

❖ Overview of the New Incentive-Based Budget Model

Beginning in Fiscal Year (FY) 2018-19, CU Denver will employ an incentive-based budget model. This new approach aligns our investments and resources with our strategic priorities by incentivizing the types of activities that drive both student and financial success. This includes generating funds, reallocating our existing resources and containing costs. Along with the incentives built into the model, CU Denver is implementing a planning and budgeting process that creates a forum for schools, colleges and the central support units to implement strategies and work together to achieve CU Denver's priorities.

❖ Making the Case for Change

Prior to 2018, CU Denver used an incremental approach to resource allocation. This is a traditional, commonly used budget model that bases budget proposals and allocations on the funding levels of the previous year. Under this model, new revenue results in equal percentage increases for all units; in hard times, budget cuts are typically across-the-board in reach.

This approach can be successful when revenue is steadily climbing. However, when a university (like ours) is financially dependent on enrollment and prone to swings in enrollment, an incremental budget can lead to financial uncertainty. Incremental budgeting typically does not encourage the type of action needed to create growth, selectively reallocate financial resources or contain costs.

In 2018, CU Denver faces a more dynamic and competitive environment than ever before. Reduced state funding, greater competition for students and increasing costs have constrained budgets. Responding to these challenges has prompted the shift from the historical incremental budget approach to an incentive-based budget model.

❖ The New Incentive-Based Budget Model

Beginning in November of 2016, a steering committee composed of cross-campus leadership was created to guide the development of a new budget model and process. The committee's work culminated in the adoption of the incentive-based budget model in October 2017.

In contrast to incremental budgeting, an incentive-based approach provides schools and colleges with greater responsibility for budget development and control, while allocating funding based on specific activities and metrics (e.g. credit hours production). This model more closely ties funding to instructional activities by allotting tuition resources relative to enrollment, which incentivizes the enhancement of revenues and management of costs at the school and college level. Also, the model provides all campus academic and administrative divisions a comprehensive, all-funds view of the institutional budget—highlighting the critical, yet often obscured, components of the institution's financial sustainability that require on-going funding commitments.

Incremental Budgeting (current):
A budget prepared based on the previous year's budget with incremental amounts added for the new budget year

Incentive-Based Budgeting (new):
Incentive-based budgeting focuses on aligning funding resources with activity levels. Increases in activity levels result in increased unit funding while decreased activity levels results in decreased funding.

❖ Model Structure

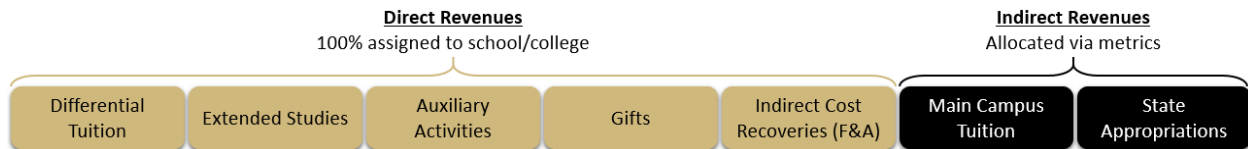
The incentive-based budget model utilizes a series of formulas, based on specific activities and metrics, to distribute revenues and administrative costs and to create a central pool of resources for cross-subsidies (subvention) and strategic initiatives in order to determine budget allocations for the schools and colleges.

The structure of the model has three key elements:

1. Revenue allocation
2. Cost allocations, both direct and administrative; and
3. Mission Enhancement Fund

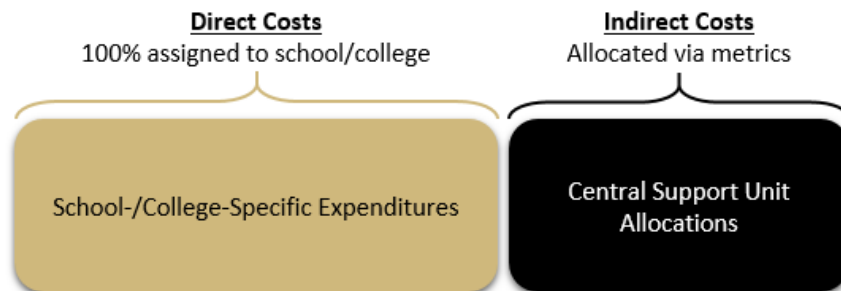
❖ Revenue Allocations

Revenue allocation is the first step in the process of determining budget allocations with the new budget model. Revenue is based on projections and falls into one of two categories: Allocable or Direct. The model credits allocable revenues to the schools and colleges via data metrics, while attributing direct revenues straight to the school or college. The following table provides details on treatment of revenues:



❖ Cost Allocations

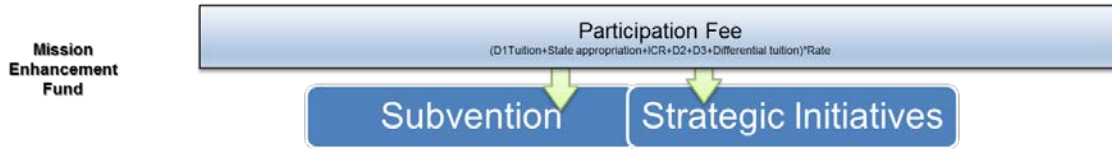
Step two in the model is cost allocations. Similar to revenues, there are two cost categories: 1) Direct or 2) Indirect. Direct costs are the projected expenses that are specific to the school or college (e.g., faculty salaries) while indirect costs are the projected expenses related to central administration (e.g. facilities, HR, Finance, etc.). The model divides administrative expenses into cost pools, referred to as Central Support Units, which are determined by function. The expense budgets for the Central Support Units are allocated to the Schools and Colleges via cost pools, each with its own allocation metric. The amount of central support unit costs attributed to a school or college their respective percentage of the selected allocation driver (metric).



❖ Mission Enhancement Fund

The final, and most critical, step in the budget model is the application of Mission Enhancement fund, which balances the economic and academic aspects of higher education, recognizing that both are needed

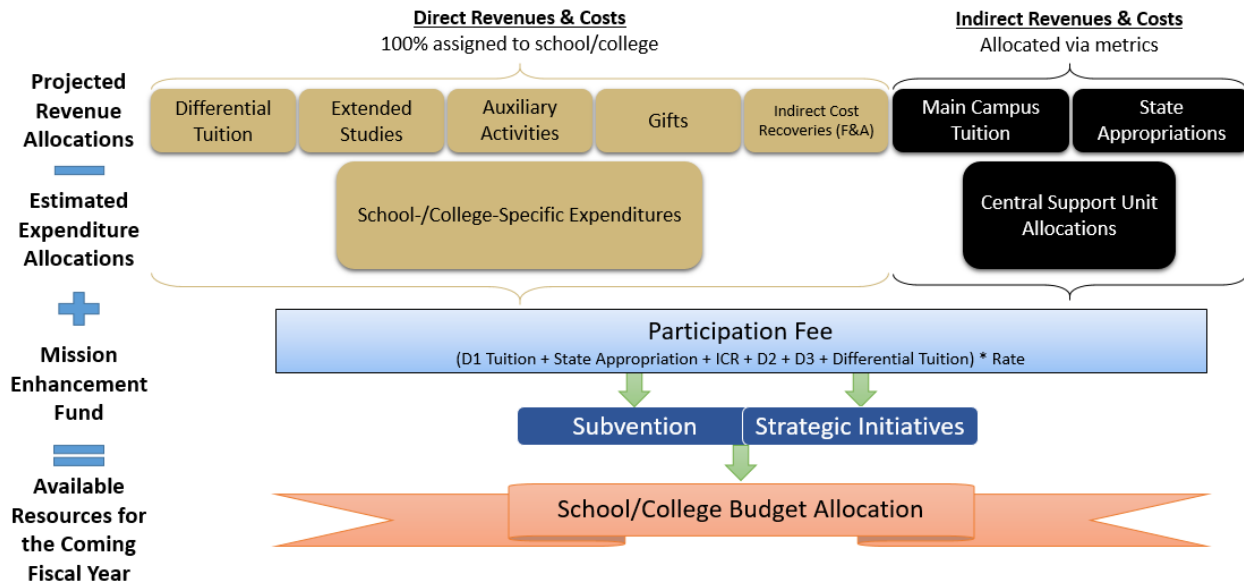
to successfully operate in a competitive and dynamic financial landscape. Created by applying a participation fee to certain revenue sources, the Mission Enhancement Fund provides support, referred to as subvention, to core academic offerings that may not generate enough revenue to meet expenses, along with providing a pool of resources for strategic initiatives.



In the annual budget setting process, leadership for the Schools and Colleges will meet with two committees, the Chancellor’s Advisory Committee on Budget and the Executive Budget Committee, to discuss proposed subvention requirements. The allocation of the Mission Enhancement Fund will strategically support higher cost academic programs, while holding the program leadership accountable to the performance of their overall program portfolio.

While subvention is set on an annual basis, the CACB and Executive Budget Committee will develop rolling 3-year guidance, which will prevent a formulaic dollar-for-dollar reduction in subvention in relation to positive margins and/or funds carried forward from the prior-year (i.e. carryforwards).

Revenue Allocation, Cost Allocation and the Mission Enhancement Fund complete the budget model picture:



❖ Success Under the New Model

Incentive-based budgeting focuses on aligning funding resources with strategic priorities. The new model maintains strategic control at the central executive level, but also provides incentives for our schools and colleges to grow, to contain costs and to reallocate resources within their budgets. The new model's success depends on a balance between local optimization and investment to the best interest of the university as a whole. Specific strategies for success include:

- Growth in enrollment – through increased recruitment and retention.
- Enhancement of high demand programs and creation of market driven programs.
- Increases in sponsored research, creative work, and grants and contracts.
- Increases in opportunities for fundraising/advancement.
- Student-centric, research-oriented and faculty-led interactions in the community, thereby increasing revenue to a school or college through enrollment growth and sponsored research.
- Collaborations that break down silos and promote a more inclusive university culture.
- Strategic use of central services in lieu of local duplicative services.
- Reallocating existing resources to higher priority functions.

Overall, the model provides incentives for the entire university community to take advantage of new markets and opportunities for growth in any kind of revenue – including enrollment, research and donations. By moving to a model that enhances understanding and articulates the real relationships between their inputs and outputs as an organization will allow for making better informed decisions driven by mission, quality, cost, and revenue considerations. In other words, by working together, with coordinated goals, actions and incentives married to guiding priorities under an incentive-based budget model, the university is poised to thrive in all areas.

You can find more resources and information on the new budget model and process here:

<http://www.ucdenver.edu/about/departments/Budget/denver-budget-model/Pages/default.aspx>