



The Board of Trustees of Oregon State University

Regular Meeting of the Finance & Administration Committee

January 18, 2018
Horizon Room, Memorial Union
Oregon State University
Corvallis, Oregon

MINUTES

Committee Members Present: Mark Baldwin, Rani Borkar (*ex officio*), Julia Brim-Edwards (*phone*), Darry Callahan, Mike Green (*ex officio*), Kirk Schueler (*chair*), Mike Thorne (*vice chair*)

Other Trustees Present: Mike Bailey, Patty Bedient, Michele Longo Eder, Paul Kelly, Preston Pulliams, and Ed Ray

University Staff Present: Ron Adams, Jennifer Almquist, Anita Azarenko, Sherm Bloomer, Susan Capalbo, Steve Clark, Debbie Colbert, Ed Feser, Becca Gose, Cindy Sagars, and Marcia Stuart

1. Call to Order/Roll/Declaration of a Quorum

Committee Chair Kirk Schueler called the meeting to order at 10:33 a.m., asked the assistant board secretary to call the roll, and noted a quorum.

2. Vice President for Finance and Administration Report

Vice President for Finance and Administration and Chief Financial Officer Mike Green started his report by noting the Board's request to continue to hear updates on anticipated federal tax reform implications. Green provided an update on steps taken since completing an external review of the university's human resources functions. He shared that efforts were underway to implement recommended organizational changes and process improvements. Green added that this will include hiring a permanent Chief Human Resources Officer.

3. Consent Agenda

a. Minutes of the September 7, 2017 Finance & Administration Committee Meeting

b. FY2018 Q1 OSU Operating Management Report

c. FY2018 Q1 Investment Reports

d. Internal Bank Annual Report

President Ed Ray noted that the FY2018 Q1 Oregon State University Investment Report included in TAB J reported that the OSU Foundation's Endowment Pool underperformed its benchmark during the quarter, and he recommended that the OSU Foundation Vice President and Chief Financial Officer be invited back to meet with the committee to discuss their management of the OSU Endowment Assets. Secretary Debbie Colbert reminded trustees that the Board's work plans for the year included at least one full report from the OSU Foundation. Following discussion, a motion was made and seconded to approve the items on the consent agenda. The motion carried.

4. Action Items

a. Capital Project Budget Amendment

Schueler asked Green to introduce this item. Green said that staff propose that the Finance & Administration Committee recommend to the Board that it increase the capital budget for the Oregon Forest Science Complex. He then introduced Anita Azarenko, associate vice president for university facilities, infrastructure and operations. Azarenko reminded trustees that the Oregon Forest Science Complex comprises the Advanced Wood Products Lab (AWP), the Field Instrument Room (FIR), and the George W. Peavy Forest Science Center (Peavy). In June 2016, the Board approved a total project of \$68.0M for the entire complex, with \$30M from state-paid bonds, \$33M from gifts, and \$5M in OSU funds. Azarenko said that subsequent to that approval, the total project costs for the Peavy portion were adjusted to \$68.0M, which include \$51.5M in direct construction costs and \$16.5M in indirect owner costs. She explained that this is due to the construction of the Oregon Forest Science Complex during a time of abnormally high economic competitive stresses as well as project delays. As a result, staff proposed an amendment to add \$11.5M in OSU funds, bringing the project total for the full complex to \$79.5M. Azarenko explained that \$11.5M was needed to complete the AWP and FIR, noting that the College of Forestry will be covering the cost through an internal bank loan. The loan will be repaid using assets including OSU Foundation sources and funds obtained from an accelerated harvest of over-mature timber on the Blodgett Tract. In response to a question from Schueler, Azarenko said that no other plans had been identified for the timber and that harvesting now would help create the opportunity to implement more successional harvesting strategies for the future. Trustee Mark Baldwin asked whether the timber was valued as an asset and how harvesting would affect the university's net position. Green said he did not immediately have available information about how the timber was valued, but he explained that the valuation would consider that the timber is being held for both research and income-producing purposes. He also noted that harvesting would simply shift one asset for another.

During the discussion that followed, Trustee Rani Borkar asked whether staff had identified areas of further potential risk. Azarenko said that the university worked with a consulting group in August 2017, and the report they prepared has been guiding the university's planning efforts; however, she noted that a guaranteed maximum price (GMP) would likely not be set for the AWP and FIR until March. Trustee Mike Thorne asked what strategies were in place to minimize escalation before the GMP is set and whether the project budget amendment would more appropriately come before the Board at that time. Green described efforts to begin engaging subcontractors, and he noted that the university had built its own contingency into the budget, which led staff to feel confident in presenting the amendment now. Azarenko added that the university was also pursuing opportunities for value engineering without affecting the program for the space. Trustee Patty Bedient expressed concern about the significant cost overruns on the project, and while she acknowledged the recent trend in escalating construction costs as a factor, she asked whether there were other factors that contributed to the overrun and, if so, what lessons staff learned from this experience that would inform future projects. Green affirmed that escalating construction costs were one reason for the increase, and he cited examples of increased projects costs for others in the state. Azarenko also provided an overview of some of the project delays, adding that the university has learned from the experiences and taken steps to improve processes across every stage of its capital project management for this and future projects. Ray

pointed to the unique construction techniques used in the project, which also impacts the project costs and timelines.

Following discussion, a motion was made and seconded that the Finance & Administration Committee recommend to the Board that it increase the capital budget for the Oregon Forest Science Complex to \$79.5M. The motion carried.

b. Ten-Year Business Forecast (includes FY2017 Financial Statement Analysis & Financial Metrics)

Schueler reminded trustees that the university's Ten-Year Business Forecast combines the university's long-term operating plan together with its long-term capital plan. He then asked Green and Sherm Bloomer, director of budget and fiscal planning, to present this item. Green said the purpose of the forecast is to identify long-term trends in the university's finances that support or jeopardize the goals of the Strategic Plan. He added that looking this far ahead provides the opportunity to consider the long-term impacts of current decisions, such as tuition rates, and take corrective action or plan for additional investments if necessary.

Green then presented an update on the financial health of the university, including comparison of key financial metrics over time. He noted that the update on the financial metrics were presented with the impact of Governmental Accounting Standards Board (GASB) Statement No. 68 and No. 71 removed. Green reported that FY 2017 performance is within the Board-approved ranges for all of the metrics except the Debt Service Coverage Ratio. Green summarized the university's overall financial position as strong, noting low leverage and adequate reserves. He said the challenge remains generating sufficient net income to see the university's wealth continue to grow and to cover capital costs; however, efforts are underway to improve those metrics over time. In response to a question by Ray about the university's debt service coverage, which he noted was lower than the limit previously set by the former Oregon University System, Green said that a low ratio is not necessarily positive if it means the university is not making strategic investments simply to hold debt low; however, if the natural result of strategic decisions is low leverage, it can generally be seen as positive. Green added that making the decision to set aside operating revenues in order to invest in capital may be difficult in the short-term, but it would benefit the university in the long-term because it reduces both the backlog and increase in deferred maintenance, and it strengthens the university's balance sheet. Ray noted that the estimated total amount appropriated for capital renewal for all seven public universities combined is only \$40M for each biennium, and Oregon State University's approach to grow its own capacity to address this need will exceed the support the state is able to provide. Schueler asked whether that strategy might negatively affect the university's future capital requests, and Green said while there is a risk, it can also strengthen the university's future requests by demonstrating the commitment to invest in maintenance. Azarenko added that the Higher Education Coordinating Commission was working on a capital prioritization rubric, and the draft included substantive points for matching funds, and the money the university has set aside for capital improvement may receive positive consideration. Baldwin expressed his support for the university's efforts to develop a strategy to address deferred maintenance needs, and Schueler also thanked Green for his leadership. Green said the provost was an important partner in setting the priority for investing in capital renewal. Next, Green spoke about the decision to present the ratios without the

impact of GASB 68 and 71, which relate to pension accounting and reporting effective for FY2015. He noted that the operating ranges were set by the Board without GASB 68 and 71, and staff recommend continuing to monitor financial metrics against those ranges until there are five years of data and the Board can more fully consider whether it wants to modify the operating ranges. Green added that the Ten-Year Business Forecast does include the required payments toward the university's net pension liability.

Next, Bloomer presented the Ten-Year Business Forecast. He started by reiterating the purpose of the ten-year forecast and emphasizing the opportunity to look far enough ahead to take corrective action or to plan for additional investments, and to carefully consider the long-term impacts of current programmatic and financial decisions. Bloomer then provided an overview of the critical assumptions that were used in building the forecast. In response to a question by Thorne, Bloomer noted that the assumptions take into account the university's strategic plans at an institutional level. As an example, Bloomer said that while the forecast assumes enrollment growth and accounts for personnel expenses associated with that growth, it does not specify where that growth will occur thus allowing colleges to work on strategic growth and then map their efforts to the institutional plan. Trustee Mike Bailey asked whether the forecast accounted for the cost associated with realizing the assumption of 33% non-resident undergraduates in Corvallis by FY2025, and Bloomer said that it did. Trustee Michele Longo Eder asked whether the assumption about the increase in institutional financial aid would be sufficient to cover students' financial needs. Bloomer said the reason it was listed as an assumption is to prompt further discussion about what the percentage of institutional financial aid should be and how the university will realize whatever targets it sets. Ray added that the ten-year forecast provides the opportunity to set programmatic and financial goals across broad categories and then to revisit those goals as the forecast is updated. Trustee Darry Callahan suggested that trustees consider what assumptions they want to explore in further detail at future committee meetings, noting that many of the assumptions presented will not be realized without strategic investments. Lastly, Bloomer showed how the forecast can be used to project the outcomes of assumptions about tuition rates, enrollment levels, and state funding dollars. Following the presentation, trustees discussed that rather than recommending that the Board approve the Ten-year Business Forecast, the committee could indicate its acceptance. Committee members agreed this more clearly addresses the fact that they are not approving the assumptions that were used in developing the forecast; rather, they are accepting the forecast as a tool that helps validate that management decisions are moving the institution in the direction the Board wants to go. A motion was made and seconded to recommend that the Board accept the Ten-year Business Forecast. The motion carried.

5. Education/Discussion Items

a. Preliminary FY2019 Tuition Scenarios and Education and General Budget Planning

In introducing this item, Schueler reminded trustees that last year they asked university leadership to broaden their efforts to engage with students and other members of the university community to get their input on the impacts of tuition rate changes. He expressed appreciation for staff's efforts to increase the tuition outreach efforts even more this year. Schueler said the purpose of the discussion was to consider several

possible tuition scenarios, noting that the committee and the full Board of Trustees will take action to set FY2019 tuition rates in April. He then asked Green and Bloomer to present this item.

Green said that discussion on budget planning and tuition recommendations for the 2018-19 fiscal year have been underway since September 2017. These have included discussions by the University Budget Committee, university leadership, the Faculty Senate Budget and Fiscal Planning Committee, and the Student Budget Advisory Council. Green said that although staff are confident that the engagement process is robust, they will continue to look for ways to expand outreach to students and opportunities to involve them in the process. Next, Bloomer provided an overview of the preliminary tuition and fee planning discussions, beginning with the three major drivers of costs and revenues: increases in rates for continuing the present level of programs; costs and revenues associated with enrollment growth; and costs or revenues associated with discrete decisions. He noted that there are two things that make the finances of higher education in Oregon different from those of some other enterprises. The first is the average inflation rate for the university tends to be higher than common measures of general inflation like the Consumer Price Index (CPI). On average, OSU's local inflation has been 1.2 percentage points higher than CPI. Bloomer said a large portion of the university's costs are for personnel expenses, and the drivers of the elevated inflation are salary and benefits rates. The second factor is the level of state funding per resident student. Bloomer reported that in FY2000, state funding was 52% of the Corvallis Education & General (E&G) budget, with tuition providing 29%. In the current year, tuition and fees account for 67% of E&G revenues for the Corvallis campus, and state funding provides 21%. Bloomer reminded trustees that they had noted after the previous year's discussions that it was helpful to discuss undergraduate tuition in reference to more than one scenario. He said that last year's discussion used scenarios in reference to different levels of state funding, and the discussions to date have considered scenarios in reference to investments or reductions that would be made at various tuition levels. Bloomer then presented three tuition scenarios, which illustrated the impacts of different tuition rates on the university's overall budget. He said the scenarios centered on a balanced budget approach bracketed by lower and higher rates with specific possible results identified. Schueler asked about Scenario A, which considered a 1.5% increase in resident undergraduate tuition and a 2% increase in non-resident undergraduate tuition and would require reductions from the planning budget of about 0.7-0.8% of projected expenditures. Bloomer clarified that the reductions would be necessary to absorb what would be an anticipated budget deficit of \$4.1M. Bloomer said the scenarios had been the focus of the discussions on budget planning and tuition recommendations, and the goal was to recommend tuition proposals to the provost in February. The proposals will be advertised to the university community for comment, and the final proposals will be brought to the Board at the April meeting. In response to a question from Ray about student engagement in the process, Bloomer said he has worked to increase outreach and engagement with a broad cross-section of students, including those who oppose any increase in tuition. Trustee Preston Pulliams expressed his support for this approach, noting that some students at the previous evening's student-trustee roundtable discussion sought greater engagement with the process. Bloomer noted the need to balance concerns expressed by students about short-term needs with a multi-year view. He then presented various scenarios indicating the ways tuition changes in one year compound and have consequences in the long-term planning. Lastly, Bloomer shared suggestions emerging from discussions by the Student

Budget Advisory Council and the University Budget Committee about strategies for planning and discussing tuition increases, moderating the impact of tuition increases on students, and finding alternative revenues to decrease the need for tuition increases.

Following the presentation, Schueler asked whether the portion of the previous year's increase to resident undergraduate tuition that had been dedicated to need-based financial aid would continue, and Bloomer confirmed that the growth in aid would be maintained. In response to a question by Thorne about the full time educational costs for attending the university, Bloomer said the Office of Financial Aid provides an estimate, which is approximately \$26,796 for the year in 2018-19 for a resident undergraduate student living on campus. Bloomer noted that \$11,070 of this is for tuition and fees, and Thorne said that it will be important to continue to consider ways to manage increases to overall costs. Bloomer noted that University Housing and Dining Services works to keep any rate increases the same as the general inflation. Trustees also discussed the strategy of considering whether some kind of four-year guaranteed rate increase could be manageable. Though some committee members expressed hesitation about guaranteeing tuition rates, several noted the benefit of transparent conversations with the university community around anticipated levels of annual increases, barring uncertainties. Committee members also discussed details around how institutional financial aid can be structured and targeted to most effectively help students in need, even those who may not qualify for traditional types of financial aid.

6. Adjournment

With no further business proposed, Chair Schueler adjourned the meeting at 9:20 a.m.

Respectfully submitted,



Jennifer M. Almquist
Assistant Board Secretary