MINUTES

BOARD OF REGENTS’ COMMITTEE ON BUDGET AND FINANCE MEETING

April 1, 2015

I. CALL TO ORDER

Committee Chair, Jan Sullivan, called the meeting to order at 1:55 p.m. on Wednesday, April 1, 2015, at the University of Hawai‘i at Mānoa, Information Technology Building, 1st Floor Conference Room 105A, 2420 Correa Road, Honolulu, Hawai‘i 96822.

Committee members in attendance: Committee Chair Jan Sullivan; Committee Vice Chair Barry Mizuno, Regent Coralie Matayoshi, Regent Lee Putnam.

Committee members excused: Regent Peter Hoffmann.

Others in attendance: Board Chair Randy Moore, Regents’ Vice Chair Eugene Bal III, Regent Acoba, Regent Nielsen, Regent Portnoy, Regent Tagorda, Regent Yuen (ex officio committee members); President David Lassner; Vice President for Community Colleges John Morton; Vice President for Administration Jan Gouveia; Vice President for Legal Affairs and University General Counsel Darolyn H. Lendio; Vice President for Budget & Finance/Chief Financial Officer Kalbert Young; UH Mānoa Interim Chancellor Robert Bley-Vroman; Executive Administrator and Secretary of the Board of Regents Cynthia Quinn; and others as noted.

II. APPROVAL OF THE MINUTES OF THE MARCH 4, 2015 MEETING

Regent Mizuno moved and Regent Matayoshi seconded the motion to approve the minutes of the March 4, 2015 meeting, as amended, which was unanimously approved.

III. PUBLIC COMMENT PERIOD

Executive Administrator and Secretary of the Board Cynthia Quinn announced that the Board Office received late written testimony from Joe Mobley which had been distributed to the committee, and three individuals had signed up to give oral testimony.

1. Dr. Joe Mobley, Professor in School of Nursing at UH Mānoa (UHM), a co-leader of the DivestUH movement, and member of the Board’s Task Group on Divestment & Sustainability, testified in support of the task group and thanked everyone for their hard work. He noted that passing the task group’s recommendations would make the University of Hawai‘i (UH) the 26th higher education institution to divest from fossil fuels and the first major research university in the United States to do so since Stanford University that only divested from coal, and makes a statement to the state that divesting from fossil fuels makes sense. He had been informed by Representative Chris Lee, Chair of the House Committee on Energy & Environmental Protection, that House Concurrent Resolution No. 222, which just passed the House, followed the example of UH by establishing a divestment task
force for all public investments and taking the first step by supporting the State Employees’ Retirement System to divest from fossil fuels.

2. Dr. Dawn Morais Webster alumna and adjunct faculty member testified in favor of divestment from fossil fuels.

3. Mark Ryan, student, testified on behalf of the RIO Sustainable UH, a club focused on sustainability at UHM, and the Student Sustainability Coalition of Hawai‘i, recognized the speed and efficiency in moving the divestment initiative forward.

Committee Chair Sullivan thanked all the individuals who provided written and oral testimony to the committee.

IV. AGENDA ITEMS

1. For Information: Implementation of System-Wide Centralized Budgeting and Prioritization

VP Young provided an informational briefing on implementation of a system-wide centralized budgeting and prioritization. He provided background on the fiscal biennium budget being considered by the Legislature for Fiscal Years 2016-2017 under House Bill 500, House Draft 1, Senate Draft 1, which was heard by the Senate Committee on Ways and Means (WAM) today. H.B. 500 as proposed by the House, aggregates all general funds appropriated to campus level programs into one system level account, of approximately $420 million in general funds into UH900, which is the system level budget program. This amount is essentially the current level of funding for Fiscal Year 2015 with a nominal $50,000 increase. In comparison, the Board of Regents requested an additional $35 million in general funds; the Governor requested a lower amount of $7.5 million.

Centralization is underway, and the UH Budget office has provided all campuses with instructions on formulating a budget for Fiscal Year 2016, regardless of the outcome of lump sum budgeting. All campuses are being asked to formulate budgets with the following aspects: All funds are to be grouped, and revenues and expenditures are to be identified by sources (general fund as an assumption, tuition & fee special funds, research training & revolving funds, and other special or revolving funds), by campus and system at the community college level; and by school, college, or operating unit at UHM, which is more than 30. University of Hawai‘i at Hilo (UHH) and University of Hawai‘i-West O‘ahu (UHWO) are being done at the campus level. The UH System is being done at the program level. Expenditures are to reflect certain explicit types of expenditures, e.g. salaries, utilities and other operations. Revenues will need explanation of assumptions around certain types of factors that will affect revenue projections, e.g., enrollment expectations/projections, tuition rates/levels, and the level of general funds appropriated. Campuses will use a scenario approach based on the current level of funding, e.g., a flat revenue approach, which assumes no increase in tuition and general fund appropriations. Campuses will adjust their revenues to account for any changes in enrollment projections, while keeping rates constant. Campuses will also be looking at a hypothetical tuition level that will satisfy initiatives and strategic investments, largely mirroring the board’s Fiscal
Year 2016 request to the Legislature, with priorities of initiatives to narrow gradients of funding levels. Depending on the outcome of the budget, the university and administration are going to be challenged during a very short period of 60 days to develop and thoroughly lay out prioritization of shortfall funding across a number of high profile program areas. The centralized budgeting and prioritization approach will encourage UH to reduce costs, increase efficiencies, trim programs, and possibly generate new operating revenues. Thus, the budget process for Fiscal Year 2016 will still be largely aspirational in terms of objectives for a true budget mostly because turnaround is short. However, the foundation of the process they set in the next 45 to 60 days, in combination with the ongoing efforts regarding the quarterly financial reports, will provide for improving financial status reporting into Fiscal Year 2016 and beyond.

VP Young also provided an update on WAM budget approach that concluded that morning. The final specifics were not yet publicly available, however, the WAM chair made it clear the Senate would not lump sum general funds into UH system as proposed by the House. The Senate version provides an additional $7 million in general funds above current funding levels that will be treated as lump sum at the system level, with the expectation that the president and regents will allocate utilizing a performance-based methodology. More accurate comparisons between House and Senate versions are pending. The next step will be conference between the House and Senate in mid-April to determine what the Legislature collectively approves and appropriates for the UH budget.

The committee raised concerns and comments regarding level of flexibility for tuition increases and guidelines on reserve funding; prediction on the budgeting method that the Legislature would follow and impact on implementing a centralized system if the budget is not lump sum; ability to aggregate monies appropriated to specific campuses; including other standard assumptions such as inflation percentage or utility costs; shortfall projections and mitigation plans; the impact of the interim UHM budget allocation model; and possibilities of reducing programs to balance the budget.

VP Young said there was flexibility for tuition increases and explained that with the objective of developing prioritization at campus level, the baseline comparison involves status quo on tuition and revenues and a scenario that constructs a revenue level rate assumption that satisfies the campus level initiatives. He expects the campuses to come in with different proposals that comply with the regent policy on reserves, and any campuses that fall below the target level of reserves are expected to provide a plan to get to the minimum. For campuses above the target level, the expectation is to only see reserves stay within the target. He added that the work was already in progress, and they expect a lot of feedback between the campuses and the budget office.

Regarding aggregating funds administratively, the university already has the statutory authority, but had not done so in the past. The Legislature currently directly appropriates monies to UHM, the John A. Burns School of Medicine (JABSON), UHH, UHWO, the community colleges in aggregate, the UH system, and to smaller units like the aquarium. These have been treated in the past as direct appropriations, and there has not been any system level interaction to aggregate those funds or control when they are aggregated. Under current statute, the university has the authority to move funds from any of one those programs regardless, and could be one administrative method to get to a lump sum
President Lassner commented that the university had used the statutory authority by mutual consent and they have to report it to the Legislature, so there is oversight. If the university chooses to move funds, they would need to be clear with the Legislature on what is being done and why. He noted that the key to administration being able to present the board with a budget is collaboration that is underway with a working group comprised of the four academic units heads, their vice chancellors or AVPs, system VPs and AVPs, along with Secretary Quinn, and the budget office. He believes the group is well aligned moving forward and being as collaborative as possible.

VP Young said the budget office is collecting feedback on metrics, criteria and assumptions from each campus to incorporate into general guidelines on assumptions for the campuses to use. For example, the increase in the rate of utilities is a likely assumption that would be used.

VP Young said based on the House version of the budget, the shortfall would be $35 million. The senate version provides $7 million, a portion of which is expected to be restricted for certain provisos. The result is a $28 to $35 million shortfall. The shortage may be greater due to anticipated decline in enrollments across the system. Addressing the shortfall is part of the budget prioritization process, e.g., campuses being asked to examine expenditure constraints, program reductions and revenue generation.

In terms of the impact on the interim UHM budget allocation model, Chancellor Bley-Vroman said 38.5% of tuition revenues are allocated based on the number of students in the fall, but that does not account for the full internal allocation. The remaining 60% of tuition revenues will be used for shared services (e.g., library, grounds upkeep, building maintenance) campus level. Details will be provided in April, but the system provides them with a methodology to allocate a portion of tuition, with a great deal of flexibility on the remainder. As they work on developing the budget within the assumptions and scenarios, it will give some possibilities that will reflect enrollment assumptions.

Regarding reducing programs, Chancellor Bley-Vroman stated that any decision has to be a collaborative effort done at the unit by deans and directors. At present, there is no intent to eliminate or make large cuts. He expects to see differential effects among units and varying prioritization, using the system level Strategic Directions as general level guidelines. All units are asked to stay within its existing allocation, while making relatively minor adjustments at the top, and to provide a prioritization within those units. Some units may close programs, others may not. That information will be fed into the annual review process of budget proposals done between the vice chancellors and the deans and directors.

The committee noted that while recognizing the 60 day turnaround time presents challenges, this approach had been discussed back in October that the university could not expect it would receive all the general funds it requested, and that the Board would not give the full tuition increase if not justified. The committee also suggested segregating fixed non discretionary costs, e.g., utility rates and insurance, to highlight good management of discretionary costs. VP Young commented that the Regent’s budget request did identify fixed and non-fixed/discretionary costs, new initiatives, and programs. However, though the Governor submits fixed costs increases as part of the
Committee Chair Sullivan thanked VP Young and Chancellor Bley-Vroman for their updates and said she looked forward to hearing more in the near future.

2. **For Information: Report by the Divestment Task Group Regarding Recommendations on Divesting from Fossil Fuels and Board Policies Regarding Sustainability**

Vice Chair Sullivan clarified that this report is being given at the committee today, and to honor Sunshine laws, it will come back a second time to the committee for action in May, and if reported out will go to the full board for action. The report was delivered by task group members Regent Sullivan, Regent Matayoshi, and Chair Moore.

Background on task group formation and membership was provided and expression of gratitude for the efforts and research that lead to the task force recommendations. The process undertaken by the task group included various meetings held by the task group and its two subgroups on March 20 the full task group met, and voted unanimously to recommend the adoption of revisions to board policy contained in the report that was distributed to the committee earlier. The divestment recommendations were summarized and noted that in 2014, the board amended Chapter 4 of board policy to include a strong sustainability component into its mission. The task group approached its work mindful of this, along with the strong public support that was evidenced. They worked closely with current investment manager UBS, with the goal to determine and evaluate if the university could achieve divestment without compromising the current, relatively low fees and costs, while maintaining a balanced portfolio and meeting investment criteria detailed in board policy. Other universities were inventoried that have made the divestment decision, and provided more detail on these specific actions, gave the task group spreadsheets of information, and also personally talked to board members that led similar efforts at other universities and investment managers that have been part of divestment efforts. UBS estimated that as of the end of last year, approximately 5% to 7% of the university’s $66 million endowment fund included investments in energy. UBS also noted that since the university only invests in mutual funds or exchange traded funds, there were no direct investments in fossil fuel companies. Some universities, such as Stanford or the University of Maine, have only made the decision to divest in direct investment, which is a step that UH has already achieved.

UBS also advised that returns from mutual funds that do not include fossil fuels are probably comparable to current funds, however, it was noted that there are presently three negative factors that argue against immediate divestment form fossil fuel companies: (1) the current range of investment styles and asset classes in fossil free mutual funds is limited; (2) generally the management costs of these funds are currently higher; and (3) there are currently no exchange traded funds that exclude fossil fuel companies. Due to these factors, the net result of an immediate and full divestment from fossil fuel companies would result in a less diversified portfolio, with a decrease in net return due to higher management fees. UBS also noted, however, that this area of socially conscious investment is growing very rapidly, and new funds and investment
vehicles are appearing.

It was agreed that in the near future there will be an increasing amount of investment vehicles and the negative factors identified will dissipate over time. The group acknowledged that the act of divestment will not directly reduce fossil fuel or carbon emissions, however, the value of divestment is to act as a leader, to galvanize the university community and the greater community to take action to invest in alternative energy, energy savings, and to change institutional behavior. For these reasons, the task group concluded that it would recommend divestment would move forward if the negative consequences identified could be mitigated, and the policy language that is being recommended in the report will enable those concerns to be addressed. Each sentence of the policy was carefully crafted and modified numerous times with input from all task group members, including UBS.

The policy revision being recommended adds a new section to chapter 8, Section 2 of Section C. Section C.1 is not changing. The proposed revision requires the board to align its investment goals with the board’s sustainability mission; that the investment manager divest from companies that produce fossil fuels and maintain a portfolio that is substantially divested, which is defined as 0% to 1% of holdings; that the investment manager shall include investments in alternative energy substitutes, where feasible; that divestment should occur in a responsible manner that considers fees while maintaining goals; that divestment should begin as soon as possible, with an outside date for completion to be on or before June 30, 2018; and the investment manager shall report on the progress of these objectives as part of its regular quarterly report to the board. UBS has reviewed the language and agreed to the criteria.

Regent Matayoshi noted that, about one year ago, the board adopted a broad policy on sustainability that recognizes Hawai‘i’s unique geographical location and the university’s leadership role in integrating sustainability throughout its teaching, research, operations and public service. The authority to develop goals, performance metrics and plans was delegated to the president. This really began two years ago by passionate, grassroots believers in the cause, and it was a good experience to work with individuals who were so passionate and almost surprised about board support. The regents support sustainability, but need to balance the financial implications, which is where collaboration was key. The first draft of the executive policy was presented at the First Annual Hawai‘i Sustainability in Higher Education Summit held on April 11, 2013, and was reviewed by about 90 participants from across the UH System. A broad and diverse group of stakeholders had input into the further development of the policy, which went through 19 drafts before presented to President Lassner who made a few more changes, and the policy was finalized just recently at the at the 3rd Annual Summit held on February 26 of this year.

The result is a comprehensive, well thought out sustainability plan created by the people, for the people. The executive policy was patterned after the University of California (UC) system, which is similar to UH in that it has 10 campuses. However, UH policy was a little less prescriptive, bearing in mind the financial constraints they needed to take into account. The task group recommended that the sustainability policy be placed in a separate section of Chapter 4. It is currently in Chapter 4, but within the
Chair Moore reported that on the requirement that all new construction and major renovations will achieve a minimum of Leadership in Energy & Environmental Design (LEED) Silver designation with a goal for LEED Gold; under discussion is to add the phrase or “equivalent” to avoid requiring $100,000 for the LEED stamp of approval, but still accomplish all the standards. That money could be used for building improvements. The word “equivalent” provides leeway in the event LEED may not be the best standard in the future. Chair Moore explained that there is a Green Globe Certification that is an alternative to LEED. The Legislature explored back in 2006, and passed a statute that directed each agency, to the extent possible, to design and construct buildings to meet LEED Silver or Green Globes rating system, which is different from LEED, or another comparable state-approved, nationally recognized and consensus-based guideline, standard or system. Both Green Globe and LEED were from the United Kingdom in the early 1990s where there was a movement to design and operate buildings in a more environmentally sensitive and occupant friendly manner. LEED has many levels (40-49 = Certified; 50-59 = Silver; 60-79 = Gold; 80+ = Platinum); as does Green Globes (4, 3, 2 or 1 globes, the more globes you have the greener you are). As a practical matter, LEED in Hawai‘i and across the country surpassed Green Globes as the environmental standard. However, the Hawai‘i Department of Education (DOE) concluded that LEED for Hawai‘i is irrelevant because not all of the LEED criteria relate to energy, and a number of criteria are not relevant to Hawai‘i, e.g., points are assigned if materials come from within 500 miles, which does not make sense for Hawai‘i. The DOE concluded that designation is in part a game of trading points and not in the best interest of the department or state, so they adopted the Hawai‘i Collaborative for High Performance School (HI-CHPS), which started out nationally based in Sacramento. Each state is allowed to develop their own and submit to CHPS Sacramento for certification that the state standards meet criteria. DOE uses HI-CHPS on the basis that LEED is familiar and well known, but not optimally relevant to construction in Hawai‘i. Thus, the term using “or equivalent” in the board policy until there is an equivalent that is widely recognized in Hawai‘i for universities indicates a commitment to LEED standard but not in a manner that precludes considering something else that is equivalent but more suitable. Otherwise, with no alternatives, the university would be severely limited, e.g., wanting only Apple smartphones. From a state procurement standpoint, that is not desirable because you want the best value for the money. It is an open issue for the task group and would come back for action at the next committee meeting for further discussion as to whether or not to modify what was voted on and approved by the task group.
V. ADJOURNMENT

There being no further business, on the motion of Regent Matayoshi and second by Chair Moore and with unanimous approval, the meeting was adjourned at 2:56 p.m.

Respectfully Submitted,

/S/

Cynthia Quinn
Executive Administrator and
Secretary of the Board of Regents