19 June, 2018

Faculty Regent Report to Faculty Senate

Dear Faculty Senate Colleagues,

The Board or Regents (BOR) met Thursday, June 7th, at 10am. Prior to the full meeting of the BOR, Dr. Morgan and Facilities AVP Kim Oatman hosted a tour of the facilities highlighted in the Facilities Task Force report presented at the May 10th meeting. This report also includes notes reflecting Dr. Morgan's "catch up" meeting with constituency leaders on June 18th, which focused on the issues discussed and voted on at the June 7th BOR meeting.

The June meeting is traditionally one of the most consequential quarterly meetings because the BOR typically considers the operating budget and personnel roster for the subsequent fiscal year. This year was no different. Before turning to the budget and related items, the BOR approved the following important actions unanimously. (For a complete list of actions considered, please consult the BOR agenda.)

- The BOR passed resolutions commended the excellent service of three outgoing regents: Mr. Paul C. Goodpaster, Ms. Rachael Malone, and Dr. Shannon Harr. (Craig Dennis, incoming staff regent, Brandon Bryer, incoming Student Government Association President, and a governor-appointed regent will be sworn in at the August meeting.)

- The BOR approved awarding the Founders Award for University Service to Dr. Frances Helphinstine, who joined Morehead's faculty in 1966 and recently announced her retirement after a distinguished career spanning more than five decades.

- The BOR ratified the Spring 2018 graduation list.

- The BOR approved eight faculty promotions to the rank of professor: Dr. Chien-Chih Peng (Finance); Dr. Elizabeth McLaren (Education); Dr. Mark Graves (English); Dr. Michael Fultz (Biology); Dr. Thomas Pannuti (Astrophysics and Space Science); Dr. Gina Gonzalez (Kinesiology); and Dr. Wilson Gonzalez-Espada (Physics).

- The BOR approved the promotion of Jason Griffith and Rodney Watkins to Librarian II.

- The BOR approved the granting of emeritus status to five faculty members: Dr. Mesghena Yasin (Economics); Dr. Janet McCoy (Communications); Dr. Francis Helphinstine (English); Dr. Jack Weir (Philosophy); and Dr. Dora Ahmadi (Mathematics).

- The BOR ratified normal personnel actions for the period March 7 – May 16, 2018.

- On recommendation of the audit committee, the BOR approved the reappointment of our current auditing firm, Dean Dorten Allen Ford, PLLC, and a minimum scope of the university's audit for FY2018.

After several careful and lengthy discussions (detailed below), the BOR also accepted/approved the following recommendations:

- Accepted third quarter financial report and third quarter budget amendments;
- Approved FY2019 operating budget, fee schedule, and personnel roster;
- Approved a new policy on budget reserve;
- Approved plans to request proposals for outside audit of financial policies;
- Approved naming of practice area at Eagle Trace Golf Course for former head golf coach, Dr. Rex Chaney;
- Approved naming of 19 spaces and furnishing in ADUC;
- Approved a recommendation to raze Butler Hall.
- Approved a recommendation by the executive committee to extend President Morgan's contract by one year, through the 2021-22 academic year.

Third quarter financial statement, budget amendments, and capital outlays

There were no concerning budget amendments in the third quarter, and revenues and expenditures proceeded according to the historical/expected pace.

The only budget amendment exceeding $200,000 was an allocation of $995,962 from Auxiliary fund balance to reimburse ARAMARK for the purchase of kitchen equipment and related items for ADUC. **This expenditure will be reimbursed** from the state-issued bond to support construction of ADUC. (Of course, as we learned earlier this Spring, the project is about $2.3 million over budget as a result of the decision, several years ago, to build Third Street Eats out of the construction allocation with the institution promising to make up the balance from fund balance this fiscal year).

The Lappin Hall cooling system replacement is listed as "in progress" during the third quarter of FY2018, and indeed remains in progress at present – more than two years after its original failure. The project is expected to be completed before the close of June, 2018/ the fourth quarter of FY2018.

FY2019 operating budget, fee schedule, and personnel roster

As everyone on campus knows, the present fiscal environment made this the most difficult year in memory to craft a balanced budget. The following revenue reductions and unavoidable increases in recurring costs, totally approximately $11 million, made significant cuts necessary for next year:

- $2,790,200 reduction in state support;
- $4,991,100 anticipated reduction in tuition revenue (including a $925,600 revenue shortfall for AY 2017-18, to be made up next year);[1]
- $815,000 one-time investment in health insurance to hold 81:19 institutional/employee contribution ratio for 2018 calendar year;[2]

[1] In recent years, we have consistently learned midway through the Spring term that the administration had overestimated tuition revenue resulting in midyear budget pressures. Dr. Andrews' last budget overestimated tuition revenue for FY18, resulting in a $926,600 revenue shortfall that will have to be made up next year. Dr. Morgan plans to take a more cautious approach to projecting tuition revenue in the hope of avoiding similar shortfalls in the future.

[2] In order to hold health insurance rates constant for the 2018 calendar year, the institution made the decision to invest $1.5 million into employee health care last Fall to keep rates constant (at the time, increases in employee contribution rates for KERS

- ~$1,500,000 in other fixed/ unavoidable costs (increases in rates for insurances/utilities/ service contracts, contractually obligated compensation increases, and strategic enrollment initiatives).

In addition to these recurring costs, the former administration committed the institution to the following one-time costs, which were borne this fiscal year:

~$700,000 for contractually-obligated purchase of the Rowan Country Detention Center;
~$2,300,000 ADUC construction/ furniture/ technology overrun;
~$800,000 third and final installment payment for Board of Education Building.

The bulk of the one-time costs noted above can be covered with one-time revenues, including property sales and the "calling back" of residual funds from construction accounts in Frankfort. While these one-time expenditures will therefore not deplete the institution's operating reserve to a concerning level, they nonetheless aggravated an already difficult budget year.

It is important to note that new budget pressures will continue to challenge the institution in coming years. Due to a last minute bill passed by the KY state legislature (HB 265), the increase in the KERS pension rate (expected to cost MSU in the vicinity of $2 million depending on staffing levels) was deferred until next fiscal year. In addition, the performance funding model mandates a further cut of $385,600 in state support for FY2020, an approximately $750,000 cut in FY21, with deeper cuts expected as the model's stop-loss provisions expire in FY22. The state has also mandated a significant increase in KTRS pension rates for FY2021 and the institution expects modest enrollment declines, particularly among international and graduate students, in coming years. If there is a silver lining, it is that the new administration is planning several years out and basing our budget forecast on more reasonable revenue assumptions than in past years.

As a result of these pressures/outlook, the administration recommended to the BOR what interim CFO Theresa Lindgren called "one of the most fiscally prudent operating budgets I have ever seen." Next year's budget contains difficult cuts across the board, cuts that have and will create real hardships in academic and non-academic units across campus. **In all, the institution trimmed spending by about $11.5 million, of which $9.7 million comes from cuts to personnel expenditures.**

While CFO Lindgren noted that there "is more work to be done aligning the budget with institutional priorities," **spending on instruction will actually increase next year in budget proportionate terms—for the first time in ten years.**

Table 1. Spending on Instruction as percentage of Education & General (E&G)

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17 Actual	2017-18 Opening	2018-19 Opening
Instruction %	41.54	40.42	37.96	36.59	36.12	34.51	33.95	32.82	31.1	33.6

Source: 2018-19 Operating Budget & Institutional Financial Summaries (based on audited financials)

Proportionately larger cuts fell on Institutional Support (the functional category that includes most administrative units), Operations & Maintenance, and the President's Office. I pause to note funding levels

and KTRS seemed likely). This drove the overall employer/employee contribution ratio to 81:19. Half of this cost will be borne in the 2018-19 fiscal year (for July – December, 2018, health benefits). In light of concerns raised by the campus community respecting the Healthcare Taskforce proposal to trim back $1.5 million in health benefits expenditures, the institution has issued an RFP to healthcare providers specifying a request for plan options that would return the institution to a 75:25 or 70:30 cost sharing arrangement. More information respecting changes to MSU's medical insurance plan for 2019 will be communicated to faculty and staff in August.

in these units because Faculty Senate has been pointing to increasing expenditures in these particular non-instructional units for years—as evidence that the former administration was *not* prioritizing the core mission of the institution. Note that Institutional Support will spend almost $3 million less next year, Operations & Maintenance will trim almost $2 million, and spending in the President's Office will be cut a further $200,000 (to about half what was spent in 2015-16).

Table 2. Non-instructional expenditures in select units/ functional categories (not adjusted for inflation)

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
President's Office	759,201	737,847	775,432	848,460	1,035,092	1,064,348	1,143,156	903,641	750,304	577,935
Institutional Support	12,892,712	13,869,044	13,412,387	13,528,464	14,680,537	16,630,544	16,559,432	16,034,342	17,342,873	14,392,495
O & M	8,727,823	9,222,653	8,812,954	8,642,717	10,704,103	11,583,553	11,498,943	12,095,896	10,354,320	8,653,582

Source: 2018-19 Operating Budget & Institutional Financial Summaries (based on audited financials)

Similarly, Athletics will absorb an almost $500,000 budget cut in FY19. Over the course of the last ten years, Athletics has seen its budget increase significantly while spending on Instruction has fallen steadily (in both dollar and budget-proportionate terms). Similarly, while the institution made deep cuts in Academic Affairs in each of the last three budget cycles, Athletics spending remained relatively stable until the cuts proposed for FY19.[3] Much as Faculty Senate has expressed alarm at increasing Athletics spending in the past, it is appropriate this year to note that the trajectory has now reversed.

Table 3. Athletics spending (not adjusted for inflation)

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17 Actual	2017-18 Opening	2018-19 Opening
Athletics	6,607,028	7,342,020	8,366,162	8,024,341	8,482,471	9,173,144	9,470,470	9,265,969	8,807,965	8,321,389

Source: 2018-19 Operating Budget & Institutional Financial Summaries (based on audited financials)

While MSU is rightly beginning to reprioritize Instructional spending, there is still work to be done. If we adjust the figures noted above for inflation, we find that Instruction has endured deeper cuts than any other division or functional category. **In inflation adjusted terms (2018 dollars), MSU spends over $11 million <u>less</u> today on Instruction than we did in 2009-10 – even though E & G revenues have grown from $106,736,085 to $121,397,900.**

Table 4. Expenditures in select units/ functional categories **in 2018 $ (adjusted per BLS inflation rate)**

	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Instruction $	48,743,488	48,241,383	45,675,545	44,089,995	45,566,590	44,839,394	43,853,385	40,313,323	37,856,307	37,489,544
President's Office	873,081	819,010	845,221	916,337	1,097,198	1,128,209	1,200,314	930,750	750,304	577,935
Institutional Support	14,826,619	15,394,639	14,619,502	14,610,741	15,561,369	17,628,377	17,387,404	16,515,372	17,342,873	14,392,495
O & M	10,036,996	10,237,145	9,606,120	9,334,134	11,346,349	12,278,566	12,073,890	12,458,773	10,354,320	8,653,582
Athletics	7,598,082	8,149,642	9,119,117	8,666,288	8,991,419	9,723,533	9,943,994	9,543,948	8,807,965	8,321,389

[3] In recent years, actual Athletics spending has been several hundred thousand dollars higher than the originally budgeted figure due to the previous administration's tradition of allocating the bulk of unallocated revenue to Athletics over the course of the fiscal year. If that trend continues, the reduction indicated from FY17 to FY18 may not actually be realized. (We will know at the conclusion of the annual audit for FY18). Dr. Morgan has indicated that going forward this tradition will end, and Athletics will be required to operate within its opening budget like the rest of the campus.

Source: 2018-19 Operating Budget & Institutional Financial Summaries (based on audited financials)

Tuition freeze

In addition to approving an operating budget (and attendant personnel roster) for 2018-19, the BOR approved Dr. Morgan's recommendation to freeze MSU's tuition rate at this year's level for AY19. While some have very reasonably asked whether it is wise for the institution to "leave revenue on the table" given our current budget constraints, I supported the recommendation because I believe MSU is at risk of pricing itself out of our market if we do not reduce tuition rates relative to in-state competitors. No Kentucky institution has raised tuition and fees as aggressively as MSU over the last ten years. And, according to IPEDS data, MSU is now one of the highest *net* cost of attendance regional universities in Kentucky for most income tranches (after all scholarship/grant aid is factored in).

I believe skyrocketing tuition is one of the reasons we have seen serious declines in the size of our entering class over the last four years, from 1,685 in 2013-14 to 1,271 in 2017-18. This is one of the most serious threats to the institution at present, particularly given MSU's high debt load. **Note that a sustained reduction of 400 entering freshmen/ year would mean an accumulated decline in overall FTE enrollment of more than 2,000 students over the course of 5-6 years.** Conversations with colleagues in Enrollment Services over the last year, who interact with potential students and their parents every day, have strengthened the impression that rising costs are increasingly turning students away (and toward other institutions). If the institution cannot reverse this trend and begin to enroll larger entering classes, our financial problems will continue for the foreseeable future *even if we increase tuition rates because our total FTE enrollment will have fallen by 20-25%.* This is particularly true under the new performance funding model, which allocates our state appropriation based on the number of graduates and credit hours generated at MSU. If we cannot attract higher numbers of FTE students, our share of the state appropriation will shrink along with tuition revenue because we will be progressing and graduating fewer students (and so delivering fewer credit hours). As such, I believe freezing tuition rates is necessary to rebuild enrollment in coming years, which is vital first step to improving our long-term budget outlook.

Policy on budget reserve

The BOR accepted a recommendation that MSU make every effort to "reserve a minimum of five percent (5%) of the University educational and general (E&G) recurring budget into a separately identified reserve account for rainy day/emergency usage." The maintenance of a 5% reserve find is in line with higher education accounting practices. It also helps to demonstrate prudent fiscal management our accreditors, CPE, higher education policymakers in Frankfort, and bond ratings agencies. (Note than one Kentucky institution was dinged by accreditors for lacking such a policy this year.)

Some have asked whether it is prudent to "put so much money aside right now" and have wondered whether this policy contributed to next year's budget pressures. **It is important to note that existing funds now categorized as "fund balance" are being re-designated as an emergency operating reserve; the institution is <u>not</u> making new/ supplemental cuts for FY19 equivalent to 5% of E&G to create a new emergency operating reserve.** Previously, fund balance was used to fund one-time expenditures *and* served as the institution's *de facto* emergency reserve. Going forward, particular one-time costs (strategic investments, non-recurring maintenance expenditures, etc.) will be budgeted as funded from fund balance where appropriate *in advance*; those funds will heretofore constitute a separate line in the budget from the institution's emergency operating reserve, which will be held apart from planned one-time investments and dipped into only in urgent/emergency situations.

CFO Lindgren and President Morgan also explained that the institution has several other "built-in" reserve funds: 5% of each unit's discretionary operating budget will be locked until midyear, to be released around January as long as Frankfort does make midyear budget cuts; half the budgeted technology outlays will be locked until midyear, also to be released midyear; in line with best practices for self-insured institutions, MSU will maintain a reserve equivalent to 15% of the previous year's eligible medical claims; and the institution has created a 5% reserve fund for auxiliary services with revenue that was previously designated as auxiliary fund balance. Together with more realistic/conservative revenue projections, these measures will hopefully prevent the annual Spring budget deficit panics the institution faced in 2016 and 2017.

Naming of Eagle Trace practice facility & ADUC spaces and furnishings

The BOR approved naming the practice area at Eagle Trace Golf Course for former head golf coach, Dr. Rex Chaney. The recently completed structure to cover the driving range at Eagle Trace was funded entirely by private money. Note that Eagle Trace is expected soon to be a revenue-neutral auxiliary enterprise. The 2018-19 budget anticipates golf course revenues of $456,500 and expenditures of $463,395, which means its net cost to the institution is expected to be about $7,000 next year.

The BOR also approved the naming of 19 spaces and furnishing in ADUC. Many of these donors were originally promised naming opportunities in the Alumni Center originally planned for the East entrance to campus. The identification of naming opportunities in ADUC has helped make possible the re-designation of several generous gifts as scholarship support. Note that increasing our scholarship endowment helps the institution recruit students by enabling us to attract/recruit students with financial aid offers.

Proposal to audit financial policies

MSU's annual audit is required by statutes and includes testing policies and processes in several areas. However, President Morgan noted that it is good practice periodically to conduct a "more global" review of the institution's "financial policies and practices." As such, Dr. Morgan recommended that the BOR authorize a review to be conducted at the conclusion of this year's scheduled audit; as noted at the meeting, it will focus "on making sure that Morehead State University utilizes best practices for accounting, transaction processes, procedures, and protocols. The process will also review capital purchases, signatory review, and general checks and balances."

The BOR accepted the recommendation to proceed with an audit of the institution's financial policies, which is expected to be modest in cost, in the neighborhood of $25,000. In addition to demonstrating fiscal responsibility to SACS and interested parties in Frankfort, the review is expected to help the institution avoid repeats of this year's ADUC surprise, and other unexpected overruns that have in recent years necessitated budget cuts in March/April. Note that the Faculty Senate Executive Council—anxious that loose controls over budget amendments and transfers, change orders & purchase orders, etc., were contributing to budget instability—has been advocating a review of this type for years.

Other notable reports

- The BOR heard a report from SGA President Rachael Malone. The SGA was very active this year. Among several notably successes, every elected SGA position was contested this year, the organization ramped up philanthropy and public service activities, SGA enhanced and focused its social media presence, and voter participation in this year's SGA elections was the highest in memory.

- The BOR heard a final enrollment report for Spring 2018. Fall to Spring retention (in FTE student terms) ticked down marginally from last year, from 90.5% to 89.7%. Year over year credit hour generation for Spring was also down, from 99,329 to 97,813. MSU's FTE enrollment is expected to continue falling for several years, even assuming the size of our freshmen classes begin to increase, because we are in the process of graduating our largest cohorts in recent history. The administration is cautiously optimistic that our first time freshman class, and housing occupancy rate, will exceed budget protections – for the first time in several years.

<u>President's evaluation & one-year extension of contract</u>

In advance of his performance evaluation, **Dr. Morgan requested that the BOR <u>not</u> consider offering him a performance bonus or salary increase given the budget pressures facing the institution**. Based on a consensus view that President Morgan's performance has been excellent under exceptionally difficult circumstances, a performance level that would ordinarily justify a raise and/or bonus, the BOR unanimously accepted the recommendation of the executive committee to offer President Morgan a one-year contract extension.[4] As such, Dr. Morgan's present contract runs four more years, through AY2022, under the terms of his initial appointment. With one exception: Dr. Morgan has requested that his contract be modified to discontinue dental coverage for his family effective July 1, 2018, in line with the administration's decision to discontinue dental coverage for MSU faculty and staff. (Note that Dr. Morgan also declined the BOR's offer to write a deferred compensation package into his contract.)

<u>Concluding Thoughts</u>

This has been a difficult year across campus. We are all being asked to do more with less, and in some cases it has been next to impossible to offer students the education they deserve given funding constraints and faculty/staff shortages. We have all also seen valued and long-serving colleagues leave the institution – some as a result of budget cuts, others to pursue opportunities elsewhere. These and other unhappy realities have left morale perilously low—and we are all being asked to go another year without salary increases with the possibility of further serious benefits cuts on the horizon.

While we continue to face serious budget challenges, I believe the institution is finally moving in the right direction. As noted above, in spite of the budget difficulties we faced this year, perhaps the most serious the institution has faced in its modern history, MSU is increasing the proportion of the E&G budget we spend educating our students—for the first time in more than a decade. In other words, the institution *finally* has its priorities right. For this reason, and because we have excellent faculty and staff working across the institution, I am confident we have turned a corner and that our budget situation will begin to improve in the coming years.

Shared governance is also improving at MSU. Under Chair Tallichet's excellent leadership, the Faculty Senate worked with Staff Congress and the new administration to bring the campus together and help foster Faculty trust in university leadership. This is vitally important for many reasons: we lead curricular reforms; we hire, tenure, and promote professors (thereby shaping the institution's future); we are the classroom experience; we create opportunities for our students; we are the face of the institution in the academy, and an important face of the institution in our communities; etc. Where the faculty trusts that the institution's

[4] BOR members have been particularly impressed by Dr. Morgan's command of MSU's budget, his data-driven approach to addressing our budget challenges, his intimate familiarity with state processes and policies related to higher ed., significant early fundraising successes, and his work rebuilding faculty trust and his commitment to shared governance.

president and top administrators are committed to the core purpose of the institution and to the principles of shared governance, the faculty's energy can be unleashed in the classroom and in service to the institution. This leads to higher morale, stronger programs, better outreach, improved student successes, and better retention rates.

I look forward to working with Faculty Senate and university administrators on several priority initiatives in the coming months. Recruiting and retention remains a top priority, to which we can all contribute by supporting recruiting initiatives, and by working in our programs to progress students to their degrees as quickly as possible while maintaining high academic standards. I know the institution faces several other threats as a result of our persistent budget pressures. Among the most serious are increased difficulty retaining and attracting excellent faculty, the ongoing reduction in the number of tenure-eligible faculty, and low faculty morale. Continued investment in Instructional/Academic Affairs, and as circumstances permit, improvements to faculty compensation are therefore critically important to the institution's long term success. With the support of Faculty Senate, I will continue to argue for these as priority initiatives/investments.

Please don't hesitate to contact me with any questions you have about this report or other comments you have about the challenges (and opportunities) facing the institution.

Sincerely,

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