MINUTES

BOARD OF REGENTS’ COMMITTEE ON BUDGET AND FINANCE MEETING

May 12, 2015

I. CALL TO ORDER

Committee Chair Jan Sullivan, called the meeting to order at 1:00 p.m. on Tuesday, May 12, 2015, at the University of Hawai‘i Campus Center Ballroom, 2465 Campus Road, Honolulu, Hawai‘i 96822.

Committee members in attendance: Committee Chair Jan Sullivan; Regent Wayne Higaki, Regent Coralie Matayoshi, Regent Lee Putnam.

Committee members excused: Committee Vice Chair Barry Mizuno, Regent David Iha.

Others in attendance: Regents’ Chair Randy Moore, Regents’ Vice Chair Eugene Bal, Regent Acoba, Regent Chuck Gee, Regent Ben Kudo, Regent Helen Nielsen, Regent Jeff Portnoy, Regent Michelle Tagorda, Regent Stanford Yuen (ex officio committee members); President David Lassner; Vice President for Academic Affairs Risa Dickson; Vice President for Administration Jan Gouveia; Vice President for Legal Affairs and University General Counsel Darolyn H. Lendio; Vice President for Community Colleges John Morton; Vice President for Research Vassilis Syromos; Vice President for Information Technology/CIO Garrett Yoshimi; Vice President for Budget & Finance/Chief Financial Officer Kalbert Young; UH Mānoa (UHM) Interim Chancellor Robert Bley-Vroman; UH Hilo (UHH) Chancellor Don Straney; Hawai‘i Community College (HawCC) Chancellor Noreen Yamane; Honolulu Community College (HonCC) Chancellor Erika Lacro; Executive Administrator and Secretary of the Board of Regents Cynthia Quinn; and others as noted.


Regent Matayoshi moved and Regent Putnam seconded the motion to approve the minutes of the April 1, 2015 meeting, as amended, and the minutes of the August 18, 2014 joint meeting, and the minutes were which was unanimously approved.

III. PUBLIC COMMENT PERIOD

Executive Administrator and Secretary of the Board Cynthia Quinn announced that the Board Office received no written testimony, and no individuals had signed up to testify.

IV. AGENDA ITEMS

VP Young gave a presentation (Attachment 1) that covered the quarterly financial report of the UH System an overview and analysis of the ending balance trajectory, revenues, expenditures and cash balances.

The committee had comments and concerns on: the status of the budget to actual reporting; if VP Young would recommend the university do budgeting on a semester basis; recognized this was new financial reporting process and change is difficult to implement in large complex organizations like UH and resistance is expected but hoped the internal sectors were cooperating and requested a report to the board of the level of resistance to help the board understand and address the challenges to move forward; carry forward cash as stated is be misleading; referred to the difficulty in forecasting ending balances due to deferred revenue and timing, and asked what percentage of that revenue would prove uncollectable; the red flag areas (e.g., personnel costs) that the board should be taking note of; and if the board could be provided accrual statements to reflect tuition properly.

VP Young responded that the goal is to provide a budget to actual report and recognize that this is only the third true quarterly report the regents have seen. Each report evolves closer to a more conventional budget to actual presentation. The goal is to construct and execute the Fiscal Year 2016 budget closer to something they can measure against actual numbers. It is challenging because budgets are not constructed quarterly, and has to be formulated at the administrative level. Budgeting on a semester basis might be more appropriate in terms of reporting, however, if the reports are utilized to make mid-year fiscal adjustments, a semester basis would not work where revenues are collected are barely semi-annual at that point. Committee Chair Sullivan suggested it would help the committee if VP Young would evaluate where they are at and how they can get to something meaningful in terms of FY16.

President Lassner indicated they had struggled with this format, and have budget to actual on an annual basis for the first time. Comparing percentages of projected to previous year was the best proxy because of the unevenness of revenue and expenditures, and the nature of the way the university collects money. Neither report is entirely satisfactory, but together these reports help track where the university is against the current year's projections compared to the previous year. Moving forward they will have more information, and next year they will have this year and the previous year in KFS to do comparisons.

VP Young could not predict how much uncollectable revenue to expect each year, but expected it to be low in tuition because of punitive recourses such as registration holds for late payments. The annual financial statements for the university show a fairly large accumulated balance of uncollectible debt or receivables, some of which is embedded in the revenue collection (e.g., 2% to 3%). It is not a significant amount on any particular year; however, it is never written off and continues to be carried as a balance on the financial statements. Regarding the areas of funding, they used the quarterly financial reports to make mid fiscal year adjustments that are managed at the campus level. Everyone is aware that certain units (e.g., UHM Athletics, Cancer Center) have shortages, but when the reports are aggregated up to campus level, the programs
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Running shortfalls may not be obvious, and these quarterly reports would not provide that level of granularity.

VP Young noted that accrual statements were a target objective, however, cash balances of the mid-year quarterly reports, do not tie into expenditure or revenue balances (e.g., one section of the report is purely cash basis and the other section does not account for accrual). It is a huge accounting challenge to get a consistent report across these three areas.

At this time, Committee Chair Sullivan recognized and welcomed new Regent Wayne Higaki of Hawai‘i County.

B. For Information: UH Mānoa Finances Briefing

Committee Chair Sullivan noted the board had asked for this deep dive topic last year, and indicated it was unacceptable to receive the materials late yesterday afternoon. There was ample notice of this briefing and an unreasonable burden upon the board to be expected to review the material with so little time, and makes it difficult for there to be good, substantive discussions. Chancellor Bley-Vroman apologized for the delay, and added that this is a new experience for them and hopes it will show the significant progress UHM made this year over the past year.

Chancellor Bley-Vroman indicated the two main goals of the briefing today were to give a high level overview of the current financial status of UHM and the plans over the next few years, and explain the complexity of the fund structure. There were three parts to the presentation: (1) UHM budget plan; (2) UHM financials; and (3) the Research Training & Revolving Fund (RTRF).

UHM Budget Plan

This portion of the presentation included an overview of fund sources, including funds used for the operations of the central core functions of UHM operations and support campus mission, and other sources of funding that were beyond the scope of today’s presentation. Also included was an overview of all UHM operating funds and fund balances, and how expenditures, revenues and cash balances have differed over the past three years (details in Appendix 1). The general and tuition fund allocation and revenue has been relatively stable, but expenditures have exceeded the amount of revenue collected and UHM has been using prior year carry forward to accommodate those expenditures. The cash balances exclude deferred income (do not include amount collected this year for next year’s expenses). The cash balances have been falling over the past few years. General funds decreased significantly in 2009, and continued to decrease over time, but stabilized in Fiscal Years 2013 and 2014, with the increased tuition revenue making up part of the gap. In terms of the tuition and fee cash balance, if UHM keeps the existing tuition schedule, things will level off and start to reach a reasonable reserve area by 2017. The 7% increase would also allow UHM to undertake other important initiatives (e.g., returning additional tuition to units with the largest number of students, recruitment, advising) and afford UHM the opportunity to do selective rebuilding. If the tuition increase was 0%, the reserves would have a negative balance by
2017. Even though not shown on the slides, a 5% tuition increase would slow the recovery rate and there would be just under 5% reserves by Fiscal Year 2017. Budget tightening has lessened the decline in the past couple of years. At one time the reserves built to over 16% and a concerted effort was made to spend down reserves. As a result the Legislature reduced funding, so the board policy on reserves helps provide a rationale to the Legislature for keeping a reasonable reserve. He indicated that their own analysis suggests 7% to 10% reserves are sufficient for UHM, which aligns with the community colleges. President Lassner noted the board policy of the 5% minimum reserve was a requirement of accreditation for the community colleges, and 16% was based on having enough to cover two month of operations as best practice.

VC Cutshaw explained that Fiscal Year 2010 was the big cut in general fund appropriations but the reserves continued to go up because UHM was in the middle of a significant tuition hike and hiring freeze, and the recession led to an increase in enrollment. VC Taylor said UHM was directed by the Legislature to spend down to 15%, which they reached in Fiscal Year 2013. VC Cutshaw noted that the differences between general funds and tuition over time and the tuition and fee cash balances differ because one column showed regular tuition and did not include outreach and summer session tuition that go back to the units. Cash balances are by fund where outreach and summer session tuition is included. It was done this way to see how regular tuition was affected. Some regents commented that the board needed to look at the whole picture and the way it was done was confusing and did not give regents the entire picture.

In terms of tuition level and affordability using university net price (gross price minus financial aid) as a percent of median income for research universities across all 50 states, UHM falls on the lower more affordable range, and even with a tuition increase UHM will still be well below average, even if the other universities did not increase their tuition. In response to an inquiry on what the gross tuition was relative to the median income of other states, VC Dasenbrock explained that UHM had the lowest level of state financial aid in the nation and no change is expected, but gross tuition data is not available regarding other states.

The committee asked what the tuition increase might mean in terms of UHM’s ability to compete for nonresident, out of state students. Chancellor Bley-Vroman responded that UHM’s out of state tuition remains very competitive, and in many states it can be better to attend UHM as a nonresident student than pay in-state tuition. VC Dasenbrock added that this year at UHM there was a perceptible increase in international undergraduate students. UHM will intentionally focus on nonresident markets in the years to come. The committee asked what percentage of revenue was derived from out of state versus in-state tuition. VC Dasenbrock said 28% of students are non-residents. Calculations are needed to exclude student athletes who receive tuition waivers along with others who are eligible for waivers, and provide that information to the committee.

Path Forward: Financial Management

VC Dasenbrock provided an overview of UHM Fiscal Year 2015 stabilization efforts; examples of cost deferrals & efficiencies in personnel, academics, research, and facilities renovations & improvements; Fiscal Year 2016 responsibility & accountability efforts,
The committee asked how many units at UHM went into deficit and required a get well plan. VC Dasenbrock explained that there were six or seven units, Engineering and School of Pacific & Asian Studies (SPAS) were on the lower end at less than $100,000, with the more serious ongoing issues at Natural Sciences and Shidler, both are dealing with long term challenges. There were some others that had gone into deficit, but he believed that every other unit has a plan to fly level next year (to spend no more than allocated). The ones with accumulated deficits include Law, Nursing, Engineering, School of Pacific and Asian Studies, and Languages, Linguistics & Literature (LLL). The plan is to have quarterly budget reviews after commencement, review projections, although, a complete hiring freeze is not possible or desirable because doing so would negatively impact tuition income from enrollment and key courses. It is a complex balancing act because there are cases where key essential hiring is warranted.

Some regents were concerned over the impact of feast-famine budgets and get well plans because at some point decisions need to be made on what can be supported, what builds and enhances our reputation nationally and internationally, and what programs support our core mission. Letting programs limp along on budget cuts and hiring freezes may not serve the university well in the end because compromising quality affects the value of the program.

Chancellor Bley-Vroman said the colleges and units at UHM are very heterogeneous, so techniques and resources available to make cuts for one college are not available for the other. They relied heavily on deans to develop appropriate responses to budget tightening within their individual units. Some measures undertaken are sustainable on either a short or long term basis, while others measures would not be sustainable on a long term basis without impacting quality.

Chancellor Bley-Vroman explained that the new budget process of realigning allocations will not immediately affect next year. Under the interim plan, allocations will be based on a measure of instructional load and students served, which is a huge step forward over the traditional, historical allocation model. The board noted that 38.5% of net tuition was being allocated to the units and asked what happened to the 61.5% balance of the allocation. Chancellor Bley-Vroman responded that the balance will go towards core services (e.g., custodial, grounds, library) campuswide based on the current actual proportion. VC Taylor added that the 38.5% was going to colleges doing instruction, and did not include support services, research units, and professional schools. There was some question on the terminology of “net tuition growth” and Chancellor Bley-Vroman explained that the realignment provides greater transparency in the way tuition is currently allocated. Every unit’s tuition allocation in the fall will reflect their appropriate share of the 38.5%. The base budget will remain constant and the proportion of general funds and tuition will be altered to reflect what that unit ought to receive, then when tuition increases, the amount will go up by their share of the 38.5%. VC Dasenbrock added that next academic year every unit will receive 38.5% of the tuition generated, which will be the baseline and there will be an additional increment because they collected more tuition this past year than the year prior. So they are distributing 38.5% of the increase in net...
tuition between this fiscal year that is just ending and the year before. It is similar to the research training & revolving fund (RTRF), which goes to the units that generated the most additional research funds.

The committee raised concerns that there were two major assumptions underlying all of this: (1) all programs cost the same, and (2) the other support units get general funds and it assumes that the current distribution is rational, which is not the case. Chancellor Bley-Vroman responded that they have systems of differential tuition that account in part for the differences in cost, and while this method did not address the rational allocation of general funds, the new model is a hybrid of revenue and activity-based that will be sensitive to activities being performed and the cost, centrality and mission-alignment of those activities will be evaluated.

**UHM Financials**

VC Cutshaw provided an overview of fund sources; special funds (details and definitions in Appendix 2); revolving funds (details in Appendix 3); UHM unit by functional type; Fiscal Year 2014 Revenue, Allocation & Transfers (details in Appendix 4); Fiscal Year 2014 Expenditures (details in Appendix 5); Fiscal Year 2014 General & Tuition Expenditure Distribution (details in Appendix 6); Fiscal Year 2014 Expenditures by Type; Fiscal Year 2013-2015 Tuition Cash Balances; and Fiscal Year 2014 Output Metrics.

VC Cutshaw indicated this section is more detailed in terms of data; the focus is dividing up expenditures by functional unit type and providing revenues and expenditures by fund source in statutes, but does not go below the statute level into the details of accounts within statute. UHM currently defines cost centers and budgets at the school/college level, not the departmental level. The School of Ocean and Earth Science and Technology (SOEST) is an anomaly because it currently has 4 organized research units (ORUs) within it with the goal next year to set up cost centers at the ORU level. She noted that in general funds and tuition expenditure distribution, 77% is in personnel, of which 67% are unionized, which presents a challenge as they try to move budget allocations around due to collective bargaining agreements in place that would have to be negotiated. The scholarships look low because tuition dollars are transferred into other special funds to pay the scholarships. The expenditures by functional unit type bar chart shows how money is spent, and of note are the instructional units, which spend 90% on personnel. The Fiscal Year 2013-2015 tuition cash balances chart is broken down by functional unit, with two units (core administrative and professionals schools) having negative balances. The bulk of the $8 million deficit in professional schools is for nursing, which carries a deficit from prior years involving temporary employees carrying full fringe that could not be converted to permanent and those fringe costs drove the budget down.

There was a question on the difference between some of the instructional units and the professional schools and if the professional schools had a tuition differential, and it was noted that the professional schools carry a larger deficit than the instructional based on allocations. Another question was raised that if cost centers are the colleges and units, and deans have the greatest knowledge and discretion on allocation decisions within their cost centers, why is there different treatment with pulling out separate cost centers for some ORUs within SOEST while other centers (e.g., Cancer Center, Pacific
Biosciences Research Center) are being integrated.

VC Cutshaw responded that certain units have requested tuition differentials (e.g., Law, Medical School, MBA program, Nursing), however the engineering program does not currently have a tuition differential. Those units charging tuition differentials get 85% of their tuition generated back, with 15% going to administrative costs. VC Dasenbrock added that those are the programs the board had previously authorized a higher than average tuition increase. VC Cutshaw reiterated that the reason for the larger deficit in the professional schools was due to the deficit situation in the nursing school.

VC Cutshaw clarified that they are budgeting the ORUs as a separate cost center within the school and will be able to pull out data. The Institute for Astronomy will be a freestanding ORU, and there are other smaller ORUs that will be part of discussions on organizational changes (e.g., social work, public health and center on aging becoming one unit), but these are discussions with many steps and union consultation that need to be considered and completed first.

The Fiscal Year 2014 Output Metrics shows unit budgets by instruction, what are their total revenues and allocations, how they spend it at the highest levels, and output. Awards are funded awards, not expenditures. A question arose regarding the discrepancy on the number of majors shown versus the number of undergraduates at UHM, and the number of majors under A&S. VC Dasenbrock responded that A&S consists largely of unclassified freshmen and sophomore students who have not declared a major, and there are costs associated with that (e.g., advising). They have counted double majors as two, and double majors are becoming more popular, but they need to look at the numbers again because 31,000 seemed high. The regents suggested possibly having a line for undeclared majors to avoid the confusion.

A reference was made to the UHM operating budget worksheets for Fiscal Year 2016 that were handed out as part of VP Young’s presentation showing Natural Sciences almost breaking even going into the year, but now projecting a $4.7 million loss, but on the output metrics Natural Sciences seem to be producing the highest number of majors and student semester hours. The committee asked how UHM would reconcile this and not penalize a unit that is now in a deficit but is actually producing more. VC Cutshaw indicated that the new budget model will divert resources to those units that produce the most. They need to address base budgets because they do not know if the general fund base is adequate, and the whole purpose of budgeting is to rebalance based on output. She added that the $4.7 million deficit in Natural Sciences developed over several years, not just one year, so it is possible there was an error on the worksheet. The committee requested that VC Cutshaw report back to them on this discrepancy and she agreed.

RTRF

VC Taylor presented an overview of how RTRF was established, the purpose, and primary allocation; Fiscal Year 2015 Indirect Cost (IDC) Source and 50% RTRF Distribution; the Vice Chancellor for Research Allocation Basis; Fiscal Year 2015 Deans and Directors (D&D) Allocation Basis and Expenditure Categories.
VC Taylor noted that the top five units (SOEST, JABSOM, UHCC, IFA, and CTAHR) constitute 77% of IDC distribution and RTRF revenues, and all these units have major off campus facilities. Of his $10 million annual distribution as VC for Research, 55% is strictly F&A, and 45% discretionary and invested back into the research enterprise. He indicated the board had been particularly interested in how the 50% RTRF distribution to deans and directors was spent, so he showed what it was for and what it is expended on.

The committee had questions and comments on: whether some of the 50% RTRF distribution to Deans and Directors was spent on things that are already budgeted as opposed to getting new equipment for hiring new faculty and what was the impact on the operating budget (e.g., do people not budget for things because they know they will get RTRF, or do they get RTRF on top of what they already budget); how well are they managing the budget; how much RTRF gets invested into repairs & maintenance of facilities; would a 7% tuition hike make everything fine despite the decrease in legislative funding; were funds actually allocated to promote more innovation, and what kind of progress was being made on the innovation side; where does quality of education and cost to provide that education interact in this stabilization proposal;

VC Dasenbrock responded that units generating large amounts of RTRF have an expectation of trends over time, and based on that they can estimate what fraction will be put into recurring costs (generally about 1/3). There are some things such as support for staff, facilities, and equipment, where the school is making an investment in research operations that are shared across the school, and they are committing a fraction of their return to those units who are generating current and future research. Decisions by Deans and Directors, Vice Presidents and Vice Chancellors are being made all the time about where to invest. The recurring costs can change over time, but at a slower pace than start up for new faculty.

Regarding how to grade the management of the budget, VC Taylor indicated that UHM would like a lower amplitude of net carry forward funds. He felt past performance was constrained by many factors, and efforts are underway to exercise more internal control to get where they want to be. VC Dasenbrock noted that there was new system financial leadership and new leadership at UHM, and they are working to address issues and welcome insight from regents. The purpose of the money is to help the university deliver programs, their research portfolio is among the best in the world, and they are marking remarkable progress with the quality of undergraduate education, so that needs to be balanced with internal decisionmaking and allocation of funds that needs to be worked on, and there is a really good plan for moving forward. Chancellor Bley-Vroman added that UHM is on the right track, but need and hope that the board will maintain the previously approved tuition increase, which they used as a basis for their plans.

In terms of RTRF being invested back into facilities, of the 50% that goes back to D&D, about 25% would be in the facilities realm (10% for repairs & maintenance/buildings & grounds; and 15% for utilities), but this is biased towards those units with large off campus facilities. At the VC level, 20% goes to pay for revenue bonds on C-More Hale and basement of Sinclair Library. He pointed out that the biggest issue is the overhead rate for UHM that is 10% to 15% lower than the rest of the county, due to the low investment of the state in facilities. He added that RTRF funds are invested in facilities
maintenance in the context of research and training, which are the limitations by statute of what these funds can be used for, the funds cannot be used for certain things.

Chancellor Bley-Vroman responded that with a 7% tuition hike, UHM would be in a state of relative stability for the next couple of years and provide the groundwork for UHM to move forward, without the tuition increase it would be extremely difficult for UHM to move forward.

VP Syrmos added that they had started making a lot of investments in innovation such as XLR8UH; hiring a new director of the Office of Technology Transfer & Economic Development; and revitalizing the Office of Technology Transfer and the Discovery & Innovation Special Fund. VC Taylor added that the partnering between the system, UHM, D&D and his office that made most of this possible.

Committee Chair Sullivan requested that VC Taylor report back to the board on two items: (1) since 35% of return to D&D is allocated to personnel, could information be provided on the policy relating to hiring, retention and tenure because these are non-teaching personnel and the board needs a way to understand how this is being handled; and (2) on dedicated research facilities, provide clarification whether these facilities are covered in repairs & maintenance by RTRF or whether these facilities are part of the UHM deferred maintenance budget request or separate and funded through RTRF.

Chancellor Bley-Vroman indicated that UHM is stabilizing in a situation that is far from ideal and noted that he had talked about “academic deferred maintenance” in earlier presentations. They have to start making decisions at the campus, college and ORU level for next year about what needs to be rebuilt, a conversation that will be much easier if the revenue situation continues to improve. The budget hearings will reveal things over the long term that would affect quality and need to be addressed.

Committee Chair Sullivan made a suggestion for the next step, subject to the agreement of the regents, which would for the board to pay attention and focus on the professional schools from a financial aspect. If the regents go through all the budget worksheets attached to VP Young’s presentation, there some unique circumstances that are not a surprise (e.g., Cancer Center, Athletics), but the other red flags were the projected deficits for the professional schools, in particular JABSOM ($1.4 million), Law School ($1.3 million), Shidler ($1.2 million), and Nursing ($4.5 million). There are real issues with these schools, some or all are proposing fee increases, and it would be good to look at them in totality. If the regents agree, she would like to ask VP Young and give him authority to evaluate the deficits and help the regents understand what is happening, how the money is being spent, how losses are being mitigated and covered, and give the board a more comprehensive view of what is going on with these schools.

Chair Moore noted that unit budgets are largely a construct of the past, and deficits or surpluses are function of allocations that were made that no longer represent anything rational. The deficits show because historical allocations have not kept up with the reality, and other units which have in relative significance declined, still maintain old allocation percentages. The fact that a unit is in deficit does not necessarily mean something is wrong with the operations; it could be the allocation mechanism. They need to
understand the whole picture, and we do not have it. UH is an $800 million enterprise and only $500 million is shown. Need to look at whether the whole enterprise is sailing or smooth waters or is there trouble. Even if sailing in smooth waters, they need to regularly look at efficiency and productivity, and how UH measures against peers in delivering a quality education at a competitive cost.

Committee Chair Sullivan agreed with Chair Moore, but was concerned that there were fee increases for the professional schools coming to the board and it is important for the board to try and understand as best we can the status of their financial situation because she does not want to look at fees in a vacuum.

There was agreement amongst the regents that if there were going to be fee proposals there needed to be more context for the board to be comfortable with it and that some of the problems could be due to the historical allocation models not being realistic. Some regents felt it was not the board’s job to micromanage; many professional schools carry a higher cost structure and exceptional salary schedule. Some professional schools such as medicine serve a social purpose that the board may want to subsidize, but others (e.g., Shidler) do not serve the same social value at large. Due to the very high cost structure, beginning with salaries, the board needs to look at those programs as a starting point to determine if a bigger differential is needed, but keeping in mind that it should not be raised too high that it becomes cost prohibitive to enter certain fields. Another regent felt that raising fees versus raising tuition or a tuition differential was an important philosophical decision, and the board should be looking into the whole structure. There was also concurrence that the board needed to look at the institution, not just programs within a campus, and also look at statewide needs and benefits, which would give the board a philosophical basis for where resources are being invested and the levels.

President Lassner indicated that he did hold back fee proposals that were ready to come to the board because he agreed they should be considered in the context of the overall budget and tuition situation. The intention is to try to bring fee proposals once or twice a year, rather than at random times, in order to provide more context. He suggested that administration makes sure to do that within the context of a complete understanding the operating budget of those units. There is an opportunity over the next 3 or 4 months to look at 3 of the 4, and hopefully the 4th as well.

The committee recessed at 3:22 p.m. and reconvened at 3:34 p.m.

C. For Information and Recommendation: Fiscal Year 2016 Operating Budget

VP Young said the presentation was the conclusion of the administration’s efforts to construct a budget proposal for Fiscal Year 2016, which included highlights of Legislative Fiscal Year 2016 general fund appropriations; budget parameters; a UHM campus budget overview; undergraduate tuition rate proposals and estimated ending Fiscal Year 2016 reserve levels; current and proposed tuition rates; administration operation budget recommendations; a Fiscal Year 2015 versus Fiscal Year 2016 comparison; estimated Fiscal Year 2016 ending Tuition & Fee Special Fund (TFSF) reserve levels; an overview UHM, UHH, UHWO, and the UH Community Colleges budgets; systemwide support; a recap of additional general fund appropriations and what the monies would be used for;
information on Title IX and VAWA funding, performance-based funding, RTRF, and other non-general funds.

He noted that UH received more general fund appropriations in Fiscal Year 2016 than Fiscal Year 2015, however, it is all encompassing of collective bargaining increases for those contracts that were already in play for next fiscal year. The difference really represents increases that the Legislature did accommodate for budgeted positions due to collective bargaining. There is a small lump sum funding of $6.38 million later in the presentation. The other sources of funds (special, federal, revolving) are reflected in the budget bill (House Bill No. 500) for the next biennium in terms of ceilings.

Regarding budget parameters, budgets were proposed at the campus level with the exception of UHM and the community colleges. Campuses were asked to submit a status quo scenario budget and a budget that gave campuses the discretion of if they needed a tuition increase to augment strategic initiatives on their campuses, what was the minimum tuition rate increase they felt comfortable proposing, provided ending balances meet targeted reserve levels and there was no fiscal imbalance at the campus level unless that campus was near the maximum reserve threshold.

As mentioned earlier, the majority of campuses are projected to meet the board’s reserve policy parameters, except for UHM, but they believe UHM is on a financial turnaround schedule that has a horizon beyond the next fiscal year. This presentation focuses primarily on the core operating budget, and other funds can be found on the worksheets contained in the appendices that were included in the packet, and are also available online for the general public. Of the $35.5 million board budget request for Fiscal Year 2015, the Legislature only appropriated an additional $7.5 million, of which $6.4 million is lump sum to system around performance objective funding and an additional $1 million to fund Title IX compliance matters.

The undergraduate tuition rate proposals and estimate ending Fiscal Year 2016 regarding reserve levels show reserve levels for each campus based on the two tuition scenarios. The forecasted ending balance for Fiscal Year 2015, or the beginning balance for Fiscal Year 2016, is shown, along with reserve thresholds, and all campuses fall within that reserve range with the exception of UHM. Additional revenues of the tuition rate increase previously approved by the board, and the outcome based on the two scenarios are also shown in the tables.

VP Young pointed out that the current and proposed tuition rates contain an error, and the proposed numbers for resident tuition rates at UHM should be the same as the currently approved 2015-2016 rates.

The operating budget recommendations are the amounts for the overall systemwide budgets for each category and source of funds based on the campuses proposed tuition rates. The change in the TFSF reserve shows that at the current proposed tuition rates what the incremental change in reserve balances at the end of next fiscal year would be to the current balance starting Fiscal Year 2016.

Regarding the comparison of Fiscal 2015 to Fiscal Year 2016 in terms of the change
in revenues and expenditures by fund, revenues are increasing, with general fund expenditures increasing and TFSF expenditures decreasing, which is largely attributable to efforts at UHM to reduce spending and help bolster their reserves with the end objective of building reserves back into the targeted range.

The estimated Fiscal Year 2016 ending TFSF reserve levels show the comparison between ending balances in Fiscal Year 2016 based on no tuition increase and the proposed tuition increases for the individual campuses. With the exception of UHM, everyone is within targeted reserve range as far as the TFSF; however, UHM has to increase TFSF revenue in order to get back up into the reserve range.

**UHM**: The UHM slides show the assumed decline in enrollment aggregated across all campuses and is not necessarily the case for individual field programs; shows the result if the scheduled tuition rate went back to status quo and also at the present tuition schedule; what UHM is budgeting for Fiscal Year 2016 to reduce expenditures; the reductions needed to stay the course if the end objective was to get to 5% reserve target as if there were a 7% increase, which is challenging given the percentage of general funds and TFSF that are embedded in personnel costs, the majority of which are protected by collective bargaining.

**UHH**: The UHH slide shows the assumed decline in enrollment; what the additional revenues from the proposed tuition rate increase would be used for; and what they budgeted for one-time CRDM projects that will be funded out of reserve balances.

**UHWO**: The UHWO slide shows a projected enrollment growth, the only campus across the system; the four objectives the additional revenues from the proposed tuition rate increase would be used for; and what UHWO would propose if there was no tuition increase.

**Community Colleges**: The Community Colleges slide shows a flat enrollment projection across the system, with no significant increase or decline; and what the additional revenues from the proposed tuition rate increase would be used for.

**Systemwide Support**: The system slide shows the primary funding sources and what the system uses them for; the reason for the forecasted operating deficit for Fiscal Year 2016; and the plan to reallocate resources for new programs.

In terms of additional general fund appropriations from the Legislature, VP Young noted that with regard to the $6.38 million in lump sum performance-based funding for each of the next two fiscal years, the funds are not specifically required to be performance-based for the first year, and are to be allocated at the discretion of the president and board. The legislative requirement for the second year is that those funds must be distributed on some performance-based outcome deliverables determined by the president and board that are centered on student success, achievement and articulation. He also explained that the $5.64 million in revenue bond expenditure authority for capital repairs at JABSOM was not new money being appropriated, the university always had that money in its revenue-undertaking funds, but the authority to expend it had lapsed.
VP Young provided a breakdown of the total Title IX/VAWA funding, the associated positions, and how the monies would be used. He indicated that most of the positions are already existing positions within the UH budget and reallocated for this purpose.

VP Young had mentioned regarding the restrictions with the performance-based funding earlier, the timeline for when performance targets will be prepared based on strategic directions and metrics, and tied to the next supplemental budget construction; the expectations for campuses for Fiscal Year 2016; how any remaining funds for Fiscal Year 2017 will be invested; and how Fiscal Year 2017 funds will be made available to campuses.

VP Young provided information on the RTRF even though it was not included as part of the overall operational budget in this presentation. The slides showed how the RTRF allocation is distributed and how RTRF overhead recovery will be distributed to campuses for Fiscal Year 2016. The reports are available online for the public and will be updated in August. The RTRF revenue projections for Fiscal Year 2016 were shown by campus, along with the estimate as of March 31, 2015, the annualized amount, forecasted adjustments. Based on the calculation, there was a reflective reduction in the overall revenue projection.

In terms of the other non-general funds, the slide showed that the funds are specified in statute for specific purposes; managed at the program level, even though they may be aggregated up to the campus level; and are supposed to be self-supporting so expenditures do not exceed revenues.

VP Young pointed out there was an extensive amount of appendices attached to the presentation that are available online, showing a scenario development at the campus level of 0% status versus the proposed tuition rate.

The regents commented concerns regarding tuition increases, what were the plans for scholarship assistance; and given enrollment projections, especially the 3% reduction, could the reduction become even larger given the amount of tuition differential.

President Lassner explained that board policy is clear about scholarship assistance, and for each unit there is a requirement as to the percentage of tuition that must be allocated to need-based aid. Last year administration changed executive policy to relax the 10% requirement relating to allocation of tuition to non-need based aid. To the extent tuition continues to go up, the amount of need-based aid would increase, but non-need based aid would be determined at the discretion of the chancellor.

VP Young added that the projects on enrollment reductions could increase, except the tuition rate increases have been published for the last three years, so all students enrolling at UH already know that tuition would be increased to 7% in academic year 2015-2016. The forecast for overall declining enrollment is based on other factors at the campus level, which is why discretion has been given to campuses to work with individual field units around what they see as individual program enrollments. Chancellor Straney added that UHH students would notice the tuition reduction, with returning students noticing immediately due to financial aid repackaging. New student enrollments are
running ahead of projections, and the proposed 4% increase would have nominal impact on those students. VP Young indicated that enrollment across the system was forecasted to slightly decline, due to UHM having the largest share of enrollment and the most significant drivers around enrollment, so any decline at UHM will affect the overall system. Chancellor Bley-Vroman noted that UHM predications are based largely on demographics, and the decline is not attributable to the existing published tuition. Interim Vice Chancellor for Students Lori Idea pointed out that nationally the 18 year old birth rates are declining over the next five years, so UHM is competing for the same amount of students nationally as other colleagues. What is important is that students coming to UHM and other campuses have been aware of the increase for some time and based decisions on that. As of yesterday, UHM packaged thousands of financial aid based on the 7% increase, and if that was reduced they would need to repackage everything. They are anticipating a robust class at UHM and are excited about that.

President Lassner acknowledged that this is the first time this had ever been done, and they received an unexpected compliment on the Kuali Financial System (KFS) from the new external auditor. KFS allows the university to capture all organizational level budget numbers across all sources of funding for the system. He thanked VP Young and Budget Director Michael Ng, both of whom have been with UH less than six months and spent most of their time at the Legislature and worked with the rest of the team to provide this presentation. He also thanked the chancellors, vice chancellors, along with VP Morton and AVP Unebasami, who collaborated to come up with these proposals. The presentation was finalized and posted six days in advance in accordance with statute, and there have been continuing internal discussions on the recommendations. The requirement was that UHM had its own number, the community colleges could have a number, and they worked hard to align UHH and UHWO to have the same number. He did not know in advance what the numbers would be, so they spent time thinking about what the Legislature had done, the financial impact on students and their families, and the board’s interest in lowering tuition from the 7%, which is relatively high for a state in which there were not substantial cuts. Over the past five years, UH has had among the highest tuition increases in the country compared to peers, coupled with the deepest cuts per full time equivalent students.

These recommendations are for resident, undergraduate tuition, the nonresident and graduate tuitions are not changing. He is recommending the board accept the community college proposal of reducing the tuition increase from 7% to 5%; accept the UHH and UHWO proposal of reducing the tuition increase from 7% to 4%; and reduce the UHM proposal of a 7% increase to 5%.

He mentioned that the $6.38 million lump sum appropriation to the system that VP Young would be used to mitigate the 2% tuition reduction. He is proposing for UHM, that $3.7 million of those funds be made available to UHM in Fiscal Year 2016, which is roughly equivalent to the 2% tuition decrease. This would mitigate things for UHM this fiscal year but not the next, however, there should be a performance funding formula in place and UHM would have the opportunity to compete for that, but the money would not be compounded. For the remaining $2.6 million portion, he is recommending they solicit proposals within the university for interventions and measures that will help achieve performance metrics, which will be aligned with the Strategic Directions the board
approved in January. The work needs to be done quickly, and they already have metrics and models to propose.

The net impact of this across the system is:

- This relieves some of the pressure and shows sensitivity to the legislative appropriation. The Title IX funding is helpful since it was already mandated. The community colleges will be in a position to implement programmatic enhancements they had to defer during the past difficult years, which have also been hard across the system due to the unfunded collective bargaining increase in the previous contract.
- UHWO can support enrollment growth as tuition does not pay the full cost of resident instruction, and this increase helps them meet those needs. They are being proactive and taking responsibility upon themselves to create a reserve for repairs & maintenance to avoid falling into the trap that other units have.
- UHH’s recommendation strategically utilizes its reserves, which are the highest on percentage basis across the system, to invest in their deferred maintenance backlog and will also be taking steps to increase student retention.
- UHM’s recommended budget did include reduced expenditures levels of about 7% or 8%, and in combination with the new revenue and the cuts would reverse multiple years of extremely alarming negative cash flow, much of which was in recurring costs, and he appreciated the work of the UHM team to pull that off. This does not get UHM to the targeted reserve range, but they do have a plan.
- While the university did not get lump sum budgeting for the entire system, the lump sum performance funding was something UH had been requesting from the Legislature for multiple years, but been denied. This could be the basis for thinking about future investments by the state if the university can prove itself, and is being provided is very helpful.

The next steps are:

- Being development of a performance funding approach and have metrics in place by September. Best practice would be to use a moving average, and they will look into the extent that can be done and the extent the metrics echo the previous ones that have been used in the past five years.
- Given the declining and enrollments, the university needs to go beyond being reactive to the demographics in our state, and take proactive measures to increase enrollment. This is not just for financial reasons as the university’s primary objective is to educate students in the state, part of which is related to how we manage enrollment. He would like to recommend a deep dive for the regents in early fall to discuss proactive measures that can be taken on enrollment management, some of which are recruiting, another piece is retention and also how we move people through the system. Declining enrollment is not a bad thing in the short run as it means the university is being successful in graduating students in four years, which can be a sign of success.
- Plan to aggressively monitor performance through quarterly financial reports; deficiencies in current reports have been noted and they will work to continue
improving those.

- It is time to begin work on the next multi-year tuition schedule, as they are entering into year four of a five year schedule, which gives them time to provide some predictability to students. The only unpredictability in this recommendation is to reduce tuition from what was advertised, which will involve a fair amount of work to repackage.

President Lassner talked about his recommendation that UHM receive a lower tuition increase than what was proposed. The system and UHM need to continue working together as it has been a good partnership and supportive program over the past year. It would be his recommendation that UHM come in with a proposal for 7% increases over the next two years, but does not think it is reasonable to have reserves reach the 5% minimum threshold within that time if revenue is being reduced from what they had been planning on for the past year. He would like some time to step back and revise the multi-year plan for financial recovery to get to the board approved reserve levels, which could take up to 4 years. Now that UHM has reversed the negative direction, he does not think it is urgent that UHM be back at 5% by a specific date. He noted that as a system, the university is within the 5% to 16% board approved reserve levels, and should there be an emergency somewhere they have the statutory authority and obligation to use institutional reserves to address it. As long as the system is over 5% in reserves, he is comfortable with his recommendation to reduce the tuition increase and giving UHM the time to achieve the reserves recovery.

He indicated that the structural enhancements are key to UHM’s financial performance, and both he and Chancellor Bley-Vroman hope the trend can continue and UHM can achieve consolidation and efficiencies on the administrative side with staffing and also effective operations.

He added that as they move forward, the university needs to maintain its commitment to academic excellence and student success, both of which help the university achieve its objectives and served the state. Program prioritization on campus and across the system also needs attention, and they are discussing a deep dive in July on what systemwide academic planning is, and challenges and opportunities.

In noting the units of concern that Committee Chair Sullivan talked about in the context of fees, they already have plans that at least three of the four units would have been be the subject of discussions around revenue and expenditure proposals coming in from the colleges, which is a great way to have a conversation that before raising fees or accepting new expenditures, there be an understanding of the financial health of those units. He also referenced the need for a business plan for the Cancer Center that was discussed by the Committee on Internal Audit, and they are committed to doing that. There is a deep dive on UHM Athletics scheduled for August with Dave Matlin, the new Athletics Director, to get his perspective on how to turn things around. He was glad that he was not asked what grade he would give at the unit and campus level, but indicated he would give them an A for improvement, because tremendous strides have been made from a year ago.

Work needs to begin on the supplemental budget proposal, in particular, the approach
to the deferred maintenance backlog, as neither prior approaches has worked. Whatever approach they come up on capital improvement and the backlog will have an impact on the operating budget (e.g., UHWO creating reserves, UHH investing reserves), and they need to come up with a new approach that addresses it, which may add costs to students.

President Lassner indicated that everything they learned through this budget process show it was a good idea, and it well worth taking this intentional approach to budgeting after knowing the outcome of legislative funding. They need to start sooner next year and expect next year will be better due to this experience. In terms of the lessons about reserves, this was the first time they were really talking about the plan to restore them, and he remarked that they did not lose reserves at UHM through a single decision and they would not be restored with a single decision, it is a multiyear effort. Depending on how the discussion goes today he noted there were two full board meetings scheduled, and by statute matters relating to the budget must be posted six days in advance. He is recommending that whatever direction the board gives on amending the tuition schedule be brought back to the board on May 21 for action, at which time the board can act to lower tuition, which gives student services a head start on making the changes with repackaging, and administration will come back on June 2 with an amended operating budget proposal that includes comments and approval of changes in tuition at 5% for UHM.

The committee expressed appreciation for the thorough presentation, and had the following questions and comments: having the opportunity to see the amendments prior to the May 21 meeting; asked for clarification if the recommendation was to accept the campus recommendations, with the exception of UHM with some plan for mitigation; noted that UHH and UHWO would be using reserves to address deferred maintenance (existing or preventative), and one reason for the steep reduction in UHM reserves was the decision to renovate Edmonson Hall, and they should be acknowledge and appreciated for those efforts; recognized that this budget process was a major departure, expressed disappointment that the university was not able to be more persuasive at the Legislature, and indicated concern that the university might be sending the message that we can get by without everything we requested; agreed the approach of separating the biennium budget request from the operating budget was extremely sensible and experience will make things better; and the projections were nice to have, but there needs to be good, accurate reporting of budget to actual.

President Lassner responded that he would be able to provide the regents with the amendments in writing. He confirmed that his recommendation was to accept campus recommendations except for UHM. He commented that 2009 was the first year of the alarming decline in reserves due to the substantial reinvestment in the UHM campus.

Other regents expressed appreciation for the holistic view of the budget on a systemwide basis, and asked if a tuition increase of more than 5% and less than 6% might be needed for UHM given the serious deferred maintenance issue.

President Lassner noted that there could be other options to address deferred maintenance at UHM such as a fee or earmarking a portion of tuition for deferred
maintenance). Last year they tried to allocate a portion of tuition to service revenue bonds to address the backlog, the board was uncomfortable with it, and the Legislature said no. Whatever they decide the strategy is with the Legislature, the issues and numbers will vary by campus, and there will need to be discussions on whether to do cash renovations or revenue bonds. No solution is being offered today as part of the operating budget for Fiscal Year 2016.

Some members of the committee respectfully disagreed with the recommendation to reduce UHM tuition increase to 5% and felt it was fiscally irresponsible and the impact to students was minimal, while others felt the impact to students was recognizable others strongly believed that it was up to the campus administrators to determine what they need in terms of tuition 5% as a minimum of the reserve threshold is low and UHM is still woefully below. The people at UHM worked long and hard to come up with the plan and prepared financial aid packages based on the previously approved 7% increase. Even though the system has healthy reserves, UHM does not, and it is time to stand up to the significantly decreased legislative funding that is adversely impacting the quality of education. Other regents felt that even with the 7% increase UHM would still violate the no fiscal imbalance of expenditures unless near 5% reserves threshold, and needed to try harder to address the situation. Some regents felt the financial aid piece at UHM was acceptable given the contributions of UH Foundation, and were not convinced UHM had tightened their belts enough. They agreed with President Lassner’s recommendation to trying to stop until progress is seen or the problem will be compounded. Some regents expressed wanting to wait to hear back from administration on the reaction to the recommendation for UHM and whether it could be done, UHM put forth a persuasive case, but the president had the systemwide point of view and his suggestion may be more palatable.

President Lassner interjected that he shared his recommendations with the officers, chancellors and VPs in advance for discussion. He is giving his best advice and will not feel badly if the regents decide on the 7% increase for UHM. The two most important things regents do is to hire and fire the president and set tuition. It is not good to question a previously approved tuition schedule, but the board requested it be revisited at this time.

Chair Moore thanked everyone for the unprecedented work on the deep dive and budget, and indicated he appreciated the president’s observations. There is no consensus among the general public about the purpose of public education, and tuition is the most difficult decision the regents make and there will never be consensus. He appreciated all the input and indicated the board should not make decisions based on what the Legislature thinks, but what is right for the university, which means taking the public sentiment into consideration. The university received funding for collective bargaining increases, and the state pays for fringe and debt service, and to say the Legislature short-changed us insufficiently acknowledges their support and the problems the state faces (e.g., Medicare, K to 12 tuition, state healthcare plans, retiree pensions and healthcare, prisons). The state has no choice with many of these areas, except for tuition at UH. It is not entirely the Legislature’s fault for where the university is. He was happy with all the recommendations because everyone one had a rational basis for support.
Chancellor Bley-Vroman respected the proposed solution, but pointed out the advantage in keeping with the approved schedule as otherwise it is difficult to plan, which can impact morale. They are trying to make big changes at UHM, many that caused significant pain, which are made more difficult when the plan keeps changing and impacts consensus as they try to move forward. UHM is in a state of deferred academic maintenance, situations have been created that are not sustainable in the long run, and deferring them more is not helpful and is unnecessary.

Committee Chair Sullivan noted that when the tuition schedule was approved there was a different chancellor and president, and the board was told the schedule would be revisited at the end of year two, so this is part of what was approved and should not be a surprise. The board tried for years to convince the Legislature to give performance based funding that had been used in other states, and is a progressive way of getting states to put in more money. There is a lack of trust with Legislatures that public institutions are spending money wisely. It is a big deal for UH to get this performance based funding and she did not want to underestimate how important it is for UH to spend the money wisely, because they are being watched. The university needs to send the right message, it is not just about tuition, but how the university is working with the state so they can get money in the future.

She asked if there was consensus among the committee members in following President Lassner’s recommended schedule to approve tuition at May 21 meeting and take up the operational budget at the June 2 meeting.

President Lassner added they will bring the board a choice and provide information in between, depending how the board votes, administration would be ready for two scenarios for the June 2 meeting. He asked for suggestions from the regents on what sort of information they would find helpful in making an informed decision. He added that a year ago Chair Moore served on a task group about tuition and that information could be distributed to the new regents.

V. ADJOURNMENT

There being no further business, on the motion of Regent Matayoshi and seconded by Regent Putnam, the motion carried with unanimous approval and the meeting was adjourned at 5:11 p.m.

Respectfully Submitted,

/S/

Cynthia Quinn
Executive Administrator and
Secretary of the Board of Regents