

MINUTES

BOARD OF REGENTS COMMITTEE ON BUDGET AND FINANCE MEETING

JUNE 3, 2021

Note: On January 30, 2020, the World Health Organization declared the outbreak of COVID-19 a public health emergency of international concern, subsequently declaring it a pandemic on March 11, 2020. On March 16, 2020, Governor David Y. Ige issued a supplementary proclamation that temporarily suspended Chapter 92, Hawai'i Revised Statutes, relating to public meetings and records, "to the extent necessary to enable boards to conduct business in person or through remote technology without holding meetings open to the public."

I. CALL TO ORDER

Chair Jan Sullivan called the meeting to order at 9:46 a.m. on Thursday, June 3, 2021. The meeting was conducted virtually with regents participating from various locations.

Committee members in attendance: Chair Jan Sullivan; Vice-Chair Randy Moore; Regent Alapaki Nahale-a; Regent Michelle Tagorda; and Regent Robert Westerman.

Others in attendance: Board Chair Benjamin Kudo; Regent Kelli Acopan; Regent Eugene Bal (ex officio committee members); President David Lassner; Vice President (VP) for Administration Jan Gouveia; VP for Legal Affairs/University General Counsel Carrie Okinaga; VP for Research and Innovation Vassilis Syrmos; VP for Information Technology/Chief Information Officer Garret Yoshimi; VP for Budget and Finance/Chief Financial Officer Kalbert Young; UH-Mānoa Provost Michael Bruno; UH-Hilo Chancellor Bonnie Irwin; UH-West O'ahu Chancellor Maenette Benham; Executive Administrator and Secretary of the Board of Regents (Board Secretary) Kendra Oishi; and others as noted.

II. APPROVAL OF MINUTES

Vice-Chair Moore moved to approve the minutes of the March 4, 2021, committee meeting, seconded by Regent Nahale-a, and the motion carried, with all members present voting in the affirmative.

III. PUBLIC COMMENT PERIOD

Board Secretary Oishi announced that the Board Office received late written comments from Dr. Lilikalā Kame'eleihiwa regarding electric utility expenses at UHM and that no individuals signed up to provide oral testimony.

IV. AGENDA ITEMS

A. Presentation on the Economic Impact of the University of Hawai'i and State Economic Forecast by University of Hawai'i Economic Research Organization (UHERO) Executive Director Carl Bonham

Dr. Carl Bonham, Executive Director of UHERO, provided an update on UHERO's most recent macroeconomic forecast for the state saying that economic recovery is occurring at a better-than-anticipated pace. He noted that one key factor contributing to this recovery has been the increase in COVID-19 vaccination rates which has led to increased consumer confidence and more normalized economic activity. The economic resurgence can also be attributed to the infusion of federal stimulus funding.

Several specific economic impacts at both the national and State level related to vaccination rates and the release of federal stimulus monies were highlighted, with Dr. Bonham stating that overall economic performance continues to improve. All signs indicate that a return to pre-pandemic United States gross domestic product (GDP) levels will be reached and surpassed by the end of the second quarter of 2021 placing GDP on a path to where it would have been had the pandemic not occurred. He stated that economic indicators also bode well for Hawaii. Tourism, the State's primary economic driver, continues to witness increases in daily visitor counts which reached 20,000 in May 2021, approximately 72 percent of the 2019 daily visitor count. It is anticipated that these figures will continue to climb as global vaccination rates increase. The steady increase in visitor arrivals has also resulted in an accelerated recovery of jobs lost during the pandemic, although job recovery has been slower than expected. However, data analysis conducted by UHERO suggests stronger job-growth throughout summer 2021.

The Council on Revenues (COR) met on May 25, 2021, and produced an updated economic and general fund revenue forecast. Although discussions on Hawai'i's economic outlook since the beginning of the pandemic have been pessimistic, the growth of real personal income, partly due to the receipt of federal stimulus funds, was better than expected and early data on State tax collections show an increase in tax revenues. COR also added nearly \$500 million in general fund revenues for its fiscal year (FY) 2021 forecast and slightly under \$1 billion for its FY 2022-2023 forecast. However, Dr. Bonham cautioned that transient accommodation tax and general excise tax figures continue to lag and that a gap of approximately \$600 million between COR's March 2020 and May 2021 forecasts still exists. As such, the State will continue to play catch-up in general fund revenue collections for several more years.

Dr. Bonham also reviewed the university's impact to the overall economy of the State explaining that, while the university's economic contributions include direct revenues generated such as research dollars and tuition, it also produced broader economic impacts through induced university-related spending. Increases in individual spending and tax revenue collections due to the escalation of lifetime earnings experienced by residents receiving a post-secondary education from the university, as well as social returns witnessed by an increasingly educated populace, were also factors imparting long-term positive impacts on Hawai'i's economy. He noted that, in FY 2020, the general fund appropriation of \$507.6 million received by the university led to \$2.1 billion in university-related spending which equates to \$3.07 spent in Hawai'i for

every State dollar received. Moreover, every \$1 million in State funds allocated to the university results in \$7.2 million in business sales; \$2 million in increased income; \$370,000 in increased State tax revenue; and the creation of 44 local employment opportunities.

Referencing UHERO's elimination of online purchases and non-local spending from its analysis on the university's economic impact to Hawai'i, Vice-Chair Moore requested clarification as to whether only value-added data was considered for purchases of items produced elsewhere but sold in Hawai'i stores. Dr. Bonham responded in the affirmative stating that UHERO attempts to estimate the import content of an item sold in Hawai'i in determining value-added data.

Vice-Chair Moore asked whether the general fund revenue projection figures were in constant dollars, adjusted for inflation, or nominal figures, not adjusted for inflation. Dr. Bonham responded that the general fund revenue projection figures were nominal. He stated that this was one of the factors considered by COR when it increased its forecast for the annual rate of economic growth from three-and-a-half to four percent for FY 2024 and beyond, which was due in part to expected inflation. Vice-Chair Moore questioned whether general fund revenues for FY 2023 will, in nominal terms, equate to general fund revenues in FY2019. Dr. Bonham replied that COR is forecasting \$7.5 billion in general fund revenues for FY 2023 as compared to \$7.14 billion in FY 2019. Vice-Chair Moore remarked that, in essence, general fund revenue collections will not have recovered to FY 2019 figures by FY 2023 when adjusted for inflation. Dr. Bonham concurred with this assessment. Vice-Chair Moore inquired about the impacts COR's improved economic forecast will have on future labor contract negotiations. Dr. Bonham opined that, given the economic forecasts, efforts to renegotiate labor contracts will more than likely occur but also surmised that the State will likely argue that general fund revenue collections are still well-below expectations and that expenses, both deferred and actual, remain. Vice-Chair Moore commented that this would more than likely mean less money in the general fund for the university.

Regent Nahale-a expressed his concern that the forecasted economic recovery is not a true reflection of the fiscal difficulties facing working class individuals and asked whether an analysis has been conducted on where the economic recovery was occurring. Dr. Bonham stated that the forecasts made were on a macroeconomic level and does not address the issue of wealth inequality which has worsened during the pandemic and disproportionately impacts individuals who can least likely bear difficult economic burdens such as women and disadvantaged single parents. The current economic recovery does not solve this issue but it is a concern that will need to be addressed in the near future.

Stating that federal stimulus funds have been used to support incomes and income levels but that job recovery data appears to indicate that individuals are returning to the same jobs they held pre-pandemic, Regent Westerman asked if the economic forecasts were an accurate indication of economic recovery. Dr. Bonham reiterated that the forecasts presented were at a macroeconomic level which could be deceiving with regards to individual economic recovery. Individuals who return to the exact same job they held pre-pandemic will most likely not experience any changes to their economic

condition and may experience a worsening fiscal situation if federal stimulus funds were used to supplant or enhance personal income over the last year. Additionally, physical and mental health impacts resulting from the pandemic impacted those who were least likely to tolerate these burdens, thereby further stressing the economic conditions of those individuals.

Regent Tagorda commented that recognizing the economic inequalities that have been highlighted and exacerbated by the pandemic, as well as the role of universities, including the University of Hawai'i, in addressing these inequalities through higher education is important. She stated that the value of higher education not only impacts individuals, but also their families and communities, and is something that needs to be taken into consideration as part of a proactive approach to addressing this issue.

B. FY 2020-2021 Third Quarter UBS Legacy Endowment Fund (Fund) Investment Performance Report

Kyle Yoneshige and Lori Hamano from UBS provided a report on the Fund for the third quarter of the fiscal year which began on July 1, 2020, reviewing both its asset allocation and investment performance. Ms. Hamano stated that the Fund consisted of cash assets, fixed-income assets, and equity assets. As of March 31, 2021, Fund assets were allocated as follows: 1.64 percent cash, 25.49 percent fixed-income, and 72.87 percent equities. Overall, the asset allocation and financial performance of the Fund is on par with, or exceeds, the established benchmarks. Internal compliance reviews conducted by UBS also confirmed that the Fund was compliant with its fossil fuel divestiture mandates and all asset allocation and investment policies. In addition, there were no material changes or weaknesses in the management of the Fund.

Mr. Yoneshige highlighted the overall portfolio performance, noting that changes were made to the format of the performance report with returns being broken down into gross returns and net returns to account for the cost structure of the Fund. He noted that the total cost of investments for the Fund is 0.493 percent and includes 0.2 percent in fees charged by UBS and 0.293 percent in fees charged by the investment manager. This equates to total annual fees of \$450,000 for management of the almost \$92 million Fund. As of March 31, 2021, the Fund experienced gross and net returns, respectively, of 2.81 and 2.68 percent for the third quarter; 19.91 and 19.48 percent for the first three quarters of the fiscal year; 11.55 and 11.18 percent over the last five-year period; and 8.64 and 8.32 percent since UBS began managing the Fund to the end of the third quarter of this fiscal year. The Fund's portfolio is performing in line with expectations over the long term and UBS was extremely pleased with the portfolio's performance for the fiscal year, especially in light of the economic impacts of the COVID-19 pandemic. It was noted that the primary drivers for this exceptional performance were the economic recovery of the United States experienced since March 2020 and the strong growth in the international economic arena. He also noted that the National Association of College and University Business Officers/Teachers Insurance and Annuity Association of America-College Retirement Equities Fund 2020 Study of Endowments was also released showing that investment fees for endowments similar in size to the Fund were approximately one percent and that the Fund has outperformed its peers by nearly two percent with respect to the five-year period of endowment performance.

Mr. Yoneshige and Ms. Hamano briefed the committee on the financial outlook of the Fund and the direction UBS was considering given the current economic condition and market situation. UBS continues to advocate for keeping the Fund's allocation in equities at its current level for a number of reasons including increased prices in all asset classes. Additionally, bond yields and returns on cash accounts continue to decrease and it currently would not make economic sense to increase asset allocation in these areas. UBS will continue to monitor the financial markets and adjust its investment strategies as more information becomes available with the ultimate goal of maintaining long-term investment strategies.

C. Discussion on Ideas for Strategic Use of Legacy Endowment Funds

VP Young gave a brief overview and history of the Legacy Endowment Fund (Fund) noting that its corpus was received and invested on behalf of the university prior to the establishment of the University of Hawai'i Foundation (UHF) and is, therefore, separate and apart from the UHF endowment fund. The Fund is currently managed by UBS Financial Services, who provides quarterly investment performance and asset allocation reports to the board throughout the fiscal year. Distributions from the Fund are controlled by Regents Policy (RP) 8.207 which currently provides the president with the authority to distribute up to 4.25 percent of the Fund's valuation, based upon a 20-quarter, rolling average of its market value. The current value of the Fund's overall portfolio is slightly less than \$92 million and the portfolio contains both restricted and unrestricted sources of funding which constrains the overall use and distribution amounts of Fund assets.

The administration has developed four concepts aimed at expanding the use of unrestricted monies in the Fund; increasing strategic investments focused on building the Fund's corpus; amending the principles related to Fund payouts; and determining the types of additional revenue that can be added to the Fund. VP Young described each concept in detail, noting their potential benefits as well as possible drawbacks, and stated that the ultimate goal of these concepts and discussions is to develop sources of funding that could consistently build the Fund and provide for more discretionary expenditures than the UHF endowment fund which consists of mainly restricted funds.

President Lassner added that he appreciated the opportunity to review the purposes for, as well as use of, monies in the Fund. He stated that the goal of this exercise was to develop innovative actions that sought to achieve an increase in the Fund's corpus and generate ideas to expand upon its uses and that the four concepts developed were a basis to begin discussions on this issue.

Board Chair Kudo opined that it was important to have discussions on effectively using the Fund to leverage economic opportunities that could assist the university in paying for operational and other costs associated with providing higher education in Hawai'i. However, he expressed his concerns regarding the investment of monies from the Fund in real estate ventures noting that decisions regarding these types of transactions will more than likely be based on recommendations made by individuals external to the university. As real estate investments are inherently risky, concepts involving these types of matters need to be fully vetted and scrutinized to ensure that

the fiduciary responsibilities of the Board regarding the Fund are met. He also stated that consideration should be given to proactively using latent real estate assets currently owned by the university to generate revenues that can be reinvested in the Fund.

Regent Westerman echoed the concerns raised by Board Chair Kudo regarding the issue of real estate investments stating that, while he supports the development of ideas to increase the corpus of the Fund, the Board needs to remain vigilant in maintaining its fiduciary responsibilities. He also stated his support for continuing discussions on the best uses for the Fund, including increasing the number and amount of scholarships in the future to retain Hawai'i's best and brightest students.

Regent Tagorda stated that she supported concepts involving expanded use of the Fund to increase the Regents and Presidential Scholarships (RAPS) as the amounts of these scholarships have not been increased despite inflation. Increasing the amounts of RAPS will allow the university to be more competitive with other institutions in attracting Hawai'i's top high school graduates. She also supported the concept of using monies from the Fund to establish a Strategic Initiatives Fund to underwrite efforts to increase educational affordability and access for students which will have a tremendous social impact on the community.

Regent Westerman questioned whether the annual distribution rate of 4.25 percent of the Fund's valuation was a maximum allowable amount. VP Young stated that the 4.25 percent distribution rate was a cap established by a recent amendment made to RP 8.207. During discussions concerning this amendment, it was decided that reducing the maximum allowable distribution rate to 4.25 percent afforded the best opportunity to continue to provide monies for things such as scholarships while preserving the corpus of the Fund in perpetuity. Prior iterations of RP 8.207 allowed the President to distribute up to 5 percent of the Fund's valuation although the amount provided was usually closer to 4.5 percent based upon the investment performance of the Fund. He also added that the amount of scholarship monies provided by the Fund always exceeded the amount drawn down for a variety of reasons. Regent Westerman asked whether it would be possible to set-aside these unexpended monies each year into a sub-account that could then be used by the administration for investments to generate revenue for the Fund's corpus. VP Young replied that this was an interesting concept that could be reviewed by the administration.

Vice-Chair Moore remarked that, considering inflation and projections for future investment performance, the 4.25 percent distribution rate may impact the corpus of the Fund in the future. He also expressed his apprehensions regarding the setting aside of funds that could be presently used for various purposes, as well as concerns regarding real estate as a long-term investment strategy. In addition, he suggested a reimagination of RAPS that provided scholarship funds in proportion to the student's financial need but also provided non-monetary benefits and student support such as mentorships, which could increase enrollment at the university.

Chair Sullivan stated her belief that the board and administration needs to review and discuss ideas to increase the Fund's corpus other than simply investing in the stock markets but that funds should not be used for speculative real estate investments.

Additionally, the administration should consider the development of concepts designed to generate revenues, such as the leasing of university-owned facilities, that can be set aside and used in a more strategic manner for specific, long-term initiatives such as the Hawai'i Promise Program.

President Lassner thanked the Regents for the discussion, noted that any actions proposed by the administration regarding the financing of revenue generating concepts would take into account the university's mission, and gave his assurances that the administration does not plan on using Fund monies for speculative real estate investments. VP Young added that this was a thought-provoking exercise intended to begin discussions about development and use of the Fund for the benefit of the university and expressed his mahalo to the Regents for sharing their mana'o on this issue.

D. FY 2020-2021 Third Quarter Financial Report

VP Young provided the financial report for the third quarter of FY 2020-2021 stating that the Department of Budget and Finance has been releasing general fund revenues allocated to the university on a quarterly basis and, as such, the allocation appears comparatively lower than previous fiscal years.

Revenue and expenditure reports were presented for each of the major units of the university. Overall, tuition and fee revenues are slightly lower than for the same time period last fiscal year but greater than the projections that were made at the beginning of this fiscal year. It was noted that revenue levels vary by campus with UHWO witnessing increases in revenue while UHM, UHH, and the community colleges have experienced a decrease in revenue. Additionally, while balances of uncollected tuition are expected to continue decreasing throughout the remainder of the academic year, the amount of billed tuition that remains uncollected continues to be higher than previous years. It was noted that the amount of uncollected tuition may be attributable to the COVID-19 pandemic and tuition payment plans being made available to students. Revenues for the other special and revolving funds, which are mainly affiliated with specific programs, auxiliary services, or business activities, including areas such as parking, housing, and athletics, also realized significant decreases due to a variety of factors such as the temporary closure of facilities, reduced on-campus presence, and the cancellation of events.

In the area of expenditures, all fund categories, with the exception of the general fund and the Research and Training Revolving Fund, experienced a significant decrease in expenditure amounts due to a variety of factors including the decline of an on-campus presence, the institution of a hiring freeze, travel restrictions, and other cash preservation strategies implemented by the administration during the last quarter of the prior fiscal year and which remain in place. While the decrease in expenditures is helping to counter some of the revenue decline that is affecting the balances of these funds, the rate of expenditure variances is not the same as the rate of revenue variances and the situation will require continued monitoring by the administration.

Vice-Chair Moore opined that there will be continued financial uncertainty for the university until there is clarification and full disclosure on the permitted use of federal relief funds. VP Young concurred stating that the full impact of federal relief funds should be better understood and reflected in the next fiscal year.

E. Research and Research Training and Revolving Fund (RTRF): Financial Reporting on Revenues and Expenditures

Chair Sullivan stated that, due to time constraints, discussions on this matter would be deferred.

F. Federal and State and Coronavirus Relief Funds to the University of Hawai'i: Expenditures to Date, and Planned and Strategic Expenditures

VP Young provided a report on the status of the expenditure of Higher Education Emergency Relief Funds (HEERF) funds received by the university from the Coronavirus Aid, Relief, and Economic Security (CARES) Act and the Coronavirus Response and Relief Supplemental Appropriations Act (CRRSAA), briefly reviewing the three tranches of funding available, the amount of funds received for each tranche, and funding restrictions. The American Rescue Plan Act (ARPA) is also expected to provide HEERF funds for the university though none have been provided to date. However, based upon criteria used for the provision of CARES and CRRSAA funds, it has been projected that the university could receive \$137.6 million in ARPA funds. He stressed that restrictions on the use of allotted federal relief funds remain in place and that uncertainty remains as the university awaits clear guidance from the United States Department of Education on some of the parameters associated with the expenditure of federal relief funds, particularly regarding ARPA funds.

As of March 31, 2021, the university expended about \$12 million of the approximately \$24 million received for direct disbursement to students in the form of grants and about \$7.6 million of the approximately \$45.5 million received for institutional expenses related to the prevention of, preparation for, and response to the COVID-19 crisis. The university received an additional \$55.5 million in HEERF funds for its status as a minority-serving institution, the majority of which remains unspent. VP Young also reviewed a breakdown of the use of CARES and CRRSAA Act HEERF funds for each campus.

Vice-Chair Moore questioned the extent to which maintenance of effort (MOE) requirements applied to HEERF funding whereby the State must provide assurances that fiscal support for higher education will be proportionally maintained relative to overall spending. VP Young replied that MOE requirements are present for ARPA funds received by the State. There are also numerous limitations on the use of HEERF funds. Although it appears that HEERF funds were not intended to be used to supplant a reduction in general fund appropriations to the university, this is not made explicitly clear in any of the acts providing federal relief funds. However, MOE requirements exist for federal stimulus funding provided to K-12 educational institutions and the State needs to be cognizant of these requirements when considering funding reductions for institutions of higher education. He cautioned that, should there be a disproportionate

reduction in general funds for institutions of higher education relative to K-12 institutions, the federal government will use the MOE requirements applicable to K-12 institutions as a gauge for appropriate punitive action. President Lassner added that, while the State can reduce general fund appropriations to the university under MOE requirements, it cannot be done in a manner that is disproportionate to the rest of State government.

G. Committee Annual Review

Chair Sullivan referenced the committee annual review matrix provided in the materials packet and asked for comments from committee members. Hearing none, she thanked board staff, administration, and committee members for their efforts over the past year.

President Lassner offered his thanks to Regent Sullivan for her service and commitment to Hawai'i and the university, her outstanding work as a member of the board, and her friendship. She was praised for her professionalism; intelligence; insightfulness; keen understanding of the complexity of the university and higher education; and courage to make the difficult decisions that were in the best interests of the university. He stated that she had been honored for her dedication and exceptional service to the university and Hawai'i with a certificate of commendation from the United States House of Representative and relayed a message of congratulations from United States Representative Kaiiali'i Kahele.

V. ADJOURNMENT

There being no further business, Regent Nahale-a moved to adjourn, seconded by Regent Westerman, and with all members present voting in the affirmative, the meeting was adjourned at 11:46 a.m.

Respectfully Submitted,

/S/

Kendra Oishi
Executive Administrator and Secretary
of the Board of Regents