Finance/Facilities Committee


Absent: Angela Faherty and Wayne Newell.

Trustee Fournier, Chair, called the meeting to order and welcomed everyone.

Financial Update. Ms. Rebecca Wyke, Vice Chancellor for Finance and Administration and Treasurer, provided a financial update and distributed the FY2011 Forecast versus Budget analysis; the Financial Analysis of FY2010 Unrestricted Operations and State Fiscal Stabilization Funds for the Year Ended June 30, 2010; and the flash reports for the Managed Investment Fund, Pension Fund, and Operating Cash Fund.

Ms. Wyke presented the Multi-Year Financial Plan (MYP) for FY2012 to FY2016. The System has developed a long-range financial planning process that evaluates the fiscal impact of key budget drivers such as enrollment, faculty & staff compensation, investments in physical plant, and State appropriation invested in the System. The purpose of this planning process is to consider the underlying financial conditions that face the System and the impact of alternative action steps that may address projected shortfalls in the future.

Like any projection and analyses, the Plan is impacted by the assumptions that are incorporated and the imperfect ability to predict the future. At a high level, it represents a valuable tool to understand how the major components of the budget can be manipulated to find a balance; however, it is important to note that actual application of any of these strategies will yield varying results.

CURRENT TREND:
The current trend for the Multi-Year Plan assumes the following factors which result in a $20 million gap by 2016:

- State Fiscal Stabilization Funds of $6-7 million annually will no longer be available;
- Tuition increases at 5% or less, annually;
- Total Appropriation is held constant (0% growth);
- Compensation increases include only adjustments for post-tenure, merit, step increases, and satisfactory performance adjustments—no COLA; and
- Healthcare at current trend.

Revenues do not keep pace with expenses and it should be noted that the Current Trend projection does not include any contingency for a reduction in Appropriation, which would increase the projected deficit. While the challenges continue, it is important to recognize that the Current Trend
MYP reflects the positive fiscal impact of various cost saving measures, including many New Challenges, New Directions initiatives and the System has worked hard to curb spending in the following areas:

- In the last three years, the System has reduced its workforce by nearly 6%.
- In FY2010 the System closed an $18 million structural gap.
- Its actual operating expenses at year-end were nearly $5 million less than the prior year.
- Additionally, our current FY2011 budget is balanced, closing a $28 million structural gap.

**Healthcare Costs:**
Healthcare costs for current employees and retired employees represent more than 55% of the current year benefits budget. The relatively new accounting requirement to recognize the future cost of retiree health care when it is earned and the soaring cost of healthcare in the United States are major drivers of the System’s overall benefit rate which is currently 51.9% of a full-time employee’s salary and is projected to exceed 60% by FY2016. The employee healthcare plan is crucial to attracting and retaining highly qualified faculty and staff, but its rapidly escalating costs crowd out the System’s ability to increase salaries and wages and invest in other mission-critical expenses.

Even without any cost of living adjustment, employee salaries in aggregate increase each year given promotions, post-tenure review, step, and satisfactory performance increases that are negotiated in bargaining-unit contracts or stipulated in employee policies. Without any cost of living adjustment, salary costs across the System will increase on average 1% annually. If just a 1% cost of living adjustment is added to those Current Trend assumptions, expenses increase an additional 0.5% annually and the System ends FY2016 with a much steeper deficit of $36 million.

The Employee Health Plan Task Force (Task Force) is focusing on improving the health status of employees and their dependents and protecting them from catastrophic cost while managing the costs of the healthcare plan. The Task Force is pursuing savings via employee education and wellness programs, and partnerships with employees, bargaining units, and healthcare providers. If the MYP incorporated the Task Force cost saving goals, it would shift the cost increases from the current trend of 8%-9% annually, to declining growth rates that begin at 6% and move eventually to a more modest 3% increase. These goals would save nearly $14 million annually by 2016 and over $35 million over the five year period.

**Capital Needs:**
Historically low capital renewal spending has contributed to a significant backlog in critical deferred maintenance estimated at $350 million. As a result, the System is not adequately protecting over $2.2 billion of physical assets. Since 2007 the System has worked with the campuses to implement a more disciplined approach to budgeting and funding capital investments by phasing in full budgeting for depreciation. Specific goals state that E&G depreciation will be fully budgeted by FY2016 and that Auxiliary Enterprise depreciation was to be fully budgeted by FY2011. However, fully budgeting for depreciation expense is only a starting point. Budgeting for current depreciation expense only does not generate enough cash to address the $350 million backlog of critical deferred maintenance.

**Sources of Operating Revenue:**
The two largest sources of operating funds are net tuition revenue and E&G State appropriation. Currently net tuition revenue (tuition and fee charges, less financial aid) represents 40% of unrestricted revenue sources and the State appropriation represents 34%. Dining and residence
revenue represents 12% of unrestricted funding and other auxiliary sales and services contribute 9%.

The Current Trend MYP assumes that the E&G State Appropriation allocated to the System is flat (0% increase). In FY2011, E&G State Appropriation funds represent 34% of the System’s operating budget. However, with costs of operations increasing at an average rate of 3% annually over the next five fiscal years, this level of support is projected to decline to 29% by FY2016. If the System received a 4% increase in State Appropriation annually through FY2016, it would have a major impact on keeping tuition affordable and closing the structural gap as E&G State Appropriation would represent 35% of the System’s operating by FY2016.

Student revenue is comprised of tuition and fees, and auxiliary dining and residence revenue. This analysis focuses on net student revenue (less financial aid). Net student revenue currently represents 52% of the current FY2011 budgeted revenues. As a flat State Appropriation becomes a smaller component of funding, student revenues are projected to grow to 57% net of aid by FY2016. This trend shows a greater cost of education shifting to students and their families. Although the Current Trend MYP increases tuition 5% or less, annually (with corresponding increases in financial aid), enrollment trends limit the growth of tuition revenue. Additionally, the System will have to pay particular attention to price sensitivity as a 5% annual increase in tuition may not be sustainable over time.

DYNAMIC TRENDS
Ms. Wyke explained that a more dynamic model would seek to improve the salary and wages component of employee compensation over time and strive to control the cost of health care by achieving manageable increases. If the System changes the assumptions in the MYP to incorporate the health care savings goals of the Task Force and to provide a 2% annual cost of living increase, the MYP results in a $42.5 million gap by FY2016. The following three possible financial scenarios under the Dynamic Trend are options to provide a path for a balanced projection for FY2016.

Scenario I:
Scenario I utilizes the System’s recently submitted biennial funding request for a 4% increase in Appropriation and, in turn, promises a 3% cap on future tuition increases. This revenue scenario reduces the $42.5 million gap by $18.3 million in FY2016. Since 2007, the System has reduced its workforce by 318 full-time equivalents (FTE), or nearly 6%. While this has been a challenging undertaking where individual institutions have struggled to maintain services and quality – there are still opportunities to employ greater efficiencies across institutional lines that would both ease the current downsizing challenges and allow for greater workforce reduction. If a 4% reduction in the workforce were instituted over the next five years, approximately 200 FTE would be eliminated and it would save an additional $17.2 million in FY2016. If the System could defy the demographic shift and retain and attract more students, a 3.5% increase over current enrollment projections would yield an additional $7 million in revenue in FY2016. These strategies result in a balanced budget for FY2016 and, while challenging, represent the best scenario for a sustainable future.

Scenario II:
Scenario II also uses the recently submitted biennial funding request for a 4% increase in Appropriation and promises a 3% cap on future tuition increases. This reduces the $42.5 million gap by $18.3 million in FY2016. However, in lieu of greater workforce reductions, this strategy forgoes the 2% annual cost of living increase and instead replaces it with a variable COLA funded...
entirely by achieving the savings goal of the Task Force. Savings would be applied to cost of living increases equal to 0.5% in FY2012 and FY2013, 0.75% in FY2014 and FY2015, and 1.0% in FY2016. This strategy reduces the gap by an additional $22.4 million in FY2016. A more moderate enrollment increase of just 1% closes the gap by providing an additional $2 million in revenue in FY2016. While this scenario balances the budget in FY2016, it neither provides adequate salary and wage compensation to sustain a talented workforce in the future, nor does it harness the opportunities for collaboration and efficiencies.

Scenario III:
Scenario III regrettably assumes no assistance from the State in improving the Appropriation to the System. Therefore, this scenario utilizes the 5% or less annual increase in tuition and flat State Appropriation through FY2016. This scenario also replaces the 2% COLA with the variable COLA funded entirely by achieving the savings goal of the Task Force. This strategy further reduces the $42.5 million funding gap by $22.4 million in FY2016. This scenario also slows the goal of fully funding depreciation to achieve only 75% of full funding for E&G infrastructure by FY2016. This strategy reduces the gap by $5.4 million in FY2016. Finally, a 3.5% workforce reduction, at the lower average compensation rate used in this scenario, closes the gap by providing savings of $14.7 million in FY2016. While this scenario also balances the budget in FY2016, its resulting trend points towards less State support and greater student and family contributions. While current evidence suggests a 5% increase in tuition will not adversely affect enrollment, this may not be sustainable over the five year period. It diminishes our ability to address the backlog of capital renewal on our campuses and does not provide adequate salary and wage compensation to attract and retain a talented workforce in the future.

Chancellor Pattenaude commended Ms. Wyke and her staff for completing a very difficult project. A great deal of work went into the development of the Multi-Year Financial Plan and it is appreciated. Trustee Wishcamper commented that the Board needs to understand how to interact with management to deal with this set of financial matrices so it is clearer what variables have the most significant impact. The System is at a turning point with the past several years cutting costs and making the organization more efficient. The System is now at a point of diminishing returns with cutting costs. He stated that the System should focus on the variables that the System has the most control over, particularly the revenue side of the financial situation and creating greater efficiencies and productivity within the System. Trustee Fournier, on behalf of the Finance/Facilities Committee, thanked Ms. Wyke and her staff for their work to develop the Multi-Year Financial Plan.

**Annual Financial Report FY2010.** Ms. Tracy Elliott, Director of Finance and Controller, reviewed the Annual Financial Report for FY2010. The University of Maine System ended FY2010 with Income Before Other Changes in Net Assets of $36.5 million and with an increase in Net Assets of $55.7 million. As a result, Total Net Assets increased 8.5% to $707 million as of June 30, 2010. Of the $55.7 million increase in Net Assets, UMS experienced a positive change in Unrestricted Net Assets of $44 million. This change was possible largely because of increases in tuition rates, $10.7 million in operating investment returns, and extraordinary efforts throughout the System to cut expenses.

Other significant financial highlights for the year ended June 30, 2010 include:
- On an FTE basis, Fall 2009 student enrollment increased less than 1% to 23,711 while on a Headcount basis student enrollment fell less than 1% to 32,340.
• UMS had a 6.0% weighted average increase in undergraduate in-state tuition and fees and a 4.7% weighted average increase in room and board rates in FY2010.

• The FY2010 weighted average student comprehensive cost of education for in-state, undergraduates is $16,431, or an increase of 5.3% from FY2009. The weighted average comprehensive cost for out-of-state, undergraduates is $29,211 or a 6.2% increase from FY2009.

• Noncapital State appropriation revenue declined 2.0% from $194 million in FY2009 to $190 million in FY2010.

• Total cash gifts (capital, endowment and operating) were $17 million in FY2010, down from $24 million in FY2009. The decline is primarily due to the significant contribution of nearly $8 million in FY2009 by the USM Foundation for construction of the Wishcamper Center and the Osher Map Library.

• The financial markets rallied for most of FY2010 with the Managed Investment Pool (including Endowments) experiencing an 11.5% net of fees return compared to -15.7% for FY2009. The UMS and affiliates’ pooled endowment funds totaled $104 million as of June 30, 2010 compared to $95 million at June 30, 2009.

• Endowment and other investments for the System and its component units (i.e., The University of Maine Foundation and The University of Maine Pulp and Paper Foundation) total $261 million as of June 30, 2010, an increase of $22 million from 2009.

• UMS experienced operating investment gains of $10.7 million in FY2010 or 5.6% compared with FY09’s return of -1.6%.

• Total notes and bonds payable were $201 million as of June 30, 2010, declining $8 million from the prior year.

• Capital asset additions, financed primarily by UMS revenue bonds, state capital bonds, and gifts, totaled $28 million in FY2010 as compared to $53 million in FY2009. Major construction in FY2010 included UM’s Advanced Engineered Wood Composites Center Expansion and Aubert Hall Lab Updates; UMF’s Emery Arts Center; and UMFK’s Powell Hall Renovations.

On a motion by Trustee Hood, which was seconded by Trustee Mitchell, the Committee agreed to forward the recommendation to approve the FY2010 Annual Financial Report to the Consent Agenda.

**Nutting Hall Renovation and Renewal, UM**. Trustee Fournier explained the proposal from UM for a $3.75 million of the General Obligation bond passed by Maine’s voters in June 2010 to improve Nutting Hall’s building systems, structure and envelope. In 2008, UM had a building evaluation and investment grade energy audit performed. These confirmed the need for building envelope improvements and heating and ventilating system upgrades including control systems to improve operational costs and energy efficiency.

On a motion by Trustee Murphy, which was seconded by Trustee McCarthy, the Committee agreed to forward the recommendation to the Consent Agenda.

**Alfond Arena Renovation and Renewal, UM**. Trustee Fournier explained the UM request for Board approval for a $4,850,000 renovation and renewal project for Alfond Arena. Recently, UM commissioned a study of Alfond Arena to identify building deficiencies and determined the structure’s remaining useful life. The study concluded that the building is structurally sound and generally in good condition; however, several capital renewal issues were identified as needing
attention. These include installation of a dehumidification system, replacement of 34 year old ice-making system, chiller, and original mechanical ventilation equipment, renovation of seating area to correct inconsistent tread height and depths for original construction to meet current safety codes; replace a 34 year old emergency backup generator; modernize various life safety and fire alarm systems; improve the sound system; improve areas of flooring; and replace worn-out dasher boards and glass.

The Harold Alfond Foundation has generously provided a $3,500,000 grant for the improvements. UM has also received a $300,000 grant from Efficiency Maine for improvements to mechanical systems that will lead to improved energy efficiency and UM will raise the remaining amount of $1,050,000 from private donors. A portion of the work may be completed this year. The remainder of the work will be designed between now and March 2011 with planned major construction between May and August of 2011.

On a motion by Trustee McCarthy, which was seconded by Trustee Mitchell, the Committee agreed to forward the recommendation to the Consent Agenda.

**Lease of Klahr Center to HHRC, UMA.** Trustee Fournier explained the request from UMA for the execution of a 99 year lease, with an additional option of 99 years, of the Michael Klahr Center to the Holocaust and Human Rights Center of Maine (HHRC). The original agreement between UMA and HHRC required that the UMA administer the construction of the Center and be responsible for the operations and maintenance of the facility. In addition, the building is to be owned by UMA and leased to the HHRC for its use. HHRC in return would allow UMA to have access to the facility for University classes and other events. HHRC as a tenant in a UMA building is responsible for generating its own operating budget. UMA & HHRC both needed to formalize the HHRC’s continued occupancy of the Center through a fully executed lease.

On a motion by Trustee Murphy, which was seconded by Trustee Mitchell, the Committee agreed to forward the recommendation to the Consent Agenda.

**Folsom/Pullen Classroom Renovation Phase II, UMPI.** Trustee Fournier explained UMPI’s request to proceed with a $2,025,000 Phase II renovation for UMPI’s primary classroom facility in the Folsom/Pullen building to improve energy efficiency, improve the teaching/learning environment, and integrate alternative energy systems. Phase II includes rehabilitation and renewal of classroom space, mechanical systems, building infrastructure, and installation of energy efficient windows. The project will also include installation of a solar/photovoltaic system that will be incorporated into the existing energy efficient heat pump and a new wood based boiler system to promote use of local renewable energy resources. UMPI will use the new systems as a teaching environment and will share the information with the community and public. Funding for the project will be $1,550,000 in Federal/State grants and $475,000 in State Bond funds.

On a motion by Trustee Mitchell, which was seconded by Trustee McCarthy, the Committee agreed to forward the recommendation to the Consent Agenda.

**Creation of School of Nursing Simulation Center, USM.** Trustee Fournier explained the request from USM to expend $767,250 of grant funding received from the Health Resources and Services Administration to create a Nursing Simulation Center in Masterton Hall on the Portland campus. The project would renovate and expand an existing two bed nursing simulation laboratory to a four bed state-of-the-art Nursing Simulation Center. The Nursing Simulation Center will be designed to
replicate healthcare environments giving USM’s nursing students the opportunity to gain hands-on simulation experience. The expanded size of the Center will accommodate the increasing number of nursing students in a way that better prepares them for the nursing workforce.

On a motion by Trustee Goodman, which was seconded by Trustee Murphy, the Committee agreed to forward the recommendation to the Consent Agenda.

**Establishment of a Science Technology Research Center, USM.** Trustee Fournier explained the request from USM to expend $850,000 of grant funding received from the US Small Business Administration to establish a Science Technology Research Center in the Bioscience Building C Wing on the Portland campus. The Center will increase the capacity to serve students enrolled in science and biology curricula, engage students in faculty-mentored research as a means to promote science based careers, and attract talented, research active teaching faculty.

On a motion by Trustee Mitchell, which was seconded by Trustee Goodman, the Committee agreed to forward the recommendation to the Consent Agenda.

**Capital Project Status Report.** Trustee Fournier briefly reviewed the Capital Project Status Report. Currently the UMS has 16 capital projects underway and all of the projects are on track or have had only minor changes.

**Miscellaneous.** Trustee Fournier stated that the Finance/Facilities Committee met on November 2, 2010. At this meeting the Committee agreed to develop a more efficient, streamlined process of reviewing projects. He proposed three questions to the Committee, which are as follows:

- Is the Committee willing to meet off-cycle more frequently to review Committee agenda items such as capital projects?
- Would the Committee be interested in a two-step process to allow more time for discussion and development of information?
- Would it be appropriate for the Committee to request from the Board final decision making authority for certain finance and facilities items based on defined criteria beyond just dollar amounts leaving for the whole Board a higher level of scrutiny on fewer items?

The Committee discussed these questions and decided it would be beneficial to meet more frequently to review agenda items, that a two-step process would allow more time for discussion, and the Committee will request final decision making authority from the full Board for certain finance and facilities items. The Committee will need to develop the criteria for the increased authority level.

Adjournment.

Ellen Doughty for
J. Kelley Wiltbank, Clerk