Board of Trustees
Finance Committee Meeting

Thursday, February 18, 2016
4:00 pm – 6:00 pm (or until business concludes)
DeBoer Room, Hannon Library

MINUTES

Call to Order and Preliminary Business

Chair Nicholson called the meeting to order at 4:01 pm.

The following committee members were present: Paul Nicholson, Lyn Hennion, April Sevcik, Dennis Slattery and Steve Vincent. Trustee Les AuCoin participated by videoconference. The following member was not present: Jeremy Nootenboom. Trustees Bill Thorndike and Roy Saigo (ex officio) were also present.

Other meeting guests included: Craig Morris, Vice President for Finance and Administration; Dr. Susan Walsh, Provost and Vice President for Academic and Student Affairs; Jason Catz, General Counsel; Mark Denney, Associate Vice President for Budget and Planning; Steve Larvick, Director of Business Services; Drew Gilliland, Director of Facilities Management and Planning; Ryan Brown, Head of Community and Media Relations; Gordon Carrier, Computing Coordinator; Don Hill, Classroom and Media Services Manager; Shane Hunter, Senior Financial Management Analyst; Janet Fratella, Vice President for Development; Sabrina Prud'homme, Board Secretary; Kathy Park, Executive Assistant; David Coburn, OSA; and Olena Black, League of Women Voters.

Colin Sanders-Estrada from Sightlines was present to discuss the prioritization of capital projects. Penny Burgess, Director of Treasury Operations from the University Shared Services Enterprise (USSE), joined by teleconference to present the current investment report.

The agenda was amended to exclude the bond funding item for the Science Building. The full Board of Trustees previously handled the item in a special meeting, thereby omitting the need for committee action.

Trustee AuCoin moved to approve the January 21, 2016 meeting minutes and, with the motion, asked if additional thought had been given to visiting the Science Building. Chair Nicholson indicated that it is something he wants the committee to do. Trustee Vincent seconded the motion and although he recused himself from the biomass/cogeneration discussion reflected in the minutes, he requested a correction on page 5, noting the backup to the natural gas boiler is oil. No other changes were noted. The motion passed unanimously.

Public Comment

There was no public comment.

Vice President's Report
Craig Morris presented the dashboard and offered to answer any questions; none were asked. Chair Nicholson added that all elements were on target or better.

Mr. Morris informed the committee that the HECC presented "marching orders" for the seven universities' budget submission. That submission is due April 1 and the capital construction request is due May 1. The vice presidents of finance and administration met to discuss how to proceed and, along with support staff, to develop numbers for the current service level (CSL). Mr. Morris then described the budget submission process.

On a flip chart, he illustrated the state's biennium allocations for higher education: Public University Support Fund (PUSF) at $665 million; State Programs at $38.5 million; Statewide Programs that are housed at Oregon State University at $118.5 million; Sports Lottery at $8.2 million; and Debt Service at $151.6 million – for a total of $981.8 million.

The CSL issue focuses almost entirely on the PUSF, which is where the dollars allocated to SOU through the HECC model come from. Mr. Morris said the budget process for SOU is now like a non-state agency that receives state allocations and SOU is supposed to receive an inflationary increase (e.g., 3 percent) of the PUSF. The seven universities identified significant costs that will be incurred beyond the 3 percent, the two biggest being 1) the increases in PERS retirement costs and health insurance, and 2) the cost of union agreements and the potential increase in minimum wage. Adding all of those, except minimum wage, raises the desired CSL to 7.8 percent and 7.9 including minimum wage. The vice presidents have talked with the HECC and legislators, the majority of whom agree with this CSL calculation. The HECC requires three scenarios be addressed in the budget submission: 1) if PUSF stays at $665 million; 2) if it increases by 7.8 percent plus another 10 percent; and 3) if the CSL is 7.8 percent but PUSF decreases 10 percent. The seven universities will submit a consolidated report addressing the three scenarios, indicating impact by institution.

The universities also will prepare a portfolio of 11 scenarios to analyze different funding possibilities. Chair Nicholson clarified that the scenarios are based on the assumption of no other cost changes, which may not be the case. The narratives are not what the boards would necessarily do, but rather what the institutions see as logical alternatives. The vice presidents will present the report to the presidents at their next council meeting then present to the boards and finance committees. Mr. Morris expects to have a draft report for review and if necessary, revision, at the next committee meeting.

Trustee Hennion asked where the money would come from to fund the universities if the state does not provide them. Mr. Morris said that is the ultimate question adding that scenario-planning is common and lets the legislature know what would happen if the budgets are cut or increased. Responding to her question about competition for funding among the larger and smaller institutions, Mr. Morris said the focus at this point is on changes to the $665 million, as the funding model dictates how that money will be distributed. A 10 percent decrease in the PUSF would result in a decrease of more than 10 percent for SOU because the larger universities have better numbers in the areas the funding model emphasizes.

In response to Trustee AuCoin's question about the legislature's total budget, Mr. Morris indicated the projection for 2017-'19 is for a $165 million decrease, which, in a $13-14 billion budget, is not a significant amount. Though, historically, the first, deepest cuts are in higher education.

Biomass/Cogeneration Project Prioritization Options (Action)
Chair Nicholson introduced the topic, saying a few trustees expressed their passionate views on the subject at previous meetings, as did members of the public. There was not enough support for the biomass/cogeneration option but SOU needed to move forward with something. Trustee Vincent recused himself from participating in the conversation.

Trustee Sevcik moved that SOU select natural gas boilers as the campus heating option to be included in the university's request to the HECC for 2017-2019 capital funding at an estimated cost of $2.5 million. Trustee Slattery seconded the motion and added that future nomenclature for this project should become "boiler replacement." Save for Trustee Vincent's abstention, the motion passed unanimously.

Trustee AuCoin recommended that SOU administration inform community members that biomass/cogeneration is no longer an option under consideration. Ryan Brown duly noted the recommendation.

2017-19 Prioritization of Capital Projects
Mr. Morris introduced Colin Sanders-Estrada of Sightlines to discuss and present the campus profile, backlog of deferred maintenance, future capital renewal and recommendations.

Mr. Sanders-Estrada discussed nationwide trends of building construction in higher education, with an overlay of SOU's, noting the trends are similar. There was a lot of construction at SOU in the 1960s and 1970s, resulting in a big portion of campus approaching the critical 50-year age threshold. At that point buildings require significant renewal and investment.

Looking at the backlog by subsystem or building component shows that HVAC systems are the most expensive need category at SOU, which is typical. Building renewal and electrical round out the top three. Trustee Vincent asked if there is a trend to lease HVAC equipment, thus reducing capital outlay. Mr. Sanders-Estrada said he has not seen that happening.

Chair Nicholson noted SOU has a total of $50 million in subsystem backlogs, which is about 10 percent of the overall replacement value of the campus, and asked if that was typical. Mr. Sanders-Estrada indicated SOU is better than the norm.

Mr. Sanders-Estrada addressed where SOU has the highest amount of backlog, with Britt Hall leading this. Mr. Morris added that the legislature has allocated $4.7 million to renovate Britt Hall and SOU will get those funds a year from this spring.

In comparing the facilities condition index by building (the proportion of the backlog to the total campus replacement value), the Student Health and Wellness Center is at the top. Mr. Sanders-Estrada added that these comparisons do not consider programmatic value; these are two components to balance and his analysis gives priority to the deferred maintenance.

Mr. Sanders-Estrada discussed the most costly backlog projects in state-supported and auxiliary spaces. Mr. Morris said SOU receives about $2-3 million in capital repairs and renewal funds from the state each biennium that can only be used on state-supported spaces. The auxiliaries have to pay for the repair and maintenance on their own spaces. Although McNeal is an auxiliary space, the legislature provided funding because the building was falling down and posed a liability risk.

Cascade involves five of the most costly backlog projects. Following further discussion, the consensus was that demolition of Cascade may be the best option. It was later noted that Cascade comprises 74 percent of the renewal amount in 2019. Mr. Morris said it would cost $2 million to tear down Cascade and $65-70 million to replace it.

The total backlog in 2015 is just over $50 million. Over the next 10 years, if SOU makes no investment as capital projects become due, the backlog in 2025 would be $130 million. The buildings with the highest backlog and capital renewal include Cascade, Susanne Homes Hall, McNeal and Britt Hall. A plan already exists for the last two.

Due to the age distribution of the SOU campus and the biennial nature of state funding, Sitelines recommended a systematic building renovation schedule prioritized by impact on backlog and future capital renewal and that factors in programmatic initiatives and SOU's mission.

Trustee Vincent asked if SOU has an electric grid crisis similar to that at OSU. Mr. Gilliland indicated SOU does not and is completely supported by the City of Ashland.

Noting it has been three years since SOU's last study, Chair Nicholson asked when the next study should be done. Mr. Morris and Mr. Gilliland will make a recommendation, but both thought every other year might be appropriate.

Investment Report – FY 2016 Second Quarter

Penny Burgess provided the investment report for the second quarter of FY16, which includes the university's operating assets invested in the Public University Fund (PUF) and the university's endowment assets managed by the Oregon State Treasury.

Directing the committee to the FY16 Q2 market commentary, which provides a general discussion on the economy and market performance during the quarter, Ms. Burgess reviewed market highlights underpinning investment performance.

She also reviewed investment returns and the PUF investments allocations in Oregon's short-, intermediate- and PUF long-term investment pools. The PUF investment return for the quarter was -0.2 percent and a positive .3 percent year-to-date. The total market value of SOU's operating cash and investment deposits on December 31 was $25.2 million, equivalent to 5 percent of the total PUF balance of $502.4 million. The short-term fund outperformed its benchmark for the quarter and year-to-date by 10 and 30 basis points respectively, and outperformed the 3 year benchmark return by 40 basis points. The intermediate-term pool outperformed its benchmark for the quarter by 10 basis points and underperformed its benchmark by 30 basis points year-to-date. The long-term pool outperformed its benchmark for the quarter by 10 basis points but lagged the benchmark by 110 basis points year-to-date. The year-to-date underperformance of the intermediateand long-term pools was attributable to the average portfolio duration variance with each pool's respective benchmark in addition to price volatility in the corporate bond segment of the portfolios.

The PUF's investment manager is addressing the average portfolio duration variance by purchasing securities with longer maturities in an effort to reduce the benchmark variances. During the quarter, the PUF administrator distributed over $110,000 of earnings to SOU.

Next, Ms. Burgess discussed the endowment assets which were invested in a separately managed account by the Oregon State Treasury as of December 31. The total return for the quarter was a positive 3.4 percent and a negative 2.8 percent year-to-date, outperforming the recommended policy benchmark by 10 basis points for the quarter and 50 basis points year-to-date. The total market value of SOU's endowment investments on December 31 was just under $2.1 million.

Ms. Burgess remarked that she and Mr. Morris recently discussed the existing SOU Endowment Fund Investment Policy, which was inherited from OUS. The OUS policy was crafted for a $70-80 million endowment pool and featured an investment strategy which allocated dollars to multiple asset classes, including alternative investments. Given the SOU endowment fund size of $2 million, the State Treasury recommended a simplified asset allocation of 70 percent to global equities, 30 percent to fixed income and has been managing the portfolio with this strategy since late June 2015. Due to the difference of investment strategies, she and Mr. Morris feel it would be prudent to update SOU's existing investment policy in accordance with the current strategy and benchmark. Obtaining approval from Chair Nicholson, Ms. Burgess will bring a draft endowment fund policy to the committee for review during her next investment update.

Enrollment Update
Provost Walsh discussed enrollment, noting that the funnel was a little down, which is common at this time of year, as ebbs and flows in the numbers are expected. However, enrollment is up 3.8 percent from winter term last year.

The Provost's Office is gathering numbers from the recent preview weekends. The February event had 413 attendees, which was a 25.9 percent increase, and historically, was the largest February event. She also noted that admissions counselors are at local high schools holding application workshops; the admissions office has started a phone campaign to complete applications; and admissions personnel have visited the Klamath and Rogue community colleges several times to recruit students.

Trustee Vincent passed along a compliment to the admissions office from the KCC board chair, Jeff Ball. Chair Ball complimented SOU on the process for KCC students to transfer to SOU, even in comparison to OIT. Dr. Walsh commented that SOU is now seeing the results of years of hard work arranging the partnerships with KCC, RCC and the articulation agreements.

Year-end Projections / Pro-forma
Delivering the year-end projections, Steve Larvick discussed various highlights from the budget forecast slides he presented, most of which are in line with earlier projections. The

athletic post-season travel activities substantially impacted the figures.

To demonstrate the impact funding changes have on the operating revenues and fund balance, Mr. Morris changed various forecast figures on the pro forma to offer the committee various scenarios. Responding to Trustee Hennion's inquiry on determining the right fund balance, Mr. Morris said SOU is beating the retrenchment plan target of 10 percent. What pushed SOU into its last retrenchment was spending the fund balance down, then spending it down again. Responding to Trustee Vincent's question about a fund balance benchmark, Mr. Morris said the OUS standard was no lower than 5 percent and no higher than 15 percent.

Trustee Slattery clarified that an increase in tuition revenue could be achieved through a combination of increased enrollment and raised tuition. Chair Nicholson pointed out the forecast also makes the assumption that staffing levels are not changed.

Responding to Trustee Hennion's question about raising tuition, Mr. Morris said the HECC would have to approve any increase over 5 percent. He added that the retrenchment plan and pro forma assume a 3 percent increase.

Pointing out that state allocation is one-third of SOU's revenue, Trustee Vincent asked if there was a scenario to build the fund balance in case of a total loss of state allocation. Mr. Morris said University of Oregon has done that but its state allocation is only 11 percent of its total revenue.

Budget - Enrollment Projections

Mark Denney described the process used for projecting FY17 enrollment. SOU has FY16 known data for fall. To the known data for winter, he added advanced southern credit statistics based on last year's winter term. Then, using FY15 figures and a conservative 1.1 percent down, he added the projected balance of FY16 for spring and summer to obtain the enrollment for FY16. He then calculated the retrenchment target of .2 percent growth to get the projected enrollment for FY17, adjusting each tuition category by its historical trend but making sure each nets out to the .2 percent growth.

Mr. Denney discussed the projections for each tuition category, highlighting the largest categories: the resident undergraduate 1.31 percent decline, the WUE undergraduate 4.43 percent growth and the online undergraduate .11 percent growth. This does not take into account efforts to recruit more resident undergraduate students. Even so, SOU has done better this year recruiting those students than what a historical look would have projected.

Answering Chair Nicholson's query about the dark side to being too conservative, Mr. Denney said that if SOU says no to budget opportunities because it believes the revenue will not be there, the opportunities may pass. Mr. Morris added that one way around that is to add certain items if enrollment increases to a specified point.

Dr. Walsh chairs the Tuition Advisory Council (TAC), comprised of students, faculty and administrators. TAC recommended a 3 percent increase for all undergraduate tuition (SOU is second lowest for resident and third lowest for nonresident) but no increase for graduate tuition (SOU is third highest for resident and third lowest for nonresident). Mr. Denney will present this recommendation to campus groups over the next few weeks, then will provide feedback and a recommendation to President Saigo and his cabinet. Next month, President Saigo will present to the committee a recommendation on tuition rates and mandatory fees. The board will make a final decision in a future meeting.

Addressing Chair Nicholson's question about whether TAC did tuition comparisons with California schools, Mr. Denney said TAC looked at Chico State, Sacramento State, UC Davis and Humboldt. SOU's resident rate was significantly lower than theirs. However, comparing their semester-based academic year to SOU's term-based year, the rates were pretty close. Mr. Denney said it was difficult to compare because the California schools use a flat rate for 0-6 credits and for 7 or more credits. He used costs for 15 credits but doubted students take that many credits per term or semester.

At the March meeting, Mr. Denney will give a presentation on mandatory fees. Mandatory fees are published in the fee book and are used to compare SOU to other universities. Adding all the mandatory fees together, SOU is the second lowest in the state.

The TAC is considering a $13 increase in the student incidental fee based on the referendum to support Schneider Children's Center and an additional 1-3 percent increase; the student group is debating whether to create a reserve to support athletic post-season travel. TAC is also considering increasing the rec center fee to $75; increasing the student health fee 3 percent; increasing the residence and dining fee 4 percent; and making no change to the building fee because that is set by the legislature. The TAC is also discussing raising the single room rate to get demand and availability more in line.

Mr. Denney addressed limits on tuition and fee increases. The HECC or legislature must give prior approval for any increase in total tuition and mandatory fees by more than 5 percent. For the 2016-2017 academic year, justification must be provided to the HECC if resident undergraduate or mandatory fees increase by more than 3 percent individually.

Mr. Denney then analyzed 2016-17 resident undergraduate costs for 15 credits per term. Responding to Trustee Slattery's question on financial aid, Mr. Morris said a student's budget increases when the university increases tuition and fees but only the federal government can increase the amount a student can borrow over an academic career.

Adjournment
Chair Nicholson adjourned the meeting at 6:07 pm.

Date: March 17, 2016

Respectfully submitted by,

Sabrina Prud'homme
University Board Secretary