To: President Warren Brown **6/02/15**
Cc: College Council
From: The Budget Advisory Committee
Subject: Report on Budget Plan FY 1516

INTRODUCTION:

The BAC reviewed in detail the memo sent by President Brown ('Update on Budget Process' 4/20/15) to understand our objective and the scope of our undertaking. We determined our work would be to provide a recommendation on the feasibility of the college funding the schedule of known commitments and requests as additions to the existing FY 1415 state operating budget. Please refer to **Schedule A** (the Schedule), attached.

As in past years, the committee sought to answer these questions:

What source of money is being used to fund the Schedule?
Is that source or sources valid/sustainable?
What risk factors should be considered, and can those factors be accurately modeled?
What unfunded FY 1516 commitments, if any, are not included in the Schedule?

In addition, BAC reviewed budget elements that potentially impact the entire state operating budget and therefore indirectly impact the college's ongoing ability to fund the Schedule; e.g. the new state-wide budget allocation model being developed for implementation in FY 1617. The committee also reviewed the district-wide FTES shortfalls during FY 1213, 1314, and 1415; the in-fiscal-year tuition allocation reduction in FY1415 due to tuition revenue shortfall; and in particular, the effect of the college's adjustment to this tuition shortfall by increasing its reliance on International Student Revenues.

Having completed its analysis, the committee offers the following.

RECOMMENDATIONS:

- ***Delay decisions on New/Continued Funding Requests (Schedule item numbers 18 through 33) until August 2015, when the effects of state legislative action, and the college's Carryforward amount are known with certainty.***
- ***Fund Permanent level requests (Schedule items 18 through 21) only through reallocation of existing Permanent level funding within the requesting Executive Unit (EU), or by reallocation of such funds across EUs.***
- ***Weigh very carefully any further reliance on International Student Revenues to fund the college's operating budget. This applies to both college level International Programs (IP) and non-college level Intensive English Programs (IEP). However, particular attention should be directed toward the college's use of IP revenues.***
- ***Prepare for the fact that already known Permanent level commitments by the college will essentially deplete the Permanent level Contingency Reserve (CR), meaning the college will likely enter fiscal year 2015-16 with inadequate Permanent level resources by which to fund***

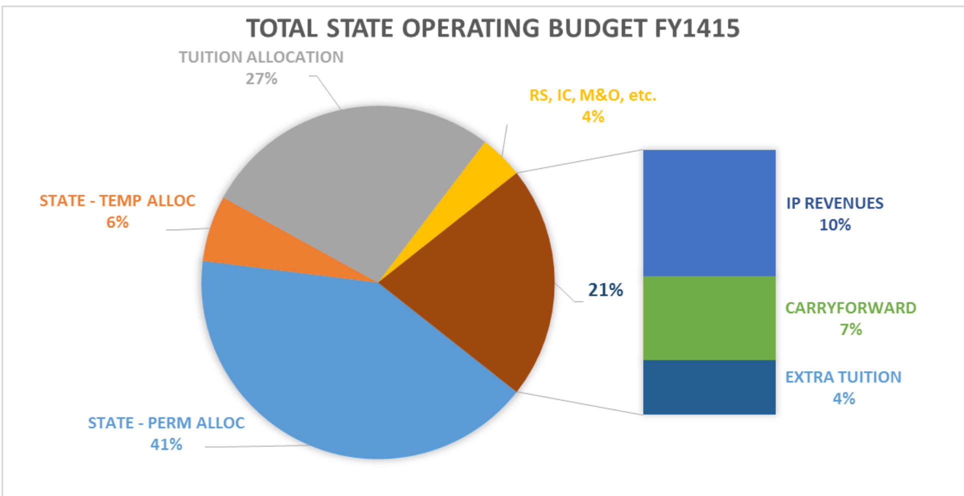
future needs (including existing mandatory salary increases or new legislatively enacted increases).

- ***Redirect the college's attention to its existing budget to identify resources that can be redirected (reallocated) to newly identified needs.***
- ***Enlist the resources necessary to fully understand the complexity and conditions that result in the college's annual Carryforward (i.e., its annual operating balance)***

PRIMARY CONCERN:

Of primary concern to the committee is the college's **continuing increased reliance on IP revenue** to fund its operating budget. The college's tuition allocation reduction (due to enrollment decline across the district) in FY1415 has precipitated a major shift in the way the college uses IP revenues – moving those revenues from the status of supplemental funding source, to that of ***primary*** funding source for both Permanent and Temporary budget increases. IP revenues now provide **ten percent** of the college's operating budget (shown below), and **twelve percent** of the college's $26.5M Permanent level budget.

Chart 1



Detail Amounts 1

STATE - PERMANENT ALLOCATION	$13,225,077		
STATE - TEMPORARY ALLOCATIONS	1,933,231	$15,158,308	47%
TUITION ALLOCATION		8,756,204	27%
IP REVENUES (**10% of $32M**)	**$3,250,000**		
OTHER (RS, IC, M&O, etc.)	1,279,228	4,529,228	14%
		$28,443,740	89%
	CARRYFORWARD	$ 2,156,838	7%
	EXTRA TUITION	1,407,624	4%
		$ 3,564,462	11%
TOTAL STATE OPERATING BUDGET FY1415		**$ 32,008,202**	100%

Concern over the above is coupled with the committee's perspective that IP is an *inherently volatile* program, both in the short and long term - subject to both short and long term downward effects of world events (political, financial, environmental), as well as the basic economic principle that rising markets eventually level out or decline. In addition, it is our understanding that when IP enrollments fall, they fall suddenly (as in from one academic quarter to the next).

PRESSURE ON IP PROGRAM AND ELEVATED RISK:

The committee further developed its model (created in FY 12-13) of the college's use of IP revenues in order to visualize and estimate the effects of additional demands, and the sensitivity of IP revenues to changes in IP enrollment levels and makeup (ratio of college to non-college level students). The model indicated that based on FY1415 performance, the IP program must enroll a minimum of **700 FTES**, of which 74% must be college level, simply to meet the existing annual Permanent level college operations support requirement of $3.25M.

After adding in estimates for additional demands in 1516 (items #1 through #17 of the Schedule) and factoring in a reasoned estimate for Carryforward (to cover part of the costs), the committee concluded that IP must ***at minimum*** duplicate its 1415 performance of 980 FTES for the program to cover the college's need for operating support, and IP's own operating costs.

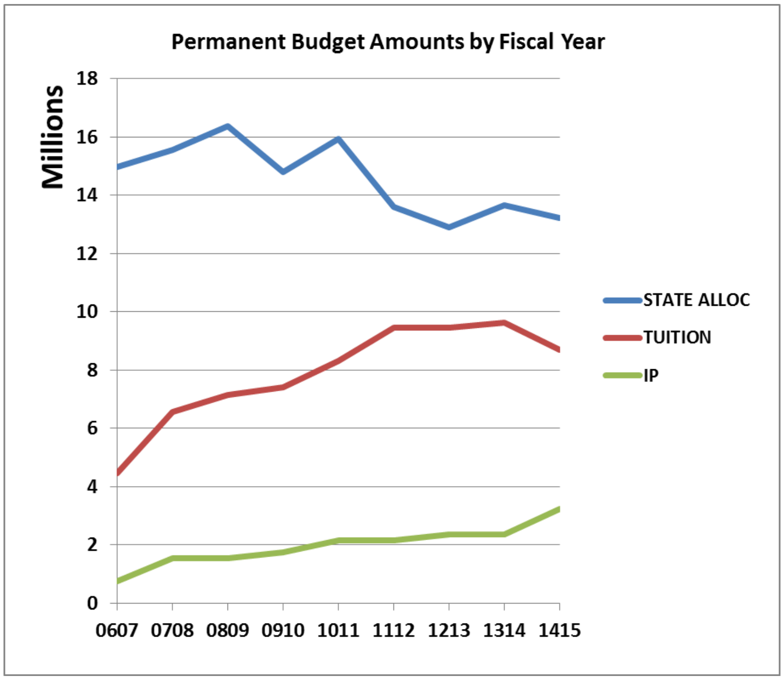
This indicates the point has now been reached in which IP must ***necessarily*** maintain its existing enrollment levels to meet the college's annual need. If the college adds to that need through additional operating budget increases or through adjustments to offset decline in regular student enrollments (as experienced in FY1415), *the condition will intensify – increasing pressure on the IP program, and elevating the college's exposure to risk*. In addition, other factors on the near horizon must be considered once established, such as implementation of the new SBCTC allocation model and its potential impact on the college's annual FTES allocation.

Estimates cited in this section are necessarily based on a reasoned set of parameters and assumptions. The committee is very willing to provide a demonstration of its modeling methodology for critical review, if that is considered of value by President Brown.

TREND:

The movement by the college to increase its reliance on IP revenues is the end result of a chain of events originating in the economic collapse of 2008. That crisis led to a substantial reduction in state allocation (hard funding), with those lost funds being replaced by increased tuition revenues (through increased tuition rates). Subsequent enrollment drop (over the past three years) has resulted in a reduction in tuition revenues and IP revenues in turn are now being used to make up for that difference. This is illustrated in the following graph and figures:

Chart 2



Detail Amounts 2:

SOURCE	0607	0708	0809	0910	1011	1112	1213	1314	1415
STATE ALLOC	14,960,596	15,545,464	16,379,007	14,800,020	15,922,216	13,606,003	12,895,802	13,650,089	13,225,077
TUITION	4,476,062	6,574,456	7,148,584	7,424,422	8,320,104	9,441,983	9,441,983	9,636,983	8,681,204
IP REVENUE	**750,000**	**1,550,000**	**1,550,000**	**1,750,000**	**2,150,000**	**2,150,000**	**2,350,000**	**2,350,000**	**3,250,000**
TOTAL	20,186,658	23,669,920	25,077,591	23,974,442	26,392,320	25,197,986	24,687,785	25,637,072	25,156,281

DEPLETING EFFECTS ON CONTINGENCY RESERVE:

Until now, a mitigating factor in this movement to IP reliance has been the college's Contingency Reserve (CR). As described in last year's BAC memo, the CR is an operating budget set aside (uncommitted operating funds), which the college has carefully increased, managed, and maintained since its budget crisis of 1999-2000.

If fully implemented, Schedule Items 1 through 4 will result in the Permanent level CR being reduced from its current $676K (**2.6%** of the Permanent budget) to approximately $235K. Further known unavoidable Permanent salary adjustments (already in-process reallocations and salary placements not applicable to the Schedule) will further lower this amount to $150.6K (only **0.6%** of the Permanent budget), as shown below:

Detail Amounts 3:

					Amt as Pct of $26.5M 1415 PERM BGT
	CURRENT PERMANENT LEVEL CONTINGENCY RESERVE AMT		**$ 676,374**		**2.6%**
	LESS: ITEM #1 through #4 from SCHEDULE				
#1	SLC: ESTIMATED ADDNL PERM LEVEL FUNDING 1516	$ (236,659)			
#2	LAB SIMULATIONS TECH POSITION ($75K salary + $20.7 benefits)	(95,700)			
#3	STIPEND RATE INCREASE 6% (from $33 to $35 per hr; $15,050 + $2,550 benefits)	(17,600)			
#4	PAY INCREASES - HOURLY (to $13 per hr)	(90,950)	**(440,909)**	$ 235,465	
	LESS: KNOWN SALARY ADJUSTMENTS NOT ON THE SCHEDULE			**(84,853)**	
	PROJECTED OPENING PERMANENT LEVEL CONTINGENCY RESERVE AMOUNT FY 1516			**$ 150,612**	**0.6%**

This is its *lowest level since FY 2004-05* and means that, in the committee's estimation, the college faces entering FY1516 with inadequate contingency funding to cover Permanent level needs and requests (such as Classified increment adjustments, reallocations, adjustments for new hire salary levels, and the New Permanent level requests cited in Items 18 through 21 of the Schedule). Again, there are potentially substantial additional factors on the near horizon that will need to be addressed, once established (e.g. effects of current legislative action, and the downward effects of the new SBCTC allocation model when implemented). In order to provide the necessary funding in 1516, the college will need to do one or both of the following:

- *Permanently reduce an existing Permanent budget item; i.e., reallocate existing resources.*
- *Permanently increase its reliance on a local funding source – IP Revenues, Running Start, Indirect Cost Recoveries.*

Please note that while necessarily included as potential additional funding sources, the levels of revenues generated by Running Start and Indirect Cost Recoveries, in comparison to IP Revenues, make these options limited in effect.

CONCLUSION AND CLOSING COMMENTS:

The BAC thanks President Brown and the Vice Presidents for the importance placed upon this process, and for their prompt and thorough responses to our requests for assistance in our efforts. In closing, after considerable discussion, the committee offers the following observations and suggestions.

The movement to reliance on IP as the primary funding source for both Permanent and Temporary funding of college needs and/or initiatives; the resultant pressure on the IP program and elevated risk for the college; and the recent depleting effects on the colleges Contingency Reserve should be considered warning signs of a significant shift in the college's fiscal condition. They send a clear signal for the college to proceed with caution in increasing the current budget, particularly at the Permanent level.

During its deliberations on the New/Continuation Funding requests (Schedule item numbers 18 through 33), and reflecting on similar evaluations in past years, the committee observed that this annual process can be likened to the college engaging in a *self-funded grant program*. Assuming adequate funding is available, this is not an issue. However, like regular grant programs, attention must be directed to what will happen when the "grant" expires. The committee respectfully offers the opinion that ***the college has now reached the point, fiscally, where simply adding funding to absorb the activity into its ongoing operations is not a sustainable option.***

The committee again thanks President Brown for your support, and for this opportunity to serve the interests of the college.