UNIVERSITY OF TORONTO

BUDGET REPORT

2003-2004.

March 14th 2003

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UNIVERSITY OF TORONTO BUDGET REPORT, 2003-04.

1. INTRODUCTION.

The Budget Report, 2003-04 serves two purposes. First it updates, utilizing the most current information available, the assumptions in the *Long Range Budget Guidelines and Projections, 1998-2004* first approved by Governing Council in April 1998. Second, it presents for approval the budget for each division, including those budgets determined pursuant to Contractual Obligations and Policy Commitments. It also indicates the funding available in the Administrative and Academic Priority Funds, the Enrolment Growth Fund and the Canada Research Chairs Fund. The Budget Report, 2003-04 is the last budget in the planning period associated with the *Raising Our Sights* planning process.

2. FISCAL CONTEXT

As they entered the 1990's the University of Toronto and all other Ontario universities were experiencing a period of relative financial stability and recovery; government grants and tuition were increasing at rates slightly above the general inflation rate, and budget reductions were, relatively speaking, modest in scale. With the full onset of the economic recession in 1992 through 1994, operating grants were frozen and then reduced through the Social Contract ($17.3 million) and the Expenditure Control Plan ($5 million). Tuition fees increased by a range of 8 to 10 per cent annually to partially compensate for the loss of grant revenue. The Ontario Student Assistance Plan was modified by government from a combined grant/loan program to an all-loan program as a cost reduction measure.

In 1995 the new government fulfilled its election promise to further reduce operating grants to universities by $280 million, a loss of $53.9 million to the University of Toronto. Again as a partial offset to the loss of grant revenue, government permitted significant increases in tuition fee rates; 20 per cent in 1996-97 and 10 per cent on average in each subsequent year up to and including 1999-2000. Tuition fees were deregulated for international students, and for students in some professional and all graduate programs.

Government operating grants revenue reached a peak at approximately $400 million in 1992-93, fell to $339 million in 1997-98 and is projected to rise to $413M in 2003-04 with the introduction of a number of new funding envelopes targeted to enrolment increases and performance indicators. However during the past decade, the system-wide *Government operating funding per BIU* has decreased in absolute terms by over 16% and in real terms by considerably more. At the same time, tuition revenue will increase from $100 million in 1992-93 to a projected $320 million in 2003-04, as a result of tuition fee rate and enrolment increases. Starting in 1996-97 the Government mandated that 10% of the revenue from tuition fee increases be spent on student aid; this was increased to 30% in 1997-98 and subsequent years.

The practical effect of the Government funding policy has been that the university has had to internally absorb a significant portion of cost increases for compensation, library acquisitions and utilities by way of budget reduction. The university's expenditure patterns have also changed significantly over this period: support for student aid has increased dramatically, from $7.7 million in 1991 to a projected $95.9 million in 2003-04. In effect the increase in expenditures on student financial aid is approximately 40% of the increase in tuition revenue making the University of Toronto one of the most accessible in the Country. Library acquisition costs have continued to increase sharply throughout the period, from $9 million in 1991 to a projected $22.2 million in 2003-04.

In 2000 the Government announced a cap on tuition fee increases for all regulated programs in each of the five years 2000-01 to 2004-05 at 2% per year, not compounded. The tuition fee schedule for 2003-04 that the Business Board will recommend to Governing Council for approval includes 5% fee increases for new and continuing domestic students in the deregulated programs with the exception of new students in programs in business (MBA), dentistry, computer science, engineering, information technology and law where the revenue from larger increases is being used to enhance quality in these programs.

3. Updated Long Range Budget Projections Through 2003-04.

Table 1 presents the revised Long-Range Budget Projections, updated to reflect new information and changes in the *Guidelines*' assumptions. The last column shows the variance from the projections contained in the previous Budget Report, i.e. 2002-03. The following are the highlights of the updated projection.

Revenue

- Government operating grants are forecast to decrease by $4.4 million from than previously budgeted due to the removal of the inflation provision for 2003-04 and the projected relief in 2002-03 of $3.2 million, either through a special grant envelope or some relaxation in tuition regulation, partially offset by grant revenue from increased enrolment. The model now includes an assumption that we will receive full average operating funding for all undergraduate enrolment increase in 2003-04 (~ $5.6M) but does not anticipate an increase in operating funding per student to meet inflationary cost increases.
- Tuition revenue is $21.6 million higher than previously forecast, reflecting increased enrollment and higher tuition fee increases in programs in computer science, engineering, dentistry, law and business.
- The Federal budget contained an annual allocation of $225 million for the indirect costs of federally funded research. The University's portion of these funds is assumed to be $15.8 million in base in 2003-04 up from the $14.6 million received OTO in 2001-02.
- Investment revenue has been reduced to $11.3 million in 2003-04 some $2.4M below the baseline level. The cost of amortization of investment losses has increased from $5.6M to $10.0M in 2003-04.

Expense

- The operating budget now includes funding of $11.7M of debt service costs reflecting the central administration's contribution to the total debt service costs associated with the Capital Budget, (see Section 6). This charge subsumes the debt service costs already in the budget for the $90M of loans which funded the University Infrastructure Investment Fund and the $5M payment to the MARS project for a net increase of $2.8M.
- The enrollment growth fund, representing revenue-sharing agreements for increased grant and fee revenue associated with enrolment increases, is $15.9 million higher than previously budgeted.
- An allocation of $1.25M will be used to assist a limited number of divisions who are in transition in 2003-04. The provision of this funding to divisions will be dependent on attainment of performance objectives developed by agreement with the Provost.

The Net Result

- Revenues have increased by $9.3 million in 2003-04 over previous forecasts, while expenditure requirements have grown by $27.7 million, increasing the annual shortfall from

$3.8 million to $22.2 million. If left uncorrected, this would result in an accumulated deficit of $44.1 million as of April 30, 2004.

- Eliminating this shortfall and containing the accumulated deficit to within policy limits requires a base budget reduction of 4.45% ($22.2M) and a OTO clawback of 1.46% ($7.3M) in 2003-04.

Budget Strategy: Toward a New Budget Framework 2003-09

The budget for 2003-04 ensures that the University will exit the current six-year planning period in compliance with the budget guidelines; that is to say, that the annual budget will be in balance and that the accumulated deficit will be within policy limits. The Long Range Projections in the Budget Report for 2002-03 included a base budget cut of 1.5% in 2003-04 to achieve a balanced budget. Unfortunately the combination of not realizing increases in government operating revenues per student to cover increased costs and the projected increase in the rate at which the indirect cost of federal research would be assessed, together with reduced investment returns have required that the base cut be increased to 4.45% to produce a balanced budget. Also a 1.46% one time only (OTO) cut will be required to maintain the accumulated deficit below the maximum permitted, i.e. 1.5% of the operating budget.

There are a number of potential sources of increased revenue which if realized will, in the first instance, be used to reduce or eliminate this OTO cut. These include:

- The provision by the Provincial Government of full average funding for enrolment above the Enrolment Target Agreement (ETA) for 2002-03.
- A modest increase in the rate at which the indirect cost of federal research is assessed. The amount allocated in the Federal Budget was an increase of 12.5% over the OTO funding in 2000-01 while the projected increase in the funding realized by the University is only 8% reflecting the University's increased volume of federal research.
- The creation of a Double Cohort Quality Enhancement Fund currently being considered by the Provincial Government.
- Increased Accessibility Funding for graduate enrolment expansion to deal with issues arising from the undergraduate enrolment expansion.

The new budget framework for 2004-05 through 2008-09 will establish a new set of budget strategies and must necessarily deal with several significant structural issues in the budget including;

- the lack of recognition of inflationary costs in the provision of Government Operating funding,
- volatile returns on the University's investments,
- increased pension costs resulting from the dwindling surplus in the pension funds and a gap between projected earnings in a weaker investment climate and the University's pension liability,
- heavy demands for infrastructure funds,
- the cost of maintaining new space.

Table 1

Budget projections, page 1

Table 1

Budget projections, page 2

4. Proposed Budget for 2003-04.

Table 2

Budget for 2003-04.

5. THE OPERATING BUDGET SPECIAL FUNDS.

The operating budget special funds receive base or one time only (OTO) transfers from operating revenues. The Administration brings forward divisional allocations from these funds to the Planning and Budget Committee for approval. Allocations from the Academic and Administrative Priorities Funds and the Canada Research Chairs Fund are made in response to the Planning Process. Allocations from the Enrolment Growth Fund reflect divisions' enrolment plans and those from the University Infrastructure Investment Fund have been in support of approved Capital Projects, renovations and other infrastructure projects.

Administrative Priorities Fund

The 1.5% reallocation requirement will not be applied to the administrative divisions in 2003-04 and so the transfer from the operating fund is reduced to the $0.7M identified in the budget guidelines to help meet the demands of the enrolment increase. The Administrative Priorities Fund will have zero carry-forward at year-end 2002-03.

Administrative Priorities Fund ($Million)

	2002-03	2003-04
Balance at beginning of year	$0.0	$0.0
Transfer from Operating Fund	$1.4	$0.7
Allocations	($1.4)	($0.5)
Unallocated balance	$0.0	$0.2

Academic Priorities Fund

Allocations from the Academic Priorities Fund (APF) are made in support of divisional plans to sustain and enhance program quality and to provide for new initiatives emerging from divisional planning processes. There are two principal sources of funding for the APF indicated in the *Long-Range Guidelines for Planning and Budgeting, 1998-2004*;

- a reallocation of 1.5% of the divisions operating budget,
- 75% of the revenue from tuition fee increases greater than 5%, net of the 30% for student aid,

The table below shows the current status of the fund. The timing of the re-allocative transfers to the APF from the operating budget was accelerated to reflect the fact that the Divisions are hiring new faculty at a faster rate than originally planned in order to deal with increased enrolment.

Academic Priorities Fund ($Million)

	2002-03	2003-04
Balance at Beginning of Year	($16.3)	($3.1)
Transfer from Operating Fund		
Reallocation Requirement	$12.3	$1.5
Quality Enhancement from Tuition Revenue	$1.6	$3.0
Other	$1.5	$1.7
Allocations	($2.2)	($3.0)
Balance at End of Year	($3.1)	$0.0

Canada Research Chairs Fund

The funding from the Canada Research Chairs Program, net of a component for central indirect costs, together with funds released from the salary budget flows to the CRCF. This program is described in detail in the discussion paper, *A Framework for Allocating Canada Research Chairs at the University of Toronto.* The initial balance for 2003-04 reflects an allocation of $4.6M in 2002-03 made up of $2.6M for Chairs outside the Faculty of Medicine and $2.0M for Chairs inside the Faculty of Medicine for 29 Chairs approved in the September and December 2001 CRC competitions.

Canada Research Chairs Fund ($Million)

	2002-03	2003-04
Balance at Beginning of Year	$7.0	$11.5
Transfer from Operating Fund	$9.1	$10.1
Allocations	($4.6)	
Balance at End of Year	$11.5	$21.6

Enrollment Growth Fund

A portion of the Tuition Fee and Government Operating Grant revenue associated with new program plans and approved enrolment growth, including that resulting from the double cohort and increased applicant pool, flows in accordance with the *Long-Range Budget Guidelines,* to the Enrolment Growth Fund for subsequent allocation to the respective academic divisions as enrolment targets are achieved. Funding for permanent expansion flows as OTO in year and as base the following year. The unallocated balance in this fund is zero at the end of each year.

University Infrastructure Investment Fund

A listing of the allocations approved from the UIIF and the current unallocated balance is shown in Table 5 of Section 6.

6. PROPOSED CAPITAL BUDGET, 2003-09.

Prior to 2001, academic capital projects were, in general, funded from a combination of campaign donations, federal and provincial government capital grant allocations and funds from the University's operating budget. Debt financing was restricted to resolving cash-flow shortfalls during construction of academic buildings but was routinely used to provide the majority of the cost of residence construction where the debt service costs were recovered from the room rental revenue. The University Infrastructure Investment Fund (UIIF) is currently the vehicle used to allocate operating budget funds to capital projects. Since 2001, the traditional sources of funding have been insufficient to meet the capital construction demands driven by research initiatives and the enrolment expansion associated first with the Access To Opportunities Program (ATOP) and now with the double cohort and demographic pressures.

The update to the *Long-Range Budget Guidelines* in the Spring of 2001 provided $30M of funding to the UIIF in each of 2001-02, 2002-03 and 2003-04 in the form of loans with the debt service costs charged to the operating budget. In addition, funding shortfalls in individual project budgets, after deployment of government, campaign and UIIF funding, were to be the responsibility of the occupying divisions. This was the first recognition that capital construction of academic buildings could no longer be funded on a cash basis and that the use of debt financing would be necessary in the future. It also argued for the evolution to a Capital Budget separate from the Operating Budget but where the Operating Budget would be one source of revenue for the debt service charges associated with the Capital Budget.

The Capital Budget proposed is a comprehensive one encompassing academic, non-academic and endowed capital infrastructure. It would include construction for academic and administrative divisions, residences, parking garages, student activities and the matching funds that are such an important part of growing our endowment capital infrastructure. Given the existence of a finite institutional borrowing capacity, the Capital Budget would enable decisions on appropriate levels of debt financing for individual capital projects to be informed by the total capital institutional debt.

A Capital Budget that includes capital projects currently approved by Governance and, in particular all that will require capital funding in 2003-04, is attached as Table 3. The majority of the expenditure allocations from the UIIF since the academic year 1999-2000 ($109.7M out of $133.2M), Tables 4 & 5, are transferred to the new budget, as is the $5M equity in MARS and the $3.3M negative balance in the Capital Renewal Fund. The $14M of matching funds previously in the 2003-04 budget projections together with matching funding commitments through to 2008-09 are also transferred. The debt service costs associated with these transfers will require an added expense to the Operating Budget estimated at $2.8M in 2003-04 rising to $7.3M by 2008-09. This expense is in addition to the $8.9M cost already in the budget projections for the $90M loan to the UIIF and the $5M equity in MARS.

It is important to note that the list of projects in Tables 3 & 4 include a number where the funding identified includes significant campaign donations that are still being sought. These projects will not go forward to the Business Board for approval to expend funds on design and construction until funding has been secured. In the meantime, since any shortfall in project funding is back-stopped by the division(s) sponsoring the project, the shortfall is catagorized as *funded by divisional/ancillary budgets*. The sub-total in Table 3 of $603.9M in the *approved projects* column cannot therefore be considered as the level of borrowing contemplated by the University for its capital construction plans. It is also possible that, if the University's budget situation were to deteriorate, it would be necessary to review the projects on the Capital Budget.

The Capital Budget is a living document and will be updated with each approval by Governance of a new capital project. It is expected that the next additions will be those associated with the current SuperBuild competition.

Table 3, Capital Budget

Table 4, Capital Budget Details

Table 5, UIIF

7. DIVISIONAL BUDGETS.

8. Appendices.

Appendix A Updated Table of Assumptions from the Long Range Budget Guidelines for Planning and Budgeting, 1998-2004.

Appendix B Contractual Obligations and Policy Commitments (COPC) List.

These appendices were distributed for the March 18th Planning and Budget Committee Meeting (and its Agenda Planning Meeting).

Appendix A, Updated Table of Assumptions from the Long Range Budget Guidelines for Planning and Budgeting, 1998-2004.

Appendix B, Contractual Obligations and Policy Commitments (COPC) List.