher end of its generic rating category;		
the modifier 2 indicates a mid-range ranking;		
and the modifier 3 indicates a ranking in the lower end of that generic rating category.		

Comment # 4. Comparisons to Michigan, claiming that the situation in Illinois is worse than in Michigan in regards to the delay of payments.

First, a technical note. The university senates conference comment refers to the situation in Michigan as UM. Please note that UM is the abbreviation for the University of Michigan. There are 15 public universities in the State of Michigan, and the University of Michigan is one of them (it is not even the largest one, as Michigan State is larger). The appropriation that was withheld in Michigan was for all 15 higher education public institutions. The university senates conference comments go on to ask whether UI is in worse shape than UM, and conclude that they are. However, as stated, this is a comparison that is irrelevant, as UM is but one of the 15 public universities in Michigan.

The claim in the response is that the original report has a “rosy” outlook for the UI system. However, it is not rosy to expect that the payments that have been delayed will eventually be repaid to the system. The only qualification is that there would be a 6% reduction in the overall appropriation; even the authors of the comments concede that a 6% reduction is not enough of a change to justify furloughs.

In Michigan, the delay of the payment (2 months or 1/6th of 2 billion was withheld in Michigan, which is quite significant.) This amounts to over \$300 million in the entire state of Michigan (again, UM is not the only public institution in the State), and is comparable to the amount owed the UI system.

Lastly, the authors cite a decade of reduction in support for higher education. However, the table below reports that the State of Michigan has seen a smaller increase in the last 10 years of higher

education appropriation than Illinois. In fact, the state of Michigan is in worse shape than the state of Illinois on almost every measure below:

Item	Michigan Rank	Illinois Rank
Per Capita Spending on Higher Education (2010)	41st (\$205)	32nd (\$233)
% Change in Higher Education Spending from 1999 to 2009	48th (+9.5%)	42nd (+24.9%)
% Change in Higher Education Spending from 2005 to 2010	48th (-2.2%)	34th (+16.7%)
% of Adults with a Bachelor's Degree or Higher	34th (24.7%)	14th (29.5%)
Ratio of Prison Spending to Higher Education Spending	2nd (1.19)	25th (0.51)
State Unemployment Rate (12/2009)	1st (14.6%)	9th (11.1%)

Sources:

Grapevine report at <http://www.grapevine.ilstu.edu/index.shtml>

Prison spending at Pew Charitable Trust Study 2/29/08

Conclusions from this table:

- Michigan supports higher education to a lesser extent than Illinois over time.
- Michigan's support for higher education has eroded more significantly than in Illinois
- Michigan's economy is in worse shape than Illinois's
- If Michigan can pay back delayed payments to higher educational institutions, so can and will Illinois.

Comment #5: Use of reserves and borrowing is not wise; administrative costs should be cut

The issue of reserves has been discussed, but in order to fully analyze the level of reserves, the June 30, 2009 financial statements must be reported. The same is true for debt levels; to fully analyze how much debt the UI system currently has, we need to analyze the June 30, 2009 audited financial statements. Having said that, using the most recent publicly available statements (June 30, 2008), it is clear that:

- The UI system has sufficient reserves to handle the short term cash flow problem
- The UI system does not have too much debt.

Conclusions based on the 2009 financial statements will be forthcoming, once the UI administration decides to reveal this information.

One area of agreement between the authors of the comments and the original report is the need to reduce administrative costs. A detailed analysis of the 2010 budget for two of the campuses reveals that administrative expenses are increasing faster than total expenses, and costs within each department are either declining or increasing at a slower rate than administrative costs.

Below is a table of 2009 and 2010 budgeted costs for the UIUC Campus. The table examines the two largest colleges, Liberal Arts & Sciences, and Engineering. In addition, two significant administrative offices are examined.

UIUC Budget Analysis, 2009 versus 2010 Budget

Division	Item	2008-09 Budget	2009-10 Budget	Dollar Change	Percentage Change
Liberal Arts & Sciences	Total Spending	206,248	214,587	8,339	4.0%
Liberal Arts & Sciences	Total Revenue from State	122,423	124,710	2,287	1.9%
Liberal Arts & Sciences	Instruction Spending	110,196	109,124	(1,072)	-1.0%
Liberal Arts & Sciences	Administration	13,836	16,316	2,480	17.9%
Liberal Arts & Sciences	Mathematics	10,005	10,570	565	5.6%
Liberal Arts & Sciences	Chemistry	9,790	9,849	59	0.6%
Liberal Arts & Sciences	Psychology	9,782	9,698	(84)	-0.9%
Liberal Arts & Sciences	English	7,748	7,490	(258)	-3.3%
Liberal Arts & Sciences	Economics	6,155	5,905	(250)	-4.1%
Engineering Division	Total Spending	201,598	217,109	15,511	7.7%
Engineering Division	Total Revenue from State	76,115	80,458	4,343	5.7%
Engineering Division	US Gov't Grant Revenue	73,352	82,151	8,799	12.0%
Engineering Division	Instruction Spending	60,571	61,000	429	0.7%
Engineering Division	Administration	5,914	6,274	360	6.1%
Engineering Division	Electric & Computer	15,071	14,762	(309)	-2.1%
Engineering Division	Computer Science	9,945	10,886	941	9.5%
Engineering Division	Physics	10,807	10,603	(204)	-1.9%
Engineering Division	Mechanical Science	9,830	9,851	21	0.2%
Engineering Division	Civil & Environmental	8,080	7,875	(205)	-2.5%
All Divisions	Provost and VC for Academic Affairs	50,141	53,508	3,367	6.7%
All Divisions	VC for Student Affairs	155,887	166,449	10,562	6.8%

Comments:

- In the Liberal Arts & Sciences division, total spending is up 4.0%.
- The State appropriation portion increased 1.9%
- Instruction spending declined while administrative spending increased. This indicates that the UI system is not being true to the core academic mission.
- For the five largest departments, three realized a decline from 2009 to 2010; only one had an increase greater than the total for the entire division.

Below is an analysis of spending at the UIC Campus:

Division	Item	2008-09 Budget	2009-10 Budget	Dollar Change	Percentage Change
Liberal Arts & Sciences	Total Spending	92,959	98,160	5,201	5.6%
Liberal Arts & Sciences	Administration	9,463	13,883	4,420	46.7%
Liberal Arts & Sciences	Mathematical Statistics & Computer Science	8,610	8,248	(362)	-4.2%
Liberal Arts & Sciences	Biological Sciences	5,556	5,640	84	1.5%
Liberal Arts & Sciences	Chemistry	5,192	5,365	173	3.3%
Liberal Arts & Sciences	English	5,864	6,140	276	4.7%
Liberal Arts & Sciences	Psychology	4,526	4,473	(53)	-1.2%
Business Administration	Administration	886	2,282	1,396	157.6%
Dentistry	Administration	4,769	6,090	1,321	27.7%
Education	Administration	2,078	2,776	698	33.6%
Engineering	Administration	2,748	3,342	594	21.6%
Nursing	Administration	3,564	4,899	1,335	37.5%
Pharmacy	Administration	858	829	(29)	-3.4%
School of Public Health	Administration	4,246	3,942	(304)	-7.2%
Applied Health Sciences	Administration	3,415	3,675	260	7.6%
University Library	Library	17,664	17,811	147	0.8%
Provost & VC for Academic Affairs	Administration	28,218	28,490	272	1.0%
College of Medicine Dean's Office	Administration	15,358	16,483	1,125	7.3%
College of Medicine - Clinical Science	Administration	4,693	6,591	1,898	40.4%
College of Medicine - Clinical Science	Psychiatry Department	10,632	10,715	83	0.8%
College of Medicine - Clinical Science	Medicine Department	4,582	4,667	85	1.9%
Office of Chancellor	Total	1,975	2,161	186	9.4%
VC for External Affairs	Total	3,084	4,062	978	31.7%
VC for Development	Total	3,206	3,182	(24)	-0.7%
VC for Research	Total	16,702	16,617	(85)	-0.5%
VC for Student Affairs	Office	527	548	21	4.0%
Campus General Admin Units	General and Unassigned	52,927	73,626	20,699	39.1%

Comments:

- In general, administrative costs have increased much faster than costs in the academic departments
- In the College of Liberal Arts & Sciences, the budget line named "LAS Administration" increased \$4.4 million from 2009 to 2010, or 46.7%. It is
- In the College of Medicine, both the dean's office and the Clinical Service administration were the beneficiaries of significant budget increases from 2009 to 2010
- There are some administrative offices that are reducing costs
- Overall, it is clear that the UIC administration needs to publicly address how they can ask for furloughs, given they are increasing their own costs and decreasing costs to several academic departments.

The authors of the response concluded that the State and the University should be viewed together, and that their problems are one and the same. In addition, it was concluded that reserves were "burned" through.

Our conclusions:

- Reserves do not get burned through unless revenues are exceeded by expenses. Until the UI system writes off the state appropriation, there will be no burning of reserves. This displays a lack of understanding of what net assets (reserves) truly represent. There is a difference between a temporary cash flow shortage and the “burning” of reserves. Here, the authors are not creating a doomsday scenario; they are creating a scenario that does not and will not comport to basic accounting principles.
- The UI system is in much better financial condition than the State of Illinois. These two institutions are not the same; the UI system gets less than 17% of its total revenue from the State. The two are not joined at the hip. We have outlined all the steps that first should be taken before refundable furloughs are implemented. There are better alternatives. Moreover, in general, asking faculty to take furloughs before all of the financial information is provided goes against the basic principles of meaningful shared governance.

In closing, then, let us emphasize that we believe that there are better alternatives than non-refundable furloughs to the short-term cash flow problem identified by the UI system president, and that these alternatives should be discussed and considered by faculty as well as administration. We are pleased that the University Senates Conference concurs at least on the possibility of implementing furloughs that would be refunded in the event the State of Illinois pays the UI system its due appropriation. We also believe that there are long standing patterns of external and internal resource allocation in the UI system that are problematic and that should be addressed and reversed. We are pleased that the University Senates Conference calls for a top to bottom review of finances in the system, and we strongly encourage that the UI system provide the faculty the 2009 audited financial statements, among other key data sources, to facilitate meaningful and thorough deliberation of these matters. And we believe, as members of the association that established, defined, and continues to advance the value of shared governance that such deliberations should proceed through various mechanisms that ensure an independent faculty voice and participation in jointly and collectively shaping current decisions and the future of the university.