AGENDA

COMMITTEE ON FINANCE

Meeting: **1:15 p.m., Tuesday, July 17, 2012**
Glenn S. Dumke Auditorium

William Hauck, Chair
Roberta Achtenberg
Kenneth Fong
Margaret Fortune
Steven M. Glazer
Henry Mendoza
Lou Monville
Jillian Ruddell
Glen O. Toney

Consent Items

Approval of Minutes of Meeting of May 8, 2012

Discussion Items

1. Approval to Issue Trustees of the California State University, Systemwide Revenue Bonds and Related Debt Instruments for Various Projects, *Action*
2. Report on the Support Budget 2012-2013 and 2013-2014 Fiscal Years, *Information*
3. Strategies to Address the Structural Deficit in the California State University Support Budget, the Contingency of a $250 Million Trigger Cut, and a Possible Tuition Fee Roll-Back, *Information*

COMMITTEE ON FINANCE

Approval to Issue Trustees of the California State University, Systemwide Revenue Bonds and Related Debt Instruments for Various Projects

Presentation By

George V. Ashkar
Assistant Vice Chancellor
Financial Services

Summary

This item requests the Board of Trustees to authorize the issuance of Systemwide Revenue Bonds and the issuance of Bond Anticipation Notes (BANS) to support interim financing under the commercial paper program of the California State University in an aggregate amount not-to-exceed $106,975,000 to provide financing for two campus projects and refinancing of certain outstanding auxiliary organization bonds. The board is also being asked to approve resolutions relating to these financings/refundings. The long-term bonds will be part of a future Systemwide Revenue Bond sale and are expected to bear the same ratings from Moody's Investors Service and Standard and Poor's as the existing Systemwide Revenue Bonds.

The projects are as follows:

1. Channel Islands North Campus Parking Lot Phase 1

During the approval of the 2008-09 Nonstate Capital Outlay program, the north campus parking lot phase 1 project was approved as part of the entrance road project. The current project being considered for financing approval consists of a surface parking lot on acquired land north of the campus involving 4.75 acres. The project will provide approximately 550 parking spaces and will add needed space to meet parking demand for students, faculty, and staff. The project will also include lighting and landscaping.

The not-to-exceed par value of the proposed bonds is $2,040,000 and is based on a total project budget of $2,211,000 with a parking program reserve contribution of $300,000. Additional net financing costs (estimated at $129,000) are to be funded from bond proceeds. The project is being supported by a two-step increase in parking fees approved by the president leading to an increase of $50 per year for 2012-13 (with a total fee of $320) and an increase of $40 for 2013-14. The project is scheduled to start construction in August 2012 with completion in November 2012.

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The following table summarizes key information about this financing transaction.

Not-to-exceed amount	$2,040,000
Amortization	Approximately level over 25 years
Projected maximum annual debt service	$146,459
Projected debt service coverage including the new project: Net revenue – Channel Islands pledged revenue programs: [1] Net revenue – Projected for the campus parking program:	 1.40 1.45

1. Combines 2010-11 information for all campus' pledged revenue programs and projected 2013-14 operations of the project with expected full debt service. Does not include any debt, revenues or expenses related to the Channel Islands Site Authority.

The not-to-exceed amount for the project, the maximum annual debt service, and the ratios above are based on an all-in interest cost of 5.33%, reflective of adjusted market conditions plus 100 basis points as a cushion for changing financial market conditions that could occur before the permanent financing bonds are sold. The financial plan includes level amortization of debt service, which is the CSU program standard. The campus financial plan projects a program net revenue debt service coverage of 1.45 in the first full year of operations in 2013-14, which exceeds the CSU benchmark of 1.10. When combining the project with 2010-11 information for all campus pledged revenue programs, the campus' overall net revenue debt service coverage for the first full year of operations is projected to be 1.40, which exceeds the CSU benchmark of 1.35.

2. Pomona Recreation Center

In September 2010, the board approved the amendment of the non-state capital outlay program and in March 2011 it approved the schematics for the Pomona recreation center project. The project will construct a three-story (approximately 120,000 gross square foot) facility that will include a gymnasium, a multi-activity court gymnasium, an elevated jogging track, weight/fitness room, rock climbing wall, recreation and lap pools, sports club spaces, multi-purpose rooms, wellness center, social lounge, juice bar, locker rooms, and Associated Students, Inc., administrative offices.

The not-to-exceed par value of the proposed bonds is $65,890,000 and is based on a total project cost of $56,950,000 with a student union program reserve contribution of $350,000. Additional net financing costs (estimated at $9,290,000) are to be funded from bond proceeds. The campus anticipates a construction start of July 2012 with construction completion in July 2014. A fee increase was approved by the campus based on an alternative consultative process and modified referendum. The student body center fee will increase by $420 per year, thereby increasing the fee to $717 effective 2014-15.

The following table summarizes key information about this financing transaction.

Not-to-exceed amount	$65,890,000
Amortization	Approximately level over 30 years
Projected maximum annual debt service	$4,430,470
Projected debt service coverage including the new project: Net revenue – All Pomona pledged revenue programs: [1] Net revenue – Projected for the campus student union program[1]:	 2.04 1.25

1. Combines 2010-11 information for all campus' pledged revenue programs and projected 2015-16 operations of the project with expected full debt service.

The not-to-exceed amount for the project, the maximum annual debt service, and the ratios above are based on an all-in interest cost of 5.56%, reflective of adjusted market conditions plus 100 basis points as a cushion for changing financial market conditions that could occur before the permanent financing bonds are sold. The financial plan includes level amortization of debt service, which is the CSU program standard. The campus financial plan projects a program net revenue debt service coverage of 1.25 in the first full year of debt service in 2015-16, which exceeds the CSU benchmark of 1.10. When combining the project with 2010-11 information for all campus pledged revenue programs, the campus' overall net revenue debt service coverage for the first full year of operations is projected to be 2.04, which is exceeds the CSU benchmark of 1.35.

3. San Diego State University Research Foundation – Student Housing Refunding

San Diego State University Research Foundation (the "Foundation"), a recognized auxiliary organization in good standing at San Diego State University, seeks Board of Trustees approval for the refunding of an existing stand-alone auxiliary organization bond issue. At the time of this write-up, the Foundation's board of directors is expected to adopt a resolution authorizing the bond refunding at a special meeting on or about July 6, 2012.

The project will be the current refunding of $9,035,000 in outstanding principal on the Foundation's Auxiliary Organization Student Residence Revenue Bonds, Series 2001, which were originally issued at a par amount of $11,000,000 to fund the acquisition and improvement of a student apartment complex. The size of the proposed refunding is at a not-to-exceed par amount of $8,500,000, and is estimated to generate a net present value savings of approximately $908,673, or 10% of the refunded bonds. The not-to-exceed amount and the net present value savings are based on a current all-in true interest cost of 3.75%, which is reflective of market conditions as of June 2012, and an average remaining bond maturity of approximately 11 years.

Assuming both refunding discussed herein proceed, for #3 Student Housing Refunding and #4 Office Building Refunding, the loan agreement for the refunding of the stand-alone 2001 bonds will be secured by a general obligation pledge of the Foundation's unrestricted revenues. In the event the Office Building Refunding described below does not proceed or proceeds only in part, the loan agreement for the refunding of the stand-alone 2001 bonds will be secured by a pledge of the Foundation's unrestricted revenues from the Student Housing Refunding and the Piedra del Sol Student Housing Project. This refunding will have a minimal impact on systemwide debt capacity, as this auxiliary debt is already included in overall CSU debt capacity calculations.

4. San Diego State University Research Foundation – Office Building Refunding

San Diego State University Research Foundation (the "Foundation"), a recognized auxiliary organization in good standing at San Diego State University, seeks Board of Trustees approval for the refunding of an existing stand-alone auxiliary organization bond issue. At the time of this write-up, the Foundation's board of directors is expected to adopt a resolution authorizing the bond refunding at a special meeting on or about July 6, 2012.

The project will be the current refundings of $32,080,000 in total outstanding principal on the Foundation's Auxiliary Organization Revenue Bonds, Series 2002A (tax-exempt) and 2002B (taxable), which were originally issued at total par amount of $34,660,000 to refund certain outstanding obligations of the Foundation, and fund the construction of certain facilities, including a parking garage and research facility. The total size of the proposed refundings is at a not-to-exceed par amount of $30,545,000, and is estimated to generate a net present value savings of approximately $1,021,527, or 3.18% of the refunded bonds. The not-to-exceed amount and the net present value savings are based on a current all-in true interest cost of 5.19%, which is reflective of market conditions as of June 2012, and an average remaining bond maturity of approximately 16 years. The savings also assume that Series 2002A are refunded with tax-exempt and taxable refunding bonds in order to preserve flexibility to sell certain properties in the future. (Series 2002B are to be refunded with taxable refunding bonds.) In the event circumstances regarding the possible future sale of assets changes before the time of the bond sale and all Series 2002A bonds are fully refunded with tax-exempt bonds, savings would be increased.

Assuming both refunding discussed herein proceed, the loan agreement for the refunding of the stand-alone 2002 A&B bonds will be secured by a general obligation pledge of the Foundation's unrestricted revenues. In the event the Student Housing Refunding described above does not proceed, or this Office Building Refunding proceeds only in part, the loan agreement for the refunding of the refunded portion of the stand-alone 2002 bonds will be secured by a pledge of the Foundation's revenues received as indirect cost recovery payments relating to research contracts. This refunding will have a minimal impact on systemwide debt capacity, as this auxiliary debt is already included in overall CSU debt capacity calculations.

Trustee Resolutions and Recommended Action

Orrick, Herrington & Sutcliffe LLP, as bond counsel, is preparing resolutions to be presented at this meeting that authorize interim and permanent financing for the projects described in this agenda. The proposed resolutions will be distributed at the meeting and will achieve the following:

1. Authorize the sale and issuance of Systemwide Revenue Bond Anticipation Notes and the related or stand-alone sale and issuance of the Trustees of the California State University Systemwide Revenue Bonds in an aggregate amount not-to-exceed $106,975,000 and certain actions relating thereto.

2. Provide a delegation to the Chancellor; the Executive Vice Chancellor and Chief Financial Officer; the Assistant Vice Chancellor, Financial Services; and the Senior Director, Financing and Treasury; and their designees to take any and all necessary actions to execute documents for the sale and issuance of the bond anticipation notes and the revenue bonds.

Approval of the financing resolutions for the project as described in this Agenda Item 1 of the Committee on Finance at the July 17, 2012, meeting of the CSU Board of Trustees is recommended for:

Channel Islands North Campus Parking Lot Phase 1

Pomona Recreation Center

San Diego State University Research Foundation – Student Housing Refunding

San Diego State University Research Foundation – Office Building Refunding

COMMITTEE ON FINANCE

Report on the Support Budget 2012-2013 and 2013-2014 Fiscal Years

Presentation By

Robert Turnage
Assistant Vice Chancellor
Budget

State Budget Overview

The budget package passed by the legislature and signed by the governor on June 27th is generally consistent with the governor's May revision. It closes an identified gap of $15.7 billion ($6.5 billion larger than the problem identified by the governor's January budget) and rebuilds a $1 billion General Fund reserve. According to the Department of Finance summary, the enacted budget package does this with $8.1 billion in spending reductions, $6 billion of added revenue, and $2.5 billion in loans, transfers and special fees. The key to the state budget is a revised initiative for the November ballot that combines elements of the governor's earlier tax proposal with elements of a prior initiative proposal by the California Federation of Teachers and other groups. This revised initiative would increase income tax rates on higher income taxpayers for seven years, starting with the 2012 tax year, and would increase the state sales tax rate by 0.25 percentage point. The increased sales tax rate would be in effect for four years, from January 1, 2013 through the end of calendar 2016.

CSU Support Budget

Assuming the voters pass the initiative, the enacted budget maintains the current sharply reduced level of state support for the CSU, but avoids further direct cuts. However, the budget also includes a mid-year "trigger cut" of $250 million to the CSU if the tax initiative fails. If this "trigger" reduction takes place, annual state support for the CSU will fall to approximately $1.8 billion, a loss of annual funding of almost $1.2 billion, or 39 percent, from the peak level of state support of nearly $3 billion in the 2007-08 fiscal year. Total state support would be at its lowest point since 1996, despite inflation and despite the fact that the CSU is serving about 95,000 more students.

Given the reductions that have already taken place, the timing of a trigger cut in the middle of the academic year, and the long lead times needed to reduce spending further, the system and its campuses have begun planning on the assumption that the trigger reductions take place. In addition, the campuses are struggling with the lingering effects of the $750 million reduction in state support that took place in the prior fiscal year. Various strategies and options for addressing both of these great budget challenges are discussed in detail in the Finance Committee's next agenda item (agenda item 3).

*Long-term Budget Plan for Higher Education***.** In its higher education chapter, the *Governor's Budget Summary* in January outlined a long-term plan for public higher education that would provide "stable and increasing state funding" starting in the 2013-14 fiscal year, provided the voters pass the governor's tax initiative. Other elements of the proposal, some of which would have taken effect in the 2012-13 fiscal year, presented significant long-term challenges and risks for the CSU. The governor's administration engaged in separate, confidential, discussions with each higher education system, seeking agreements with each system for its "part" of the long-term plan. The issues under discussion were complex and challenging; ultimately, the administration was unable to arrive at agreement with any of the three public systems.

Given the lack of specific agreements to review, the legislature ended up following the Legislative Analyst's Office (LAO) recommendation to approach higher education budgets one year at a time. Of specific interest to the CSU, the legislature followed the LAO recommendation to reject the incorporation of state debt service into university budgets. Also, as a consequence of the discussions between the CSU and the administration, the May revision included a $51.5 million positive adjustment to the CSU budget to cover increased employer rates for pension contributions that were adopted by the Public Employees' Retirement System (CalPERS). This adjustment would have been denied under the changes proposed in the January budget and the CSU would have been forced to pay the higher costs from existing resources.

Health Care Benefit Costs. One major disappointment in the final budget package is the absence of the governor's May revision proposal to make cost-sharing of health care benefits costs a matter to be decided through collective bargaining as opposed to a statutory formula. The May revision proposed the necessary statutory change, justified on a policy basis but also offering a way to responsibly reduce costs in the midst of the CSU's ongoing budget challenges, but the legislature declined to vote on the proposal. As a consequence, the CSU will continue to pay an average of 95 percent of health care benefits premiums pursuant to a statutory formula that no longer applies elsewhere in state government. The CalPERS, which negotiates the health plans and premiums on behalf of all state government, including the CSU, recently announced sharp increases in premiums for calendar 2013. Under the statutory formula, the new premiums will increase annual CSU costs by an estimated $36 million and bring total annual spending on this item to nearly $400 million.

Budget Bill Language Authorizes One-time Transfer from Continuing Education. In the event that the governor's tax initiative is not enacted, budget bill language authorizes the chancellor to transfer balances from the CSU's Continuing Education Revenue Fund (CERF) to mitigate cuts to state-supported instructional programs in the spring term. The total balance that could be moved without harming current extended education commitments is not clear at this point but is estimated roughly at $75 million. It could provide significant relief to the "state-side" of the university in 2012-13, but the relief would be one-time and restricted to that fiscal year.

Cal-grant Changes. The final budget package made various changes to reduce the cost of the Cal-grant program and to focus state resources more effectively. The legislature and governor modified much of the original proposal made in the January budget. As a consequence, most of the changes are directed at for-profit private institutions, and to a lesser extent to private not-for-profit institutions. The single change affecting CSU students was a line-item veto reducing the Cal-grant B access award by $78 (5 percent) from $1,551 to $1,473. This access award is used for books and living expenses. Approximately 50,000 CSU students are affected for the 2012-13 academic year by this change.

State's Offer of a Delayed Buy-out of a Tuition Fee Roll-Back

The most notable new development in the enacted state budget for the CSU is the proposal to "buy out" the already-implemented tuition fee increase for the 2012-13 academic year with an appropriation that would not be operative until the 2013-14 fiscal year, and only then if the November tax initiative is enacted. One of the budget trailer bills (AB 1502) includes separate appropriations of $125 million each to the CSU and the University of California *for the 2013-14 fiscal year*. Two conditions must be met if the CSU wants to access its appropriation next year: (1) the governor's tax initiative must be enacted and (2) the university must choose to reset its tuition fee rates for the 2012-13 academic year back to the levels in effect for the 2011-12 fiscal year.

Further detail and analysis of this feature of the budget package is presented in the Finance Committee's next agenda item.

COMMITTEE ON FINANCE

Strategies to Address the Structural Deficit in the California State University Support Budget, the Contingency of a $250 Million Trigger Cut, and a Possible Tuition Fee Roll-Back

Presented By

Benjamin F. Quillian
Executive Vice Chancellor and
Chief Financial Officer

Ephraim P. Smith
Executive Vice Chancellor and
Chief Academic Officer

Summary

This item explains the process of soliciting input and answering questions from a broad range of University constituents about strategies to address the pending $250 million reduction in the General Fund appropriation and the large structural deficit in the CSU operating budget. In the context of the ideas and suggestions that have been received, staff will proffer specific plans and alternatives for consideration by the Board of Trustees. In addition, a strategy for implementing a contingent roll-back of this year's tuition fee increase—as contemplated by a late development in the state budget process—will be offered for board consideration.

The Consultation Process and Identification of Strategic Solutions

At the request of the board, staff has solicited the input of University constituents to identify a variety of strategies to address the structural deficit in the operating budget and the very serious challenges that will result from the $250 million "trigger" that will be pulled if the governor's tax initiative is not passed in November. The structural deficit, as reported by the campus Chief Financial Officers, is over $130 million and results from limitations in the ability of tuition fee increases and campus spending reductions to fully match the $750 million reduction in the base General Fund appropriation during fiscal year 2011-12.

Executive Vice Chancellors Quillian and Smith have met with the campus Chief Financial Officers, Provosts, Vice Presidents for Student Affairs, and faculty members. In addition, the Executive Vice Chancellors and Vice Chancellor Brooks met with the Systemwide Budget Advisory Committee (SBAC)[1] in May to present various options and solicit input. Many of the

[1] The SBAC is comprised of students, labor leadership, faculty senate representatives, management staff and campus leaders.

options presented to the SBAC had been discussed by the Board of Trustees during its October 2011 retreat. The SBAC meeting was streamed over the web to enable students, faculty, staff and alumni to listen in, make comments and ask questions. Approximately twelve hundred students, faculty, staff and administrators participated in the SBAC webcast. Hundreds of questions and comments were received either during or after the webcast. After duplicative questions were eliminated, those questions and comments have been posted on a newly created Budget Strategies website. The PowerPoint presentation used with the Trustees and the SBAC has been downloaded over twenty-six hundred times from the website.

A second webcast was conducted in June. The format of the second webcast was changed to provide participants from around the system a greater opportunity to submit questions and comments. Dr. Keith Boyum, Professor Emeritus of Political Science and former Associate Vice Chancellor of Academic Affairs, served as moderator. The Executive Vice Chancellors and Vice Chancellor Brooks responded to the questions and comments from the participants. Those questions and comments were recorded, and they will also be posted on the Budget Strategies website.

Strategic Solutions

Numerous obstacles, both political and financial, have made it exceedingly difficult to find solutions that will keep the CSU aligned with its mission to provide a quality education for the benefit of the students and the continued welfare of the state. There is a pressing need to understand that the problem before us goes beyond addressing the possible $250 million trigger. Given the cuts that have recently taken place, the CSU needs to restore over a billion dollars in reduced state support over the next few years. Because the University simply cannot continue to operate in an environment of such great uncertainty, solutions are needed that scale automatically. There must be a clear understanding of the difference between window dressing and truly meaningful strategies. Strategies must be considered in terms of how quickly they can be implemented, how much energy will be expended and how disruptive they will be to students, faculty and staff and the communities we serve. And, given the magnitude of the challenge, there is no single strategy that will be practicable or fair. It is important to avoid placing an undue burden on the students, CSU employees or the state for that matter. In that context, the following strategies are being set forth as paths to be followed.

Fundamental Nature of the Budget Problem

It is useful to think about the budget problem as having two distinct parts: (1) addressing the as-yet-unclosed gap created by prior cuts, and (2) addressing the contingency of the $250 million trigger. A third dimension that emerged late in the state budget process is the possibility of rolling back tuition fee rates to the levels that were in effect in the 2011-12 academic year. This option—which would produce new budgetary challenges of its own—will be explored later in this agenda item.

It is also useful to view the budget problem in terms of two distinct phases: (1) the 2012-13 fiscal year—necessarily reliant on a mix of one-time resources and actions along with phasing-in of ongoing solutions; and (2) the 2013-14 fiscal year and beyond—necessarily requiring solutions that are ongoing in nature.

Budget Gap Due to Prior Cuts

As we have discussed in prior board meetings, annual state support for the CSU in the just-concluded fiscal year (2011-12) was $968 million lower than the peak state support of nearly $3 billion that was provided in 2007-08. This loss of support was compounded by an accumulation of mandatory cost increases that have not been funded by the state—such as employee health care benefits and the cost of operating and maintaining new facilities—totaling an estimated $135 million through 2011-12. Tuition fee revenue was up an estimated $593 million since 2007-08, leaving a net *negative* impact of $510 million to resources for instruction, student services and the operations of the university. Although the campuses and the Chancellor's Office have engaged in a wide range of cost-reduction actions and strategies to close this gap, a large portion of the gap in 2011-12 was covered by one-time resources and one-time deferrals on necessary purchases or projects. *It is this part of the budget gap that has not been closed by enduring expenditure reductions that constitutes the system's structural deficit*.

Looking ahead to the 2012-13 fiscal year, an estimated $132 million of tuition fee revenue is built into campus budgets from the increased tuition fee rates authorized to start Fall 2012. However, estimated mandatory cost increases unsupported by the state will rise an additional $47 million. Thus, the effective gap in fiscal resources relative to 2007-08—even with the most recently authorized tuition fee increase—will be approximately $425 million for the 2012-13 fiscal year. *This gap is based on the best-case scenario of the governor's tax initiative being passed by the voters in November*. As will be explained further, rescinding the tuition fee revenue increase—as contemplated by the enacted state budget—*would reduce revenues by $132 million and increase the size of the gap for 2012-13 to $557 million*. Moreover, similar to the situation in 2011-12, a large portion of any gap will necessarily entail further draw-down of one-time resources and other one-time actions. This is an unsustainable long-term strategy. (Even in the short run, some campuses are rapidly running out of one-time resources.) *This means that additional ongoing solutions must be found to close the gap even if the tax initiative passes*.

<u>Strategies to Address Prior Budget Gap/ Structural Deficit</u>
Some options or strategies are naturally tied to addressing the structural deficit. For example, the direction given to campuses in March to restrict admissions of new students for the Spring 2013 term is needed to address the current resources gap. Last year, the university identified a 2.4

percent reduction in its enrollment target—from 339,873 California resident full-time equivalent students (FTES) to 331,716 FTES as part of its strategy for addressing the reduction proposed by Governor Brown's first budget. This proposal was part of a required report to the legislature and governor and was approved by the legislature and governor in the final enacted budget package for 2011-12. Despite impaction (more restrictive admissions criteria) in place at 16 campuses, our latest count indicates that the university concluded the 2011-12 fiscal year having served approximately 341,250 resident FTES, or 2.9 percent above the budgeted target. This is not truly surprising, given the upward momentum on enrollments caused by the large number of admissions granted in Spring 2011 in response to the budget restoration—and legislative and gubernatorial direction—contained in the 2010-11 budget act. However, it points out that this part of the strategy for addressing the current resources gap has yet to be implemented. This "over-target" enrollment was served in 2011-12 with one-time resources, something that cannot be sustained.

In addition, there are various "synergies," administrative and instructional efficiencies, and other cost-reduction strategies—at the system level and at individual campuses—that are either in process of implementation or are under consideration that are needed to close the current resources gap on an ongoing basis. These include, among other options discussed in the consultation process, the following:

Synergies and Shared Services

As previously explained to the Board of Trustees, the synergy projects and the concept of shared services centers are already being explored and/or implemented. Although solid estimates of savings are not yet available, elimination of unnecessary duplication of services, more collaborative efforts and continued leveraging of the size of the CSU are expected to reduce expenditures in the tens of millions of dollars in the first few years of operation. As the concepts come more clearly into focus, discussions will be held with the affected collective bargaining units when hours, wages, and terms and conditions of employment may be affected. There was general support for the concept of synergies and shared services during the consultation process. Staff recommends the continuation and expansion of synergies and shared services.

Discontinuance of Academic and Athletic Programs

The academic leadership recognizes the need to begin a systematic and consultative process of eliminating programs that are of low demand, and/or unnecessarily duplicative across campuses in a given region. The amount of savings will depend on the programs to be eliminated. Staff recommends the establishment of systemwide taskforces charged to examine academic and athletic programs throughout the system and recommend program eliminations.

Alternative Strategies for Addressing the $250 Million Trigger

The signed budget package presents the CSU with increasingly difficult choices, most clearly with its feature of a $250 million “trigger” reduction in the event the governor’s tax initiative is not enacted at the November election. Given the stresses already created by prior cuts, the easy choices are gone and the $250 million trigger cut poses a mammoth challenge. There are multiple feasible approaches to address this contingency, but all feasible approaches that add to $250 million share one thing in common—they are unpalatable. Legitimate objections could be raised to each option. However, drastic reductions in state support have real consequences. If the trigger cut happens the CSU will have lost 39 percent of its annual state support relative to 2007-08 and the university will not be able to count on a turn-around in its fortunes in subsequent fiscal years.

Attachment A shows two alternative scenarios for addressing the $250 million trigger cut. One scenario involves a balance between spending reductions and revenue increases. Its intent is to have “shared responsibility for access and quality”—hence the title. This “Shared Responsibility” strategy includes the idea of a “trigger on a trigger.” Under this concept, the board would authorize at its September meeting a mid-year tuition fee increase of $150 per semester (for full-time undergraduates) or about 5 percent, but only “triggered” if failure of the tax initiative makes the $250 million trigger cut happen. This option would “solve” roughly $58 million of the trigger cut in 2012-13 and roughly $116 million in 2013-14.

This $150 per semester tuition fee option also assumes that there would be no incremental “set-aside” for additional financial aid. There are several considerations behind this approach. One is that it would require a 7.5 percent tuition fee increase—rather than a 5 percent increase—to generate the same amount of net resources to offset the budget cut if the board wanted to continue the past practice of setting aside one-third of the increment. This not only would entail a larger tuition fee increase, but in effect would result in middle income students and families subsidizing financial aid for other students. We believe this is a difficult choice to justify considering the large amounts of financial aid already in place—including almost $700 million of State University Grants (less than five percent provided by the state and over 95 percent provided by the CSU in the form of a complete tuition fee waiver or discounted fees), about $700 million of federal Pell grants, about $460 million of Cal-grants, and over $50 million of formal fee waivers, among other financial aid options that result in nearly half of CSU undergraduates paying no tuition fee at all.

Although in recent years the board has observed a practice of setting aside one-third of potential incremental revenues, it has in some years made smaller set-asides in deference to fiscal concerns. For example, in the 2004-05 fiscal year, the board set aside one-fifth of the potential incremental revenues and in 2005-06 it set aside one-fourth.

Enrollments and Jobs
Given that approximately 85 percent of the operating budget's annual spending is on salaries and benefits of faculty, staff and administrators—and given non-personnel spending reductions already underway to address the gap created by prior cuts—it is impossible to reduce spending an additional $250 million without significant reduction in spending on payroll. Generally, further reductions in the number of faculty, staff and administrators employed by the university must be accompanied by reductions in the numbers of students being served if the quality of the educational experience for enrolled students—and their access to needed courses—is to be preserved.

The revenue boost provided by the "trigger on a trigger" allows the Shared Responsibility strategy to avoid further enrollment impacts on students and minimizes consequent loss of faculty and staff jobs. Thus, the Shared Responsibility strategy avoids the 3 percent potential reduction in the 2013-14 enrollment target that was announced in March—a reduction involving approximately 12,000 students and 1,500 jobs.

The lack of revenue in the alternative strategy forces more drastic spending reductions, including a 1.5 percent reduction in the 2013-14 enrollment target and the loss of another 750 jobs.

Reducing Average Payroll Costs
Enrollment levels, program quality and the size of the work force can also be protected if the cost of salaries and benefits per employee can be reduced. This requires collective bargaining with the various unions. However, as noted, we are at a point where all the options are unpalatable and the tradeoffs are all difficult. One method for achieving this systemwide reduction in pay and benefits would be to negotiate a reduction in salary. The assumption in each scenario in Attachment A would be that the bargaining agreements on this issue would provide that the reductions would go into effect January 2013, but only if the trigger cut happens. Our current estimate is that each one percent reduction in salary results in $28.3 million of reduction in salary and salary-related benefits across a 12-month period. The Shared Responsibility strategy assumes a systemwide reduction in pay and benefits of 2.5 percent. The lack of revenue in the alternative strategy requires a larger reduction assumption—in this case, 5.25 percent.

An alternative way of reducing compensation and benefits that would not result in a reduction in pay would involve negotiating an alternative cost-sharing formula for health care benefits. Currently, the CSU share of premium cost is capped at a high level based on a statutory formula. For an individual, the employer cap is set at 100 percent of the weighted average premium cost of the four benefit plans with the highest enrollment of state employees. For each family member, the CSU must cover 90 percent of the additional cost based on those same benefit plans. As a consequence of this generous formula, annual spending by the CSU on health benefits has climbed by $60 million since 2007-08 to an estimated total of $356 million in 2011-12, despite the fact that there are about 3,000 fewer

CSU employees. The premium rates recently announced by CalPERS for calendar 2013 will increase CSU annual costs by another $36 million. The state long ago negotiated premium cost shares with its unions that are about 20 percent less expensive. For example, negotiating a cost-share similar to the state's could avoid $35 million of CSU expenditure in 2012-13 and $70 million in 2013-14 and beyond.

Faculty Assigned Time and Sabbaticals

The procedures and process for granting sabbaticals are subject to provisions in the collective bargaining agreement for faculty members. Systemwide about $12.5 million is spent to backfill for faculty members on sabbaticals. Each campus will determine if a sabbatical can be granted in a manner mindful of fiscal constraints, pursuant to the provisions of the collective bargaining agreement. A far larger amount of funds are spent on backfilling faculty for "assigned time." Assigned time is assignment to non-teaching activities in lieu of a portion of the normal teaching workload. This includes research and scholarly activities, but also things like serving on campus committees. Campuses have reduced assigned time by 13 percent since 2007-08. However, given the exigency that would be created by the $250 million trigger cut, we believe that further prioritization of workload would be feasible and necessary.

Adding a Third Tier to the Tuition Fee Structure

Adding a "third tier" to the CSU resident student tuition fee structure would dissuade students who are signing up for extra course loads by charging them full freight for course loads over what is required to complete the degree in four years. Given current constraints on ability to offer course sections, the ten percent of undergraduate students who take extra course loads are, in effect, preventing the other 90 percent from gaining fair access to a 15-unit course load, the standard under which state funding is provided to the CSU and the course load that typically is needed to complete a baccalaureate degree in four years. Access to enroll more eligible new students also is constrained. Under this "third tier" approach, students would pay an additional per-unit charge for course loads that are above 16 units, in the process providing the resources that would allow additional course sections and "seats" to be available for all students.

For the third tier to work, it needs to be coupled with two reinforcing strategies to change student behavior. First, seven percent of CSU seniors are "super seniors," that is, students who have earned five years or more of academic credit on the CSU's state-supported "dime." Their earned units are enough to complete high-unit majors and other academic interests. The first reinforcing strategy is a full-freight Graduation Incentive Fee that would be charged to "super seniors" who are continuing to enroll at CSU campuses. Coupled with current campus actions to confer degrees to "super seniors," the announcement of a Graduation Incentive Fee would have the helpful effects of graduating "super seniors," increasing graduation rates, and freeing admission slots for eligible CSU applicants.

With 10 course repeats per 100 CSU undergraduates, over 40,000 seats in state-supported classes are being taken by students who already have taken the course, at least once, on the CSU's state-assisted "dime." It generally is agreed that one "free" course repeat makes sense for young people who are experimenting and testing themselves, but policy permits students to take almost a full academic year of state-subsidized course repeats. The second reinforcing strategy is a full-freight Course Repeat Fee, applied after the "first" free course repeat. Students are unlikely to take a major prerequisite course more than twice if they must pay a Course Repeat Fee. Coupled with active advising to assist students to hone their strengths and interests in more aligned academic programs, CSU students should progress to degree more effectively.

Equal opportunities to get needed classes, opening slots for eligible CSU applicants, getting students on pathways to degree, and getting students to the degree with less cost and time to them are the primary objectives of these three strategies. It is anticipated that adding the third tier to the tuition fee structure and the marginal effects of the other fees would generate about $35 million annually, starting in 2013-14. This option not only generates needed resources in 2013-14 and beyond but makes sense as a policy change that should be considered even if there is no trigger cut.

Nonresident Tuition Supplement
Currently the CSU collects approximately $135 million annually from out-of-state and international students. These students represent a relatively modest share of total enrollment of about 4 percent. These students pay a tuition supplement of $11,160 per academic year in addition to the standard tuition fee. They also pay an additional per-unit tuition fee to the extent they take more than 30 units per year. This option assumes that a 9 percent increase in the tuition supplement (around $1,000), effective Fall 2013, would produce about $13 million in additional revenue in 2013-14. Even with this increase, total nonresident charges would be substantially less than peer institutions around the country.

One-time Transfer of Continuing Education Balances
Both scenarios assume a transfer of approximately $75 million from the CSU's Continuing Education Revenue Fund (CERF). This is a rough estimate of the balance that could be moved without harming current extended education commitments. It could provide significant relief to the "state-side" of the university in 2012-13, but the relief would be one-time and restricted to that fiscal year. Language in the enacted budget act grants this emergency transfer authority to the chancellor, but only in the event that the governor's tax initiative fails.

State's Offer of a Delayed Buy-out of a Tuition Fee Roll-back

The most notable new development in the enacted state budget for the CSU is the proposal to "buy out" the already-implemented tuition fee increase for the 2012-13 academic year with an appropriation that would not be operative until the 2013-14 fiscal year, and only then if the

November tax initiative is enacted. One of the budget trailer bills (AB 1502) includes separate appropriations of $125 million each to the CSU and the University of California *for the 2013-14 fiscal year*. Two conditions must be met if the CSU wants to access its appropriation next year: (1) the governor's tax initiative must be enacted and (2) the university must reset its tuition fee rates for the 2012-13 academic year back to the levels in effect for the 2011-12 academic year. The governor and legislative leaders are aware that the CSU not only has higher tuition fee rates in effect for 2012-13 but has already collected the higher tuition fees from continuing students. Thus, they understand that complying with the second condition of the delayed appropriation would require our board to rescind its action of last November and would require the processing of refunds to students for Fall 2012.

Based on discussion with Department of Finance and legislative staff, we believe that the board could comply with the condition—if it desires to accommodate the legislative and governor's intent—with an action at its September meeting to rescind the tuition fee increase for the full 2012-13 academic year ***contingent on voter enactment of the November tax measure***. Under this scenario, campuses would begin processing refunds or credits for Fall 2012 shortly after a successful passage of the tax measure and students registering for Spring 2013 would pay the rates in effect for 2011-12. For a full-time undergraduate who pays tuition fees, rolling back the tuition fee rates would constitute a reduction of $249 per semester, or $498 for an academic year.

On the basis of a strict fiscal analysis, the delayed appropriation proposal does not make sense for the CSU. Viewed in a larger context, however, the proposal enhances the appeal of the governor's tax initiative, a matter of great potential impact for the university's future funding prospects. From a fiscal standpoint, rescinding the tuition fee increase would create a one-time hole in the system's operating budget of $132 million for 2012-13. The $125 million base appropriation in 2013-14 would cover about 95 percent of the ***ongoing loss*** from the decision to reset rates to 2011-12 levels, but it would ***not*** compensate for the one-time loss in 2012-13.

At the time this analysis was prepared, we had been working with Department of Finance staff and legislative staff on options that could address this one-time problem. We have secured support from the governor's office for a budget "clean-up" bill that would grant the chancellor authority to move surplus balances from continuing education to mitigate impacts on state-supported instruction regardless of the outcome of the election. (The current budget bill grants this authority only if the tax measure fails.) We are hopeful that we will secure legislative support of this "fix" in a clean-up bill that would pass before the August close of the legislative session. This "fix" would address roughly half of the one-time gap that would result from a board choice to rescind the tuition fee increase. We are still exploring other options to address any remaining gap.

Attachment A
Fin—Item 3
July 17, 2012

Alternative Strategies—$250 Million Trigger Cut

Dollars in millions and approximate

		2012-13		2013-14
Shared Responsibility for Access and Quality				
"Trigger on trigger": $150/semester tuition increase eff. Spring 2013		58		116
2.5% systemwide reduction in pay and benefits, effective January 2013		35		70
Reduce faculty assigned time/release time		10		16
Charge for extra units ("third tier" pricing)		0		35
Increase non-resident tuition supplement 9 %, effective Fall 2013		0		13
One-time balances from continuing (extended) education		75		0
Other one-time resources		72		0
Totals	**$**	**250**	**$**	**250**

		2012-13		2013-14
Alternative Without Triggered Tuition Fee Increase				
Reduce 2013-14 enrollment 1.5 %/ reduce 750 faculty/staff positions*		0		30
5.25 % systemwide reduction in pay and benefits, effective January 2013		74		147
Reduce faculty assigned time/release time		15		25
Charge for extra units ("third tier" pricing)		0		35
Increase non-resident tuition supplement 9 %, effective Fall 2013		0		13
One-time balances from continuing (extended) education		75		0
Other one-time resources		86		0
	$	**250**	**$**	**250**

* Additional enrollment and faculty/staff/administrator reductions needed to get to current target of 331,716 resident FTES and fully address prior state funding cuts.

MINUTES OF THE MEETING OF
COMMITTEE ON FINANCE

Trustees of The California State University
Office of the Chancellor
Glenn S. Dumke Conference Center
401 Golden Shore
Long Beach, California

May 8, 2012

Members Present

Lou Monville, Acting Chair
Steven Dixon
Margaret Fortune
Steven M. Glazer
Henry Mendoza
Glen O. Toney
Charles B. Reed, Chancellor

Approval of Minutes

The minutes of March 20, 2012 were approved as submitted.

Report on the Support Budget 2012-2013 and 2013-2014 Fiscal Years

Mr. Robert Turnage, assistant vice chancellor for budget, reported that state revenues fell below state budget assumptions and that the governor will release a revised budget on May 14, 2012 including a revised tax initiative for the November ballot. If passed, the initiative would generate new revenue, if unsuccessful the consequence could mean more cuts to the CSU.

Trustee Monville inquired if there were any discussions with the Department of Finance (DOF) on the potential impact to the budget. This would be a good time to have strategic discussions about investing in California's economy.

Mr. Turnage responded that the DOF is very much aware that further cuts to higher education would affect the state's economy and future.

Trustee Glazer asked if the increased tuition fee revenue of $138 million for 2012-13 was incorporated into the proposed budget solutions and as revenue that can be used to fill the CSU budget gap. Mr. Turnage confirmed that the tuition fee revenue is incorporated.

Trustee Glazer inquired about missing the enrollment target by 6,000 FTEs, which resulted in loss of revenue. In making enrollment decisions in the future, he asked how much confidence can be placed in the projected revenue. Mr. Turnage commented that managing enrollment can be complicated and at times difficult in reaching the enrollment target.

Trustee Monville then called upon the members of the public who had requested to speak at the Committee on Finance. There was one speaker, Carol Shubin, faculty at California State University, Northridge, who inquired about the possibility of more severe trigger cuts.

Revenue Enhancement and Cost Reduction Strategies

Dr. Benjamin F. Quillian, executive vice chancellor and chief financial officer, stated that it is possible for the trigger cut to be more than $200 million if the tax initiative fails to pass. As requested by the board at the last meeting, various options were presented for the board to review and identify the options that most feasible. It is important to maintain the CSU's core business of a broadly accessible, quality education and to anticipate future needs and invest in that future. Dr. Quillian was joined by Ephraim Smith, executive vice chancellor and chief academic officer and Gail Brooks, vice chancellor, human resources to present the various cost reduction and revenue enhancement strategies.

Mr. Turnage stressed that the CSU faces both a possible trigger cut and a nearly billion dollar reduction in funding from the state. He stressed that it is important to remember that some options lend themselves better to addressing structural deficits and other options are better suited to address the trigger cut. Options that address the trigger cut are all difficult and require sacrifices.

The strategies discussed were:

- To what extent should the CSU reduce the number of administrative activities that are performed at each campus?
- Should the CSU close one or more campuses?
- Should the CSU consider moving one or more campuses to be independent of state funding?
- Should the CSU move some academic programs to be fully supported through tuition fees?
- Should the CSU discontinue certain academic programs?
- Should the CSU identify specializations in academic programs at identified campuses and eliminate duplication at nearby institutions?
- Should the CSU seek to increase the student-faculty ratio (SFR) by increasing the average number of students in a class?
- Should the CSU have tenured and tenure-track faculty members teach additional classes?
- Should the CSU eliminate or reduce sabbaticals for faculty?
- Should the CSU increase employee contributions toward health benefit plans?
- Should the CSU reduce employee compensation for all employee categories?
- Should the CSU reduce enrollment, and if so, to what degree?

- Should the CSU add a third tier to the current two-tier tuition fee structure for students taking more than 16 units?
- Should the CSU add a commencement incentive fee for "super seniors?"
- Should the CSU implement a "course repetition" fee?
- Should the CSU modify the tuition fee structure for masters-level programs?
- Should the CSU increase the tuition rate for nonresident students?
- Should the CSU implement a variable tuition fee structure that recognizes higher demand at some campuses?

Chancellor Reed added that although the alternatives presented seem bad, these are things that need to be considered. The CSU still will have a $400 million structural deficit even if the tax initiative passes in November. Before the CSU can move forward, it is important to see what happens with the trigger cut and the governor's May revised budget.

Trustee Fong inquired how many super seniors receive financial aid. Chancellor Reed responded approximately half of the super seniors receive financial aid. Trustee Fong also asked if tuition is increased for graduate and masters students, what the projected enrollment for the future is. Dr. Quillian responded that there may be a slight decline.

Trustee Ruddell inquired if tuition was increased at the same percentage rate for in-state and out-of-state students. Mr. Turnage commented that nonresident and international students pay the same tuition fee as in-state students plus a supplemental tuition.

Trustee Glazer asked that if we wait until July to decide on which alternatives to pursue, would any of the alternatives be lost as an option. It is difficult to understand how the board will be able to come back for one day in July and make a decision, given the magnitude of questions and dilemmas associated with each option. Chancellor Reed responded that getting information on the governor's revised budget will help in developing a structural plan. More time may be needed to make these difficult decisions.

Trustee Monville suggested holding a special finance committee meeting before the board meets in July for further discussions.

Dr. Quillian added that CSU campuses are already planning for the trigger cut.

Mr. Turnage commented that there will be a better understanding on what the legislature wants to do and what direction the CSU should take after June 15.

Mr. Gregory Washington, president of California State Student Association, noted there was a general consensus through student discussions for shared services and a course repetition fee.

Mr. Jim Gelb, assistant vice chancellor for federal relations, expressed that the senate has yet to discuss the proposals presented to the board.

Chair Linscheid provided some direction on which alternatives warranted further discussion, given the magnitude of challenges the CSU is facing.

Trustee Monville is in favor of providing the board with a chart showing the effects, cost saving versus loss of revenue, depending on the level of enrollment. This would allow the board to have more meaningful discussions on enrollment issues.

Trustee Cheyne requested that the board be careful on measures that reduce spendable income for faculty and staff as there are a lot of individuals who will be severely impacted. She also inquired about the task force investigating converting quarter campuses to semester campuses and what the potential costs and savings would be.

Dr. Quillian responded that there is a presidential task force looking into converting quarter campuses to semesters. The task force will submit their findings to the chancellor, who will decide if a recommendation will be presented to the board.

Lt. Gov. Gavin, expressed that this is more than a revenue problem, it is stated a problem of spending more than expected.

Chancellor Reed added that it is important to figure out which options would provide the greatest impact on the deficit.

Trustee Monville would like to have a special finance committee meeting after June 15, 2012 for more detailed review and discussion in preparation of the July board meeting.

Trustee Fortune stated that there is a need to hear from constituents and suggested creating a table to help distinguish which items generate major revenue.

Chancellor Reed noted that there would be a four-week window in order to get the board agenda out on time.

Dr. Quillian suggested using an already scheduled meeting of the Systemwide Budget Advisory Committee, which consists of campus presidents, faculty, union representatives and students, to solicit input from constituents.

Trustee Fong expressed his distress at the $400 million structural deficit and the increase in mandatory costs. Education is very important but for the CSU to move forward, there needs to be enhanced revenue or reduced expenses, otherwise the deficit will always be an issue.

Chair Linscheid agreed with having a broad consultation done and getting more public opinion and input.

With no further questions, Trustee Monville proceeded to the next item on the agenda.

Approval to Issue Trustees of the California State University, Systemwide Revenue Bonds and Related Debt Instruments

Mr. George Ashkar, assistant vice chancellor for financial services, presented the item requesting approval to authorize the issuance of systemwide revenue bonds and the issuance of Bond Anticipation Notes (BANS) to support interim financing under the commercial paper program of the CSU. The total project cost is $10,134,000. Additional net financing costs of $1,151,000 will be funded from bond proceeds.

The San Diego Aztec Shops, Ltd. – University Towers Renovation project is included in a previously approved 2011 amendment of the non-state capital outlay program. The project renovation includes upgrades to the nine-story, 560-bed residence hall, food service facility, restrooms, entryways, lobby and selected exterior and landscape improvements.

With no questions, Trustee Monville called for a motion on the resolution, which was approved.

Proposed Title 5 Revision: Dissolution of Auxiliary Organizations

Dr. Quillian, presented the item, which gives the chancellor authority to approve the distribution of assets, when there is dissolution of an auxiliary. The chancellor will provide reports to the board detailing how these assets are distributed to a successor organization.

With no questions, Trustee Monville called for a motion on the resolution, which was approved.

Trustee Monville adjourned the Committee on Finance.