BUDGET AND FINANCE COMMITTEE

January 29, 2016

Minutes

The meeting was called to order at 11:33 a.m. by Governor Massaron in Room FGH of McGregor Memorial Conference Center. Secretary Miller called the roll. A quorum was present.

Committee Members Present: Governors Massaron, Kelly, Nicholson, Thompson, Pollard; and Professor Romano, Faculty Alternate Representative; Zachary Rich, Student Representative, and Aaron Szpytman, Student Alternate Representative

Committee Members Absent: Professor Beale, Faculty Representative

Also Present: Provost Winters, Vice Presidents Decatur, Hefner, Johnson, Lessem, Staebler, and Wright; and Secretary Miller

APPROVAL OF MINUTES, December 4, 2015

The Minutes of the December 4, 2015 meeting of the Budget and Finance Committee were approved by acclamation, as presented.

CONTINGENCY RESERVE

There were no requests for transfers from the Contingency Reserve Fund, and the FY 2016 balance remains at $500,000.

HOUSING MASTER PLAN

Vice President Decatur introduced the presentation for the Housing Master Plan. The University has experienced a tremendous demand for housing the last few years but has been unable to fill that demand. The administration, therefore, has developed a Housing Master Plan for the next ten years. Mr. Tim Michael, Associate Vice President of Auxiliary Business Affairs and Director of Housing, will review the history of campus housing since 2002 and discuss the implementation of the Plan. Mr. Decatur will cover the Plan's financing and budgeting over the ten-year period.

Mr. Michael presented slides illustrating the building layouts on the campus. With the exception of the University Towers apartment building on Cass Avenue in the southern part of the campus, the current five housing facilities are grouped in a residential precinct in the northwest corner of campus. The advantage to this location is the proximity to the Student Center, the Fitness Center, and the Undergraduate Library, giving the 2500 residents access on a 24-hour basis.

Reviewing the history of the residential facilities, 1800 beds in Ghafari and Atchison Halls and the Towers Residential Suites were completed between 2002 and 2006. From 2005-2008 the housing system struggled with low occupancy and operating deficits. However, 2008-2009 saw a 90% occupancy in both apartments and residence halls. A market demand study done in 2010 showed that there was an unmet demand that would probably continue. However, at that time enrollment was declining and it was decided not to pursue additional housing. By Fall 2012, though, occupancy was again full and there have been wait lists every year since. The Market Demand study was repeated in Fall 2014, showing that the demand had increased. In Fall 2015 a record number of 3147 students lived on campus, essentially doubling the number of students since 2001. To accommodate the overflow, the University arranged to house students at the St. Regis Hotel, supported by 24-hour shuttles and staffing, and also constructed accommodations in the lounges at the Towers Residence Hall.

The housing situation needs to be remedied, and a planning process was begun at the request of President Wilson to look into ways to provide more housing with new construction or engaging with outside partners. Major renovations of the existing facilities have already begun. A review of the DeRoy Apartments showed deferred maintenance costs of almost $38 million, compared to the cost of a new facility at $50 million, resulting in the recommendation to replace DeRoy with new housing. During 2015, the administration developed the Housing Master Plan and also issued RFPs to engage the development community and understand what was available in the marketplace, all with the goal of constructing a financially feasible housing plan over a ten-year period.

Mr. Michael showed data on the three types of housing available on campus— semi-suite, full-suite, and apartment style—the existing bed count, the current demand and deficit of 850 beds, and a projected deficit of 1500 beds when DeRoy goes offline. The plan involves demolition of DeRoy Apartments, the renovation of the remaining five buildings, the construction of two new apartment buildings to be built along Anthony Wayne Drive, and the conversion of the Thompson Home to student housing. Of the existing buildings, Chatsworth Apartments will undergo the most renovation, turning it from unfurnished apartments to suite-style housing and almost doubling the occupancy of that building.

In terms of the time line, the administration would like to convert and open the Thompson Home in the fall of 2017, construct the new apartment buildings and open them in 2018 and 2019, and demolish the DeRoy Apartments in 2019. The plan is to have a capacity of 3750 beds by the fall of 2021. It is expected there would still be an unmet demand of 100 beds but the administration feels it is a manageable number, giving some flexibility if enrollment differs or student demand changes. By 2027 all of the existing buildings would be considered new or newly renovated, providing about 800 more beds than currently available.

In response to Mr. Rich's question about parking, Mr. Michael said there will not be additional parking construction. The two new apartment buildings will be built on the surface Lot 41 in front of Structure 2. Parking structure 1, just north of the Law School, has a great deal of capacity, and some students may have to be shifted to that structure to accommodate the loss of the parking lot. Mr. Michael then turned the presentation over to Vice President Decatur to discuss the financial aspects of the plan.

Mr. Decatur stated that the ultimate goal in financing the Housing Master Plan is to preserve the University's debt capacity to the largest extent possible for top priority academic and research facilities. To do so, the University is studying the possibility of using a private partner who would issue the debt, or a private equity partner, who would bring equity cash to the project as well as issue the debt. In both cases, the University will not have issued the debt and it will not show up on its balance sheet. The alternative is that Wayne State funds the plan and all the debt appears on its balance sheet as well as on its credit. However, a key variable was Moody's and S&P's determination of how much of the debt, if any, would show up on the University's credit, and that opinion would not be given until the administration is well into the evaluation process. A determination to place the debt on the University's credit would be a disadvantage, since in order to go with a private partner the University must pay additional fees, and under those circumstances it would be much less expensive if the University funded the construction on its own. Therefore, the administration has been evaluating the RFPs to find what will be listed on its credit to try to avoid the situation, and to be prepared to pursue either the private equity/private partner strategy or, if necessary, the traditional strategy.

To illustrate the potential benefits of a private partner, Mr. Decatur showed a detailed chart comparing the costs of the Chatsworth conversion if WSU funded the plan, at $31.2 million, to those by a private partner at $29 million. The detailed breakdown of the costs, however, show where private partners would have advantages over a public university. Chatsworth is a historic structure and eligible for historic tax credits, which are not available to a university. Private partners are likely to have relationships with firms that could drive down construction costs. These two advantages, together with the equity contribution by the partner, would require financing by the partner of only $14.4 million as opposed to the University's full cost of $31.2 million. With regard to revenue and operating expenses, it is important to remember that private partners work for a return on their investment and that gets reflected in the cost. The challenge for the University would be to negotiate controls over how quickly student housing rates increase. A source of revenue for the University would be a ground lease, since almost all such financing structures and contracts with private developers include a ground lease payment to the university.

Vice President Decatur reviewed the general assumptions and the financial performance expectations within the Housing Plan. The Housing Division has been subsidized at $1.25 million per year, a subsidy that will be gradually phased out by 2027. During the difficult early years, the Division incurred a deficit of $4.75 million that has been left on the books because it was considered more important to use available funds for deferred maintenance. However, the administration will begin addressing that deficit during the next ten years. Annual room and board rates, an important negotiating point with any private partners, should increase no more than 3-5%, and annual revenues and expenses are subject to change in negotiation. Mr. Decatur noted that private partners, because they are a private entity, are subject to property taxes, and the university could help to obtain a tax abatement for them during that 10-year period; on the other hand, certain conditions could result in a tax increment for the University. The financial performance expectations he and his staff worked out with housing and investment consultants assume that annual cash flow will remain positive and reach consistent growth after the 10-year period. The Housing Reserve balance will vary but always remain positive, and an annual ground lease payment will be made by the private equity partners for projects, beginning in 2019 with continuing growth over the period of the agreement. The last charts illustrated the implementation and financing of the housing projects, listing the projects in the order they would be done and showing the funding mechanism, the renovation type, and the total project cost. Mr. Decatur noted that each of the projects would come to the Board for separate approval. The charts also showed the debt incurred by the University and by the private partner, as well as the equity contributions of each, both as a total project cost and by year through 2027.

Mr. Michael returned to the discussion and gave a quick review of the housing situation. The University recently found an owner who is renovating an apartment complex near campus and will rent the entire building of 150 rooms to the University. Having the building available lets the University meet the last-minute needs of international students, transfer students, and late-enrolled graduate students, populations that they have been unable to help. It also frees up more space in the residential precinct for undergraduate students and the larger freshman class that is expected. The Thompson Home when it opens in Fall 2017 will add 60 beds, and the new apartment buildings, roughly 420 beds each, are expected to open in the Fall of 2018 and 2019.

Mr. Michael expressed his appreciation to everyone who contributed to the development of the Master Housing Plan, including resident students, residence hall association leadership, his staff, and staff from Facilities, Planning and Management. The administration now has a complete facility audit knowing exactly what the conditions are in each building and what major investments must be made to maintain them at a high level for the students. He also stressed that this is a plan that is based on assumptions that might change over the ten-year period. The partnerships his division has developed with other areas of the University, such as Enrollment Management, Admissions, Financial Aid, the deans and the colleges, all are important and will affect how the plan develops. Mr. Michael added there is a great deal of interest on campus, and it was good to see how students expressed their feelings about living on campus, how it has supported their academic progress, and connected them to the institution. A successful Master Housing Plan would continue that feeling of engagement with students. Mr. Michael concluded the presentation.

Governor Massaron asked if the Plan is being presented to the Board for adoption. Secretary Miller replied that this is an informational report, and Mr. Decatur added that it will be regularly monitored and possibly adjusted depending on the circumstances. Each of the individual projects will come to the Board for approval.

Mr. Rich asked about the housing demand for the current winter term, and whether there is a wait list this winter. Mr. Michael replied that there are always vacancies in the winter semester because students drop out, transfer, or take leaves of absences, usually beginning in December. All the extra students at the hotel have moved back to the main campus, the lounges have been emptied, and the residence halls are currently 95% occupied. There are no waiting lists since those students are contacted and accommodated as spaces become available.

Professor Romano asked about the length of the waiting list and whether it is cut off at a certain point and no additional names added. Mr. Michael replied that last summer the wait list started July 23 for both the residence halls and the apartments; the apartment wait list reached 500 by mid-August and the residence halls about 150. His staff kept in daily touch with students prioritizing students according to who could commute, if necessary. It is difficult to manage the wait lists, however, since many students who already have a room often ask to be placed back on the list for different types of accommodations. Professor Romano explained that his concern is whether students who are placed on wait lists or turned away in the summer decide to leave Wayne State and go elsewhere. In such a case, wait lists could influence enrollment negatively, and he felt this would be a good issue to examine.

A second question dealt with how types of housing are decided upon. Apartments would be more expensive than suites or dorm rooms, and he wondered whether the decision process considers costs for undergraduates, and what is the mix of undergraduate and graduate students. Mr. Michael replied that Brailsford and Dunlavy, the national consulting firm that did both the market demand studies, sent a 100-question survey to the entire student body asking in great detail the type of housing they would like and at what price point. It turned out the greatest demand is for one-, two- and four-bedroom apartments for undergraduates. That is the type that will be built on Anthony Wayne Drive, as furnished apartments that will be rented by the private bedroom. The demand is clearly for undergraduate housing; students want a private bedroom but are still interested in living with others. The new apartment buildings, however, will not be limited to undergraduates. Upperclass students even graduate/professional students could live there. Mr. Michael anticipates that many of the floors will be designated for residentially based learning communities.

Governor Thompson said she wanted to get a better understanding of the Wayne State versus private partner option for implementing the project, especially the negative aspects of working with a private partner such as fees and property taxes. Vice President Decatur reiterated that the primary goal is to keep the debt off the University's balance sheet and off its credit so that it can be reserved for academic and research facilities. Funding the housing construction in the traditional manner would mean squeezing out other priority facility projects. He explained that not all private partners are the same. Different firms have different approaches that vary broadly. A traditional 3P, public-private-partnership often entails creating a separate non-profit corporation that owns the facility and manages it; they are non-profit so there is a waterfall of funds. Ultimately some net income comes back to the University. The developer takes a fee up-front and a fee throughout the operation or the term of the contract. The University's preference is a private equity partner who comes in with cash and will take out the debt. The debt will be off the University's balance sheet but the question is whether it is off its credit.

The challenges include first, negotiating the details of student life. The University wants to manage student life, and not all developers are conducive to that. Another point of negotiation is maintenance of facilities. Private equity partners have an investment in the building, so they do not want to let deferred maintenance accumulate, and neither does the

University. Finally, the fees for the rate of return are subject to negotiation. A private equity arrangement is looked at as a real estate transaction, so they are looking at anywhere from 9% to 13 or 14%. Mr. Decatur restated that the University's foremost desire to have active student life programs and living/learning communities in the buildings; the rest is subject to negotiation.

Mr. Rich questioned what the University's plans are to avoid a situation it currently has with DeRoy, a 40-year-old building that must be demolished, while Chatsworth, built in 1929, is still viable. Mr. Decatur replied that the University is developing financial pro formas that will result in income to be put into housing reserves for re-investment. With reference to DeRoy, he explained that the building is very much an exception. There were problems from the beginning of construction, with a class action lawsuit involving the manufacturer of some of the materials. There have been many repairs and significant renovations of the envelope of the building, but it has reached a stage where it no longer makes sense to invest in the building. In the future, the administration hopes to avoid similar situations during construction; it also plans to build the funding of deferred maintenance into its financial plans.

Mr. Rich wondered whether a parking lot could be assigned to student residents, especially since the two lots on Anthony Wayne Drive will be eliminated. Mr. Decatur replied that he understand there will have to be adjustments; however, no decisions have been made yet and that will be one of the issues up for review as the plan is implemented.

Governor Massaron questioned whether there was student participation during the development of the Housing Plan; specifically, whether Student Center staff was contacted. Mr. Michael responded that members of the Residence Halls Association (RHA) participated during the development of the plan. The RHA serves as a housing office advisory board; it is based on a national model and is part of all university housing divisions. Governor Massaron suggested that the administration also consult with the Student Center staff during the implementation of the Housing Plan.

Governor Nicholson noted that the University's mission is research and academics. He wondered if the University should continue with the business side of housing and focus on its real mission. Vice President Decatur replied that is one of the options the administration is reviewing. One such model exists currently in the U.S. at the University of Georgia, which sold their entire housing across all of their universities to a separate related organization and negotiated for control over their student life programs. It is a new model, and the organization has approached other universities in Michigan and around the country. Wayne State is certainly amenable to the idea of turning over the physical aspect of the housing business and focusing instead on the educational and research mission, but it will insist on maintaining control on the living/learning communities and the student life experience.

Professor Romano had several comments. First, he referred to the list of financing projects and noted that the Towers are listed twice. Mr. Michael clarified that those are two separate buildings. The University Towers, with a $52 million project cost, is the building on Cass Avenue; the Towers with a $19 million project cost refers to the residence hall on Anthony Wayne and Kirby. Second, Professor Romano called attention to the $217 million in new debt. He understood that the $1.5 million annual subsidy to housing will gradually be paid down during the next ten years, but asked whether the administration expects that the revenue from housing will cover all the debt costs later on. Mr. Decatur responded that is the over-riding assumption and primary goal of the Housing Plan, that housing must be self-supporting. Finally, Professor Romano commented that the faculty had no input on the development of the plan, even though this issue will profoundly affect the University. He stated that in the future, faculty consultation should be part of any major plan to change the University. Vice President Decatur replied that the administration plans to create a facility planning group that will include Faculty Senate participation.

THOMPSON HOME CONVERSION TO STUDENT HOUSING

Vice President Decatur next presented a recommendation to begin design phase activities for the conversion of the Thompson Home to student housing, which was one of the projects listed in the Housing Master Plan. The building was constructed in 1874 and since 1990 housed the School of Social Work, which has just relocated and left Thompson Home vacant.

> **ACTION** – upon motion by Professor Romano and seconded by Governor Nicholson that the Budget and Finance Committee recommend that the Board of Governors authorize the President, or his designee, to award contracts to begin design phase activities for eventual construction to convert the Thompson Home into residential student housing for a cost not to exceed $350,000. Funding for this project will be provided from the housing maintenance reserve.

Governor Pollard noted that the DeRoy apartment building, constructed in 1972, is scheduled for demolition. Since the Thompson Home was built in the 1870s, he wondered what its life expectancy was for student housing, and specifically whether the modern amenities that students expect nowadays can be built into the structure; also, whether there will be 24-hour security.

Mr. Decatur replied that DeRoy is a unique situation, given the manufacturing defects in the original building materials. The Thompson Home, on the other hand, is a substantial historical structure which has a great deal of character that will be attractive to many students. The project plan includes a community kitchen on each floor as well as on the lower level, IT, a new stair tower, improved sound attenuation, and upgrades to the life, safety, and electrical systems. Mr. Michael added that the building is structured to maximize the living/learning concept. The floor plates are resident rooms around a large common space for about 15 students per floor, and there is a good deal of study area and community space in the building, as well as a public dining room that could accommodate large dinners. All of the security features that are present in each of the residential buildings will be provided, including 24-hour security. In response to Mr. Rich's question, Mr. Michael said that air-conditioning and an elevator for the five-story building will also be provided.

> **ACTION** — Upon motion by Professor Romano and seconded by Governor Nicholson, the Budget and Finance Committee recommended that the Board of Governors authorize the President, or his designee, to award contracts to begin design phase activities for eventual construction to convert the Thompson Home into residential student housing for a cost not to exceed $350,000. Funding for this project will be provided from the housing maintenance reserve. The motion carried.

HARWELL FIELD BASEBALL BUILDING

The next recommendation dealt with the design and construction of the Harwell Field Baseball Building, which would be built behind home plate on the baseball field. The project cost of $1,660,000 would be provided from funds raised by the Athletic Department. Vice President Decatur explained that in 2013 the Department, in conjunction with the Ernie Harwell Estate and Foundation, announced the establishment of the Harwell Field project, as an outreach effort to raise funds to construct the building in recognition of Ernie and Lulu Harwell. The project will benefit not only WSU's baseball team, the last college baseball team still active in Detroit, but will also serve as a resource and destination for camps, youth leagues, and high schools that use the facility throughout the year.

Governor Kelly asked for more specifics on the use of the facility as a display area for baseball memorabilia, and whether it is an appropriate use of the grant money. Associate Vice President Sears replied that the largest quantity of space allocation will be a display area in the center of the building for the various artifacts and memorabilia presently housed with the Detroit Public Library and the Detroit Historical Society. There is also meeting space, as well as storage and bathroom facilities. Future plans include a press box and stadium bleachers and possibly baseball locker facilities. He added that the funds were raised for the specific purpose of using the facility as a display area.

Governor Thompson asked whether any of the funds raised would be placed into an endowment to be used for future maintenance, and if not, what would be the impact on the University budget. Vice President Decatur replied that there will be some maintenance and custodial costs that will be funded out of the Athletic budget, but that the gift itself is designated entirely for the construction of the facility. In addition, staffing would be provided since the display area would be open to the public during regular business hours. In the ensuing discussion, some committee members expressed concern about the University's having to incur maintenance and staffing costs for the building, and Professor Romano asked whether the Athletic Department expects an increased budget or whether the costs will be taken out of their existing budget. Mr. Sears explained that he expects the costs of maintenance and operations to be about $15-$20,000 per year. In terms of staffing, he understood that the Athletic Director would provide existing staffing for scheduled events and for guests viewing the collection, so that there would not be any additional costs. There would not be a charge to view the collection, since the building is intended as a community service.

> **ACTION** — Upon motion by Governor Pollard and seconded by Mr. Rich, the Budget and Finance Committee recommended that the Board of Governors authorize the President, or his designee, to design, solicit bids, and award contracts to construct the Harwell Field Baseball Building located on the Matthaei Athletic Campus for a project cost not to exceed $1,660,000. Funding for this project will be provided from funds raised by the Athletic Department for this purpose. The motion carried, with Governors Massaron and Thompson abstaining.

Governor Massaron asked that the administration provide written explanations and responses to some of the questions that were raised in the discussion. President Wilson apologized for the Athletic Director's absence, explaining that he was in a meeting with the donor.

ANNUAL REPORT ON THE LONG-TERM INVESTMENT PROGRAM FOR THE FISCAL YEAR ENDING SEPTEMBER 30, 2015

Vice President Decatur presented the informational report named above that was prepared by his staff and the New England Pension Consultants, the University's financial advisor. The endowment value as of the end of FY 2015 was $288 million, representing a 4% loss for the fiscal year. The peer median return was a loss of 2.1%, which meant that WSU's performance ranked it at the 76th percentile. Mr. Decatur indicated this was unacceptable, and the Foundation and its Investment Committee have already made changes in asset allocation strategy and a change in some managers, and have also adopted a new investment policy that mirrors WSU's peer institutions and adopts best practices. Finally, the Foundation has been considering alternative models and an RFP process for either an investment advisor or an outsourced chief investment officer. Mr. Decatur stressed that the goal is to improve the investment performance of the endowment fund to match or do better than WSU's peers. The endowment funded approximately $13.2 million of university programs during the prior year and is an important resource for the University's academic programs and scholarships.

Governor Massaron indicated that once the Foundation's Investment Committee makes its decisions, he would like a report on the rationale for the selection of the model that is chosen. He said it is important that the decision be made soon and implemented quickly, adding that the report was not satisfactory and the endowment fund must be managed more effectively.

FY 2015 GENERAL FUND YEAR-END REPORT

Associate Vice President Kohrman presented the FY 2015 year-end report comparing the General Fund approved budget with the actual results. The revenue area showed an increase of $11.5 million above budget, or a positive variance of 2%, while expenditures and transfers were $15.6 million above budget, or a –2.7% variance, leaving a decrease in the fund balance of a negative $4.1 million.

The positive revenues were a result of increased enrollment and tuition fees of $8.9 million above budget, as well as increased research activity and indirect cost recovery revenues of $2.6 million above budget. On the expenditure side, facility services had a positive variance of $4.1 million over budget as a result of the rate changes from the Public Lighting Department to DTE Energy. However, compensation and fringe benefits and early retirement resulted in costs of $17 million over budget, and General Operating expenses came in at $2.9 million over budget.

Mr. Kohrman also showed charts that reviewed budget performance over the last ten years. The first chart compared WSU's performance with that of the Higher Education Price Index (HEPI), similar to the CPI but using only indeces relating to higher education such as faculty salaries and utilities. Both WSU and HEPI have averaged 2.5% over the ten-year period.

The second chart looked at the budget versus actual variance by both revenue and expense for each year from 2007 through 2015 and averaged the totals over the nine-year period. The revenue has averaged about .8% better than the budget, while expenses also averaged .4% above budget with a negative variance.

The final chart provided the calendar for preparation of the FY 2017 budget. Mr. Kohrman noted that although the State of Michigan Budget Outlook from the Revenue Conference projected a surplus of just under $500 million, he expects that a good portion of those funds will be allocated to the Detroit Public Schools and the city of Flint. At the next Board meeting on April 1, the administration will present the housing rates for approval, and the School of Medicine tuition rates will be presented for approval at the May 6 meeting. At the June 25 meetings, the administration will present for approval the FY 2017 tuition and fee rates, the FY 2017 General Fund budget, and the FY 2017 Auxiliary Fund budget. Additional meetings will be held with the Student Senate, the Academic Senate and its Budget and Policy committees, as well as with Board members.

Professor Romano noted the buy-down of the receivables for the Pharmacy School and asked if the receivables from the School of Medicine were included. Vice President Decatur explained that Mr. Kohrman's report focused on the FY 2015 General Fund budget versus actual performance. The FMRE write-down referred to by Professor Romano does not show up in the General Fund; it appeared on the balance sheet and reduced the unrestricted net assets. That issue will be considered at the next audit committee meeting when the audited financial reports will be reviewed, after which the administration will present an overview of FY 2016 compared to 2015 at the next Board meeting

PURCHASING EXCEPTIONS

The administration presented a report of purchase orders greater than $25,000 that were issued in October and November 2015 without soliciting competitive bids. There were no questions or discussion.

ADJOURNMENT

There being no further business, the meeting adjourned at 12:53 p.m.

Respectfully submitted,

Julie H. Miller
Secretary to the Board of Governors