



Budget Office



Agenda

- Budget Office Announcements/Updates
- Presentation by Ivan Samstein
- Position Management
- Equipment Depreciation
- Questions





THE UNIVERSITY OF CHICAGO

BUDGET MANAGERS MEETING

IVAN SAMSTEIN
VP & CFO

NOVEMBER 27, 2018

Consolidated Financial Results for the Year Ended June 30, 2018

FY2018 Highlights

- The University of Chicago consolidated audit report received an “unmodified” opinion from KPMG.
- Primarily driven by pledges and other non-operating gifts, investment gains in excess of endowment payout, and an increase in the discount rate resulting in a sharp decrease in pension and other postretirement benefit obligations, consolidated net assets increased by \$328.5 million to \$8.7 billion at June 30, 2018.
- The consolidated University ended the fiscal year with a \$3.8 million operating surplus as compared to a \$27.6 million surplus in FY2017.
- On a stand-alone basis, the University ended the fiscal year with a \$24.6 million operating deficit, net of a withdrawal of \$50.0 million of Funds Functioning as Endowment (FFE).
- Following is a high-level summary of the University’s consolidated balance sheet as of June 30, 2018 and the FY2018 consolidated changes in net assets and results of operations.

Consolidated Results of Operations – Summary

Following is a high-level summary of the FY2018 \$3.8 million consolidated operating surplus as compared to the \$27.6 million surplus generated in FY2017:

(\$ in thousands)

	2018				Consolidate d 2017
	University	Medical Center	MBL	Consolidate d	
Revenue:					
Tuition-net of student aid	467,297	-	501	467,798	424,717
Government grants and contracts	335,779	-	12,710	348,489	367,577
Private gifts, grants, and contracts	408,272	7,501	8,618	424,391	369,819
Endowment payout	404,462	54,640	4,431	463,533	444,583
Patient care	286,768	2,000,117	-	2,286,885	2,128,591
Auxiliaries and other income	472,664	157,235	5,097	634,996	566,301
Total revenue	<u>2,375,242</u>	<u>2,219,493</u>	<u>31,357</u>	<u>4,626,092</u>	<u>4,301,588</u>
Expenses:					
Compensation	1,539,784	943,550	22,201	2,505,535	2,344,682
Depreciation	202,406	125,032	4,417	331,855	321,327
Interest	132,333	43,924	1,019	177,276	166,571
Supplies, services, and other expenses	575,297	1,066,733	15,562	1,657,592	1,495,072
Total expenses	<u>2,449,820</u>	<u>2,179,239</u>	<u>43,199</u>	<u>4,672,258</u>	<u>4,327,652</u>
Subtotal	(74,578)	40,254	(11,842)	(46,166)	(26,064)
Net gain on sale of assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>44,687</u>
Excess (deficiency) of operating revenue over expenses before FFE draw	(74,578)	40,254	(11,842)	(46,166)	18,623
FFE draw	<u>50,000</u>	<u>-</u>	<u>-</u>	<u>50,000</u>	<u>9,000</u>
Excess(deficiency) of operating revenue over expenses	<u>(24,578)</u>	<u>40,254</u>	<u>(11,842)</u>	<u>3,834</u>	<u>27,623</u>

Consolidated Changes in Net Assets – Summary

Primarily driven by pledges and other non-operating gifts, investment gains in excess of the endowment payout, and an increase in the discount rate resulting in a sharp decrease in pension and other postretirement benefit obligations, consolidated net assets of the University increased by \$328.5 million in FY2018 from \$8.4 billion at June 30, 2017 to \$8.7 billion at June 30, 2018. The following table provides a more detailed analysis of this increase.

(\$ in thousands)

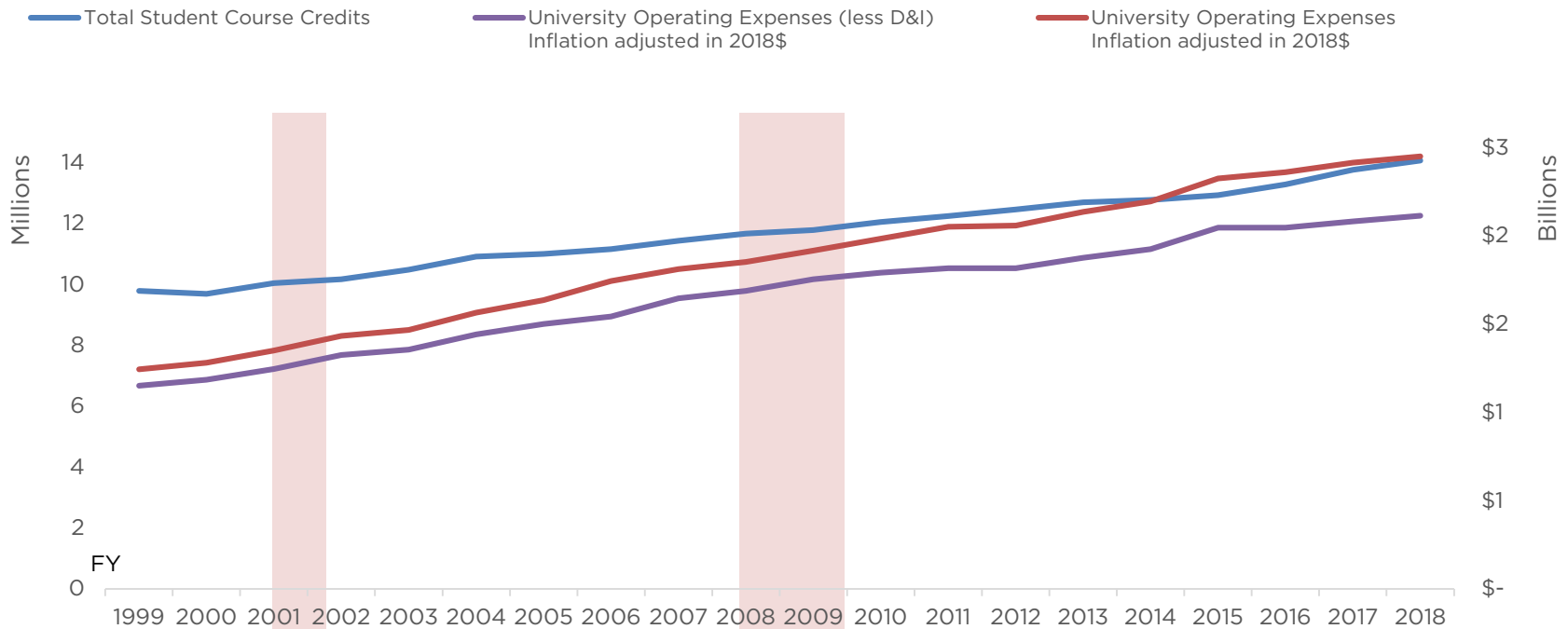
	2018				Consolidated 2017
	University	Medical Center	MBL	Consolidated	
GAAP excess (deficiency) of operating revenue over expenses before FFE draw	(74,578)	40,254	(11,842)	(46,166)	18,632
FFE draw	50,000	-	-	50,000	9,000
GAAP excess (deficiency) of operating revenue over expenses	(24,578)	40,254	(11,842)	3,834	27,623
Pledges and other non-operating gifts	238,578	5,048	2,764	246,390	334,589
Investment gains, net of endowment payout	121,101	20,557	1,857	143,515	326,581
Draw from FFE in support of operations	(50,000)	-	-	(50,000)	(9,000)
Pension plan curtailment (reduction of unfunded liability)	-	-	-	-	64,241
Pension and other postretirement benefit plan changes, net of benefit expense	80,758	2,661	(98)	83,321	34,669
Change in value of derivative instruments	11,281	24,635	1,291	37,207	67,401
Loss on debt refinancing	-	-	-	-	(27,028)
University operating support provided to MBL	(10,828)	-	10,828	-	-
Contribution of Ingalls net assets	-	-	-	-	322,862
Other changes	(89,430)	(43,833)	(2,484)	(135,747)	(161,486)
Increase in net assets	276,882	49,322	2,316	328,520	980,452
Net assets beginning of year	6,478,121	1,770,945	170,169	8,419,235	7,438,783
Net assets end of year	6,755,003	1,820,267	172,485	8,747,755	8,419,235

University Financial Stress Test

UChicago Demand Largely Inelastic

- University of Chicago's demand (and correspondingly operating expense) is largely inelastic to market volatility

University of Chicago (University-only)



Notes:

Standard course = 100 credits

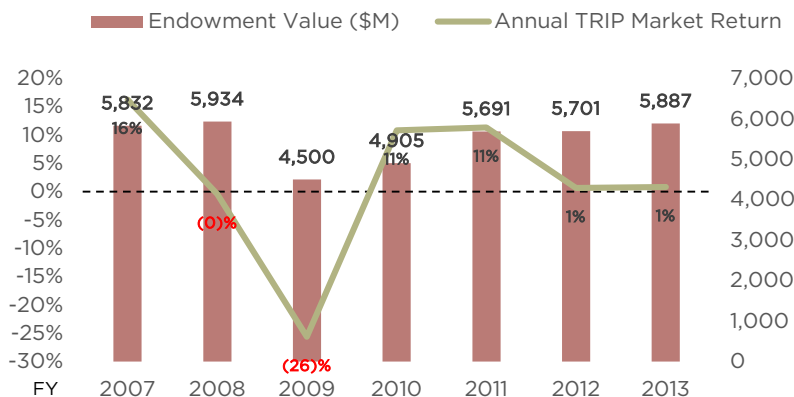
Excludes Law School, which uses different standard credit system (3 units of credit)

Academic year 2012 adjusted to account for transition to administrative credits

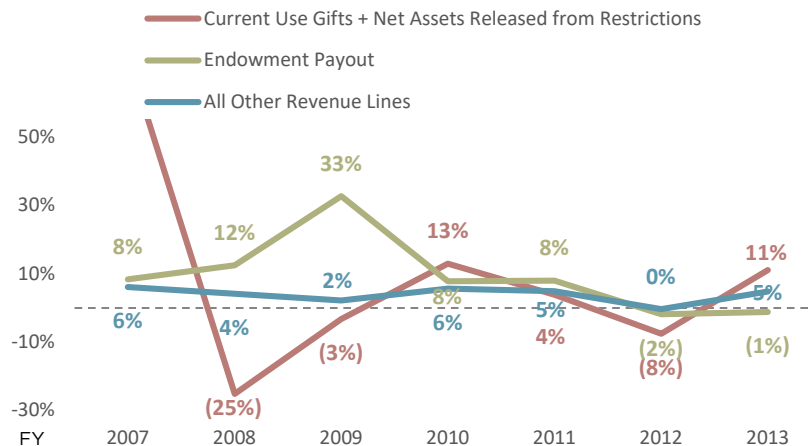
Operating Revenue Volatility with Market Exposure

- Market-based volatility focused primarily on fundraising and endowment (other operating revenue largely insulated in aggregate)
- Fundraising has strong correlation with fiscal year-end S&P 500 close
- TRIP payout formula's 12-month lag on a 36-month reference period average means market downturn will hit balance sheet first while impact to endowment payout will increase each successive year until the negative quarters cycle out of the formula

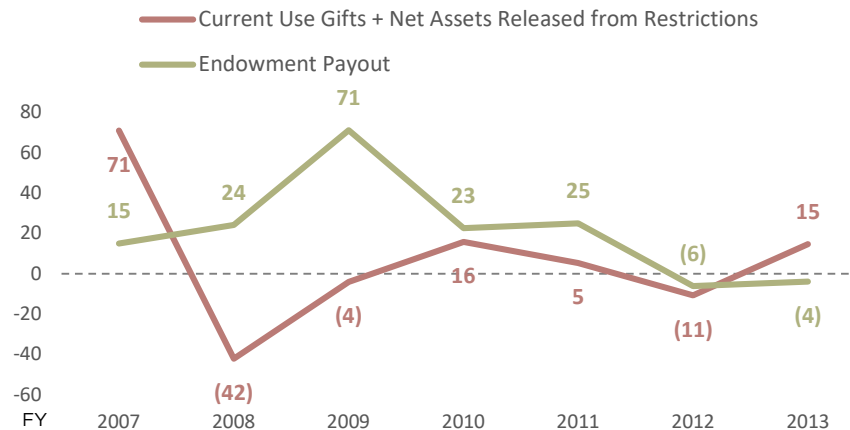
Endowment Value (University-Only)
and Annual TRIP Return



Historical Operating Revenue
YOY Change (%)



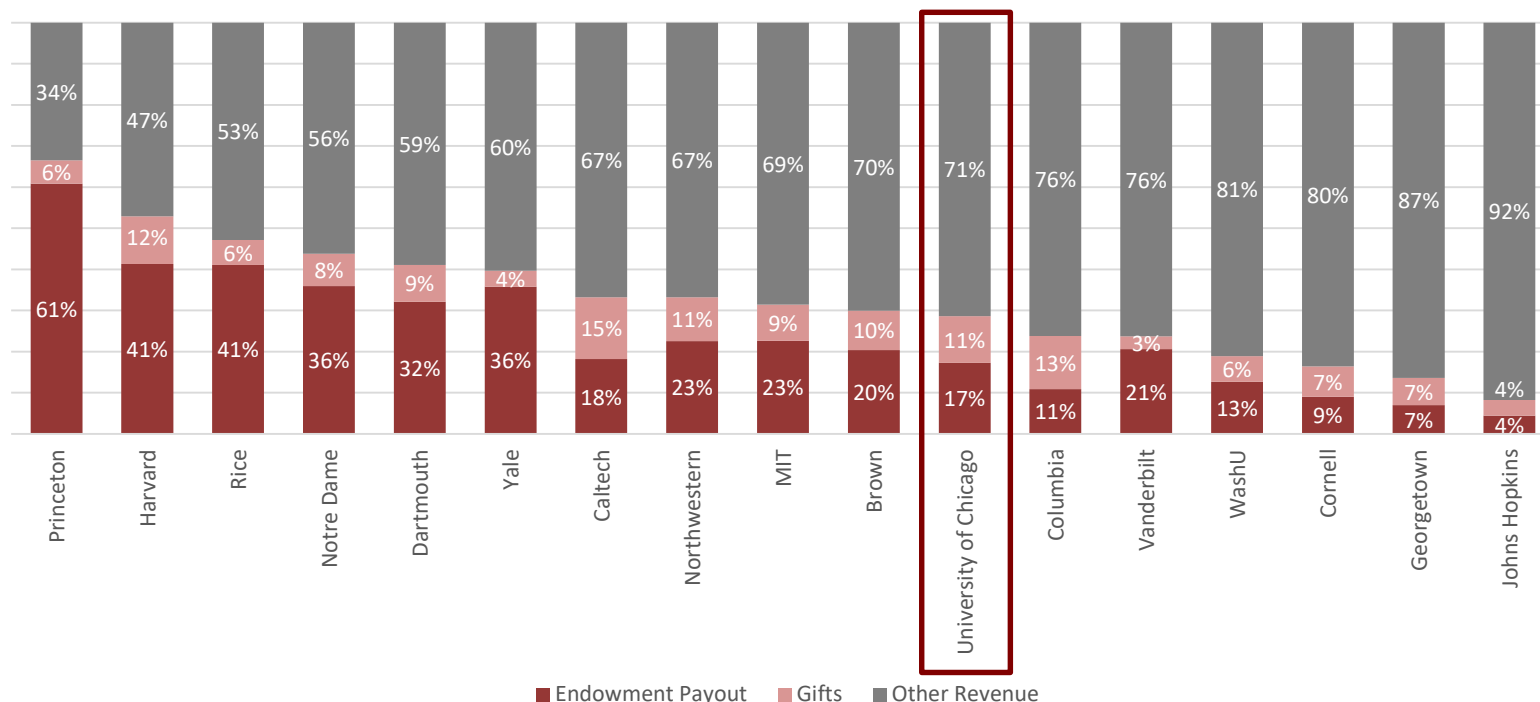
Historical Operating Revenue
YoY Change (\$M)



Peer Operating Revenue Composition

- Compared with peers, UChicago has relatively moderate exposure to endowment and gift revenue

Peer Group Consolidated Operating Revenue Composition (2017)



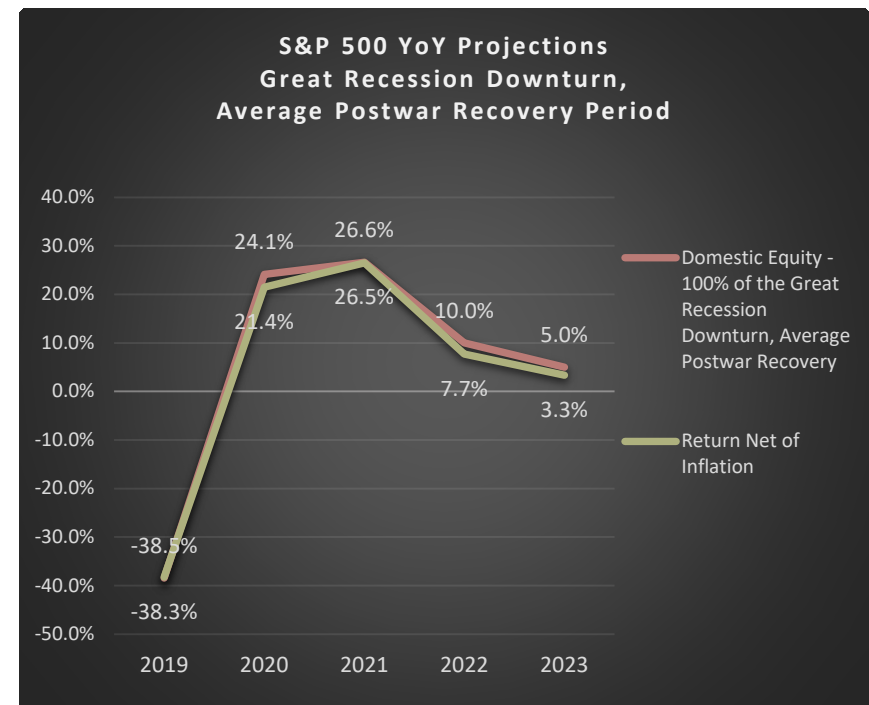
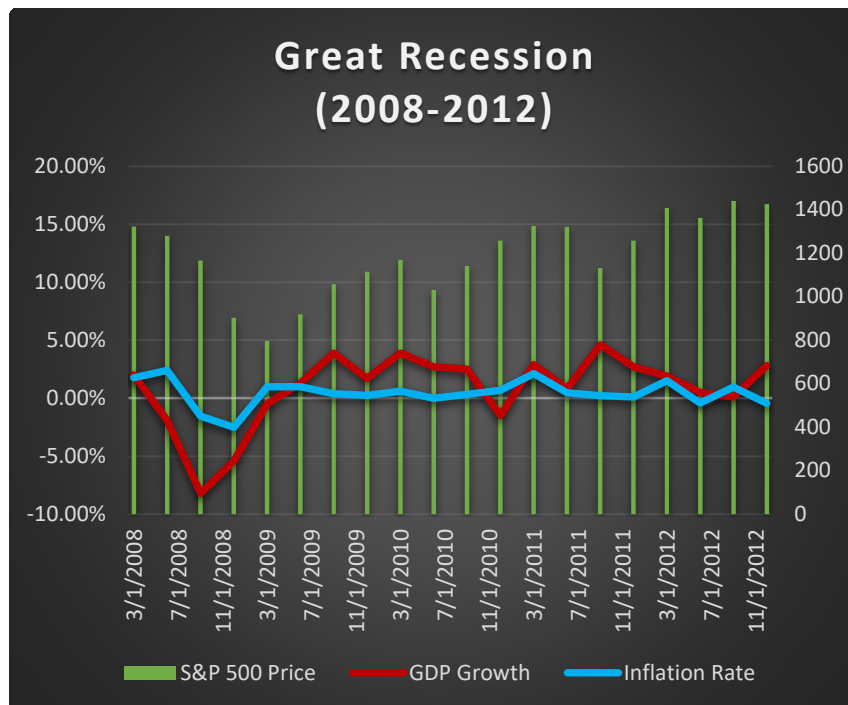
Notes:

Peer group defined as elite private universities from Moody's 2017 Medians data

- Includes institutions with a school of medicine and affiliated hospital
- Excludes institutions that directly own hospital (for purposes of isolating University-only revenue)

Stress Test Historical Reference Case

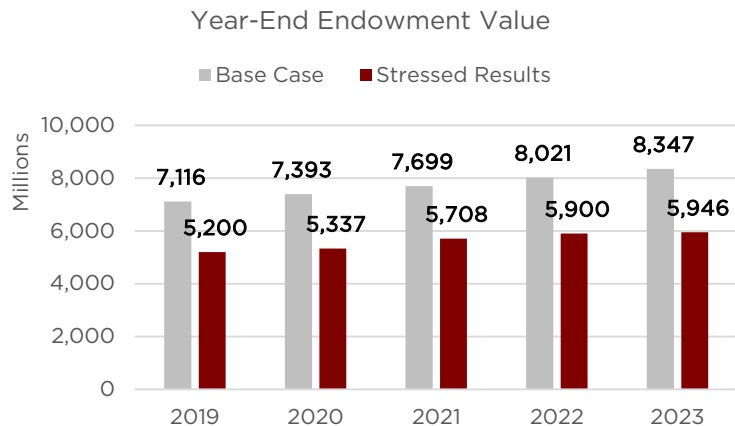
- Domestic equity markets saw returns nearing negative 40% (net of inflation) during the four historical quarters (Q1-Q4 2008) selected for year one of the stress test
- To model a typical postwar market recovery, we apply a six-quarter straight-line gain from the market trough (historical average time to prior market peak) before normalizing returns
 - The average came out to 17 months whereas the Great Recession's recovery lasted 49 months



Stress Test - Impact on Net Income

\$ in millions (University only)

- These tables show the estimated impact of our downturn scenario on net income
- Philanthropy, being highly correlated to the year-end value of the S&P 500, sees a dramatic decrease in the first 3 years relative to base
- Conversely, the endowment payout is hit hardest in the out years as the effects of a lower market value and negative returns cycle through the payout formula



FY	2019	2020	2021	2022	2023
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BASE CASE

Philanthropy	359	367	370	373	376
Endowment Payout	427	417	419	429	437
All Other Revenues	1,723	1,873	1,966	2,041	2,110
Total Revenue	2,509	2,657	2,755	2,843	2,923
Operating Expenses	2,539	2,654	2,749	2,830	2,925
Net Income	(30)	3	6	13	(2)

STRESS SCENARIO EXCLUDING ANY MANAGEMENT ACTIONS

Philanthropy	229	275	344	369	381
Endowment Payout	427	399	389	372	354
All Other Revenues	1,723	1,873	1,966	2,041	2,110
Total Revenue	2,379	2,548	2,699	2,783	2,845
Operating Expenses	2,539	2,654	2,749	2,830	2,925
Net Income	(160)	(106)	(50)	(47)	(80)

DELTA TO BASE

Philanthropy	(130)	(92)	(26)	(4)	5
Endowment Payout	(0)	(18)	(30)	(57)	(83)
All Other Revenues	-	-	-	-	-
Total Revenue	(130)	(109)	(56)	(60)	(78)
Operating Expenses	-	-	-	-	-
Net Income	(130)	(109)	(56)	(60)	(78)

Q&A



Budget Office

UNIVERSITY OF CHICAGO POSITION POSTING PROCESS CHANGE

KATRINA SPENCER

Assoc. Vice President of Finance and University Budget Director

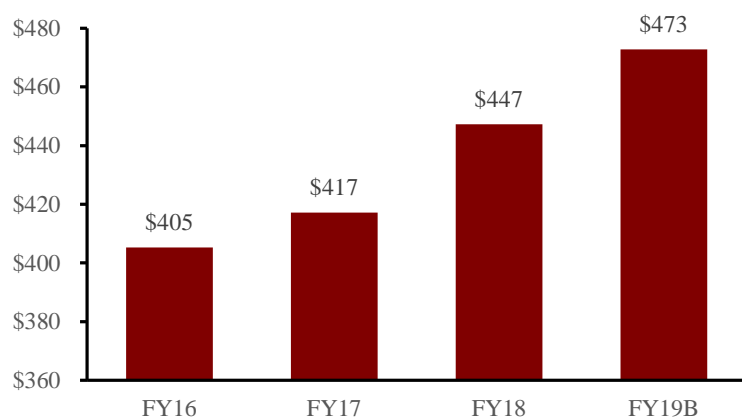
NOVEMBER 27, 2018

What is the impetus for the change?

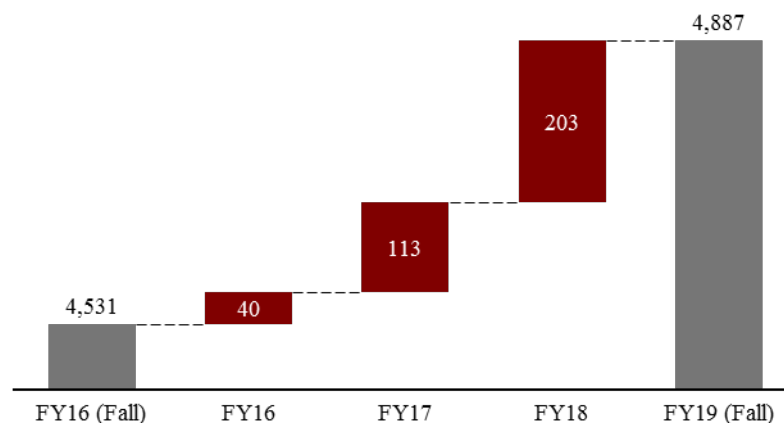
Since FY16, total University staff has increased by 356 FTE or 8%, while overall compensation expense has increased by \$68M or 17%.

University (less BSD) Total Staff Salary Growth

(\$ millions)



University (less BSD) Total Staff FTE Growth



- While growth drivers at a macro level are well understood (strategic investment in research, enrollment, and gifts), additional detail is needed to provide a better understanding of what is driving the rate of staff growth relative to faculty hiring.
- This requires a new process to collect the right information, to ensure that new staff hires are aligned with strategic goals, and to better manage the rate of staff growth.



Why is the University implementing this change?

University leadership made the decision to make this change after a thorough review of the current process and an evaluation of industry best practices.

University leadership is concerned about the rate of growth

- With compensation comprising 63% of the University's total expense base, the current growth rate will lead to an unsustainable cost structure that limits future strategic growth opportunities
- There is concern that staff are growing too fast in relation to overall growth in enrollment, but there is not detailed information to understand what is driving the change
- The current growth rate not sustainable in the event of an economic downturn or recession

The current process is not standardized across the University

- Variation at the department and division levels is inconsistent and inefficient
- Information is not collected uniformly, creating data consistency and quality issues
- Lack of transparency in current hiring decisions makes analysis difficult

Not sufficient detail to understand drivers of growth

- The information collected during the hiring process does not provide the right level of detail for understanding or reporting on drivers of staff FTE and compensation growth

Current process is not in line with peer institutions

- The majority of our Ivy+ peers have standardized requisition and hiring processes and are collecting data that helps them manage compensation expense more efficiently
- The current process at UChicago is not in line with current industry best practices

The new process will be effective as of December 1, 2018.



What positions does the new process impact?

DOES NOT Impact:

- Faculty positions
 - Including OAA, Lecturer, Sr. Lecturer, etc.
- Student positions
- Temporary positions
- Post Doc positions
- BSD (current process remains the same)

DOES Impact:

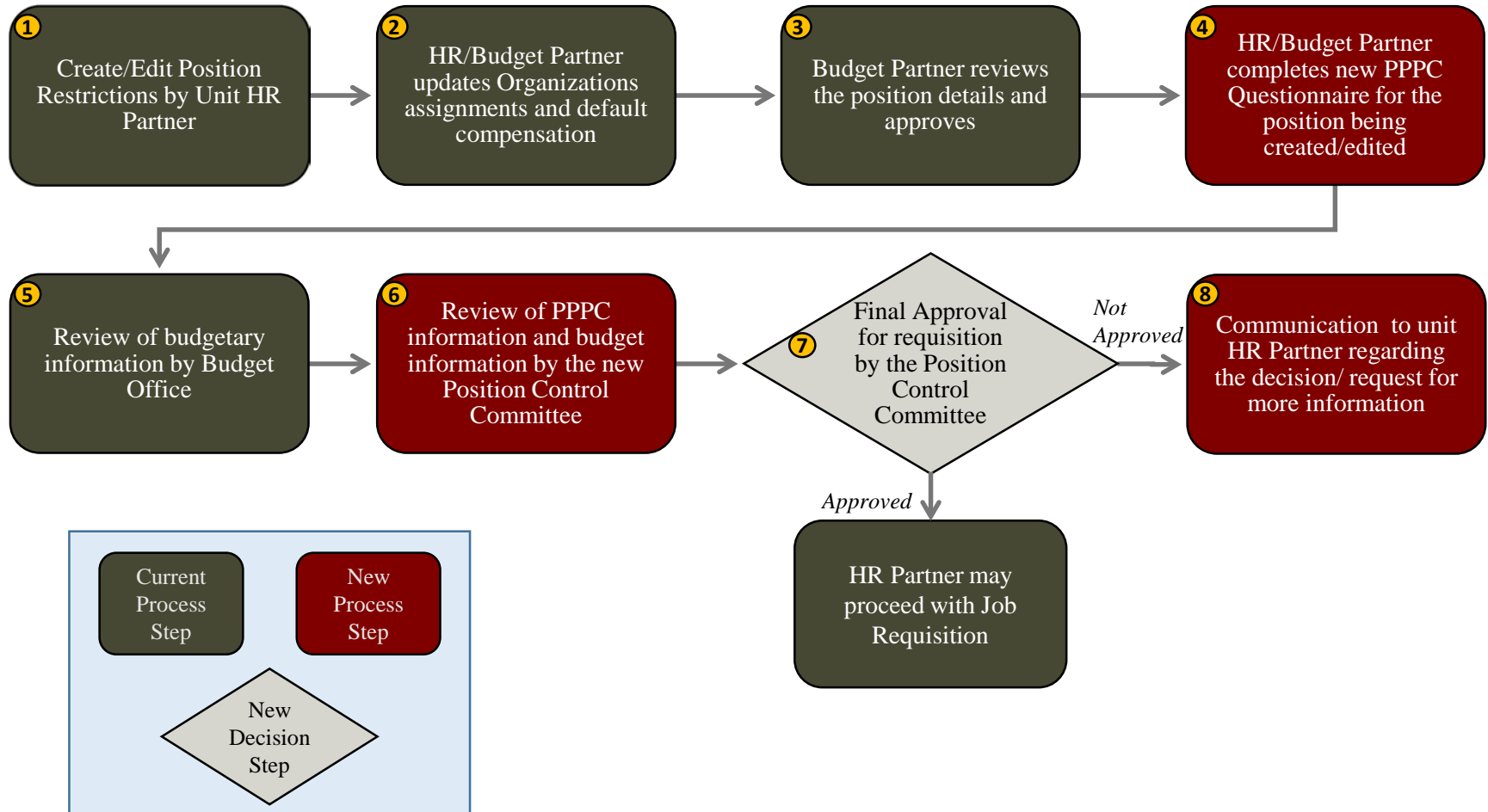
- Staff positions
 - Including all permanent and continuing staff

This change DOES NOT impact Units' FY19 Budget Targets.



Process map of the change

The new process requires units to complete a new questionnaire, a committee will then review each request and approve, deny or request more information.



What is the change to the posting process?

The overall workflow has not changed but a new questionnaire is now included within the workflow with 9 additional fields to be completed.

Step	Description
4	Unit Budget Partner or HR Partner will fill out additional questionnaire with 9 new questions: <ol style="list-style-type: none">1. What is the key purpose of this position? (<i>Revenue Generating, Critical to federal, state other regulatory compliance, Critical to divisional mission - Teaching/Research, Student Support/ Enrollment growth, Faculty Support, Operational need, Strategic initiative, Other</i>)2. Please provide a justification and detailed support for the creation of this position.3. Why is this position critical now? What happens if this position is not filled?4. Could the responsibilities be shared among existing positions? Why or why not?5. Enter all the FAS accounts funding this position.6. Select the FAS account types that will be funding this position. (<i>Unrestricted Operating, Grants & Contracts, Current use gifts, Endowment, Recharge, Auxiliary, Other</i>)7. If refill, enter the Chicago ID of the previous incumbent.8. If refill, enter the annual salary of the previous incumbent.9. If refill, enter the termination date of the previous incumbent.
6	The committee reviews requests and makes decision to approve or decline a position or request additional information from the unit
8	If position is declined or additional information is needed, the request will be sent back to Step 4, and a communication will be sent to the responsible manager notifying them of the decision and additional steps.



Why the new committee to review postings?

The committee will perform due diligence to ensure that new positions align with overall University strategic goals and to better understand growth drivers.

Who is on the Committee?

- Provost Daniel Diermeier (or designate)
- CFO Ivan Samstein (or designate)
- AVP of HR Casey Cook (or designate)



How often will the committee meet?

- The Committee will meet weekly to review positions.

What will the committee be looking for in the review?

- Do positions align with priorities? Have other options been considered to fill these needs? Is the unit anticipating meeting its budget target and/or does this request present budget problems? (etc.)
- If you have questions, please email budgetoffice@uchicago.edu or call (773) 834-5680.



Questions?





Budget Office

CHANGES TO EQUIPMENT DEPRECIATION ALLOCATION FY20 BUDGET

NOVEMBER 2018

Equipment Depreciation Allocation Model

As a follow up to our communication last spring (3/30/18) we have done a thorough analysis of the Equipment Depreciation Allocation Model.

Finding: Allocating equipment depreciation does not provide sufficient incentives or penalties to change behavior in a meaningful way, but adds unnecessary administrative complexity.

- Unit purchasing decisions are unlikely to be influenced by the equipment depreciation allocation, as purchases are often research-driven.
- Unlike space costs where units can optimize costs by moving/trading/reducing space -- units either have to purchase the equipment and/or get Provost's approval for capital expenditures.
- Much of equipment is paid for by research funds or IT, but the equipment credit and depreciation are unrestricted.
- Input sought from Research, Provost's Office, IT, and academic units. All recommend that we not continue allocating Equipment Depreciation.

Decision: Equipment will be purchased as one-time expense. All credit and depreciation activity outside specific recharge activity will be held Centrally. (This is how it was done historically.)



Current Treatment of Capital Equipment

In FY18 & FY19, a unit buys capital equipment and receives an offsetting credit at year-end.

FY18 & FY19

Operating budget line items	Unit Budget	Notes:
Capital Equipment Purchase (6XXX)	100,000	Current year purchase
Equipment Capitalization Credit Allocation (9477)	(100,000)	Zeroed out with capitalization entry at YE
Equipment Depreciation Allocation (9476)	105,000	FY19 budget=FY18 budget
Unit Bottom-line	105,000	



Current Treatment of Equipment Depreciation

Units are charged equipment depreciation expense based on guidance provided. Budget Office held FY19 equipment depreciation at FY18 rates due to complexities and time constraints of updating figures.

FY18 & FY19

Operating budget line items	Unit Budget	Notes:
Capital Equipment Purchase (6XXX)	100,000	Current year purchase
Equipment Capitalization Credit Allocation (9477)	(100,000)	Zeroed out with capitalization entry at YE
Equipment Depreciation Allocation (9476)	105,000	FY19 budget=FY18 budget
Unit Bottom-line	105,000	

In a fully implemented Equipment Depreciation model, each year the depreciation allocation would increase based on the previous year's equipment purchases and decrease based on equipment purchases from a number of years ago that are now full depreciated.



Decision for FY20 Equipment Depreciation

The University will return to the former treatment for equipment depreciation where the unit covers the cost of capital equipment purchases within their operating budget. No capitalization credit or equipment depreciation is allocated to the unit.

FY20 - Beyond

Operating budget line items	Unit Budget	Notes:
Capital Equipment Purchase (6XXX)	100,000	Current year purchase
Unit Bottom-line	100,000	



FY20 Equipment Depreciation Budget Process

Provide Target Adjustments (Reduce Expense Budget) to units with Budgeted Equipment Depreciation Allocation.

Each unit that received an equipment depreciation budget adjustment in FY18 will received an equal offsetting budget adjustment for FY20. There is no budget impact to units.

	FY18	FY19	FY20
Equipment Depreciation - Target Adjustment	100,000		(100,000)
Equipment Deprecation - Expense	(100,000)	(100,000)	-



What is FY20 Budget Impact?

Unit budget impact will depend on funding source for capital equipment: grant, recharge operation or operating budget.

CURRENT

Operating budget line items	Unit Budget	Notes:
Capital Equipment Purchase (6XXX)	100,000	Current year purchase
Equipment Capitalization Credit Allocation (9477)	(100,000)	Zeroed out with capitalization entry at YE
Equipment Depreciation Allocation (9476)	105,000	FY19 budget=FY18 budget
Unit Bottom-line	105,000	

FUTURE

Operating budget line items	Unit Budget	Notes:
Capital Equipment Purchase (6XXX)	100,000	Current year purchase
Equipment Capitalization Credit Allocation (9477)	(100,000)	Zeroed out with capitalization entry at YE
Equipment Depreciation Allocation (9476)	105,000	FY19 budget=FY18 budget
Unit Bottom-line	100,000	



Equipment Depreciation Allocation

QUESTIONS?

