

Audit and Finance Agenda Item

Meeting Date: 8/31/09

Title of Item: Public Hearing on 2009-10 Budget

Background and Analysis:

In accordance with Title 5 Section 58301, the governing board is required to hold a public hearing on the adoption of the 2009-10 proposed budget of the District for the year ending June 30, 2010. The Board will be asked to officially adopt the budget at its meeting of September 14, 2009.

Enclosed for your information is a memo from Interim Chancellor Mike Brandy and a copy of the proposed 2009-10 budget.

Recommendation: (specify if information only) Vice Chancellor of Business Services Andy Dunn recommends ratification

Submitted by:	Andy Dunn
Additional contact names:	Mike Brandy
Is backup provided?	Yes

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August 31, 2009

To: Board of Trustees
From: Mike Brandy, Interim Chancellor
Subject: 2009-10 Operating Budget

Mission of Foothill-De Anza Community College District

The mission of the Foothill-De Anza Community College District is student success. We accomplish this by providing access to a dynamic learning environment that fosters excellence, opportunity and innovation in meeting the diverse educational and career goals of our students and communities

It is our focus on students that has guided all of our decisions about how to structure the budget within the current environment of declining state resources. Our sole reason for existence as a district is to provide educational opportunities for our community. We will, in fact, be able to provide many educational opportunities during the 2009-10 academic year as we will receive more than \$180 million in General Fund revenues to support our class schedule and student support services. We anticipate serving about 36,000 full time equivalent students (FTES) in 2009-10 and need to maintain our focus on the resources available and how to best use those resources to fulfill our mission.

The impact of the national recession has caused a sharp decline in the state's receipt of sales, property, and personal income taxes. These tax sources provide the revenue the state relies upon to fund community colleges. The reality of these diminished tax sources is that the state had to make painful cuts to services in all sectors within the state, including education. The district has attempted to prepare for these reductions over the last eight months, although the exact nature of the reductions was not known until the governor signed the state budget on July 28, 2009. There are still many details we do not yet understand, a few of which will be highlighted later. However, the bottom line is that we are looking at a \$10.6-12.4 million reduction in state funding in 2009-10. Even after the cuts we have already made our expenses are expected to exceed revenue by \$3.8 million.

The district's 2009-10 budget has been one of the most complex budgets to construct due to wide swings in the methods of revenue reduction considered by the state. With the July signing by the governor, we saw no fewer than three versions of the state budget within a single year. Although the July budget restatement addressed a nearly \$26 billion state imbalance, it did so by relying on numerous one-time solutions. These one-time solutions, when coupled with continued volatility in major state tax revenues, suggest ongoing risk to the revenue assumptions underlying this most recent state budget. We may well see additional state budget reductions during the 2009-10 year.

Following is a review of the district's current budget situation, strategy and implementation:

Retroactive Cuts for 08-09

In May and June 2009, we were anticipating \$4.7 million in retroactive cuts for the 08-09 year. Those cuts did not materialize in the final state budget, due in part to technical difficulties with Proposition 98. If there is a silver lining to the signed budget, it is that these mid-year cuts did not occur. Our enthusiasm for that is tempered by the fact that the state found no new money to fund Prop 98 at a higher level in 2009-10, so now we are concerned that a "deficit" factor will be deducted from our apportionment starting in Spring 2010. Since the mid-year cuts did not materialize, our district closed the fiscal year with a larger-than-expected ending balance.

Student Enrollment Fees

Fees have been increased from \$13 per quarter unit to \$17 per quarter unit effective for the fall quarter, but the entire increase is retained by the State as an offset to deeper community college cuts. We have implemented this change of fees in our registration systems.

General Apportionment Reduction

Based on the state's budget reductions, approximately **\$6.3 million** was reduced from the district's Tentative Budget revenue estimates. This reduction in general funding will lead to a "workload reduction" that will match funded enrollment with available funding, which the state projects will reduce funded enrollment by 3-4%. While this is an unfortunate consequence of the state budget, it is essential to keep per-student funding in line with the statutorily prescribed funding levels and avoid a permanent erosion of quality. Based on this latest information from the state, we will continue to implement the strategy of a 5% reduction in course sections and will adjust that strategy as necessary as we move through the fall, winter and spring quarters.

Expense Reductions Resulting from a Reduced FTES Base

As a result of the state's reducing funded enrollment and our decision to reduce the class schedule by about 5%, we are reducing the part-time faculty budget by about 62 FTEs, representing a savings of about **\$2.5 million**.

Categorical Program Reductions

The state policy to deeply cut categorical programs will have a profound impact on student and staff support programs. Most of these categorical programs have emerged over the years and have become a critical element for student success. The cuts to the programs are extremely deep, ranging from cuts of 32% to 100%, with the possibility of up to ½ of the cuts being offset by federal funds only during the 2009-10 year. There is uncertainty surrounding the receipt of those federal backfill funds; earlier state projections assumed \$130 million in federal backfill, and more recent estimates suggest that figure may only be in the \$60 million to \$90 million range.

In 2008-09 we received about \$17.5 million in funding for categorical programs. We will now receive a cut of **\$7.8 million** with the possibility of \$3.5 million in one-time federal funds for 2009-10 to partially offset those cuts this year.

The colleges are in the midst of examining options to implement these reductions. Obviously, since staff and contracts are in place for the 2009-10 year, there are limited options for significant program reductions in 2009-10. The state granted districts some flexibility to move remaining categorical funding from one categorical program to another. This could lead to the wholesale abandonment of some categorical programs in order to restore funding to other critical categorical programs. While federal funds may offset some of the categorical reductions in 2009-10, the planning has to be aggressive now so that program design for 2010-11 can be finalized with enough time to implement the those changes. Consequently, 2009-10 will be a bridge year for these programs; the real effect of the deep cuts in state funding will be felt in 2010-11. At this point, it is expected that all categorical programs would be reduced in scope collectively to live within the new revenue estimates, with the particular program details determined by the colleges. We are not anticipating any “encroachment” to the General Fund. **Our cuts to categorical programs after federal backfill could be between \$4.3 million and \$6.7 million.**

FHDA Budget Goals for 2009-10

Our goal for 2009-10 is first to focus on student access and success. All of our budget decisions are based on these goals. The departmental program reviews in place at the colleges continue to be the basis for allocation of teaching and non-teaching dollars. Our fiscal goal is to balance the 2009-10 budget, so that current revenue will cover current expense. When all the various changes in revenue and expense are factored in to the 2009-10 budget, we forecast that **ongoing expenses will exceed ongoing revenue by about \$3.8 million.**

Enrollment Management

The colleges have established FTES targets on which our apportionment revenue is based. The WSCH/FTEF ratio assumption for 2009-10 is 544. For the 2009-10 year the colleges will be building a schedule of classes within their allocation of FTEF (Full time Equivalent Faculty). It is critical that we achieve our FTES target so we can earn the maximum apportionment revenue we are entitled to receive. With the 5% reduction in FTEF allocations for 2009-10, the enrollment management teams are carefully assessing

course offerings to ensure they are aligned with our core mission. De Anza has a remaining challenge to make up the FTES lost by the Job Corp program. This means that De Anza is still anticipating on-campus growth in 2009-10, even with the state cut to FTES.

Our focus is now on a two-year goal to balance the budget

Our remaining operating deficit for 2009-10 is about \$3.8 million based on the latest set of assumptions on revenue and expense. Fortunately, we are not forced to eliminate costs now, since the district carries enough unrestricted ending balance to cover expenses through the 2009-10 year.

However, it is essential that we finalize our plan this year so the budget can be reduced by **\$3.8 million** in ongoing expense prior to the start of the 2010-11 fiscal year.

Since it is already August 2009, we must take a careful look at what may happen to our budget in 2010. While there is great uncertainty in the revenue we will receive in 10-11, we are fairly confident about some of the expense increases we are likely to experience in 10-11. The known expense increases for 10-11 include the following, for a total of \$1.6 million:

Step and column increases for staff:	\$850,000
PERS rate increase:	\$800,000 (The district contribution to PERS is expected to climb from 9.7% in 2009-10 to 11.3% in 2010-11)
Medical Benefit increases:	\$0 (We have assumed that district costs for medical benefits would <u>not</u> increase in 10-11 as a result of program changes under discussion with the unions)

The combined total of the 2009-10 deficit plus the projected 10-11 expense increases is \$5.4 million (\$3.8M plus the known anticipated increase in expenses of \$1.6M). Consequently, we are initiating a process with the colleges to identify \$5.4 million in cuts for the 10-11 year to achieve a balanced budget.

This round of reductions needs to be made with the assumption that we would achieve our FTES funded goal for 10-11, which at this time is the same as the 2009-10 FTES goal. Consequently, the vast majority of these cuts would have to come from the non-teaching side of the budget, a daunting task to say the least.

This occurs because we will need to maintain our existing level of full-time equivalent faculty to be able to offer enough courses to meet the FTES goal to receive all the apportionment we are entitled to in the 2009-10 and 2010-11 year.

Strategic Use of Ending Fund Balance

The unrestricted fund balance in the General Fund (Fund 14) and the Internal Service Fund (Fund 61) was \$27.7 million on 6/30/09. We are extremely fortunate to

have a large ending balance to help us prepare for the likelihood of additional state funding reductions in 2010-11.

This resource gives our district a unique opportunity to develop a multi-year strategy to use fund balance to help us weather the storm for the next two years. The components of the strategy to use fund balance are as follows:

1. **Set aside “escrow funds” from the ending balance to carry filled positions slated for reduction, through June 2010: \$3.6 Million.** This is consistent with our budget strategy of the last 6 months.
2. **Fund the remaining operating deficit in 2009-10 for one year: \$3.8 million.** This is consistent with our budget strategy over the last 6 months.
3. **Retain net college carryovers for their strategic uses over the next 2 years: \$11.0 million.** The colleges are actively engaged in finalizing plans to exhaust their fund balances over a 2-year period so that the deep cuts to the categorical programs can be phased in and to backfill B Budgets that were cut too deeply.
4. **Eliminate the Board Stability Fund and create a “Revenue Protection Fund”: \$7.0 million.** Every state expert believes that the current-year state budget is over-appropriated and that the one-time fixes in the 202009-10 budget will not be available in 2010-11. Consequently, it is our early opinion that we could see another apportionment reduction in 2010-11 similar to the revenue reductions in 2009-10.
5. **Establish a “Medical Rate Stabilization Fund” in the Self-Insured Fund to allow district and employees to smooth rate increases in future years: \$5 million.** Changes to the district medical plans are under discussion with the unions, but if the district were to stay self-insured, then this fund could be used to smooth rate increases in future years.
6. **Carry forward the reserve for elections: \$292,000.** Since no candidate filed to run against Trustees Swenson and Cheng on August 7, 2009, there will be no election costs in the 2009-10 fiscal year. We recommend carrying forward \$292,000 and resume budgeting \$292,000 as an operating expense payment in 2011-2012, so we will have about \$600,000 to pay for the Fall 2011 election.

The attached table, “Unrestricted Ending Balances Sources and Uses” (Projections as of 8/11/09) shows a summary of the ending balance as noted above.

In summary, the structuring of the district budget for 2009-10 continues to focus on student access and retention. We have a very dedicated staff with deep leadership talent throughout the organization whose goals are to fulfill our mission to serve students. The creativity and dedication of the staff will enable our district to maintain the quality of

education we offer our students and to maintain FHDA as a leader in community college education.

A component of our strategy to insure student success is also focused on aggressively identifying new revenue sources, for example:

Grants: We have recently been awarded some major grants and are aggressively seeking additional federal funding for workforce and economic development grants. We are also considering possibilities for funding a grants development position in order to support the work of the presidents, vice presidents, deans, directors and faculty who are pursuing these grants.

Foundation: The Foundation Board has also set their fundraising goals for 2009-10 to try to backfill some of the cuts the district received from the state. We are particularly focused on using the Foundation to find alternate sources for some of the cuts we are experiencing in the categorical programs.

Parcel Tax: There have been some very preliminary discussions to see whether this source of revenue could be used to backfill cuts to the district budget and whether we think voters would approve this funding for our community college district. This type of short term funding may be the solution to restore critical programs during the next 4-5 years until the state economy starts to rebound.

Advocacy: The final component of our budget strategy is advocacy. We are committed to informing our community and our legislators about the role that our district can play in economic recovery and how the student demand for our classes cannot be met with this level of state funding. We will continue to inform the state legislators about the student impact of various policy decisions on funding they will likely have to consider again for 2010-11.

