

FCR 10

Office of the President
December 14, 2004

Members, Board of Trustees:

PILOT PLAN FOR THE DISTRIBUTION AND USE OF PROFESSIONAL INCOME UNDER THE
UNIVERSITY OF KENTUCKY CENTER FOR MANUFACTURING,
LEAN PROGRAM

Recommendation: that the Board of Trustees approve the “Pilot Plan for the Distribution and Use of Professional Income under the University of Kentucky Center for Manufacturing, Lean Program.” The pilot operation of the plan will be for two years, retroactive from July 1, 2004 and extending to June 30, 2006.

Background: The University of Kentucky Center for Manufacturing has built a program of courses and workshops to teach “Lean Manufacturing” to industry. “Lean Manufacturing” is a set of practices and philosophies to improve manufacturing operations. It is based on practices and philosophies initially pioneered by Toyota. This program has become very successful, and its clients include companies from around the world. Demand for expanded services makes it essential that the Center have the ability to attract new faculty instructors, as well as provide a competitive compensation package to all faculty instructors.

The attached “Practice Plan” provides a structure for the use of the income generated by the courses and workshops for industry. While this plan is based on the “practice plans” used for clinical income from faculty in UK medical colleges, it varies from existing practice plans. Under the terms of the plan, income is received and managed within the college in accordance with university regulations, as opposed to being managed by a separate corporation. Additionally, this plan is limited to a single center.

The plan serves multiple purposes, allowing current instructors in the program to share in revenue from expanded course offerings and allowing the hiring of new instructors with anticipated compensation that is competitive with the market.

At the end of the two-year pilot operation, the program will be evaluated by the Office of the Provost and the Office of the Treasurer, and a recommendation will be made at that time either to continue the program or terminate it.

Action taken: Approved Disapproved Other _____

UK Center for Manufacturing

**Pilot Plan
for the Distribution and Use of Professional Income
under the University of Kentucky Center for
Manufacturing, Lean Program**

I. PURPOSE

The purpose of the Center for Manufacturing Lean Program Income Distribution Plan (The Plan) is to provide a pilot plan basis for determining the distribution and use of funds generated through the UK Center for Manufacturing Lean Program activities by a designated set of faculty. The Plan is developed and is to operate under policies established by the University of Kentucky.

II. APPLICABILITY

The Plan is applicable to designated members of the faculty who are responsible for direct teaching and curriculum development of courses to industry in the Lean Manufacturing and related Lean Enterprise areas. These faculty members will be referred to as “*principals*” below. Faculty who are principals are expected to contribute to the support and growth of the Lean programs, as well as support activities of the Center for Manufacturing, the Manufacturing Systems Engineering Program, the College of Engineering, and the University at large.

This pilot plan shall not be effective until approved by the University of Kentucky Board of Trustees. The term of the plan is until June 30, 2006, unless earlier terminated by the Board, and at the end of that period is subject to extension, modification, or termination, based upon the evaluation from the Office of the Provost and the Office of the Treasurer, and subject to the approval of the University of Kentucky Board of Trustees.

III. GOVERNANCE

The Board of Principals will include all principals of The Plan and the Director of the Center for Manufacturing. All principals will have equal voting rights on the Board. The Director of the Center for Manufacturing has voting rights in the case of ties. The Board of Principals will establish and recommend reward distribution policies (see item IV.3 below) and policies for membership of the principals. The recommendations are then forwarded to the *Oversight Committee* for implementation and oversight.

The Oversight Committee of The Plan will consist of the following:

1. The Director of the Center for Manufacturing
2. The Business Manager of the Lean Program
3. The Curriculum Manager of the Lean Program
4. Three members external to the College of Engineering, appointed by the Dean of Engineering
5. The College of Engineering Business Officer.

The Business Manager of the Lean Program and the Curriculum Manager of the Lean Program are appointed by the Director of the Center for Manufacturing from the principals in the plan. The College of Engineering Business Officer serves in a non-voting capacity, unless also appointed by the Dean as an external member.

The Oversight Committee will have the following responsibilities:

- review any recommendations of the Board of Principals on reward distribution policies and membership policies for compliance with University regulations and fairness to the participants;
- implementation of policies recommended by the Board of Principals;
- resolution of issues raised by the Board of Principals regarding distribution policies and membership policies;
- Periodic review of licensing and pricing policies.
- other important issues as they occur.

Decisions of the Oversight Committee regarding distribution policy and membership policy will be made by vote. A quorum for a meeting is five of the six voting members. In cases of disagreement on strategic issues or on major financial issues, then the Oversight Committee will seek council from the Dean of the College of Engineering, whose decision will be final.

The Oversight Committee will keep a written record of all its decisions. The record will be made available to principals, administrators, and others upon request.

IV. GENERAL OPERATIONS

1. **The Primary Account:** An account (The Primary Account) will be established to which income will be deposited, expenses will be paid, and remaining income distributed.
 - i. **Income from Principals:** All income from all professional activities of the principals shall be placed in the Primary Account. This includes income from non-credit courses, workshops, trainings, consultations, retainers, and honoraria, and all other professional income earned by the principals from University of Kentucky affiliated or non-affiliated activities. This excludes patent royalties. It also excludes publication royalties for books which were published prior to January 2004, and in general any books without UK affiliation, without UK branding, and without use in a UK program. Specific cases on exclusions of such publications will be decided by the Oversight Committee.
 - ii. **Base Salary of Principals:** Base salary for the principals will be paid from the Primary Account. This includes fringes on the base salary.
 - iii. **Direct Expenses:** All direct expenses of lean program activity will be paid from the Primary Account. This includes direct operating expenses of travel, marketing, printing/duplicating, communications, workshop venue expenses, program development expenses, conference coordination expenses, etc. It includes the 9-month base salaries of the principals (discussed above). It also includes staff and student time directly attributed to lean program activity.
 - iv. **Indirect Expenses:** Indirect expenses for lean program activity will be deducted from the Primary Account. Indirect expenses include building telephones, office copiers and supplies, accounting and business support, administrative and clerical support, computing support, Center-level marketing, etc. These are expenses that represent a resource or service in the Center that is shared among several Center programs and which in part supports the Lean Program activities. Expenses to be charged as indirects are to be determined by the Director of the Center for Manufacturing.
 - v. **Provost Tax:** Any “Provost Tax” associated with income or expenses of the Lean Program will be paid from the Primary Account. Currently, there is within the University a proposed 2.5% tax on all externally generated income. The calculation of the tax will be subject to whatever policy is in place within the University at the time of the activity.
 - vi. **Dean Tax:** A “Dean Tax” will be paid from the Primary Account. This tax will be calculated as 10% of the funds remaining in the account after direct and indirect expenses. (Note this excludes “reward pools” as defined below.)
 - vii. **Reserve Account Expenses:** The Reserve Account will be established as per section IV.5 below. If the reserve account is expected to fall below its required level, then the amount required to recover the account

to its required level will be considered an expense of the Primary Account.

2. **Overhead Rate:** The University, through the University of Kentucky Research Foundation (UKRF), has established “indirect” rates. These are rates that are negotiated with agencies of the Federal Government. The “Indirects” paid by the Lean Program income will not be less than the “Off-Campus Other Sponsored Activity” indirect rate established by UKRF. “Indirects” will include charges associated with the Provost Tax, the Dean Tax, and the Indirect Expenses as outlined above. In the event that over any fiscal year, the Provost Tax, the Dean Tax, and charged Indirect Expenses do not total the off-campus indirects rate established by UKRF, then the difference will be made available to the Center for general support operations.
3. **The Reward Pool:** Income in the Primary Account less all expenses above will be termed the “*Reward Pool*”.
 - i. **Reward Pool Divisions:** The Reward Pool will be divided among the following categories:
 - *Shared Reward Pool:* A share of the reward pool will be divided evenly among principles according to the percentage of their distribution of effort assigned to the program. No less than 20% of the reward pool will be assigned to the Shared Reward Pool.
 - *Individual Reward Pool:* A share of the reward pool will be divided among the principals according to a measure of their activity in the program. For example, this measure could be defined in terms of revenue producing activity days.
 - *Academic Enrichment Pool:* This pool could be used to pay for academic enrichment purposes according to policies as defined by the Oversight Committee and the Board of Principals, subject to regulations of the University, provided however that such purposes are within the Internal Revenue Service guidelines for ordinary and necessary business expenses. Such uses may include normal professional expenses of faculty, such as travel to professional meetings and subscriptions. Such expenditures may also include fellowships, graduate student stipends, books, research support including both equipment and salaries, faculty recruitment, visiting researcher expenses, and other legitimate academic enrichment for the program. Any expenditure of funds from the Academic Enrichment Pool shall require written authorization by the Director of the Center for Manufacturing. The unexpended balance, if any, in the Academic Enrichment Pool at the end of the fiscal year shall be carried forward to the following year. The Academic Enrichment Pool is to be established as an “unrestricted” account within the University, and all expenses must follow university policy on such accounts. No less than 10% of the Reward Pool will be assigned to the Academic Enrichment Pool.

Payments to principals from the Shared Reward Pool or the Individual Reward Pool will be considered as a “salary supplement” within the University policies.

- ii. **Fringe Benefits of Reward Pool:** Any distributions of the reward pool that are directly distributed to principals as a form of pay will first have all applicable fringes deducted. This includes any applicable employer taxes. Fringes that are paid on these distributions will follow the University policies on “salary supplements”. (For example, although the University withholds and pays FICA on salary supplements, salary supplements are not part of regular pay and thus not considered for calculation of other benefits or contributions such as insurance, retirement, etc.)
- iii. **The Reward Pool Distribution:** The distribution of the Reward Pool among the different sub-pools, and the distribution of the sub-pools among the principals, will be defined by written policy established by the Oversight Committee under guidelines established by the Board of Principals. These policies should recognize expectations of activities in support of the Center, the College of Engineering, and the University. These policies must be defined within the first 30 days of each fiscal year for the distribution within the fiscal year.
- iv. **Reward Pool Calculation:**
 1. **Annual Anticipated Remuneration:** Before the beginning of each fiscal year, the Oversight Committee will consult with each principal and establish a target of expected activity during the year. Based on the targeted activity of all principals and the estimates of all expenses, an estimate is made for the Reward Pool for the year. Based on those estimates, each principal will be told an “*Annual Anticipated Remuneration*” (AAR) consisting of that principal’s base salary and expected distributions from the reward pool. The AAR of each principal will be reevaluated regularly during the fiscal year, as per item 3 below.
 2. **Monthly Payments:** The salary payment received by a principal each month will be at least $1/12^{\text{th}}$ of the principal’s 9 month base salary (as per section 1.ii above). If the AAR of the principal is greater than the base, then the payment will be calculated as follows: The AAR less all payments (salary and reward pool and fringes) dispersed to the principal so far in the fiscal year, divided by the remaining months of the fiscal year including the current month. However, any AAR payments above the base salary can only be based upon prior revenues and those revenues scheduled within 90 days.
 3. **Reevaluation:** Expense estimates and revenue estimates from the Lean Program activities (both expected and completed) and the AARs of principals will be evaluated at least once each quarter of the fiscal year using a reevaluation process approved

by the Oversight Committee and by the Director of the Center for Manufacturing.

4. At the end of the fiscal year, any positive difference (underpayment) between the AAR evaluated for the FY just completed and the amounts distributed to a principal can be paid (with deduction of fringes) to the principal. Any negative difference (overpayment), will be deducted from the principal's next year's AAR.

v. **Reward Pool Examples:** (These are for illustration purposes only. Distribution plan details may be different).

Example 1: At the beginning of the fiscal year, it is estimated that there will be \$400,000 in the reward pool. Suppose for this example that 50% of this will be distributed in the Shared Pool, 40% in the Individual Pool, and 10% in the Academic Enrichment pool.

- There are 10 principals in the plan, and each is completely supported by the plan. Thus, each principal is expected to receive $(\$400,000 * 50\%) / 10 = \$20,000$ from the Shared Reward Pool, less applicable taxes and fringes.
- Suppose that the distribution policy for the individual reward pool were based on total share of "days taught", for some appropriate definition of "days taught". Of the 10 principals, six of them are expected to each teach 50 days each, and the remaining four are expected to teach 25 days each. Since there are expected to be a total of 400 days taught, the six principals who taught more days are expected to receive $(\$400,000 * 40\%) * (50/400) = \$20,000$ each from the Individual Reward Pool, and each of the remaining principals receive $(\$400,000 * 40\%) * (25/400) = \$10,000$ each (less applicable taxes and fringes).

Example 2: Principal X has a base salary of \$75,000 and is one of the principals who is expecting to teach 50 days. Under the expected distribution above, he has an Annual Anticipated Remuneration of $\$75,000 + 20,000 + 20,000 = \$115,000$, which is \$9583 per month in disbursements, including applicable fringes.

Example 3: In the fourth month of the fiscal year, the expenses of the program and the targets of the principals are reevaluated. There is no change, so the monthly payment is unchanged.

Example 4: In the fourth month of the fiscal year, the expenses of the program and targets of the principals are reevaluated. It is estimated that Principal X will teach 25 days above the original target of 50, boosting the expected total in the Reward Pool to \$450,000. Supposing the total days of the group is at 425, then the Shared Reward Pool annual expected distribution will now be \$22500, and the Individual Reward Pool annual expected distribution will now be \$31765, for a total new AAR of \$129265. The new monthly disbursement (including fringes) will be

calculated as $(\$129264 - (3 * \$9583)) / (9 \text{ months}) = \$11168/\text{month}$ for the remaining months of the fiscal year, at least until the next reevaluation.

Example 5: The same as in the preceding example, except that Principal X will teach 25 days less than the original target of 50, with the expected amount in the Reward Pool falling to \$350,000. If the total days of the group is now 375, then the new AAR is \$101833, for a new monthly disbursement (including fringes) of \$8120 per month for the remaining months of the fiscal year, at least until reevaluation.

Example 6: At the end of the fiscal year, Principal X had activity corresponding to an AAR of \$99,000, but actually received disbursements (including fringe) of \$101833. The deficit of \$2833 will be subtracted from the principal's next year's AAR.

4. Other Income:

- i. Income from faculty and staff of the University who are fully supported from the Lean Program will have revenue from their activities handled as described in section IV.1 above. This includes principals and non-principals fully supported under the Lean Program.
- ii. Income in the Lean Program from activities of:
 - A faculty member of UK who is not a principal, or
 - A UK staff member of UK who is not fully supported by the Lean Program,
 - Individuals or groups from outside the University, such as a partner organization, consultant, or temporary instructor.

In the case of income from such sources, the income will have applicable license fees, direct expenses, indirect expenses, and appropriate University and College taxes deducted from it, as well as salary reimbursement and associated fringe in the case of University (non-principal) employees. Salary reimbursement for non-principals, when appropriate, can be redirected to other uses of the non-principal, including travel, student support, or summer salary. The income that is remaining will be split evenly between the Academic Enrichment Pool, the Share Pool, and the Center for Manufacturing. The license fee for externally licensed programs that have been developed by the principals shall return 40% of the license fee, after deducting for any direct expenses, to the creators for distribution to these principals based on their predetermined level of contribution.

- iii. It is expected that any University of Kentucky faculty or staff who is not a principal but with associated salary savings significantly above their annual 12 month salary will be allowed to become a principal, within the membership guidelines established in section V below.
- iv. In the case of a course or activity with primary development by a particular faculty or staff, that faculty or staff will have a right of first refusal, within reason, to present that course or activity. Upon refusal, other qualified faculty or staff can be given or assigned that presentation or activity.

5. **The Reserve Account:**

- i. **Purpose of the Reserve Account:** The reserve account is used to recognize that over short periods, the expenses and income of the Primary Account may not keep a positive balance. The Reserve Account is used to ensure that any reasonable deficit in the Primary Account during normal operation will be covered, for the benefit of the principals, the Center, and the University. In no event will the University or college make any reward payments from general funds, and if quarterly operations reveals a need for increased retention, the Reserve Account may be increased.
- ii. **Required Reserve Level:** At the beginning of each fiscal year, the Reserve Account *required reserve level* shall be defined at 2/12ths of the expected Annual Revenue of the Primary Account. If the Reserve Account does not already contain this required reserve level, then the difference will be established as an expense of the Primary Account, as discussed in section 1.vii above. If the Reserve Account contains more than the required amount, then upon approval of the Oversight Committee, the excess funds from the Reserve Account can be returned to the Primary Account.

V. Membership

All principals of the plan will have faculty status. They will report to the Director of the Center for Manufacturing. Their appointment will be subject to the policies of the University, the College of Engineering, and the Center regarding faculty appointments. Other policies for membership of the plan will be established by the Board of Principals. A principal can be any faculty level, including regular faculty and lecturers. The University of Kentucky is an equal opportunity employer, and membership as a principal requires objective criteria that does not discriminate with regard to sex, sexual orientation, race, ethnic origin, national origin, color, creed, religion, age, or political belief, Vietnam-era veteran status, disabled veteran status, or physical or mental disability, or on the basis of application for or service in the Uniformed Services.

All principals are employees of the Center for Manufacturing in the College of Engineering at the University of Kentucky. All members are expected to contribute to the goals and operation and growth of the Center for Manufacturing, the College of Engineering, and the University. All principals will be subject to regular performance review and contract renewals, in accordance with standard university procedure. All principals will be subject to the policies of the Center, the College, and the University.

Before a faculty member can become a principal of this plan and participate in the reward pool, he or she must sign an agreement indicating that he or she has received a copy of the governing document, will abide by the governing document, and has received notice of the University's position on ownership of material created by University faculty and staff for non-credit lean manufacturing activities or license. A copy of the principal agreement is given in Appendix A.

Appendix A

Agreement for Membership as a Principal for Income Distribution Plan of the Center for Manufacturing Lean Program.

Principal: _____

By signing below, I am indicating my agreement to participate as a principal in the Income Distribution Plan (The Plan) of the Center for Manufacturing Lean Program, as set forth in the attached Governing Document. This agreement includes the following:

1. As per the Governing Document, I agree that all income from all professional activities will be subject to The Plan, including income from non-credit courses, workshops, trainings, consultations, retainers, honoraria, and all other professional income earned through University of Kentucky affiliated or non-affiliated activities, but excluding some income as indicated in the Governing Document. Among those items with excluded income are books published prior to January 2004, which I specifically list below:

[Title], [Author], [Publisher], [Date]

2. I agree that as an employee of the University of Kentucky, I will constructively contribute to the goals and growth and operation of the UK Center for Manufacturing, the College of Engineering, and the University. Furthermore, I understand that I am subject to the policies and procedures of the UK Center for Manufacturing, the College of Engineering, and the University.

Signature: _____

Date: _____

Received:

- Governing Document dated Sept. 20, 2004
- March 25 2004 memorandum of legal counsel on UK intellectual property ownership position.

Appendix B

Example Reward Distribution Policy

This is an example reward distribution policy. The actual distribution policy is subject to change as per the procedures described in the Governing Document.

The Reward Pool will be divided as follows:

- 30% into Shared Reward Pool
- 60% into Individual Reward Pool
- 10% into Academic Enrichment Pool

The Shared Reward Pool will be divided evenly among all principals.

The Individual Reward Pool will be distributed according to “units” of activity. A unit of activity can be assigned to a principal according to the following:

- Each day of direct revenue activity is assigned one unit. This would include days for teaching a course, a workshop, or other activity. This does not include (under the current policy) activity for development or preparation.
- For credit courses taught for the Manufacturing Systems Engineering program, each credit is worth two units. Thus, for a three credit hour course with full responsibility by a principal, six units will be assigned.
- For Business Manager of the group, administrative responsibilities are recognized by 6 units.
- For supervising research grants and thesis students supported on research grants, each \$25K of direct spending will add one unit.
- For developing a new course, the effort will be recognized by a number of days commensurate with the effort and value of the new addition.

Appendix C

Example Membership Policy

This is an example membership policy. The actual membership policy is subject to change as per the procedures described in the Governing Document.

A faculty member can become a principal of the plan if they actively teach and contribute to the Lean Manufacturing Program of the Center for Manufacturing, and if the revenue that they generate is expected to exceed 130% of their base salary.