2019-2020 TOTAL EXPENDITURES – IMPLICATIONS FOR TOTAL EXPENDITURE TARGETS

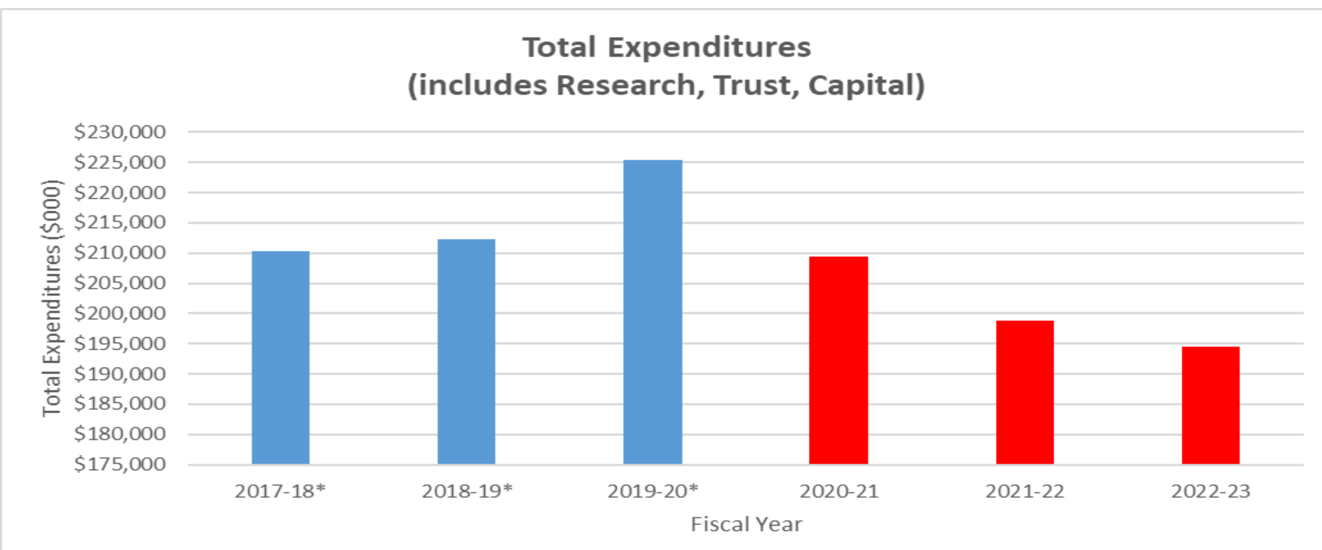
Investment Management Agreement

Late in 2019 the Provincial Government announced that each Alberta Post-Secondary Institution (PSI) will be required to sign off on an Investment Management Agreement (IMA) which will include the institution's mandate, a financial commitment from government (i.e. provincial grants), mutual priorities, and performance metrics to facilitate the allocation of outcomes-based funding. The IMAs were introduced to ensure government and institutions are focused on meeting the needs of the province. For more detailed information on the IMA refer to the 2020-2021 Budget Brief Investment Management Agreement.

On June 1, 2020 the Minister of Advanced Education announced that it will be delaying the implementation of the IMAs to a future date, due to the impact and uncertainties facing post-secondary institutions because of COVID-19. The delay of the IMAs has not relieved the University of the requirement to meet the total expenditure target starting in 2020-2021, which has a significant negative budgetary impact on the institution. Refer to the 2020-2021 Budget Brief Total Expenditure Targets for a more thorough explanation of this metric.

Total Expenditures

Total expenditures are the most heavily weighted performance metric (40%) in the new outcomes-based funding model. The Province chose 2018-2019 as the base year for the establishment of the Total Expenditure Targets for 2020-2021 and beyond. Choosing 2018-2019 as the base year for the expenditure targets has created a substantial issue for the University as in 2019-2020 the University had significant increases in expenditures ($13.1 million) that have not been taken into consideration by the Province and thus requires exceptional budget reductions in 2020-2021 for the University to meet the total expenditure targets.



*As per audited financial statements

The following is an explanation of the increase in total expenditures in 2019-2020, the majority of which are a result of the new Science Commons facility.

			($000)
2018-2019 Total Expenses (as per audited financial statements)			$ 212,264
2019-2020 Expenditure Increases			
1. Science Commons operating expenses		$ 3,000	
2. Science Commons amortization expense		$ 6,317	
3. Scholarships transferred from Advanced Education		$ 1,347	
4. Severance Costs		$ 2,097	
5. Artwork donations		$ 26	
6. UAPP liability valuation change		$ (278)	
7. Expenditure Inflation increases		$ 591	$ 13,100
2019-2020 Total Expenses (as per audited financial statements)			$ 225,364

1. & 2. Science Commons operating expenses and amortization expense – The new Science Commons (science and academic building) facility was completed in 2019-20 fiscal year and thus operating costs and amortization expenses increased.
3. Scholarships - Advanced Education transferred to the University scholarships that were previously administered and paid by Advanced Education, which then increases the scholarship expense on the University's financial statement. Although the scholarships are still funded by Advanced Education, the revenue and expense now are recorded in the University's financial statements, and thus appears as an expense for the University. The scholarships transferred from the Province are the Indigenous Career Award, the Alberta Graduate Excellence Scholarship, the Community Leadership & Academic Success Scholarship, and the Alberta Athletic Award.
4. Severance Costs - In order to balance the University's budget as a result of the reductions in our Provincial operating grant, employee layoffs were necessary. Layoffs require severance costs to be paid as per employee collective agreements. These costs will increase the expenses for the University but were required in order to reduce expenditures on salaries and benefits in future years.
5. Artwork Donations - The UofL has an extensive and renowned art collection and thus it attracts significant artwork donations each year. Accounting standards require the donated artwork be recorded as donation income, with the corresponding amount included as an expense (zero impact on the operating statement bottom line).
6. Universities Academic Pension Plan (UAPP) – liability valuation change (actuarial gains and losses) are recognized in our financial statements but the University does not have any control over accounting for this expense. There could be gains or losses each year on the valuation of our obligation which impact our expenses. Pension premiums expenses paid are already included in our total expenses.

The above adjustments to our expenditures in 2019-2020 should be taken into consideration by the Province in setting the total expenditure targets since most of the costs will be on-going expenditures. The increase in the expenses does not mean the University has been inefficient but are a result of the various circumstances outlined above. If the Province had adjusted the total expenditures targets for the above listed expenditures, the impact on the University to achieve the total expenditure target would be reasonable.

Increased revenues may result in increased expenditures

Although the Province is encouraging post-secondary institutions to generate external revenue and be less reliant on the Provincial operating grants, there are many revenue generating activities that, due to accounting principles, as well as the conditions of receiving the external revenue, will result in a matching increase in expenses.

The major concern that the University has with the total expenditure target is that the Province is only considering one side of the ledger, expenditures, and ignoring the revenue ledger. In many cases the University will receive revenue to offset the expense.

Situations that give rise to this revenue and expense recognition issue include the following:

- Restricted grants

  When a research grant is received by the University, this will increase expenses. There is no bottom-line impact on the University's operating statement since the expenses are exactly offset by the research grant revenue. Increased spending increases revenue; decreased spending decreases revenue. Expanding research activity at the University is one of the fundamental priorities of the University.

  A further example of this is the recent grant from the Mastercard Foundation. The University received a $15 million grant ($3 million per year for 5 years) from the Mastercard Foundation in late 2019 to provide support for indigenous student education. This grant will increase our expenditures $3 million per year, with the offsetting grant revenue. Expenditure targets need to be increased by $3 million in the next 5 years to recognize these expenditures.

  This same scenario exists for the Dhillon donation for the School of Business which received a $10 million donation in 2017, receivable over 8 years.

- Artwork donations

  The U of L has an extensive and renowned art collection and thus it attracts significant artwork donations each year. Accounting standards require the recognition of the donated artwork in revenue as donation income, with the corresponding amount included as an expense (zero impact on the operating statement bottom line). These amounts should be excluded from expenditures since there is a corresponding revenue amount.

- Insurance covered expenditures

  All expenditures which are offset by insurance proceeds should be excluded from the total expenditure target since there is a corresponding revenue amount.

- Capital grants

  Capital grants are recognized as revenue as amortization expense is recorded over the useful life of the asset purchased with the capital grant. There is no net impact on the University's operating statement. The amortization expense for our new Science Commons facility, for example, represents a significant expense increase ($7.05 million annualized) for the University on our audited financial statements that cannot be reduced. The University is appealing to the Province that this expense, along with the new, non-optional expenses associated with operating the Science Commons (approximately $3 million per year) need to be included and increase the total expenditure target.

Total Expenditure targets may be offset by revenue targets being exceeded

The University has been verbally informed from Advanced Education that if the revenue targets are exceeded, the amount that the target is exceeded may reduce the impact of the total expenditure target. This is good news and will perhaps provide some relief by reducing the budget reductions required. As an example, if the University exceeds its revenue target by $6.5 million due to an increase in donation revenue, the expense target may be reduced to $2.3 million by the offset of the $6.5 million.

REVENUE TARGET EXCEEDED		
		2020-2021
Revenue target		$ 218,444,390
Actual revenue realized (e.g. due to donation increases)		$ 225,000,000
Excess actual over target		$ 6,555,610
Expense target reduction		$ (8,895,082)
Reduced Expense target reduction		$ (2,339,472)

It is important to note that the offset of the exceeded revenue target will not benefit the University in relation to increases in research grant revenue, for example, since any increase in research grant revenue will also have a corresponding increase in total expenses as the grant revenue is spent.

Continued dialogue with Advanced Education

Senior administration, as well as the University's Board of Governors, has been in constant contact and discussions with Advanced Education and the Provincial Treasury to outline the significant negative impact the total expenditure target metric has on our University and our required budget reductions. As a result of the MacKinnon Report on Alberta's Finances, which was released in September 2019, the Province is determined to reduce the expenditures of post-secondary institutions to be more in-line with the expenditures per student to the comparative provinces. The MacKinnon report indicated that Alberta spends approximately $10,000 more per student than the compared provinces (BC, Ontario and Quebec). There are many historic reasons for the difference in spending levels between the provinces but by imposing the expenditure targets with such a short timeline to achieve them, puts the institutions in very difficult budget circumstances.