

September 19, 2017

**SETTING A CONTEXT FOR FISCAL YEAR 2019
BUDGET DEVELOPMENT**

Submitted for: Informational

Summary: *Setting a Context for Fiscal Year 2019 Budget Development* is intended as an overview for the Board as it develops its Fiscal Year 2019 budget recommendations. It is presented to help stimulate thought and discussion with Board members and staff at state universities and higher education agencies.

Traditionally budget development for the coming year would focus primarily on the current status and the previous year. However, the Fiscal Year 2018 budget comes at the conclusion of a 25 month budget impasse that significantly impacted higher education delivery in Illinois. Also, higher education funding had already experienced an extended decline in state support prior to the impasse. This is not a situation where we are working from incremental change over an extended period. It is important to document the full scope of the impact of both the impasse and the period ten to 15 years prior to the impasse. It also is important to document the excellent efforts of community colleges, public universities and others in the higher education community to continue to meet the mission of higher education in Illinois, even as resources have diminished.

Action Requested: None



SETTING A CONTEXT FOR FISCAL YEAR 2019 BUDGET DEVELOPMENT

*When looking to the future, remember the past,
particularly Fiscal Year 2016*

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ILLINOIS BOARD OF HIGHER EDUCATION



**“Those who don’t study history are doomed to repeat it.
Yet those who *do* study history are doomed to stand by
helplessly while everyone else repeats it.”**



Looking Back to Plan the Future

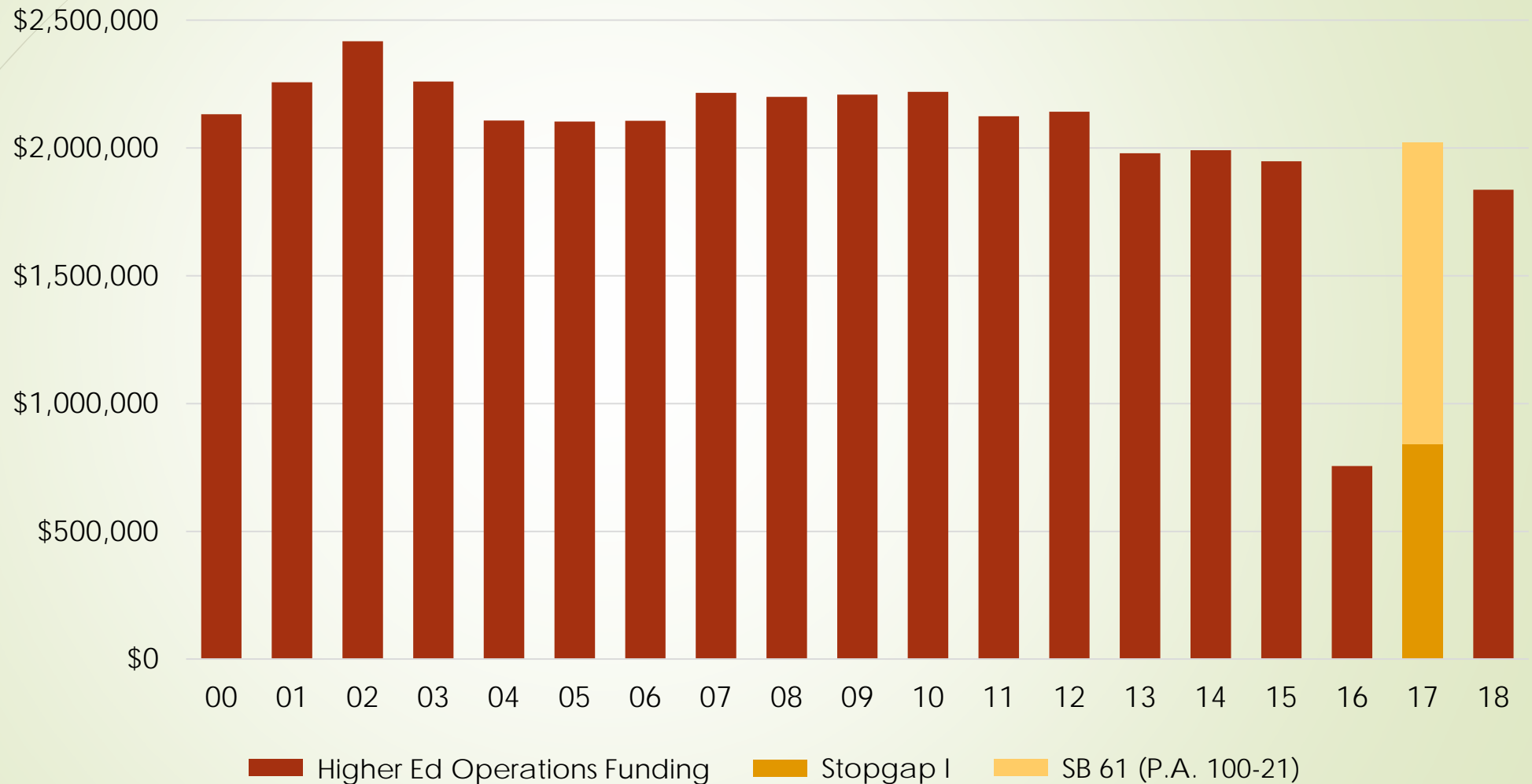
- ▶ Budget development process is inherently forward looking
- ▶ In a perfect world we would like to focus on the future
- ▶ However, the most significant aspect of where Illinois higher education starts is where it came from
 - ▶ Decline in state funding for operations & grants starting FY12 & really all the way back to FY02
 - ▶ Pensions displacing operating funding in state appropriations
 - ▶ The budget impasse took a heavy toll
 - ▶ Only 30% of FY15 funding for FY16
 - ▶ New FY18 base 10% lower than FY15/FY17
- ▶ Negative impacts of the past must be taken into account as we look towards the future




Review of Trends in Illinois Higher Education Funding

Problems Building Even Before the Budget Impasse
Heavy Blow from the Impasse

Higher Education Funding – FY 2000-2018



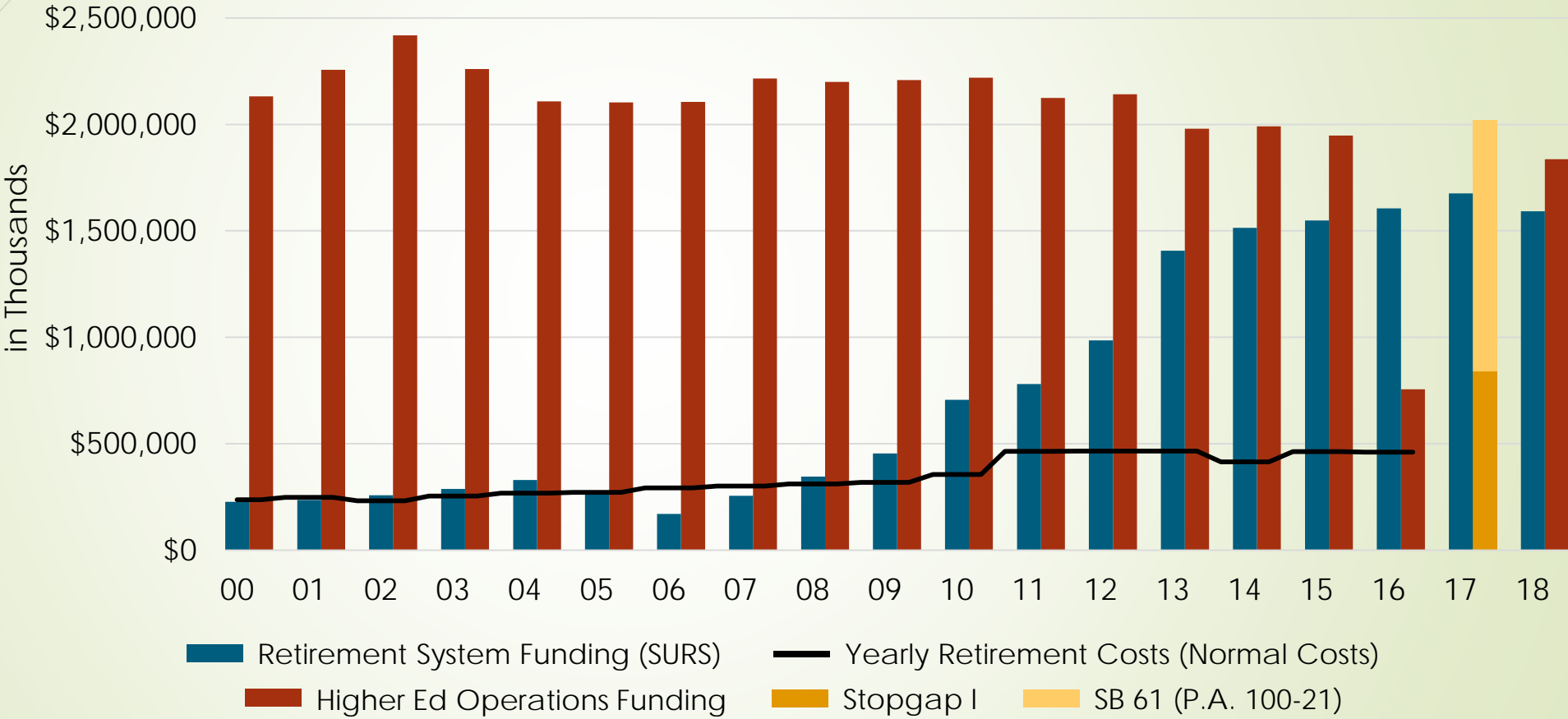
Note: FY17 amount includes Personal Property Tax Replacement Fund and the Fund for the Advancement of Education in addition to General Funds



Higher Ed. Funding, Excluding Pensions

- ▶ Funding for higher education other than pensions peaked in FY02 at \$2.4B
- ▶ Between FY04 and FY12 funding increased by just 1.6%
 - ▶ Resulting in a substantial decline in buying power against any measure of inflation
- ▶ Steeper cuts have been experienced since FY12
 - ▶ Including the 10% cuts in most areas for FY18
- ▶ Greatest impact came from FY16
 - ▶ Lose of \$1.2 B overall
 - ▶ Something universities & colleges could not anticipate

State Pension Funding to SURS Compared to Higher Education Funding Fiscal Years 2000-2018 (General Funds)



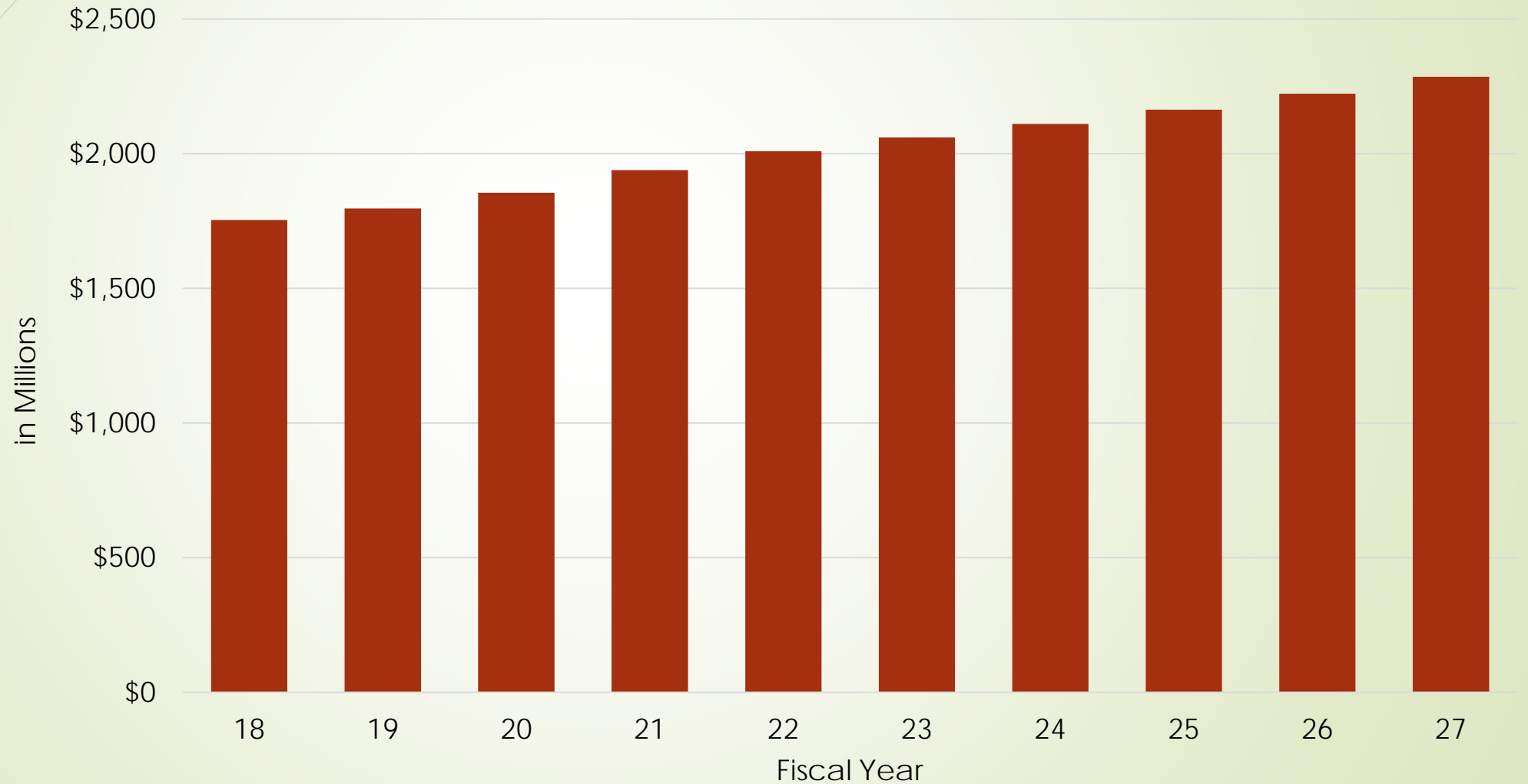
Note: In FY04, a special payment of \$1.4 billion that was made separately to SURS is not factored since it was a one-time payment as the result of bonds sold by the State in July, 2003. FY17 amount includes Personal Property Tax Replacement Fund and the Fund for the Advancement of Education in addition to General Funds

Pension Costs Dominate HE Funding Growth

- ▶ While funding for higher education operations declined, pension funding has increased sharply
- ▶ Normal Pension Costs = amount SURS calculates is required to cover 100% of the pension costs of persons employed that year
- ▶ SURS appropriations have soared as the state attempts to address historic underfunding based on a schedule to reach 90% funding for all obligations by 2045 as set by state law
 - ▶ Every dollar above the normal cost line goes to pay past obligations
- ▶ NOTE: FY18 amount represents the appropriations & is based on estimates of savings from pension changes
 - ▶ The appropriation is significantly less than the amount certified by SURS to meet state obligations under state law

SURS Projected Total State Contributions

Fiscal Years 2018-2027



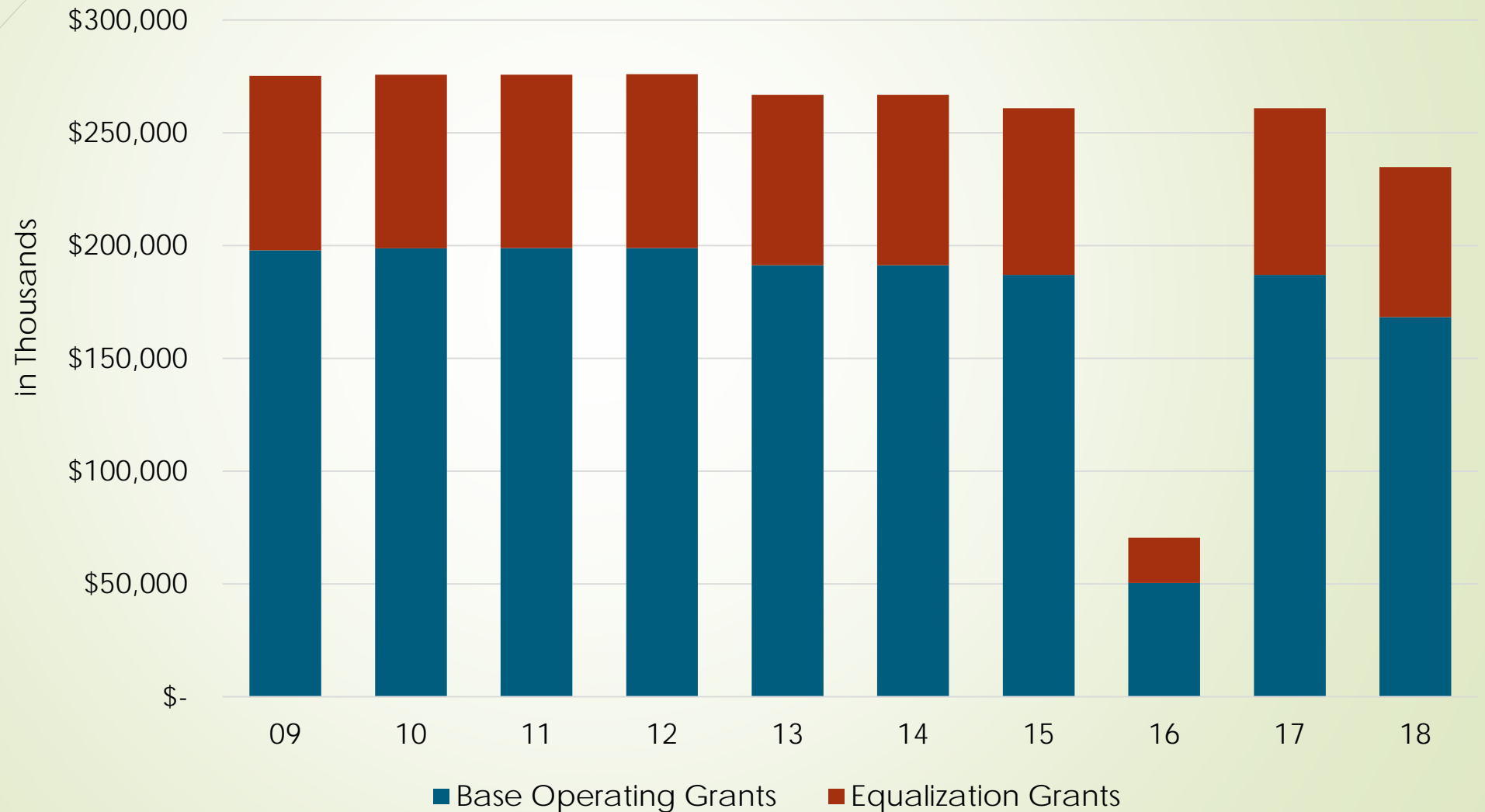


Pension Pressures Will Continue to Increase

- ▶ Normal pension costs only rise slowly in line with salaries paid
 - ▶ Changes in assumptions could make it go up as well but also down
- ▶ 2016 normal costs actually were slightly less than for 2015
 - ▶ Layoffs & hiring freezes mean 2017 normal costs will decline as well
- ▶ Obligations to cover past pension liabilities will continue to increase as the state mandated amounts required to reach 90% funding continue to increase
- ▶ The situation is the same for other state pensions
- ▶ Growth in required payments to pension funds represents a significant & growing competitor for scarce state resources

State Appropriations for Community Colleges

Fiscal Years 2009-2018





Community College Funding

- ▶ FY17 funding was equal to FY15 but comes after funding for FY16 was just 30% of FY15
- ▶ Reserve funds had to be tapped, financially weakening most
- ▶ No expectation of any funding to make-up reduced FY16 funding
- ▶ With only partial funding provided for FY17 until after the year was finished, reserves continued to be drawn down
- ▶ With payments flowing again for FY17, colleges have received some funds & finances will recover somewhat as the year progresses
- ▶ But, the 10% reduction for FY18 continues the downward trend in funding for community colleges

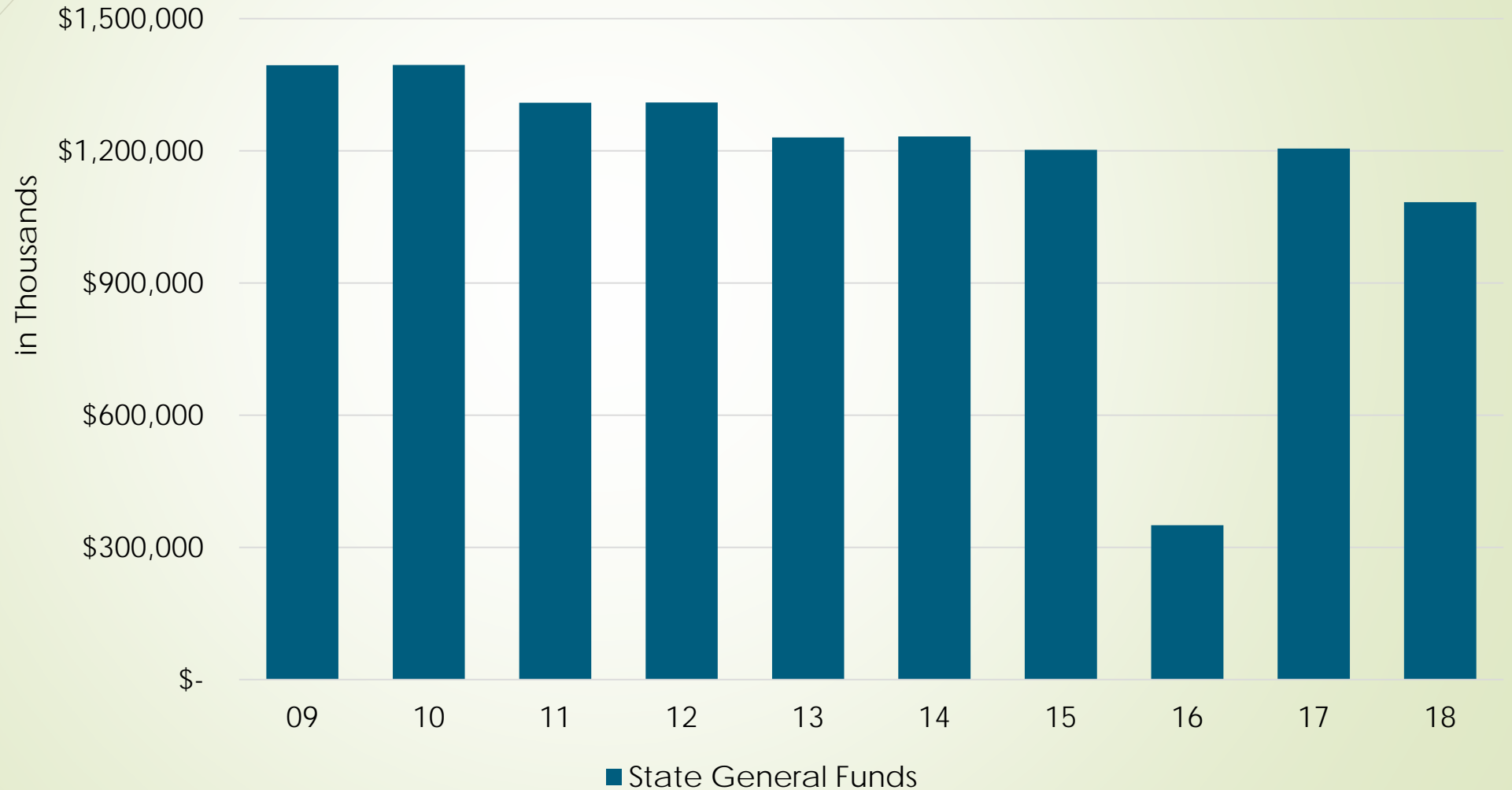


Community College Funding

- ▶ Community colleges were to depend on property taxes, state dollars & tuition & fees in relatively equal proportion
- ▶ Property taxes covered a relatively constant portion of costs since 2000 until the budget impasse, decreasing from around 44% to 42%
- ▶ The proportion of costs covered by the state have declined by almost half, from approximately 28% to <15% by FY15
 - ▶ State share will be even lower for the years since (to be included in FY19 budget request)
- ▶ Tuition & fee revenues have filled the gap
 - ▶ This trend is unlikely to change with a 10% reduction in state funding for FY18
- ▶ Community colleges are the most affordable higher education alternative but this trend presents an affordability challenge for those most in need

State Appropriations for Public Universities

Fiscal Years 2009-2018

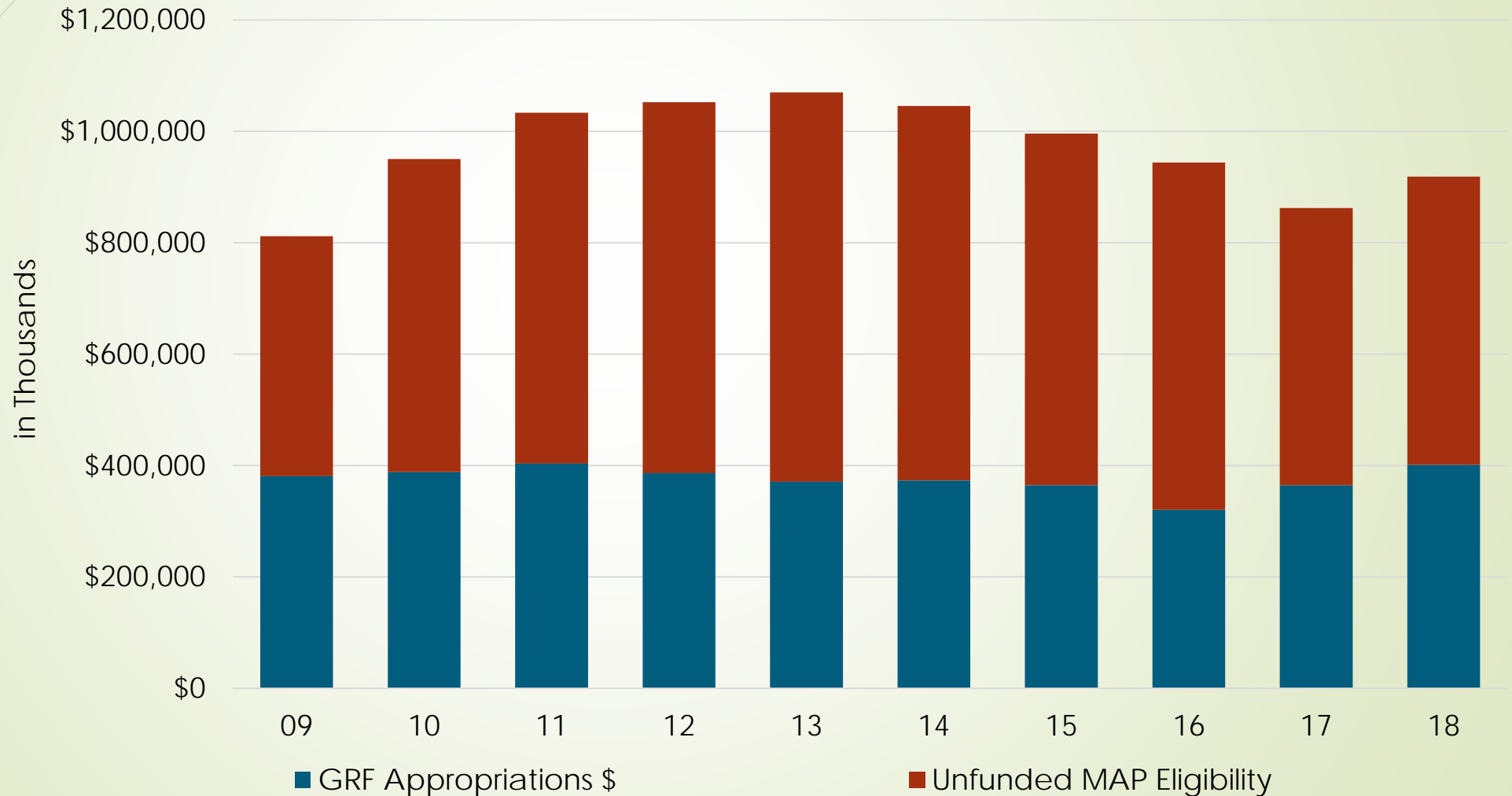


Public University Funding

- Universities faces problems similar to those discussed for community college but even more pronounced
- Universities do not have property taxes to depend on
- 2001: State General Revenue, 72.3% vs. Income Funds, 27.3%
- 2015: State General Revenue, 38.7% vs. Income Funds, 61.3%
- 2001-2015: State Support, -14.8%, Income Funds, +250%
 - To be updated for FY19 budget request, % support will have declined farther
- In spite of FY17 funding equal to FY15, FY18 10% reduction continues a trend of reduced state support
 - in addition to dramatic loss of FY16 funding
- Not receiving 46% of their FY17 appropriations until after the end of the fiscal year put additional pressure on universities until funds started flowing

Monetary Award Program Funding History

Fiscal Years 2009-2018





Monetary Award Program Funding

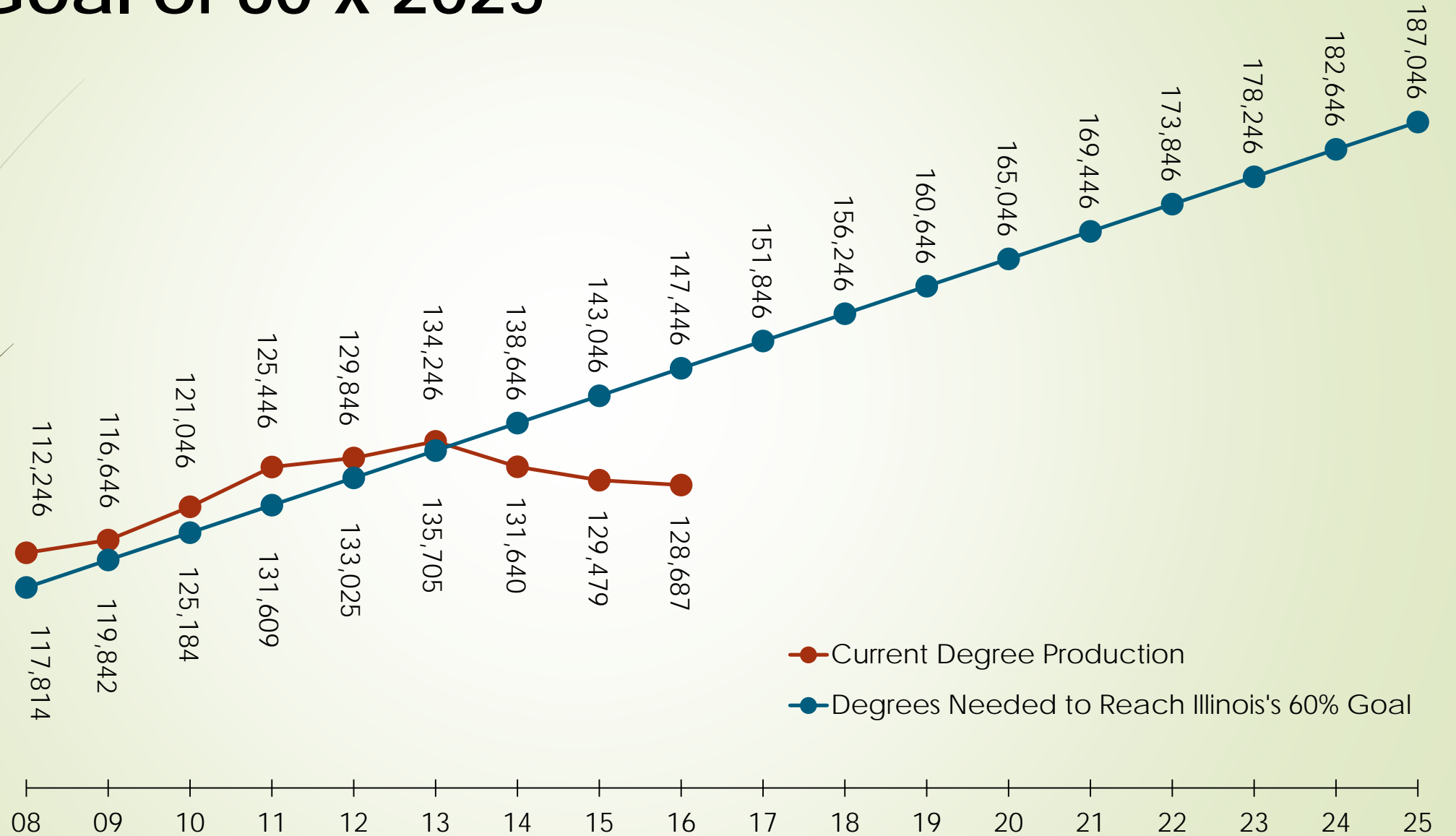
- ▶ With a 10% increase for FY18 MAP is a bright spot but the story is less positive from a historic perspective
- ▶ MAP funding declined significantly between FY11 & FY16
- ▶ FY17 funding equaled FY15 but was not passed until after June 30
- ▶ ISAC could only plan for FY17 funding equal to the lower FY16 level
 - ▶ They have been able to adjust FY17 allocations since to address identified needs
- ▶ In spite of the 10% increase for FY18 to \$401.3 M, the appropriation is lower than the \$403.5 M peak FY11 appropriation
- ▶ Proportion of eligible costs funded fell from 47% in FY09 to 34% in FY16
 - ▶ Effectively a cut of 27.7% in what MAP covered
- ▶ Projected proportion of eligible costs covered increases to 43.7% for FY18 but still below the 47% for FY09



Growing Deferred Maintenance

- ▶ Deferred maintenance is another underlying problem for community colleges & universities
- ▶ Deferred maintenance at universities & community colleges has roughly doubled in the last decade to over \$4 B
- ▶ Little funding for capital of any kind for many years
- ▶ Approximately 80% of the \$139 M capital appropriated for FY18 was for new construction
- ▶ Three of the FY18 projects have been approved to start
 - ▶ The rest likely will not be approved in the near term due to limited fund availability in the Capital Development Fund

Goal of 60 x 2025





Meeting the 60 x 2025 Goal

- ▶ Ultimately, the important question is whether higher education is making the state competitive by preparing citizens for the workforce
- ▶ The 60 x 2025 goal is an excellent distillation of that measure
- ▶ GOAL: 60% of adults with degrees or certificates by 2025 based on the expectation that 60% of jobs will require a degree or certificate by 2025
- ▶ Illinois was progressing towards the goal until FY13 but the state has moved away from the goal line since
- ▶ Trend away from the goal started before the budget impasse
- ▶ Downturn in enrollments during the impasse exceeded national trends



Other Pressures

- Higher education also faces some significant, hidden pressures
- Unfunded mandates include:
 - Health insurance payments – \$45 M paid by public universities
 - Veteran's Tuition Waivers – FY16: Universities, \$17.1 M, Comm. Colleges, \$6.3 M
 - National Guard Tuition Waivers – FY16: Universities, \$7.3 M, Comm. Colleges, \$12.5 M
 - Cap. Development Board – 3% management fee of capital projects
 - Procurement rules were loosened last year but remain costly & burdensome
 - Pension changes that push future payments on to employers



Pension Law Changes

- ▶ Employer responsible for the employee normal cost on the amount earned in excess of Governor's salary (\$177,500 in FY18)
- ▶ Creation of Optional Hybrid Plan (OHP = defined benefit & defined contribution) at a future implementation date determined by SURS
- ▶ New employees hired on or after implementation of the OHP choose between the self-managed (SMP), OHP, traditional defined benefit or portable defined benefit plan
 - ▶ OHP will be the default plan for employees who do not select a plan
- ▶ Employer responsible for the costs of new employees, other than those selecting SMP, hired on or after the implementation of the OHP
- ▶ Employers responsible for existing employees who elect to switch to the OHP
- ▶ These changes will create a new pressure on higher education funding going forward



Past is Prologue?

- ▶ Will history be repeated?
- ▶ Will the state go back to the same old path?
- ▶ Let's hope not
- ▶ BUT it will take a special effort to remind people of the damage left by the budget impasse
- ▶ *WHY? It seems so obvious?*



No Easy Button

- ▶ Traditional budget development focuses on the just finished year (FY17) & the budget year (FY18)
- ▶ Budgeting for the following year (FY19) starts from that base
- ▶ Anything prior to FY17 is only highlighted in what we provide in addition to the basic forms
- ▶ The trend lines tell a compelling & worrisome story
- ▶ However, **the budget impasse left a mark of historic significance**
- ▶ Receiving only 30% funding for FY16 was a painful hit no other major sector of state government had to endure
- ▶ Normal budget process & natural tendencies make it hard to get attention to the lasting damage of the budget impasse



Swimming Against the Current

- ▶ There is an endless list of demands for limited resources
 - ▶ Starting with increasing pension pressures
- ▶ In spite of the income tax increase, the state still has \$15 B in debt
- ▶ Generally believed the budget still is not in balance
 - ▶ There will be pressures to make even more cuts
- ▶ Strong tendency to overlook what was done in the past
 - ▶ It is inconvenient to recognize the negative consequences of past actions, even severe shocks like the FY16 budget



Swimming Against the Current

- Assumption you are dealing with the money you have just fine
- Assumption there always is waste that can, and should, be cut
- Reserves are critical to healthy universities & colleges but it's a difficult concept for many to grasp
 - The state has \$15 B in unpaid bills & huge pension debt
 - State agencies do not have reserves, except for special funds
 - Special fund sweeps continue, including to our Distance Learning Fund
- Expect continued accusations of administrative bloat




FY19 Budget Development Plan

- ▶ Continue focus on historic funding & related trends
 - ▶ Almost all sectors of state government were cut & everyone waits to get paid but no sector was cut as much as higher education
 - ▶ Important to note reductions started before the budget impasse
- ▶ Document the damage done & lingering impact of the budget impasse
 - ▶ Work with universities & ICCB to develop a set of measures
 - ▶ Include a 1-2 page summary developed by each university to tell their story of response, resilience & recovery
 - ▶ Work with ICCB to include something similar for community colleges
 - ▶ Emphasize the disproportionate impact of the budget impasse on higher education



FY19 Budget Development Plan

- ▶ Describe the prudent & thoughtful actions universities & community colleges took to protect the core mission of higher education
 - ▶ Emphasize how colleges & Universities focused cuts on some what might identify as “bloat”
 - ▶ Emphasize the importance of the 60 x 2025 goal as a means of making the state competitive
 - ▶ Promote the need for adequate funding, stability and certainty
- 



Questions?

