AGENDA

COMMITTEE ON FINANCE

Meeting: **1:50 p.m., Tuesday, September 8, 2015**
Glenn S. Dumke Auditorium

Adam Day, Chair
Peter J. Taylor, Vice Chair
Silas H. Abrego
Kelsey M. Brewer
Rebecca D. Eisen
Douglas Faigin
Debra S. Farar
Margaret Fortune
Lupe C. Garcia
Lillian Kimbell

Consent

Approval of Minutes of Meeting of May 19, 2015

1. California State University Annual Investment Report, *Information*
2. 2016-2017 Lottery Revenue Budget, *Information*
3. Update on 2015A and 2015B Systemwide Revenue Bond Issuance, *Information*

Discussion

4. Update on Governmental Accounting Standards Board (GASB) Statement No.68—Accounting and Financial Reporting for Pensions, *Information*
5. Planning for the 2016-2017 Support Budget, *Information*

MINUTES OF THE MEETING OF
COMMITTEE ON FINANCE

Trustees of the California State University
Office of the Chancellor
Glenn S. Dumke Conference Center
401 Golden Shore
Long Beach, California

May 19, 2015

Members Present

Rebecca Eisen, Acting Chair
Talar Alexanian
Debra S. Farar
Margaret Fortune
Lupe Garcia
Lou Monville, Chair of the Board
Timothy P. White, Chancellor

Trustee Eisen called the meeting to order.

Approval of Minutes

The minutes of March 25, 2015 were approved by consent as submitted.

Approval to Issue Trustees of the California State University, Systemwide Revenue Bonds and Related Debt Instruments for Projects at San Francisco State University and San Diego State University

Mr. Robert Eaton, Assistant Vice Chancellor for Financing, Treasury, and Risk Management presented two projects for which staff requested financing through the CSU's Systemwide Revenue Bond (SRB) and commercial paper programs. He noted that additional action was approved for the second of these projects in the Committee on Campus Planning, Buildings and Grounds.

Mr. Eaton presented the first project, the Mashouf Wellness Center project at San Francisco State University. He stated the project's budget was $86.5 million of which $29.7 million would be paid from student union reserves and the balance, $56.8 million would be financed. The requested not-to-exceed amount of $67,935,000 also included an additional $11 million related to financing costs. He added that the debt service coverage ratios for this project are good, exceeding the CSU benchmarks for both the campus and the program, and stated staff recommended approval of financing for the project.

Mr. Eaton introduced the second project, the San Diego State University Research Foundation Engineering and Interdisciplinary Sciences Complex. He stated that the San Diego State

University Research Foundation would finance and lease the project to the campus and that the project's budget was $79.7 million and would be funded from multiple sources: $25 million from auxiliary reserves; $4.7 million from campus reserves or the CSU's 2015-2016 capital improvement program; and up to $50 million from financing. He added that the requested not-to-exceed amount of $57,925,000 also included an additional $7.9 million for financing costs related to the transaction. He also noted that the not-to-exceed amount was based on the absence of any fundraising, however, the campus would be planning a fundraising campaign and any dollars raised in support of the project would be used to reduce the financing component accordingly.

Mr. Eaton stated that the debt service coverage ratios for this project were good, exceeding the CSU benchmarks for the campus, the auxiliary, and the project. He added that staff recommended approval of financing for the project.

Trustee Taylor inquired if the student body center fees used to fund the debt service for the Mashouf Wellness Center were fees the students voted upon. Mr. Eaton responded yes, there was a referendum that took place in 2009 and it was approved by the students.

Trustee Taylor further inquired about coverage ratios. He asked if the coverage levels were set when the SRB program was created. Mr. Eaton responded that they were established in 2002 and indicated that staff was currently looking at revising those ratios under the new capital financing authorities. Trustee Taylor stated that he would be glad to be part of that review and Mr. Eaton indicated that staff would appreciate his input.

Trustee Eisen inquired about Mashouf Wellness Center project and the accurateness of the chart that was presented to the board. She pointed out that the board had reviewed the project in July 2012 and approved the schematics in May 2014. Mr. Eaton responded that the 2012 action was likely an amendment to the master plan. He added that financing is generally the last step in that process with respect to board approvals.

The committee recommended approval to issue Trustees of the California State University, Systemwide Revenue Bonds and Related Debt Instruments for Projects at San Francisco State University and San Diego State University (RFIN 05-15-08).

Approval to Extend the Bond Anticipation Note and Bond Sale Dates for an Auxiliary Project at California State University, Fullerton

Mr. Eaton stated this item requests board approval to amend the resolutions authorizing financing under the CSU's commercial paper and Systemwide Revenue Bond programs for the CSU Fullerton Auxiliary Services Corporation, Western State University College of Law Acquisition Project. He added the amendments would extend the dates by which interim financing and bonds may be issued.

He stated that in 2012, the board authorized financing to allow the Fullerton Auxiliary Services Corporation to purchase a facility adjacent to the campus, commonly known as Western State University College of Law, for campus academic programs. Through a sale-leaseback arrangement, the seller was allowed to remain in the facility as tenant for up to three years. Mr.

Eaton stated that since that time, the tenant has been delayed in finding a suitable replacement site, thus extending the amount of time that the tenant will need to stay at the facility. This in turn required similar extension on the terms of interim financing and bond financing for the facility. He stated the board is being requested to approve resolutions to extend the date to sell bond anticipation notes and bonds to September 2018.

Chancellor White clarified that the CSU is accommodating the request of another educational institution because of their inability to find adequate space. He added that there was a choice to deny their request but felt that at the collegial level it was inappropriate because students would have been negatively affected. He inquired if there are any additional costs associated with appropriate professional decision.

Mr. Eaton responded that there are no additional costs. He stated that, through provisions in the lease arrangement on the extension, the campus would continue to receive lease payments at the fair market rate. He added he had confirmed that the campus programs would not be disadvantaged by this extension.

The committee recommended approval to extend the Bond Anticipation Note and Bond Sale dates for an auxiliary project at California State University, Fullerton (RFIN 05-15-09).

Report of the 2015-2016 Support Budget

Mr. Ryan Storm, Assistant Vice Chancellor for Budget, stated that he would provide a brief recap of the Trustees' Support Budget, the Governor's January and May Revision proposals, a report on the legislative budget hearings, and next steps.

Mr. Storm indicated that the development of the 2015-2016 state budget began last fall when the Trustees adopted a $269 million budget request that would increase funded enrollment, invest in student success and completion initiatives, and invest in academic facilities, among other things. The first state response to the Trustees' budget request came in January when the Governor's Department of Finance issued its 2015-2016 budget proposal. He stated that the most significant components of that proposal were an increase of $119.5 million that could be used for operating and capital needs of the CSU, a one-time appropriation of $25 million to address the CSU's most pressing deferred maintenance and infrastructure needs, and a one-time appropriation of $25 million for another phase of the Innovation Awards.

Mr. Storm then moved on to the May Revision, stating that it was the Governor's and Department of Finance's opportunity to alter the January budget proposal. The May Revision, he stated, consisted of an additional $38 million of permanent, reoccurring dollars to the CSU support budget. He added that this additional funding was to support two board priorities: student success and completion initiatives and new funded student enrollments. He added that this was the first time in a few years that the Governor's administration has provided new, permanent support budget funding and explicitly stated how that funding should be spent. Altogether, the Governor proposed an increase of $157.5 million from the general fund, plus $35 million of new, one-time funding that would pay for energy efficiency and renewable energy projects on CSU campuses.

Mr. Storm stated the May Revision was an encouraging step, considering the limited resources that have been provided to CSU since recovery from the Great Recession began in 2012-2013. He added, however, that the CSU has done its part in containing costs, leaving tuition flat for four years in a row, keeping funding requests at a minimum for several years, and has not received funding restorations like other state programs during these good economic times. He stated that the CSU has and would continue to request full funding of the Trustees' support budget plan from the state and do its best to advocate for a budget that would allow the university to fulfill its obligations to the people of the State of California.

Mr. Storm then discussed the budget subcommittees for education finance in the Assembly and the Senate and stated that several hearings were held this spring on the Governor's higher education budget proposals. He added that many legislators have expressed an interest in expanding capacity on CSU campuses, both in new student enrollments and more access to courses and supportive services for current students. He stated that as a result, staff is working with the Legislature to improve the CSU's budget picture with the end goal of producing additional degree-holding graduates that could serve California.

Mr. Storm then presented the next steps on the support budget. He indicated that the state is less than two months away from completing its 2015-2016 budget and explained the milestones that would follow. First, he stated that the Assembly and Senate would independently wrap up their post-May Revision budget hearings this week and would make decisions on the governor's and their own budget proposals. Secondly, the houses would hold budget hearings to reconcile differences between their budget plans in order to create a single budget plan. Then, he stated the legislature would vote on a final state budget in the middle of June. He added that the governor may veto portions of the budget and approve the remainder by June 30. What this means for the CSU is there is no budget reduction, however the Governor's plan is significantly less than the trustees' budget request.

Mr. Storm stated that with final state budget decisions still to be determined, there is not enough information to determine a final budget for the CSU for the approaching fiscal year at this meeting. Instead, Chancellor's Office staff will await final state decisions before finalizing the CSU budget, pursuant to the resolution (RFIN 11-14-05) passed in November 2014 that authorized the chancellor to adjust and amend the support budget to reflect changes in the assumptions upon which the budget is based. Chancellor's Office staff will provide proper notification to the Trustees.

Trustee Monville thanked the entire team for their ongoing efforts in advocating for the CSU in Sacramento. He added that additional baseline funding, not one-time finding, will help the CSU make long term decisions and planning for the future of California. He asked Mr. Storm to elaborate on the dialogue the CSU is having in that regard. Mr. Storm stated that decisions were a reflection of estimated revenues by the Department of Finance and what is believed to be sustainable over a long period of time. He added that typically with one-time funding, the CSU could invest in deferred maintenance, capital projects, and instructional equipment, which are very limiting.

Trustee Monville stated that the board has been focused on graduation initiatives and time to degree, which partially depend on additional tenured faculty. He added that if the board is to make that a strategic investment and improve those areas, ongoing and not one-time dollars are needed. He stated the board is committed to work with the governor and legislature to advocate for the dollars we need.

Trustee Brewer asked Mr. Storm to expand upon the constraints that Proposition 98 and Proposition 2 present for the CSU. Mr. Storm responded that Prop 98 is a constitutional guarantee that there would be a certain amount of money always dedicated to education. He added that during the recession, K-14 funding had significant reductions and that part of that constitutional framework required that as money becomes available within the state, the state needs to maintain or put more money back into those areas of K-14 education. He added that approximately 40 percent of all state general fund reserves go to K-14 but that nearly all of that necessary repayment to K-14 education due to the recession is completed. Prop 2 is a way for the state to deal with the ups and downs of a volatile revenue stream and this is one more program taking money out of the mix that could be used for discretionary programs like the CSU. He added overall, the amount of money dedicated towards the CSU has been reduced a bit.

Trustee Taylor stated that he is curious about the pilot project at University of California (UC) Riverside regarding cost and expense control on a department by department basis and its applicability to CSU. He was also curious as to whether there are any conversations regarding UC's exploration of hybrid defined benefit and defined contribution program and how that applies to the CSU. Mr. Storm responded that there have been some initial conversations with the governor's Department of Finance regarding activity-based cost modeling. He added that staff would continue that discussion and whether it makes sense for the CSU to explore it. Ms. Lori Lamb, Vice Chancellor for Human Resources stated that the system has the authority to offer a voluntary defined contribution plan in addition to its defined benefit plan. She added that staff is working on retirement plan options with a consultant and that a comprehensive pro-con analysis from their consultant in the next 30-60 days and the results will be brought to the board.

Trustee Eisen inquired about the historical funding levels of the CSU. Chancellor White stated that the CSU is $405 million below funding levels in 2007-2008 in absolute dollars. He added that, although the CSU is still below historic levels of funding, the advocacy efforts have helped. He then paused to recognize the achievement of the May Revision and stated that it reflected the CSU students, faculty, staff, and trustee efforts. Advocacy, he added, is helping to create pressure to move the needle in a meaningful way. He stated that additional funding is needed to create opportunity and access for students in California's future.

California State University Auxiliary Organizations

Mr. Steve Relyea, Executive Vice Chancellor and Chief Financial Officer, stated that the presentation was an update on CSU's auxiliary organizations, as requested at the March board of trustees meeting. He added that there are currently 86 CSU auxiliary organizations. These organizations provide essential services and activities, and are vitally important to ensuring student success and the financial strength of the university. Each auxiliary organization must have an operating agreement with the CSU. The agreement outlines its function and responsibilities to the university.

Mr. Relyea described auxiliary organizations as separate legal entities created to support the educational mission of the university. They are self-supporting, do not receive funds from CSU's operating budget, and are subject to California corporate law, the Education Code, and the policies of the CSU. He added that each organization had an operating agreement with the campus and trustees that specified the activities it is allowed to perform and that each organization is required to submit its annual budget and program offerings to the campus president for approval. He stated that upon review, the president may instruct the organization to not implement a specific program or expenditure, if it is deemed to be inconsistent with either the policies of the Board of Trustees, or campus policy.

Mr. Relyea indicated that the services typically provided by auxiliary organizations include: associated student body programs, student unions, and recreation centers; programs that support research, special projects and scholarships; foundations that manage grants, endowments and gifts; organizations that run dining services and bookstores; and areas that support real estate transactions and public private partnership agreements. He then turned the presentation over to Mr. John Griffin, Auxiliary Organizations Association President, to talk about the contributions of these organizations.

Mr. Griffin discussed examples of the valuable contributions of several auxiliary organizations and how they were supporting student success by providing students with hands-on-learning opportunities, preparing students for the workforce, increasing research opportunities, funding scholarships, retaining and recruiting faculty, helping students save money on textbooks, and providing support for capital improvement projects.

Mr. Relyea thanked Mr. Griffin and asked President Hagan to talk about his experience with auxiliary organizations. He added that President Hagan was the Chief Financial Officer (CFO) at CSU, Fullerton prior to becoming the president at CSU, Dominguez Hills. In both of these roles he has had an opportunity to interact with auxiliary organizations.

President Hagan stated that at CSU, Dominguez Hills auxiliary organizations provide important services that support student success. An important role for auxiliary organizations relates to supporting capital infrastructure needs. As financial support for the CSU has both declined and shifted dramatically, identifying new revenue streams has become critical.

He stated that auxiliary organizations allow the campuses to act with greater flexibility. One area that auxiliary organizations have helped to address is affordable housing. Significant home prices throughout Southern California are a deterrent to recruiting entry level faculty and staff. At CSU Fullerton, the business auxiliary worked to develop homes that could be leased to faculty and staff at below market rates. Likewise, CSU, Dominguez Hills envisions developing housing in a similar way.

He then referred to the Stub Hub Center at CSU, Dominguez Hills. In 2003, the foundation auxiliary organization assisted in building this sports entertainment venue for the campus and community. This privately developed center provides world class sporting facilities to the south bay community. The StubHub Center has transformed the community and increased the university's engagement with the region. The partnerships allowed for millions of dollars in renovations for CSU, Dominguez Hills athletic fields and facilities and produces annual revenue for the university of approximately $500,000 which is used for student scholarships and planned capital project debt service.

He concluded by stating that every president could talk about how they have utilized auxiliary organizations to help with fundraising and capital projects. The CSU's auxiliary organizations have become an essential element in CSU's efforts to meet the needs of its students.

Mr. Relyea thanked President Hagan and concluded by stating that campuses use auxiliary organizations in many beneficial ways to support the university's mission to empower student success.

COMMITTEE ON FINANCE

California State University Annual Investment Report

Presentation By

Robert Eaton
Assistant Vice Chancellor
Financing, Treasury and Risk Management

Summary

This item provides the annual investment report for fiscal year 2014-2015 for funds under the California State University Investment Policy.

Background

Most CSU funds are invested through the CSU Systemwide Investment Fund-Trust (SWIFT) investment portfolio, which was established in July 2007 for the purpose of enhancing centralized cash and investment management. On a daily basis, net investable cash from the Chancellor's Office and campus-controlled bank depository and disbursement accounts is pooled and moved into SWIFT for investment. All SWIFT cash and securities are held by US Bank, the custodian bank for SWIFT, and for investment management purposes the SWIFT portfolio is divided equally between two investment management firms, US Bancorp Asset Management and Wells Fargo Asset Management (formerly Wells Capital Management).

The State Treasurer also provides investment vehicles that may be used for CSU funds. The Surplus Money Investment Fund (SMIF) is used by the State Treasurer to invest state funds, or funds held by the state on behalf of state agencies, in a short-term pool. Beginning fiscal year 2014-2015, the agreement with the state was lifted, which required the CSU to maintain a minimum balance of approximately $310 million in the SMIF during prior fiscal years to assist in the funding of payroll. The Local Agency Investment Fund (LAIF) is used by the State Treasurer to invest local agency funds. For 2014-2015, the CSU did not invest funds in LAIF. The year-end results for these two funds are reported in Attachment A.

The California State University Investment Policy in effect during fiscal year 2014-2015 is included as Attachment B.

Market Summary

For the fiscal year ending June 30, 2015, U.S. Gross Domestic Product grew by 2.4%, with solid contributions from consumption and housing offset by tepid growth in government and exports. Employment conditions continued to improve as the unemployment rate fell from 6.1% at the end of June 2014 to 5.3% at the end of June 2015. Nonfarm Payrolls added 2.9 million jobs in the fiscal year, an increase of 283,000 over the previous fiscal year. Driven by a strong U.S. dollar and declining oil and commodity prices, inflation stayed well below the Federal Reserve's (Fed's) 2% target range.

The basic conduct of monetary policy was relatively unchanged during the fiscal year. The Fed kept the federal funds target range at 0.0% to 0.25%. It also completed the tapering process of its asset purchase program in October 2014 and, as expected, continued to re-invest principal proceeds in order to maintain a stable portfolio size. The year ended with considerable investor disagreement over the timing and pace of any Fed rate tightening. One camp, seemingly favored by Fed Chairman Janet Yellen, favors an "earlier and gradual" timing and pace of rate hikes versus the more traditional accommodative stance of a "later and faster" timing and pace. Other factors complicating the Fed's decision are the strong dollar and international concerns such as Greece and China, which can impact the stability of financial market conditions.

Credit market conditions were less favorable in the fiscal year ending June 30, 2015 versus the prior period as credit spreads widened meaningfully during the year, particularly for corporate securities. Generally, balance sheet fundamentals remained relatively solid for entities rated A or higher. However, driven by challenging conditions for revenue growth and very low interest rates, some companies conducted more mergers and acquisitions, or re-leveraged their capital structures for the benefit of shareholders, which eroded credit quality around the edges. As a result, rating agency activity was skewed toward the negative during the year, further pressuring credit spreads. In addition, investors demanded higher yields as the markets became more skittish over concerns about Greece, Puerto Rico, China, Ukraine / Russia and the direction of U.S. monetary policy.

Investment Account Performance

As of June 30, 2015, the asset balance in the SWIFT portfolio totaled $3.22 billion. The objective of SWIFT is to maximize current income while preserving and prioritizing asset safety and liquidity. Consistent with the California State University Investment Policy and state law, the portfolio is restricted to high quality, fixed income securities.

As of June 30, 2015, the SWIFT portfolio's holdings by asset type were as follows:

Cash	0.81%
US Treasuries	22.50%
US Government Agencies	35.84%
Corporate Securities—Long Term	35.95%
Corporate Securities—Short Term	4.90%
	100.00%

The SWIFT portfolio provided a return of 0.71% during the 12 months ended June 30, 2015. This return was greater than the benchmark for the portfolio, which is a treasury based index.

	SWIFT Portfolio	SWIFT Benchmark[1]	LAIF[2]
1 Month Return	-0.004%	0.023%	N/A
3 Months Return	0.112%	0.122%	0.073%
12 Months Return	0.710%	0.648%	0.268%
Annualized Return since SWIFT Inception	1.376%	1.849%	1.116%

Update on the California State University Investment Authority, Policy, and Portfolio Review Initiative

As presented to the board at its January 2015 meeting, staff has been reviewing the existing legislation governing the CSU's investments and working with key partners in the legislature, the Department of Finance, and the State Treasurer's Office to change that legislation in order to provide the CSU with greater investment flexibility and increased earnings on its existing base of funds. Discussions with these key partners are ongoing. The goal is to provide the CSU with the same investment flexibility as the University of California, which has broader latitude in the types of investments it may choose when investing its funds, and which has been able to earn significantly higher returns than the CSU. This potential for additional revenues would have a meaningful impact on the CSU's ability to address a variety of needs, including its deferred maintenance and critical infrastructure backlog.

Along with possible legislative changes, staff will conduct a review of the CSU's investment policy and present appropriate amendments to the policy to the board for discussion and approval at a future meeting. Based upon any legislative and policy changes, staff would then work to restructure the CSU's investment portfolio to meet the CSU's needs.

[1] Bank of America Merrill Lynch 0-3 Year Treasury Index
[2] LAIF investment returns are provided for reference only

Surplus Money Investment Fund (SMIF)
The Surplus Money Investment Fund (SMIF) is a vehicle used and managed by the State Treasurer to invest State funds, or funds held by the State on behalf of State agencies, in a short-term pool. Cash in this account is available on a daily basis. The portfolio's composition includes CD's and Time Deposits, U.S. Treasuries, Commercial Paper, Corporate Securities, and U.S. Government Agencies. As of June 30, 2015, the amount of CSU funds invested in SMIF was approximately $90 million.

SMIF Performance

Apportionment Annualized Return		**Quarterly Apportionment Yield Rate FYE 06/30/06 - FYE 06/30/15**	
FYE 06/30/15	0.25%	Average	1.78%
FYE 06/30/14	0.24%	High	5.24%
		Low	0.22%

Local Agency Investment Fund (LAIF)
The Local Agency Investment Fund (LAIF) is a vehicle used and managed by the State Treasurer to invest local agency funds. All investments are purchased at market, and market valuation is conducted quarterly. As of June 30, 2015, there were no CSU funds invested in LAIF.

LAIF Performance

Apportionment Annualized Return		**Quarterly Apportionment Yield Rate FYE 06/30/06 - FYE 06/30/15**	
FYE 06/30/15	0.27%	Average	1.79%
FYE 06/30/14	0.25%	High	5.25%
		Low	0.23%

The California State University Investment Policy

The following investment guidelines have been developed for use when investing California State University funds.

Investment Policy Statement

The objective of the investment policy of the California State University (CSU) is to obtain the best possible return commensurate with the degree of risk that the CSU is willing to assume in obtaining such return. The Board of Trustees desires to provide the Chancellor and his designees with the greatest possible flexibility to maximize investment opportunities. However, as agents of the trustees, the Chancellor and his designees must recognize the fiduciary responsibility of the trustees to conserve and protect the assets of the portfolios, and by prudent management prevent exposure to undue and unnecessary risk.

When investing CSU funds, the primary objective of the CSU shall be to safeguard the principal. The secondary objective shall be to meet the liquidity needs of the CSU. The third objective shall be to return an acceptable yield.

Investment Authority

The CSU may invest monies held in local trust accounts under Education Code Sections 89721 and 89724 in any of the securities authorized by Government Code Sections 16330 and 16430 and Education Code Section 89724 listed in Section A, subject to limitations described in Section B.

A. State Treasury investment options include:

- Surplus Money Investment Fund (SMIF)
- Local Agency Investment Fund (LAIF)
- State Agency Investment Fund (SAIF)

Eligible securities for investment outside the State Treasury, as authorized by Government Code Section 16430 and Education Code Section 89724, include:

- Bonds, notes or obligations with principal and interest secured by the full faith and credit of the United States;
- Bonds, notes or obligations with principal and interest guaranteed by a federal agency of the United States;

- Bonds or warrants of any county, city, water district, utility district or school district;

- California State bonds, notes, or warrants, or bonds, notes, or warrants with principal and interest guaranteed by the full faith and credit of the State of California;

- Various debt instruments issued by: (1) federal land banks, (2) Central Bank for Cooperatives, (3) Federal Home Loan Bank Bd., (4) Federal National Mortgage Association, (5) Federal Home Loan Mortgage Corporation, and (6) Tennessee Valley Authority;

- Commercial paper exhibiting the following qualities: (1) “prime” rated, (2) less than 180 days maturity, (3) issued by a U.S. corporation with assets exceeding $500,000,000, (4) approved by the PMIB. Investments must not exceed 10 percent of corporation’s outstanding paper, and total investments in commercial paper cannot exceed 30 percent of an investment pool;

- Bankers’ acceptances eligible for purchase by the Federal Reserve System;

- Certificates of deposit (insured by FDIC, FSLIC or appropriately collateralized);

- Investment certificates or withdrawal shares in federal or state credit unions that are doing business in California and that have their accounts insured by the National Credit Union Administration;

- Loans and obligations guaranteed by the United States Small Business Administration or the United States Farmers Home Administration;

- Student loan notes insured by the Guaranteed Student Loan Program;

- Debt issued, assumed, or guaranteed by the Inter-American Development Bank, Asian Development Bank or Puerto Rican Development Bank;

- Bonds, notes or debentures issued by U.S. corporations rated within the top three ratings of a nationally recognized rating service;

B. In addition to the restrictions established in Government Code Section 16430, the CSU restricts the use of leverage in CSU investment portfolios by limiting reverse repurchase agreements used to buy securities to no more than 20 percent of a portfolio.

C.

Furthermore, the CSU:

- Prohibits securities purchased with the proceeds of a reverse repurchase from being used as collateral for another reverse repurchase while the original reverse repurchase is outstanding;

- Limits reverse repurchase agreements to unencumbered securities already held in the purchased with the proceeds of the repurchase (but in any event not more than one year) and;

- Limits reverse repurchase agreements to unencumbered securities already held in the portfolio.

Investment Reporting Requirements
Annually, the Chancellor will provide to the Board of Trustees a written statement of investment policy in addition to a report containing a detailed description of the investment securities held by the CSU, including market values.

(Approved by the CSU Board of Trustees in January 1997; and as amended in September 2011 and November 2013)

COMMITTEE ON FINANCE

2016-2017 Lottery Revenue Budget

Presentation By

Ryan Storm
Assistant Vice Chancellor
Budget

Background

On November 6, 1984, California voters approved Proposition 37, known as the California Lottery Act. The Lottery Act allows for the expenditure of lottery revenues to supplement funds allocated for public education. To date, the California State University has received apportionments from the state based on total full time equivalent students totaling $1.07 billion, which equals approximately 3.7 percent of all lottery revenue distributed for educational purposes. Recently, annual CSU lottery fund receipts have averaged $45 million per year.

The Lottery Act codifies the Legislature's intent that lottery funds be used "exclusively for the education of pupils and students" and that no funds can be used for non-instructional purposes, such as the acquisition of property, construction of facilities, or financing research. To that end, the CSU has adopted guidelines to ensure that lottery funds are used only for and in support of instruction or instructional-related purposes.

Each year, the CSU Board of Trustees is asked to adopt a systemwide lottery revenue budget that incorporates CSU guidelines and adheres to Lottery Act provisions. The budget identifies expected lottery receipts that the CSU will receive in the budget year and the program areas for allocation of those receipts, including an expenditure allowance for the general management of lottery fund operations and reporting requirements. Approximately 90 percent of anticipated lottery receipts are allocated directly to campuses for instructionally-related programs and activities. Remaining funds are allocated for CSU programs that assist student education, such as the Summer Arts, Pre-Doctoral, and Doctoral Incentive programs. Only about 1.3 percent of lottery resources are used by the Chancellor's Office to manage lottery fund operations and reporting requirements.

CSU allows for the carryforward of 50 percent of annual lottery allocations to the campuses to address long-range educational programs, instructional equipment purchases, or instructional program development that crosses several years. The CSU chief financial officer reviews campuses' lottery balances to ensure appropriateness, and approves planned uses of campuses' balances in excess of policy guidelines.

The board has delegated authority to the chancellor for management of lottery fund receipts, which are used to supplement the total amount of money allocated to CSU for public education in accordance with state statutes. The CSU prepares a formal report on lottery fund revenues and expenditures each May to the Governor and Legislature, in accordance with the 2015-2016 Budget Act. The board receives an updated report at the September and November meetings.

2016-2017 Lottery Budget Proposal

The lottery revenue budget proposal for fiscal year 2016-2017 is presented to the Committee on Finance as an information item.

The total lottery budget for 2016-2017 is projected at $49.2 million. After setting aside $5 million for CSU's systemwide reserve, $44.2 million is available for allocation. The proposed budget includes a small increase of $63,000 for system programs administration. The chancellor, as the chief executive officer of the CSU, is delegated authority for development and oversight of the lottery budget and for the deposit, control, investment, and expenditure of lottery revenues received.

Beginning CSU lottery reserves of $5 million are used to assist with cash-flow variations due to fluctuations in quarterly lottery receipts and other economic uncertainties. Interest earnings on lottery balances are managed by the chancellor in accordance with CSU revenue management program guidelines and procedures.

After setting aside $5 million for beginning reserves, the $44.2 million 2016-2017 lottery budget proposal remains principally designated for campus-based programs and three system-designated programs that have traditionally received annual lottery funding support. The 2016-2017 budget proposes a small increase of $63,000 for Chancellor's Office administration of the lottery fund and for system programs administration, bringing the total to $607,000—or about 1.3 percent of total projected lottery revenues. The increase is due to higher salary and healthcare costs. As compared to the 2015-2016 lottery budget, no other changes are proposed for the 2016-2017 lottery budget.

System-Designated Programs

Of the $44.2 million available for expenditure, $4.6 million will be allocated to the three system-designated programs and administration costs as follows: the Chancellor's Doctoral Incentive Program ($2 million), which provides financial assistance to graduate students to complete doctoral study in selected disciplines of particular interest and relevance to the CSU; the California Pre-Doctoral Program ($814,000), which supports CSU students who aspire to earn doctoral degrees and who have experienced economic and educational disadvantages; the CSU Summer Arts Program ($1.2 million), which offers academic credit courses in the visual, performing, and literary arts; and lottery fund and system programs administration costs ($607,000).

Campus-Based Programs

The remaining $39.5 million in 2015-2016 lottery revenue will continue to be used for campus based programs ($31.5 million) and increased financial aid for the trustee-approved Early Start program ($8 million). Campus-based program funding is undesignated and allows presidents flexibility in meeting unique campus needs. Traditionally, projects receiving campus-based funds have included replacement and purchase of new instructional equipment, curriculum development, and scholarships. Early Start program funds will provide campus-based financial aid as need-based fee waivers to ensure that student financial hardship is not a barrier to enrollment in the Early Start summer curriculum. The program serves first time freshman students who are deficient in math and/or English skills through additional college preparatory instruction during the summer term prior to matriculation at any of the CSU campuses.

The CSU lottery revenue budget proposed for 2016-2017 is as follows:

2015-2016 Adopted and 2016-2017 Proposed Lottery Budget

	2015-2016 Adopted Budget	**2016-2017 Proposed Budget**
Sources of Funds		
Beginning Reserve	$ 5,000,000	$ 5,000,000
Receipts	44,100,000	44,163,000
Total Revenues	$ 49,100,000	$ 49,163,000
Less Systemwide Reserve	*(5,000,000)*	*(5,000,000)*
Total Available for Allocation	**$ 44,100,000**	**$ 44,163,000**
Uses of Funds		
System Programs		
Chancellor's Doctoral Incentive Program	$ 2,000,000	$ 2,000,000
California Pre-Doctoral Program	814,000	814,000
CSU Summer Arts Program	1,200,000	1,200,000
	$ 4,014,000	$ 4,014,000
Campus-Based Programs		
Campus Programs	$ 31,542,000	$ 31,542,000
Campus Early Start Financial Aid	8,000,000	8,000,000
	$ 39,542,000	$ 39,542,000
Lottery Fund & System Programs Administration	$ 544,000	$ 607,000
Total Uses of Funds	**$ 44,100,000**	**$ 44,163,000**

In fiscal year 2014-2015, similar to years prior, the majority of lottery allocations were spent on instructional and instructionally-related programs and services to supplement the CSU operating budget.

The following table summarizes how lottery revenues were spent in 2014-2015, which also includes funds available from prior years:

2014-2015 Lottery Fund Expenditure Report
System-Designated & Campus-Based Programs
(in thousands)

Program Support Area		**Expenditures**	**Percentage of Total Expenditures**
Academic Programs and Support	$	21,777	39.3%
Library Services		15,959	28.8%
Student Services		5,951	10.8%
Administration & Reporting		2,740	4.9%
Financial Aid		8,949	16.2%
Total Expenditures	**$**	**55,376**	**100.0%**

The 2014-2015 lottery expenditures were $19.2 million above the 2013-2014 expenditures of $36.1 million. The difference is attributable to lottery fund receipts from the state that exceeded revenue estimates, resulting in higher balances. The Chancellor’s Office was able to use the carry forward balances in 2014-2015 to fund several systemwide and campus programs, such as library services, early assessment program support, and technology initiatives.

COMMITTEE ON FINANCE

Update on 2015A and 2015B Systemwide Revenue Bond Issuance

Presentation By

Robert Eaton
Assistant Vice Chancellor
Financing, Treasury and Risk Management

Summary

The Systemwide Revenue Bond (SRB) program traditionally provides capital financing for revenue generating projects of the California State University – student housing, parking, student union, health center, continuing education facilities, certain auxiliary projects, and other projects approved by the CSU Board of Trustees. In addition, under the CSU's new capital financing authorities, the SRB program provides capital financing for the CSU's capital improvement program.

In August 2015, the CSU issued two SRB series, 2015A and 2015B, totaling $1,063,675,000, of which $1,034,370,000 was tax-exempt and $29,305,000 was taxable. Of the total issued $684,710,000 was for new money projects, including systemwide infrastructure improvement projects, and commercial paper payoff, at an all-in true interest cost of 3.95%. The CSU took advantage of low interest rates and issued $378,965,000 in bonds to refund existing debt, producing net present value savings of $57 million. The refunding of debt will save SRB programs across the CSU approximately $3.1 million in annual cash flow savings.

COMMITTEE ON FINANCE

Update on Governmental Accounting Standards Board (GASB) Statement No. 68 Accounting and Financial Reporting for Pensions

Presentation By

Steve Relyea
Executive Vice Chancellor and Chief Financial Officer

Summary

This item provides an update on the implementation of Governmental Accounting Standards Board (GASB) Statement No. 68 – Accounting and Financial Reporting for Pensions, which requires the CSU to recognize its share of the State's net pension liability in its audited financial statements.

Background

As reported to the CSU Board of Trustees in previous meetings, GASB 68, which is effective for fiscal year 2014-2015, requires each governmental employer participating in a pension plan to recognize a proportionate share of the collective net pension liability on the face of the employer's financial statements. CalPERS provides the information to the State Controller's Office for all state employees. The State Controller's Office then breaks down the CSU's proportionate share.

According to the information received from the State Controller's Office in August, the CSU's proportionate share of the State's net pension liability as of June 30, 2015 was approximately $5.9 billion.

At the time of drafting the agenda, Chancellor's Office staff and the CSU's external auditor, KPMG, are examining the State Controller's calculations. Upon completion of that examination, allocable amounts will be distributed to the 23 campuses and the Chancellor's Office for incorporation into CSU's 2014-2015 Financial Statements.

Bond advisors are aware that GASB 68 is a financial reporting requirement affecting all public universities and governmental entities.

COMMITTEE ON FINANCE

Planning for the 2016-2017 Support Budget

Presentation By

Ryan Storm
Assistant Vice Chancellor
Budget

Summary

As part of the preparation of the California State University (CSU) support budget request for the 2016-2017 Governor's Budget, the CSU Board of Trustees will be provided preliminary assumptions for purposes of crafting a budget request to the governor that will be presented to the board for review and approval in November 2015.

State Budget Overview

The California State Constitution requires the submittal of the governor's budget proposal each year by January 10. In order to meet consequent deadlines of the submittal of budget requests to the Department of Finance, it is necessary to commence planning for the requested 2016-2017 CSU Support Budget.

The significant tax revenues produced by Proposition 30 and the ongoing economic recovery allowed the state to begin anew to invest in public higher education. Specifically, it is estimated that state tax revenues will have increased by $28.2 billion between the recession low point of 2011-2012 and the current fiscal year 2015-2016—a 32 percent increase. CSU has benefited from the state's recovery with permanent General Fund increases of $125.2 million in 2013-2014, $142.2 million in 2014-2015, and full funding of the trustees' 2015-2016 support budget request of $216.5 million in the recently-enacted state budget. Also, the economic recovery will allow the state to set aside $3.5 billion in operating reserves and retire $1.9 billion of operating debt in 2015-2016. Under current assumptions, the state's operating debt will be completely eliminated by 2017-2018.

While the state has made significant strides on the path to economic recovery, significant expenditure obligations and risks persist. The state is challenged by long term debts, deferrals, and budgetary obligations in excess of $200 billion, according to estimates by the Department of Finance. Examples of these obligations include health and pension obligations for state employees and teachers and deferred maintenance. While the state's economy is steadily growing, capital gains taxes make up a significant portion of the state budget revenue picture and because this revenue source is highly volatile it can dramatically swing from one year to the next.

If the state's economic recovery continues, revenues could grow between three and five percent per year through 2017-2018, but slow to one percent in 2018-2019, according to projections by the Department of Finance. The outlook over the next three fiscal years ranges from continued constraint to some level of opportunity.

The Governor's Multi-Year Funding Plan for CSU

In January 2013, Governor Brown's budget proposal included a multi-year plan to provide funding stability to CSU and the University of California (UC). This plan calls for state funding increases to the two universities totaling $511 million each over the course of four years, culminating with the 2016-2017 fiscal year. Recognizing that both CSU and UC endured state funding reductions in equal dollar amounts during the recent fiscal crisis and that an ongoing investment in the university systems is important to the vitality of the state's economy and people, the governor's administration has since added additional years and new permanent funding commitments to the plan. The cumulative, potential increase occurs in annual increments as follows (actual funding provided by the state noted in parenthesis):

- $125.1 million in 2013-2014 (provided by the state)
- $142.2 million in 2014-2015 (provided by the state)
- $119.5 million in 2015-2016 ($216.5 million provided by the state)
- $139.4 million in 2016-2017
- $155.4 million in 2017-2018
- $134.6 million in 2018-2019
- Cumulative, potential increase in funding = $816.2 million

Although the legislature never formally adopted this multi-year plan, it did approve the first and second year increases of $125.1 million and $142.2 million, and with the governor's consent went above and beyond in 2015-2016 to fully fund the CSU support budget request of $216.5 million. If the increases through 2018-2019 remain at the actual and proposed levels, the new six year total would be $913.2 million. This is very close, but still shy of the cuts totaling approximately one billion dollars from 2008-2009 through 2011-2012.

One tenant of the governor's multi-year funding plan is that the universities not increase tuition between 2013-2014 and 2016-2017. CSU's support budget is dependent on two revenue sources: state general fund and tuition revenue. Each makes up approximately half of the support budget. With the governor's multi-year plan, the CSU has limited opportunities to expand enrollment, fund compensation increases or make larger steps toward removing bottlenecks and improving student success outcomes after accounting for inflationary increases and growing mandatory cost obligations.

The State's Funding Plan Does Not Meet CSU's Needs for 2016-2017

In 2015-2016, the state fully funded the CSU support budget request for the first time since 2006-2007. This preliminary 2016-2017 proposed budget plan will allow the CSU to meet its mandatory cost obligations, fund compensation and grow systemwide student enrollment three percent, while also dedicating funds to student success and completion priorities. Additionally, significant progress can be made on infrastructure and deferred maintenance needs. The estimated $2.5 billion backlog of deferred maintenance and critical infrastructure projects continues to grow and will continue to require additional funds in each state budget to deliver the type of infrastructure that our campuses need in order to offer the best possible student experience. The governor's multi-year funding plan would provide a $139.4 million increase in 2016-2017, which is only enough to fund the minimum cost increases required by the CSU and allow for modest enrollment growth of one percent.

2016-2017 CSU Support Budget—Preliminary Planning Approach

In this agenda item we share with the board a preliminary plan for the crafting of a support budget request for 2016-2017. The planning approach represents a credible statement of the university's key funding needs. At this planning stage, it is important for the board to provide input on its fiscal policy priorities for 2016-2017.

The preliminary incremental budget request and expenditure plan is summarized below. At this point, these estimated amounts are approximate and would add to our 2015-2016 base budget of just over $5 billion.

Proposed Incremental Increase in Expenditures:

• Mandatory Costs (health benefits, pensions, & new space maintenance)	$46.0	million
• 2% Compensation Pool	$68.0	million
• 3% Funded Enrollment Growth	$106.0	million
• Student Success and Completion Initiatives	$50.0	million
• Facilities and Infrastructure Needs	$25.0	million
Total Ongoing Expenditure Increase	**$295.0**	**million**

Sources of New Revenue

• General Fund Revenue from Governor's Multi-Year Plan	$124.4	million
• Middle Class Scholarship Redirected Funds	$15.0	million
• Net Tuition from 3% Funded Enrollment Growth	$54.6	million
• **Preliminary Board of Trustees Additional Request**	**$101.0**	**million**
Total Additional Revenue Needed	**$295.0**	**million**

Mandatory Costs

Mandatory costs are costs that have already been determined by state law, CSU policy, and operational needs. At this point in time, there is little to no discretion over these costs.

Compensation Pool

The compensation pool is based on the current agreements reached through the collective bargaining process. The multi-year impact of these agreements is to provide three percent in 2014-2015, and two percent in 2015-2016 and 2016-2017. This item would conditionally commit $68 million to the compensation pool, pending final agreements.

Funded Enrollment Costs

There is strong current and future demand for a CSU education. Between 22,000 and 32,000 students each year have been denied access during the fall admission cycles between 2010 and 2014 because the university did not have sufficient financial resources from the state to admit these students and provide them with a quality education. In terms of the future, it is anticipated that demand for a CSU education will likely grow due to enrollment funding provided to the California Community Colleges. Specifically, the community colleges received new enrollment funding equivalent to 30,000 additional full-time equivalent students (FTES), or 60,000 headcount, in the 2014-2015 and 2015-2016 state budgets. The CSU may begin to see an increase in applicants from these cohorts of community college students seeking to complete their degrees at the CSU. Access to education and the preparation of the state's future workforce depends on the state investing in the CSU.

The proposed expenditure plan to support enrollment represents a three percent increase in FTES, or approximately 10,700 FTES. This increase would allow for growth in the number of students admitted and served, as well as accommodate existing demand by current students for additional courses (allowing improved time-to-degree), and for some campuses to consider a move back to a state-supported summer term. The costs of accommodating additional enrollment are covered by additional tuition revenue from new students and state general fund. For planning purposes, a one percent increase in enrollment would cost approximately $35.5 million and would provide access to approximately 3,560 FTES or 4,300 new students.

Student Success Completion Initiatives

The CSU will continue to invest in people, programs, and strategies which facilitate degree completion and student success. Complementing the objectives of the graduation initiative, resources will support tenure-track faculty hiring, enhancements to academic and career advising, reduction of bottlenecks to student academic progress, programs which improve student academic preparation, and expansion of high-impact practices which strongly correlate with retention. The categories of costs associated with these investments are as varied as the initiatives themselves, but at their core, these initiatives require professional staff and faculty with the expertise to teach, research, advise, implement, program, counsel, coordinate, and analyze the many facets of these initiatives. For planning purposes, we estimate a salary and benefit cost of $100,000 per faculty and $75,000 per staff. As a result, $50 million would allow each campus the opportunity to hire between 20 and 25 new faculty and staff to support campus-based student success and completion initiatives.

Facilities and Infrastructure Needs

The CSU's backlog of facilities maintenance and infrastructure needs is massive and growing. Even with the state statutorily changing the way it handles CSU academic-related infrastructure needs by providing the CSU with the autonomy to self-determine CSU's capital program, the state will need to provide additional revenue for the CSU to aggressively capitalize on the new program. The CSU will receive $35 million per year to finance the university's most pressing renewal projects from the 2014-2015 and 2015-2016 capital outlay budget. While this is in addition to a one-time $25 million state appropriation for deferred maintenance projects also in 2015-2016, this commitment of funds is far from adequate to halt the growth of the CSU's $2.5 billion deferred maintenance backlog. Roughly $150 million per year is needed to keep up with our aging infrastructure; this amount does not include reducing the backlog.

Agenda item 2 of the September 8-9, 2015 meeting of the Committee on Campus Planning, Buildings and Grounds, Approval of the Draft 2016-2017 Capital Outlay Program and the Draft 2016-2017 to 2020-2021 Five-Year Capital Improvement Plan, includes the draft priority list (Attachment B) for the 2016-2017 capital outlay program. The list prioritizes critical infrastructure and utility renewal projects in addition to other academic program needs that would be financed using the 2016-2017 support budget requested amount of $25 million. The CSU is separately requesting $50 million from the state to further address the deferred maintenance backlog and $90 million of cap and trade funds to implement greenhouse gas and energy reduction projects.

Preliminary Revenue Plan

The preliminary expenditure plan continues to addresses many of the CSU's educational and operational needs. But if required to do so, it would be exceedingly difficult for the CSU to operate within the confines of the governor's multi-year funding plan. Increased mandatory costs and compensation pool costs together would consume approximately $114 million of the $139.4 million available from the governor's multi-year funding plan. With the addition of $18 million from tuition revenue associated with a one percent enrollment growth, this leaves approximately $43 million to address enrollment, student success, and facilities. For illustration purposes, if the remaining $43 million were spread evenly among the remaining items, CSU would be able to serve 3,560 new FTES, hire two to three student success and completion-related faculty or staff per campus, and finance approximately $45 million of facility and infrastructure needs. This scenario would do very little to serve prospective and current student needs and would only marginally address the deferred maintenance and critical infrastructure backlog.

At this preliminary stage, the planning effort focuses on stating the CSU's needs and being positioned for opportunity. Accounting for enrollment growth revenue and the governor's funding commitment of $139.4 million, these recommended items would require additional new ongoing revenues from state and/or tuition revenue sources of roughly $155.6 million.

Conclusion

This is an information item, presenting a preliminary framework for the 2016-2017 CSU Support Budget request to the governor and the Department of Finance. Estimated amounts for each item on the above lists may be revised, based on updated information, in the course of preparing the budget for the board's review and approval. The board will be presented with an updated and detailed support budget recommendation in November 2015 as an action item.