

FCR 1

Office of the President
June 24, 2003

Members, Board of Trustees:

OPERATING BUDGET FOR FISCAL 2003-04

Recommendation: that the Operating Budget for Fiscal 2003-04 as submitted, including the authorization set forth in the letter of transmittal, be approved and ordered recorded as an integral part of the University's financial system with the necessary fiscal control being exercised for the collection and appropriation of income and for the expenditure of departmental appropriations in accordance with authorized fiscal policies and procedures and accepted as a basis of maximum expenditures for fiscal 2003-04.

Background: The 2003-04 Operating Budget of the University of Kentucky is presented for approval by the Board of Trustees. Copies of the budget document have been made available to the members of the Board.

Action taken:

Approved

Disapproved

Other _____

June 24, 2003

Members of the Board of Trustees:

I am pleased to submit for your consideration and approval the 2003-04 University of Kentucky Operating Budget. The University is in a time of change – decreasing state support, increasing enrollments and higher expectations. The recommended operating budget for FY 2003-04 totals \$1.392 billion, an increase of \$19.9 million or 1.5 percent over FY 2002-03. The development of the proposed budget was a challenging task. In addition to managing a recurring state budget reduction while enrolling more students, we continue to strive to become one of America’s top 20 public research universities and a catalyst for intellectual, social, cultural and economic development for the Commonwealth. This budget reflects the goals and objectives set forth in our new Strategic Plan which is also being presented to you for approval. Given our limited resources, our budget objectives for FY 2003-04 include:

- Fund a modest salary increase for faculty and staff
- Avoid passing on any health insurance cost increases to our employees
- Provide more scholarships to students on both a need- and merit-basis, and
- Fund program improvements that invest in our future.

“One University”

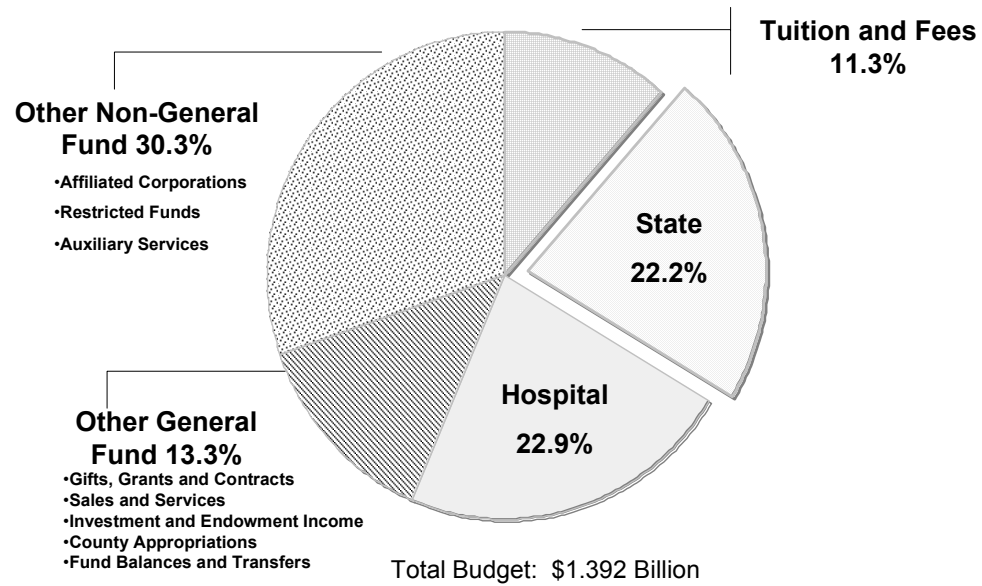
The recommended FY 2003-04 budget reflects my continued commitment to implement an organizational structure and the operational processes that support the “One University” concept. This budget reflects significant organizational changes as we transition to the Provost model. The full implementation of the Provost model will facilitate the University’s ability to capitalize on its intellectual diversity through the integration of all its resources. Many support functions and services performed by the UK Chandler Medical Center were integrated with similar units in the rest of the campus with the goals of maintaining high quality support services and achieving significant cost savings totaling \$2 million.

Revenues and Other Fund Sources

State Appropriations.

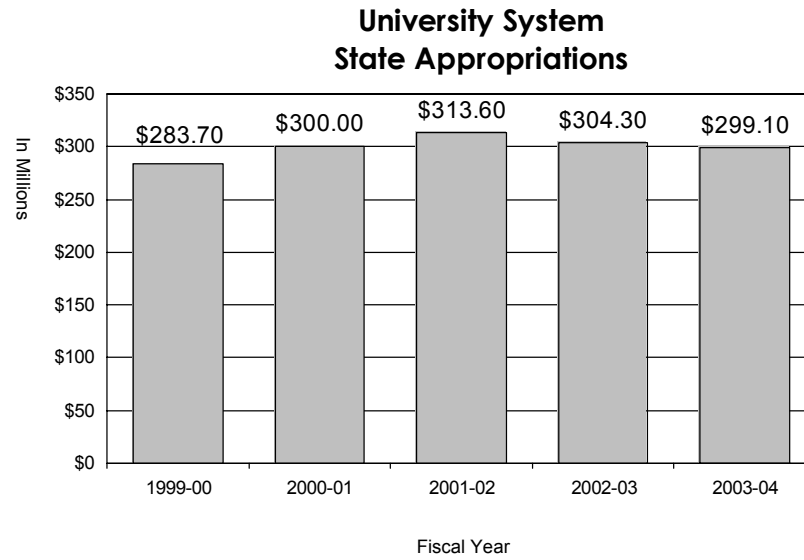
As shown below, state appropriations will account for approximately 22.2 percent of the institution's operating budget in FY 2003-04.

FY 2004 Revenues

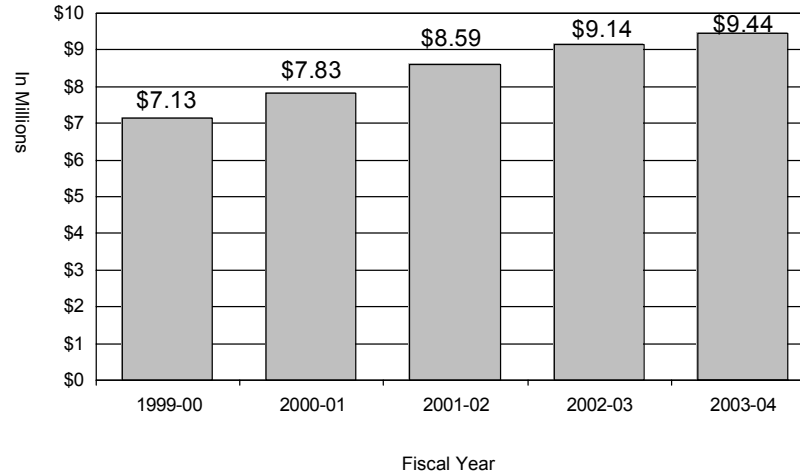


The Commonwealth of Kentucky's 2002-04 biennial budget was recently enacted by the 2003 General Assembly and signed by the Governor. For the third consecutive year, the University will experience significant decreases (both recurring and nonrecurring) in state appropriations. The University System's FY 2003-04 state appropriations will total \$299.1 million, \$14.5 million less than the original FY 2001-02 appropriated amounts. The Lexington Community College's FY 2003-04 state appropriations total \$9.4 million, 9.9 percent greater than its original FY 2001-02 appropriated amounts.

The University was able to absorb the FY 2001-02 \$6 million recurring cut in state appropriations without impacting the institution's academic programs. As the reductions have become more severe, all primary areas have been affected. In order to protect the academic programs as much as possible, the FY 2003-04 budget reflects an average 1.5 percent budget reduction for the Colleges and other academic units while the support units were subject to an average 2.23 percent reduction in General Fund supported expenses. The following graphs reflect the University System's and the Lexington Community College's original budgeted state appropriation amounts for the past five years.



Lexington Community College State Appropriations

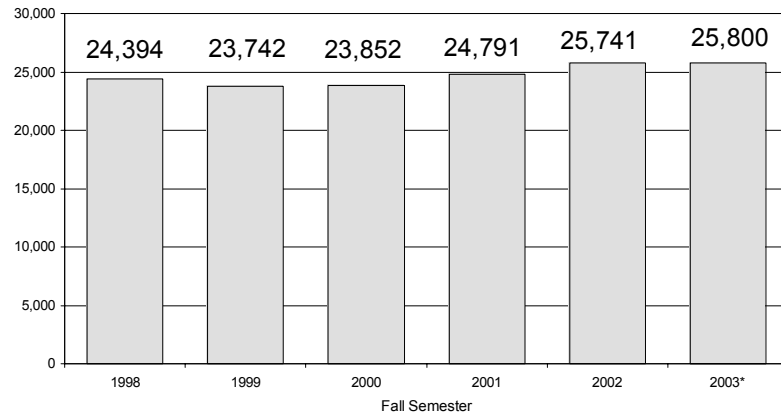


The recently enacted state budget includes debt service in FY 2003-04 to issue \$120 million in taxable bonds for the Endowment Match Program. The University of Kentucky will be eligible to match \$67 million with private gifts to create and enhance endowed chairs, professorships, and mission-related activities. We estimate the state bond proceeds to be available this fall. The state budget also includes a \$155 million agency bond pool authorization for the public, postsecondary education institutions. The University has been allotted \$61.9 million of the agency bond authority to construct student housing and a parking structure. The debt service on these bond issuances will be funded with Housing and Dining revenues and parking revenues, respectively. Finally, the state budget includes a recurring \$275,500 appropriation to the University for the Center for Research on Violence Against Women.

Tuition and Fees.

The University continues to enroll more students. As shown in the following charts, the University System's headcount enrollment has grown by 1,889 to 25,741 students from fall 2000 to fall 2002. The enrollment growth is primarily attributed to a 22.4 percent increase in the first-time freshmen class from fall 2001 to fall 2002 and a 30 percent increase in enrolled doctoral students over the past five years.

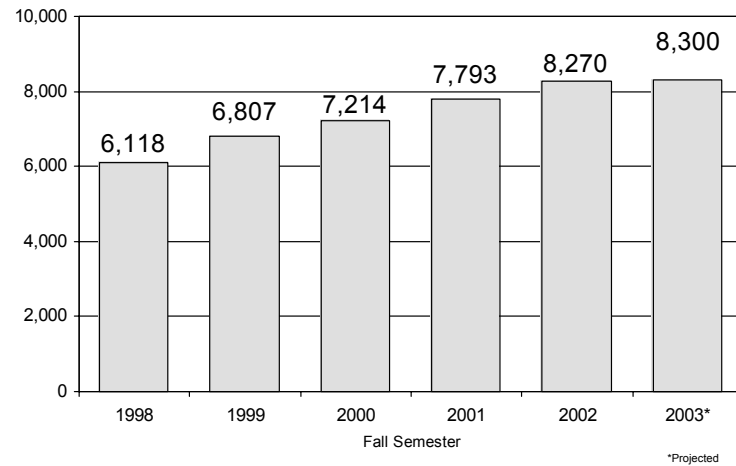
**University System
Headcount Enrollment**



*Projected

The Lexington Community College enrollment growth is also dramatic, increasing by 35.2 percent, or 2,152 students, since fall 1998.

Lexington Community College Headcount Enrollment



In April 2003, the Board of Trustees approved a 15 percent increase in undergraduate, resident tuition rates for the University System. The Board of Trustees approved an 8 percent increase in resident tuition rates for the Lexington Community College in September 2001. Based on the approved tuition rates and projected enrollments of 25,800 and 8,300 at the University System and LCC, respectively, the recommended budget includes \$157.3 million of tuition and fee revenue (an increase of \$17.4 million, or 12.4 percent, over FY 2002-03).

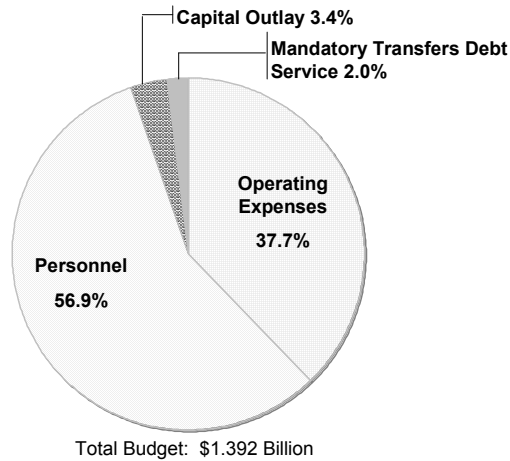
Internal Reallocations.

In order to cover the recurring state budget reduction and achieve our budget objectives, we had to reallocate a significant amount of funds internally and continue to use nonrecurring funds, including year-end fund balances. The proposed FY 2003-04 budget reflects a total internal reallocation of approximately \$9 million dollars, including \$2 million from the transition to the Provost model.

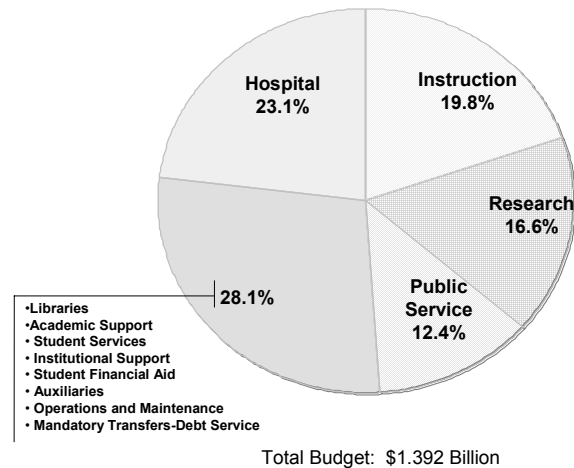
Allocation of Resources

As shown below, personnel expenses will account for 56.9 percent of the institution’s total operating budget in FY 2003-04. In addition, instruction will account for 19.8 percent of the institution’s expenses by function.

FY 2004 Expenses by Natural Category



FY 2004 Expenses by Function



Budget Highlights.

The recommended FY 2003-04 operating budget reflects our budget objectives for the year. Some highlights from the recommended budget follow. The amounts listed below represent the total cost to those units supported with General Funds (i.e., state appropriations, tuition, investment income, etc.):

- ❖ As reflected in the Strategic Plan, competitive salaries for faculty and staff are imperative for the University to become one of the 20 best public research institutions in the nation. Given the limited resources available, the FY 2003-04 budget includes an average salary increase of 3 percent for faculty and staff, to be distributed based upon merit. The budget also includes funds for faculty promotions, a 2 percent increase in salaries for teaching assistants and a 2 percent minimum salary grade scale adjustment. Total cost for salary enhancements: \$9.8 million.
- ❖ The University has assumed the total increase in health insurance premium costs of approximately 9.6 percent for its employees. With the exception of pharmacy costs, employees will see no change in their health insurance costs. Total cost increase of the Employee Health Insurance Program: \$2.6 million.

- ❖ The institution's scholarship budget has been increased to cover the tuition rate increase, a new need-based scholarship program, funding for the second year of the Legacy Tuition Scholarship Program, and continued support for the Governor Scholars and Governor School for the Arts Scholarships Program. The budget includes \$1 million from the University of Kentucky Athletics Association, Inc. in support of the increased scholarships. Total scholarship increases: \$4.6 million.
- ❖ Over \$4 million of recurring and nonrecurring funds are budgeted for the strategic investment in high-priority academic and research programs, recruitment and appointment of college and program leadership, and support for enrollment growth and improved retention as listed below.
 - Subsequent to the Report of the Futures Task Force, a call for proposals was issued to advance the Futures priority areas. Based on the proposals received, over \$550,000 will be invested in seven initiatives. These initiatives support the School of Music; plant bioengineering in the College of Agriculture; risk-related behavior in the colleges of Medicine, Arts and Sciences, and Communications and Information Studies; race, ethnicity, and civic identities in the College of Arts and Sciences; organic chemistry; genomics (Biology); and foreign language education for the College of Arts and Sciences and the College of Education.
 - \$500,000 to support a call for proposals for the Medical Center colleges to advance the Futures priority areas.
 - The Board of Trustees recently approved a 25 percent increase in the professional tuition rates for Law, Business and Economics, Dentistry, Medicine and Pharmacy effective fall 2003. Approximately, \$1.3 million of the tuition revenue generated from these rate increases will be invested directly in the respective professional programs.
 - \$700,000 for the strategic investment in high-priority programs including: the enhancement of the College of Law in response to the American Bar Association accreditation issues; the further development of the Center for Oral Health Research in the College of Dentistry; support for the School of Architecture in the College of Design;

enrollment growth in the pharmacy doctorate program; and enrollment growth in the School of Public Health masters and doctoral programs.

- \$670,000 for graduate student support to address the increased cost of tuition waivers and health insurance provided to teaching assistants, research assistants, and fellowship recipients.
- \$460,000 for academic administration and leadership initiatives including supplemental funds for the recruitment and appointment of new deans and directors and an operating expense incentive program to increase first to second year student retention and extramural funding.
- ❖ Over \$1 million to the Lexington Community College for program improvements to support increased enrollments including part-time instructors, faculty and staff positions, instructional equipment, supplies and operating expenses.
- ❖ \$100,000 for a Quality Enhancement Program to invest in program improvements identified through periodic reviews.
- ❖ \$300,000 to offset inflationary costs for monographs, serials and journals in the University Libraries.
- ❖ \$476,300 for maintenance and operation of new facilities coming online, including the Gill Building and the Center for Rural Health.
- ❖ \$1 million for renovating and equipping classrooms.
- ❖ \$2.2 million towards the ERP, the replacement of the finance, human resources, and student information systems.
- ❖ \$499,300 for the enhancement of the institutional data warehouse, to support the interface with Immigration and Naturalization Service's database in compliance with federal immigration laws, and a virus protection software site license.
- ❖ \$54,000 for a programming position in Research Information Services to support the Graduate School.

- ❖ \$390,000 to improve the lighting at the Guignol Theatre.
- ❖ \$390,000 to improve the HVAC in the Reynolds Building No. 1.

Conclusion

I hereby request that the Board approve this operating budget and the appropriation and allocation of all fund balances for future operations, to include amounts necessary to cover accounts receivable and inventories that will represent assets on the audited balance sheet of the University of Kentucky for FY 2002-03. These balances are in addition to those incorporated in the proposed budget. Since the books of accounts of the University of Kentucky are maintained on a full accrual basis, this action will provide the funds necessary to maintain a sound financial position during the 2003-04 fiscal year.

The FY 2003-04 budget recommended for approval has been a challenging task. This budget reflects our Strategic Plan – we have focused on faculty and high-priority academic programs. Given the state budget picture, we will not make the progress we had hoped for, but neither will we stand still. We will make notable gains in 2003-04. For this I thank my budget staff, administrators, and the faculty and staff who will make progress a reality in the new fiscal year. Finally, I thank the Board of Trustees for their continued encouragement and support and I look forward to working with you in the year ahead to achieve even greater good for our University and the people of the Commonwealth.

Lee T. Todd, Jr.
President