COMMITTEE ON FINANCE

Strategies to Address the Structural Deficit in the California State University Support Budget, the Contingency of a $250 Million Trigger Cut, and a Possible Tuition Fee Roll-Back

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Summary

This item explains the process of soliciting input and answering questions from a broad range of University constituents about strategies to address the pending $250 million reduction in the General Fund appropriation and the large structural deficit in the CSU operating budget. In the context of the ideas and suggestions that have been received, staff will proffer specific plans and alternatives for consideration by the Board of Trustees. In addition, a strategy for implementing a contingent roll-back of this year’s tuition fee increase—as contemplated by a late development in the state budget process—will be offered for board consideration.

The Consultation Process and Identification of Strategic Solutions

At the request of the board, staff has solicited the input of University constituents to identify a variety of strategies to address the structural deficit in the operating budget and the very serious challenges that will result from the $250 million “trigger” that will be pulled if the governor’s tax initiative is not passed in November. The structural deficit, as reported by the campus Chief Financial Officers, is over $130 million and results from limitations in the ability of tuition fee increases and campus spending reductions to fully match the $750 million reduction in the base General Fund appropriation during fiscal year 2011-12.

Executive Vice Chancellors Quillian and Smith have met with the campus Chief Financial Officers, Provosts, Vice Presidents for Student Affairs, and faculty members. In addition, the Executive Vice Chancellors and Vice Chancellor Brooks met with the Systemwide Budget Advisory Committee (SBAC)\(^1\) in May to present various options and solicit input. Many of the

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\(^1\) The SBAC is comprised of students, labor leadership, faculty senate representatives, management staff and campus leaders.
options presented to the SBAC had been discussed by the Board of Trustees during its October 2011 retreat. The SBAC meeting was streamed over the web to enable students, faculty, staff and alumni to listen in, make comments and ask questions. Approximately twelve hundred students, faculty, staff and administrators participated in the SBAC webcast. Hundreds of questions and comments were received either during or after the webcast. After duplicative questions were eliminated, those questions and comments have been posted on a newly created Budget Strategies website. The PowerPoint presentation used with the Trustees and the SBAC has been downloaded over twenty-six hundred times from the website.

A second webcast was conducted in June. The format of the second webcast was changed to provide participants from around the system a greater opportunity to submit questions and comments. Dr. Keith Boyum, Professor Emeritus of Political Science and former Associate Vice Chancellor of Academic Affairs, served as moderator. The Executive Vice Chancellors and Vice Chancellor Brooks responded to the questions and comments from the participants. Those questions and comments were recorded, and they will also be posted on the Budget Strategies website.

Strategic Solutions

Numerous obstacles, both political and financial, have made it exceedingly difficult to find solutions that will keep the CSU aligned with its mission to provide a quality education for the benefit of the students and the continued welfare of the state. There is a pressing need to understand that the problem before us goes beyond addressing the possible $250 million trigger. Given the cuts that have recently taken place, the CSU needs to restore over a billion dollars in reduced state support over the next few years. Because the University simply cannot continue to operate in an environment of such great uncertainty, solutions are needed that scale automatically. There must be a clear understanding of the difference between window dressing and truly meaningful strategies. Strategies must be considered in terms of how quickly they can be implemented, how much energy will be expended and how disruptive they will be to students, faculty and staff and the communities we serve. And, given the magnitude of the challenge, there is no single strategy that will be practicable or fair. It is important to avoid placing an undue burden on the students, CSU employees or the state for that matter. In that context, the following strategies are being set forth as paths to be followed.

Fundamental Nature of the Budget Problem

It is useful to think about the budget problem as having two distinct parts: (1) addressing the as-yet-unclosed gap created by prior cuts, and (2) addressing the contingency of the $250 million trigger. A third dimension that emerged late in the state budget process is the possibility of rolling back tuition fee rates to the levels that were in effect in the 2011-12 academic year. This
option—which would produce new budgetary challenges of its own—will be explored later in this agenda item.

It is also useful to view the budget problem in terms of two distinct phases: (1) the 2012-13 fiscal year—necessarily reliant on a mix of one-time resources and actions along with phasing-in of ongoing solutions; and (2) the 2013-14 fiscal year and beyond—necessarily requiring solutions that are ongoing in nature.

Budget Gap Due to Prior Cuts

As we have discussed in prior board meetings, annual state support for the CSU in the just-concluded fiscal year (2011-12) was $968 million lower than the peak state support of nearly $3 billion that was provided in 2007-08. This loss of support was compounded by an accumulation of mandatory cost increases that have not been funded by the state—such as employee health care benefits and the cost of operating and maintaining new facilities—totaling an estimated $135 million through 2011-12. Tuition fee revenue was up an estimated $593 million since 2007-08, leaving a net negative impact of $510 million to resources for instruction, student services and the operations of the university. Although the campuses and the Chancellor’s Office have engaged in a wide range of cost-reduction actions and strategies to close this gap, a large portion of the gap in 2011-12 was covered by one-time resources and one-time deferrals on necessary purchases or projects. It is this part of the budget gap that has not been closed by enduring expenditure reductions that constitutes the system’s structural deficit.

Looking ahead to the 2012-13 fiscal year, an estimated $132 million of tuition fee revenue is built into campus budgets from the increased tuition fee rates authorized to start Fall 2012. However, estimated mandatory cost increases unsupported by the state will rise an additional $47 million. Thus, the effective gap in fiscal resources relative to 2007-08—even with the most recently authorized tuition fee increase—will be approximately $425 million for the 2012-13 fiscal year. This gap is based on the best-case scenario of the governor’s tax initiative being passed by the voters in November. As will be explained further, rescinding the tuition fee revenue increase—as contemplated by the enacted state budget—would reduce revenues by $132 million and increase the size of the gap for 2012-13 to $557 million. Moreover, similar to the situation in 2011-12, a large portion of any gap will necessarily entail further draw-down of one-time resources and other one-time actions. This is an unsustainable long-term strategy. (Even in the short run, some campuses are rapidly running out of one-time resources.) This means that additional ongoing solutions must be found to close the gap even if the tax initiative passes.

Strategies to Address Prior Budget Gap/ Structural Deficit

Some options or strategies are naturally tied to addressing the structural deficit. For example, the direction given to campuses in March to restrict admissions of new students for the Spring 2013 term is needed to address the current resources gap. Last year, the university identified a 2.4
percent reduction in its enrollment target—from 339,873 California resident full-time equivalent students (FTES) to 331,716 FTES as part of its strategy for addressing the reduction proposed by Governor Brown’s first budget. This proposal was part of a required report to the legislature and governor and was approved by the legislature and governor in the final enacted budget package for 2011-12. Despite impaction (more restrictive admissions criteria) in place at 16 campuses, our latest count indicates that the university concluded the 2011-12 fiscal year having served approximately 341,250 resident FTES, or 2.9 percent above the budgeted target. This is not truly surprising, given the upward momentum on enrollments caused by the large number of admissions granted in Spring 2011 in response to the budget restoration—and legislative and gubernatorial direction—contained in the 2010-11 budget act. However, it points out that this part of the strategy for addressing the current resources gap has yet to be implemented. This “over-target” enrollment was served in 2011-12 with one-time resources, something that cannot be sustained.

In addition, there are various “synergies,” administrative and instructional efficiencies, and other cost-reduction strategies—at the system level and at individual campuses—that are either in process of implementation or are under consideration that are needed to close the current resources gap on an ongoing basis. These include, among other options discussed in the consultation process, the following:

**Synergies and Shared Services**
As previously explained to the Board of Trustees, the synergy projects and the concept of shared services centers are already being explored and/or implemented. Although solid estimates of savings are not yet available, elimination of unnecessary duplication of services, more collaborative efforts and continued leveraging of the size of the CSU are expected to reduce expenditures in the tens of millions of dollars in the first few years of operation. As the concepts come more clearly into focus, discussions will be held with the affected collective bargaining units when hours, wages, and terms and conditions of employment may be affected. There was general support for the concept of synergies and shared services during the consultation process. Staff recommends the continuation and expansion of synergies and shared services.

**Discontinuance of Academic and Athletic Programs**
The academic leadership recognizes the need to begin a systematic and consultative process of eliminating programs that are of low demand, and/or unnecessarily duplicative across campuses in a given region. The amount of savings will depend on the programs to be eliminated. Staff recommends the establishment of systemwide taskforces charged to examine academic and athletic programs throughout the system and recommend program eliminations.
Alternative Strategies for Addressing the $250 Million Trigger

The signed budget package presents the CSU with increasingly difficult choices, most clearly with its feature of a $250 million “trigger” reduction in the event the governor’s tax initiative is not enacted at the November election. Given the stresses already created by prior cuts, the easy choices are gone and the $250 million trigger cut poses a mammoth challenge. There are multiple feasible approaches to address this contingency, but all feasible approaches that add to $250 million share one thing in common—they are unpalatable. Legitimate objections could be raised to each option. However, drastic reductions in state support have real consequences. If the trigger cut happens the CSU will have lost 39 percent of its annual state support relative to 2007-08 and the university will not be able to count on a turn-around in its fortunes in subsequent fiscal years.

Attachment A shows two alternative scenarios for addressing the $250 million trigger cut. One scenario involves a balance between spending reductions and revenue increases. Its intent is to have “shared responsibility for access and quality”—hence the title. This “Shared Responsibility” strategy includes the idea of a “trigger on a trigger.” Under this concept, the board would authorize at its September meeting a mid-year tuition fee increase of $150 per semester (for full-time undergraduates) or about 5 percent, but only “triggered” if failure of the tax initiative makes the $250 million trigger cut happen. This option would “solve” roughly $58 million of the trigger cut in 2012-13 and roughly $116 million in 2013-14.

This $150 per semester tuition fee option also assumes that there would be no incremental “set-aside” for additional financial aid. There are several considerations behind this approach. One is that it would require a 7.5 percent tuition fee increase—rather than a 5 percent increase—to generate the same amount of net resources to offset the budget cut if the board wanted to continue the past practice of setting aside one-third of the increment. This not only would entail a larger tuition fee increase, but in effect would result in middle income students and families subsidizing financial aid for other students. We believe this is a difficult choice to justify considering the large amounts of financial aid already in place—including almost $700 million of State University Grants (less than five percent provided by the state and over 95 percent provided by the CSU in the form of a complete tuition fee waiver or discounted fees), about $700 million of federal Pell grants, about $460 million of Cal-grants, and over $50 million of formal fee waivers, among other financial aid options that result in nearly half of CSU undergraduates paying no tuition fee at all.

Although in recent years the board has observed a practice of setting aside one-third of potential incremental revenues, it has in some years made smaller set-asides in deference to fiscal concerns. For example, in the 2004-05 fiscal year, the board set aside one-fifth of the potential incremental revenues and in 2005-06 it set aside one-fourth.
Enrollments and Jobs

Given that approximately 85 percent of the operating budget’s annual spending is on salaries and benefits of faculty, staff and administrators—and given non-personnel spending reductions already underway to address the gap created by prior cuts—it is impossible to reduce spending an additional $250 million without significant reduction in spending on payroll. Generally, further reductions in the number of faculty, staff and administrators employed by the university must be accompanied by reductions in the numbers of students being served if the quality of the educational experience for enrolled students—and their access to needed courses—is to be preserved.

The revenue boost provided by the “trigger on a trigger” allows the Shared Responsibility strategy to avoid further enrollment impacts on students and minimizes consequent loss of faculty and staff jobs. Thus, the Shared Responsibility strategy avoids the 3 percent potential reduction in the 2013-14 enrollment target that was announced in March—a reduction involving approximately 12,000 students and 1,500 jobs.

The lack of revenue in the alternative strategy forces more drastic spending reductions, including a 1.5 percent reduction in the 2013-14 enrollment target and the loss of another 750 jobs.

Reducing Average Payroll Costs

Enrollment levels, program quality and the size of the work force can also be protected if the cost of salaries and benefits per employee can be reduced. This requires collective bargaining with the various unions. However, as noted, we are at a point where all the options are unpalatable and the tradeoffs are all difficult. One method for achieving this systemwide reduction in pay and benefits would be to negotiate a reduction in salary. The assumption in each scenario in Attachment A would be that the bargaining agreements on this issue would provide that the reductions would go into effect January 2013, but only if the trigger cut happens. Our current estimate is that each one percent reduction in salary results in $28.3 million of reduction in salary and salary-related benefits across a 12-month period. The Shared Responsibility strategy assumes a systemwide reduction in pay and benefits of 2.5 percent. The lack of revenue in the alternative strategy requires a larger reduction assumption—in this case, 5.25 percent.

An alternative way of reducing compensation and benefits that would not result in a reduction in pay would involve negotiating an alternative cost-sharing formula for health care benefits. Currently, the CSU share of premium cost is capped at a high level based on a statutory formula. For an individual, the employer cap is set at 100 percent of the weighted average premium cost of the four benefit plans with the highest enrollment of state employees. For each family member, the CSU must cover 90 percent of the additional cost based on those same benefit plans. As a consequence of this generous formula, annual spending by the CSU on health benefits has climbed by $60 million since 2007-08 to an estimated total of $356 million in 2011-12, despite the fact that there are about 3,000 fewer
CSU employees. The premium rates recently announced by CalPERS for calendar 2013 will increase CSU annual costs by another $36 million. The state long ago negotiated premium cost shares with its unions that are about 20 percent less expensive. For example, negotiating a cost-share similar to the state’s could avoid $35 million of CSU expenditure in 2012-13 and $70 million in 2013-14 and beyond.

Faculty Assigned Time and Sabbaticals

The procedures and process for granting sabbaticals are subject to provisions in the collective bargaining agreement for faculty members. Systemwide about $12.5 million is spent to backfill for faculty members on sabbaticals. Each campus will determine if a sabbatical can be granted in a manner mindful of fiscal constraints, pursuant to the provisions of the collective bargaining agreement. A far larger amount of funds are spent on backfilling faculty for “assigned time.” Assigned time is assignment to non-teaching activities in lieu of a portion of the normal teaching workload. This includes research and scholarly activities, but also things like serving on campus committees. Campuses have reduced assigned time by 13 percent since 2007-08. However, given the exigency that would be created by the $250 million trigger cut, we believe that further prioritization of workload would be feasible and necessary.

Adding a Third Tier to the Tuition Fee Structure

Adding a “third tier” to the CSU resident student tuition fee structure would dissuade students who are signing up for extra course loads by charging them full freight for course loads over what is required to complete the degree in four years. Given current constraints on ability to offer course sections, the ten percent of undergraduate students who take extra course loads are, in effect, preventing the other 90 percent from gaining fair access to a 15-unit course load, the standard under which state funding is provided to the CSU and the course load that typically is needed to complete a baccalaureate degree in four years. Access to enroll more eligible new students also is constrained. Under this “third tier” approach, students would pay an additional per-unit charge for course loads that are above 16 units, in the process providing the resources that would allow additional course sections and “seats” to be available for all students.

For the third tier to work, it needs to be coupled with two reinforcing strategies to change student behavior. First, seven percent of CSU seniors are “super seniors,” that is, students who have earned five years or more of academic credit on the CSU’s state-supported “dime.” Their earned units are enough to complete high-unit majors and other academic interests. The first reinforcing strategy is a full-freight Graduation Incentive Fee that would be charged to “super seniors” who are continuing to enroll at CSU campuses. Coupled with current campus actions to confer degrees to “super seniors,” the announcement of a Graduation Incentive Fee would have the helpful effects of graduating “super seniors,” increasing graduation rates, and freeing admission slots for eligible CSU applicants.
With 10 course repeats per 100 CSU undergraduates, over 40,000 seats in state-supported classes are being taken by students who already have taken the course, at least once, on the CSU’s state-assisted “dime.” It generally is agreed that one “free” course repeat makes sense for young people who are experimenting and testing themselves, but policy permits students to take almost a full academic year of state-subsidized course repeats. The second reinforcing strategy is a full-freight Course Repeat Fee, applied after the “first” free course repeat. Students are unlikely to take a major prerequisite course more than twice if they must pay a Course Repeat Fee. Coupled with active advising to assist students to hone their strengths and interests in more aligned academic programs, CSU students should progress to degree more effectively.

Equal opportunities to get needed classes, opening slots for eligible CSU applicants, getting students on pathways to degree, and getting students to the degree with less cost and time to them are the primary objectives of these three strategies. It is anticipated that adding the third tier to the tuition fee structure and the marginal effects of the other fees would generate about $35 million annually, starting in 2013-14. This option not only generates needed resources in 2013-14 and beyond but makes sense as a policy change that should be considered even if there is no trigger cut.

Nonresident Tuition Supplement
Currently the CSU collects approximately $135 million annually from out-of-state and international students. These students represent a relatively modest share of total enrollment of about 4 percent. These students pay a tuition supplement of $11,160 per academic year in addition to the standard tuition fee. They also pay an additional per-unit tuition fee to the extent they take more than 30 units per year. This option assumes that a 9 percent increase in the tuition supplement (around $1,000), effective Fall 2013, would produce about $13 million in additional revenue in 2013-14. Even with this increase, total nonresident charges would be substantially less than peer institutions around the country.

One-time Transfer of Continuing Education Balances
Both scenarios assume a transfer of approximately $75 million from the CSU’s Continuing Education Revenue Fund (CERF). This is a rough estimate of the balance that could be moved without harming current extended education commitments. It could provide significant relief to the “state-side” of the university in 2012-13, but the relief would be one-time and restricted to that fiscal year. Language in the enacted budget act grants this emergency transfer authority to the chancellor, but only in the event that the governor’s tax initiative fails.

State’s Offer of a Delayed Buy-out of a Tuition Fee Roll-back
The most notable new development in the enacted state budget for the CSU is the proposal to “buy out” the already-implemented tuition fee increase for the 2012-13 academic year with an appropriation that would not be operative until the 2013-14 fiscal year, and only then if the
November tax initiative is enacted. One of the budget trailer bills (AB 1502) includes separate appropriations of $125 million each to the CSU and the University of California for the 2013-14 fiscal year. Two conditions must be met if the CSU wants to access its appropriation next year: (1) the governor’s tax initiative must be enacted and (2) the university must reset its tuition fee rates for the 2012-13 academic year back to the levels in effect for the 2011-12 academic year. The governor and legislative leaders are aware that the CSU not only has higher tuition fee rates in effect for 2012-13 but has already collected the higher tuition fees from continuing students. Thus, they understand that complying with the second condition of the delayed appropriation would require our board to rescind its action of last November and would require the processing of refunds to students for Fall 2012.

Based on discussion with Department of Finance and legislative staff, we believe that the board could comply with the condition—if it desires to accommodate the legislative and governor’s intent—with an action at its September meeting to rescind the tuition fee increase for the full 2012-13 academic year contingent on voter enactment of the November tax measure. Under this scenario, campuses would begin processing refunds or credits for Fall 2012 shortly after a successful passage of the tax measure and students registering for Spring 2013 would pay the rates in effect for 2011-12. For a full-time undergraduate who pays tuition fees, rolling back the tuition fee rates would constitute a reduction of $249 per semester, or $498 for an academic year.

On the basis of a strict fiscal analysis, the delayed appropriation proposal does not make sense for the CSU. Viewed in a larger context, however, the proposal enhances the appeal of the governor’s tax initiative, a matter of great potential impact for the university’s future funding prospects. From a fiscal standpoint, rescinding the tuition fee increase would create a one-time hole in the system’s operating budget of $132 million for 2012-13. The $125 million base appropriation in 2013-14 would cover about 95 percent of the ongoing loss from the decision to reset rates to 2011-12 levels, but it would not compensate for the one-time loss in 2012-13.

At the time this analysis was prepared, we had been working with Department of Finance staff and legislative staff on options that could address this one-time problem. We have secured support from the governor’s office for a budget “clean-up” bill that would grant the chancellor authority to move surplus balances from continuing education to mitigate impacts on state-supported instruction regardless of the outcome of the election. (The current budget bill grants this authority only if the tax measure fails.) We are hopeful that we will secure legislative support of this “fix” in a clean-up bill that would pass before the August close of the legislative session. This “fix” would address roughly half of the one-time gap that would result from a board choice to rescind the tuition fee increase. We are still exploring other options to address any remaining gap.