



April 15, 2014

MEMORANDUM

TO: Vice Presidents
Chancellors

FROM: David Lassner
Interim President

A handwritten signature in black ink, appearing to read 'David Lassner', written over the printed name and title.

**SUBJECT: FISCAL BIENNIUM 2015-2017 (JULY 1, 2015 TO JUNE 30, 2017)
BUDGET POLICY PAPER AND INSTRUCTIONS**

Pursuant to Board of Regents (BOR) Policy 8-3 on biennium budget development, attached are preliminary documents to guide you in the development of your Fiscal Biennium (FB) 2015-2017 budget request. These items were discussed in the systemwide budget forum on April 2, 2014.

As noted at the forum, this biennium budget process will not be an exercise in proposing Program Change Requests but will include a review of current and planned expenditures and revenues from multiple sources of funding.

Our expectation is that each Vice President and/or Chancellor will work with your respective leadership and constituent groups in developing a campus FB15-17 budget request, using the guidance provided in the following attached documents.

- (1) FB 2015-2017 Budget Policy Paper, adopted by the BOR at their March 2014 meeting;
- (2) Executive Policy on Financial Reserves establishing campus operating reserves pursuant to BOR Policy 8-3, as amended at the November 2013 BOR meeting; and
- (3) Instructions from University System Administration for development of campus budget requests, including Timeline for FB2015-17 budget submissions (new) and budget review process.

Fiscal Biennium 2015-2017 (July 1, 2015 to June 30, 2017)

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Please be aware that the Instructions and Timeline are subject to change, pending final decisions by the State Legislature that impact our Fiscal Year 2015 budget request. Revised Instructions, Timeline and worksheets will be issued in early May, if necessary.

Should you have any questions about these documents, please don't hesitate to contact Laurel Johnston, University System Budget Director via laurelaj@hawaii.edu or 808-956-7323.

Attachments

c: Cynthia Quinn, Executive Administrator and Secretary to the Board of Regents
Laurel Johnston, Director of University Budget Office



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March 14, 2014

MEMORANDUM

TO: Board of Regents
VIA: David Lassner, Interim President
FROM: Joanne Itano, Interim Executive Vice President for Academic Affairs; Howard Todo, Vice President for Budget and Finance/Chief Financial Officer
SUBJECT: 2015-2017 Biennium Budget Policy Paper

Section 8-3 of Board of Regents (BOR) policies sets forth guidance for the preparation of the biennial budget policy paper. The document establishes the environmental context for budget building and articulates the University's general program, policy, and management objectives and institutional priorities that guide the preparation of the biennium budget.

I. Environmental Context

The following describe the events and developments that impact the University and its resources during this 2015-2017 biennium budget planning process.

The State's Need for More College Graduates

A skilled labor force is essential in today's global, knowledge based economy, therefore increasing the educational capital of the state remains at the forefront of the University's priorities. With fewer young adults going to college, there is an urgent need to increase the educational attainment of our 25- to 64-year old working age adults. As of 2010, 42 percent of the Hawai'i's working age population held a postsecondary degree. Estimates reveal that at the current rate of degree production within the state, the percentage of degree holders by the year 2025 will be at 47 percent. Given the estimate that 65% of the jobs in the Hawai'i will require postsecondary education and training, this translates into a shortage of approximately 60,000 degree holders. The University of Hawai'i, as the state's sole public higher education system, is committed to playing the major role in closing the state's projected educational attainment gap and will continue to support the statewide 55 X 25 Campaign to increase the percent of working age adults with degrees.

Strategic Initiatives to Meet State Needs

Currently, the University is updating its overall systemwide strategic directions and priorities for the next three biennia, from 2015-2021. Work is actively underway to reframe the strategic initiatives and add new performance measures on productivity and efficiency that will be linked to budgeting processes. The strategic initiatives for 2015-2021 are as follows:

- Hawai'i Graduation Initiative (HGI) – UH will continue to build on our past work (increase degrees/certificates awarded to 10,000 by 2015), through specific strategies that include: strengthening the K-12 to UH pipeline; increasing student success and completion on our campuses; and understanding, anticipating, and aligning the University's curricula with community and workforce needs. The University must also maximize its opportunities to increase the number of graduates through UH West O'ahu, the University's "startup" campus, which serves some of the most underrepresented populations in the State.
- Hawai'i Innovation Initiative (HI2) – UH will help create more high-quality jobs and diversify Hawai'i's economy by leading the development of a \$1-billion innovation and research enterprise in Hawai'i over the next ten years. The University is working in partnership with the private sector and government to create this third major economic sector for the State. Implementation strategies for HI2 will include: advancing the UH research enterprise; infusing entrepreneurship education across UH campuses; increasing the commercial utilization of UH ideas and innovations; collaborating in new public-private partnerships; and investing in core infrastructure.
- 21st Century Facilities (21CF) – UH must eliminate the substantial deferred maintenance backlog and modernize facilities to meet 21st century needs for learning, teaching and research. Facilities and campus environments must be safe, sustainable and support modern higher education practices. This is a systemwide problem on all but our newest campus, and particularly acute at our flagship Mānoa campus. Strategies for moving forward will include: adoption of model policies and practices to improve project planning, procurement, and long-term management and sustainability; organizational review and restructuring to improve efficiency and effectiveness; and committed funding to achieve outcomes and prevent the backlog from recurring once it has been eliminated.
- High Performance System of Higher Education – UH is committed to accountability, transparency and managing costs by leveraging the full potential and efficiencies available to a unified statewide system of public higher education. Strategies for

achieving higher performance will include: providing a diverse student body with multiple entry and exit points across the state; coordinated academic pathways and articulated program offerings; streamlined administrative and support processes; efficient utilization of facilities; exploration and implementation of new instructional approaches; and enhanced use of metrics for productivity and efficiency.

Review of Current Tuition Schedule

The University is currently in the second year of a five-year tuition schedule that was approved by the BOR in 2011. The current schedule ends in academic year 2016-2017, the second year of the 2015-2017 fiscal biennium. A review is currently being conducted by the University administration and a BOR task group to evaluate the increases already approved for the last two years of the current schedule. This review will consider the outcomes of the 2014 Legislative session and the University's needs as identified through this biennium budget planning. A recommendation to the full Board is expected by September 2014 regarding what changes, if any, should be made to the tuition schedule for academic years 2015-16 and 2016-17.

Financial Reserves

In November 2013, the BOR approved a new policy mandating operating reserves for non-general funds, which recommends maintaining two months (16 percent) of operating reserves. The BOR delegated the detailed implementation of this reserve policy to the Administration. The BOR reserve policy further directs that the development of the biennium budget shall include consideration of unrestricted non-general funds and reserve levels. For the 2015-17 fiscal biennium, the University administration will provide more detailed instructions and recommend that each campus establish and maintain operating reserves at a minimum level of 5% and that reserves greater than 16% be explicitly justified or invested.

Fiscal Year 2014-15 Operating & Capital Improvement Budget Priorities

The University of Hawai'i has requested additional recurring general funds in the FY 2015 supplemental operating budget, most significantly, \$14 million to restore faculty salary reductions in the first two years of the current six-year collective bargaining agreement and \$19.5 million for the three percent faculty salary increases that were agreed to in the fifth and sixth years of that agreement.

Should the University System receive these additional general funds, and should the Legislature authorize revenue bonds as requested, \$14 million per year will be committed

to pay debt service on revenue bonds to reduce approximately \$200 million of the system wide backlog of \$478 million in deferred maintenance projects.

In addition, the BOR FY 2014-15 Supplemental Budget request includes important operating budget requests for capacity to execute repairs, maintenance and capital renewals at the campus and system level; to strengthen the foundation of West O'ahu operations; and for initiatives that support increased educational success and economic development for the State.

General Fund Appropriations to University System

For the current FY 2014, the University of Hawai'i's general fund appropriation increased by \$9.26 million. The FY 2015 supplemental budget request, as approved by the Governor and submitted to the legislature for current consideration, asks for an additional \$37.5 million in general fund support. These increases are a positive sign after the recession, during which the University saw its general fund support reduced by \$62 million (15 percent) from \$422 million in FY 2010 to \$360 million in FY 2011.

Council on Revenues Projections/General Fund Surplus

On March 11, 2014, the state Council on Revenues significantly downgraded the State's general fund forecast for the current FY 2014 to zero growth, and reduced the projection for the two ensuing fiscal years, FY 2016 to 5.5 percent and FY 2017 to 5 percent from 5.7 percent. Cumulatively, this represents a reduction of \$200 to \$300 million in state general revenues for the ensuing 2015-2017 fiscal biennium. Additionally, while in January 2014, the Governor announced that while FY 2013 ended with a general fund surplus of close to \$844 million dollars, the Governor's financial plan commits a significant portion of the surplus to recapitalize the State's "rainy day" fund and hurricane relief fund as well as contribute to a 10-year plan to address the under-funded liability in the state employee pension fund

II. Program, Policy, and Management Objectives and Biennium Budget Development Assumptions

Given the expected modest growth in state revenues and the competing statewide needs for additional resources, it is incumbent on the University to develop a realistic budget request that recognizes the financial condition of the State and makes strategic use of existing resources. Should additional general funds be received in FY 2015, there will be an opportunity to re-balance the revenue mix of general fund and non-general fund support for FB 2015-17.

At the same time, it is imperative that the University provides concrete plans for strategic growth in which the State can invest. To this end, the strategy for development of the biennium budget will be consistent with the following principles:

- The biennium budget will be grounded in the University's strategic directions and priorities;
- A holistic approach, considering all revenue sources, will guide the biennium budget development strategy, including an evaluation of each campus' base budget and their respective operating reserves in conjunction with any requests for additional funds.

Objectives of the biennium budget building process are as follows:

- Allocate new general funds and tuition revenues in a way that incentivizes units to improve productivity, efficiency, and alignment with strategic directions, using established metrics;
- Incorporate regularly scheduled monitoring of budgeted versus actual expenditures into all financial reviews and future budget building processes;
- Non-general fund operating reserves shall be maintained as required by BOR policy and Executive guidelines;
- A schedule of operating and maintenance expenses for existing and new facilities will be established and evaluated as part of the 2015-2017 biennium budget;
- Academic programs will align with strategic directions and performance measures;
- The deferred maintenance backlog at the Mānoa campus will be eliminated over the next 10 years and at the other campuses in FY 2016.

Furthermore, the following assumptions will be applied in the biennium budget building process for the operating and Capital Improvements Project (CIP) budgets:

Operating Budget Assumptions

- The Executive and House Budgets for FY 2015 include the BOR-requested general fund appropriations of \$33.5 million for faculty salary restoration and negotiated salary increases;
- If the \$33.5m for faculty salary support is appropriated and revenue bond authorization approved by the Legislature, \$14m million of tuition revenues will be allocated for debt service on revenue bonds to address deferred maintenance;

- A final payment from FY 2015 tuition revenues will complete the “payback” of deferred salary to faculty;
- Future collective bargaining costs for all bargaining units will be provided through state general fund appropriations;
- Utility rates and usage (the factors of utility costs) will be projected for each fiscal year based upon the last two fiscal biennia, factoring in cost savings from energy conservation efforts and new facilities coming online;
- Student enrollment projections at all UH campuses are expected to be flat except at West O’ahu for fall 2015 and 2016. West O’ahu’s headcount enrollment is anticipated to increase by 265 students in Academic Year (AY) 2016 and 231 students in AY 2017;
- As required by Executive policy, Mānoa, Hilo and West O’ahu will allocate at least 19 percent of FY 2015 tuition revenues toward institutional aid in FY 2016 and 20 percent of FY 2016 tuition revenues toward institutional aid in FY 2017. The Community College campuses will allocate 11 percent of tuition revenues toward institutional aid for both fiscal years. This translates to an average of \$52 million in institutional aid each academic year.
- For biennium base budget planning purposes only, assume that tuition remains flat at the 2014-15 levels through the biennium. Actual tuition rates will be finalized based on the results of the 2014 Legislative Session and specific needs identified through this biennium budget planning process;

Capital Improvement Project (CIP) Budget Assumptions

- General funds or general obligation bond funds will be appropriated for annual capital renewal needs and for major renovation and modernization;
- The moratorium on new construction continues for the 2015-2017 fiscal biennium, with limited exceptions as previously approved by the BOR.

III. Productivity and Efficiency Measures

As noted in section I, the University is updating and expanding its performance measures. The updated 2015-2021 set of measures will include productivity and efficiency measures. The goal is to link biennium budget allocations to these productivity and efficiency measures.

The following are potential measures currently being considered:

Productivity measures

- a. The number and rate of students who graduate and graduate on time;
- b. The number and success rate of students who transfer;
- c. Success rates of part-time, Native Hawaiian, low-income and under-represented students;
- d. Post graduate outcomes.

Efficiency measures

- a. Educational and institutional costs per Full Time Equivalent (FTE) student;
- b. Educational and institutional costs per completion/transfer;
- c. Average number of credits of graduates relative to requirements;
- d. Number of programs with five or less graduates;
- e. Ratios of students to faculty, to staff and to Executive/Managerial employees;
- f. Student Semester Hours/Full Time Equivalent (SSH/FTE) instructional faculty;
- g. Kilowatt hours utilized/square foot;
- h. Classroom utilization (measure to be developed using AiM/R25 data).

IV. Next Steps

In accord with BOR Policy, upon approval of this budget policy paper the President shall issue formal instructions to major units on preparation of the biennium budget. These instructions will be based on the priorities, assumptions and guidelines contained in this paper.

Submittals from the major units will then be used to prepare an integrated biennium budget proposal for the University of Hawai'i, which will be reviewed and approved by the BOR and then utilized for the preparation of formal documents that will be submitted to the Governor and Legislature in accord with applicable statutes and instructions.

Fiscal Biennium 2015-2017 Budget Instructions

Pursuant to Board of Regents (BOR) policy Section 8-3, the following instructions provide University System guidance and the process for the preparation of campus operating and capital improvement budgets for Fiscal Biennium (FB) 2015-17, which begins July 1, 2015 and ends June 30, 2017. The BOR has approved the 2015-2017 Biennium Budget Policy Paper (BBPP), which sets forth the environmental context for budget building and general program, policy and management objectives, and institutional priorities to guide the preparation of the biennium budget. The most significant difference from past budget development, is the adoption of a holistic approach for FB2015-17. Accordingly, the strategy for development of the University System biennium budget will be consistent with the following principles:

- The biennium budget will be grounded in the University’s strategic directions and priorities; and
- Consideration of all revenue sources will guide the biennium budget development strategy, including an evaluation of each unit’s base budget and their respective operating reserves in conjunction with any requests for additional funds.

For the purposes of these instructions, “unit” is defined as the major program budget units, including: Mānoa (100, 110 & 881), Hilo (210 & 220), West O’ahu (700), the Community College System (800), and Systemwide Programs (900).

Step 1 -- Review of FY2014-15 (FY15) Financial Projections and Initiatives

Following the 2014 legislative session, each unit will be provided a projection of their operating revenues and expenses for FY15 (July 1, 2014 to June 30, 2015) based on the assumptions in the BBPP and actual FY15 appropriations. Each unit shall review these projections for reasonableness and describe the major initiatives underway through FY15 to advance the strategic directions of the University and improve efficiency. Due to the urgency of providing a safe environment for all students, faculty, and staff, all campuses will need to reallocate tuition revenues that become available in FY15 towards achieving full compliance with Title IX and VAWA requirements (Part of 21CF).

Step 2 -- Calculation of Operating Reserve for FY2014-15 (FY15)

Attachment 1 contains the proposed Executive Policy on Operating Reserves. Each unit will be provided a calculation of estimated operating reserves as of June 30, 2015, based upon the proposed Executive Policy. If a campus cannot achieve these minimum operating reserves, the Chancellor shall develop a plan to attain a minimum operating reserve as part of their biennium budget request. If a campus has or requires operating reserves greater than 16 percent as outlined in the BOR's Policy on Operating Reserves, the Chancellor shall justify the purposes for which such additional reserves shall be used as part of their FB2015-17 biennium budget request.

Step 3.1 – Calculation of FB15-17 Base Operating Budget

The following assumptions will be considered by each unit in the development of their FB2015-17 base operating budget revenues and expenditures:

- Fall 2015 and Fall 2016 student enrollment projections will be flat at all campuses, except West O'ahu;
- Tuition rates will not increase beyond the 2014-15 levels set in the present tuition schedule, pending further review and consideration by the BOR as part of FB2015-17 biennium budget development;
- Mānoa, Hilo and West O'ahu will allocate at least 19 percent of FY15 tuition revenues toward institutional aid in FY16 and 20 percent of FY16 tuition revenues toward institutional aid in FY17, whereas the Community College campuses will allocate 11 percent of tuition revenues toward institutional aid in both fiscal years;
- \$14M of general funds will replace \$14M of tuition revenues being used for faculty salary restoration; and
- Utility rates and usage will be projected by each campus for each fiscal year in FB2015-17 based upon the last two fiscal biennia (FB11-13 and FB13-15), factoring in cost savings from energy conservation efforts and new facilities coming online.

Step 3.2 – Calculation of FB15-17 Capital Improvement Project (CIP) Budget

The following should be considered by each unit in the development of their FB2015-17 CIP budget revenues and expenditures. Note that considerations that relate to legislative appropriations may be adjusted as more information becomes available:

- The legislature will continue to appropriate general obligation bond funds for annual capital renewal needs and for major renovation and modernization;
- \$14M of tuition revenues will be re-allocated from salaries to debt service for revenue bonds to address deferred maintenance, with the exception of the West O’ahu campus, which shall retain its proportionate share of tuition revenues as it has no deferred maintenance; and
- The BOR moratorium on new construction continues for the FB15-17, with limited exceptions as previously approved by the BOR.

Step 4 – Investment in Strategic Directions and Performance Improvements

After the calculation by each unit of their FB15-17 base operating budget and CIP budget requirements, each unit will delineate a priority list of proposed additional investments in program enhancements that align with and advance the University System’s Strategic Directions for 2015-2021. A separate form will be provided for this purpose, and will request details such as: description of the program enhancement; how the proposed additional investment will advance specific strategic direction(s); the means of finance (new general funds or tuition increase beyond 2014-15 levels) of such additional investment and the projected return on investment; and specific measures to evaluate program outcomes.

In addition, units will describe their plans to increase productivity and efficiency over the current state. Examples of such plans could be:

- Plans to recruit more students, including non-residents;
- Plans to reduce costs through enhanced use of technology;
- Plans to eliminate classes, degrees and /or programs with low enrollment that are not high priority;
- Plans to consolidate administrative units; and
- Other plans to increase productivity and efficiency or reduce costs.

Each unit will be provided a set of productivity and efficiency measures for 2015-2021. These measures will be used to guide the allocation or reallocation of unit resources and/or to reward achievement of performance targets that advance the University System's Strategic Directions.

Step 5 – Next Steps

FB2015-17 budget proposals from the units will be based upon final instructions and a timetable, which will be transmitted to the units prior to the end of the Spring 2014 semester. These final instructions, in conjunction with the results of the 2014 legislative session and the BOR's determination of tuition rates for the 2015-2017 Academic Years, will guide the development of the University System's FB2015-17 proposal. Note that these various factors may result in reallocation of general funds between major program budget units. The University System leadership will engage in additional public discussion about the FB2015-17 budget proposal at a BOR Workshop in August 2014, with the goal of final review and approval of the FB2015-17 budget proposal at the September 2014 BOR Meeting to meet late September 2014 deadlines for budget submissions to the Governor.