

Draft  
FINANCE REPORT  
05/03/16

## Overview of District Fiscal Condition

Three of the last four years, MPC has spent more than it received in unrestricted general fund revenues. The shortfall has been covered from one-time funds, primarily from transfers into the unrestricted general fund from the self-insurance fund and one time revenues from the state. The budget for 2015-16 also reflects a structural deficit but a lesser amount than the preceding year. While the 2014-15 budget reflected a deficit, the actual results were slightly positive due to savings accruing during the fiscal year.

The district has implemented some cost reductions but not at a rate to match revenue losses. The main reason for revenue loss is a decline in the district's ability to generate funded FTES.

While MPC may be able to employ a similar strategy of drawing down one-time funds for another year, the need to develop a plan to address the issue by producing new revenue, reducing expenses and becoming more efficient is now very important and more urgent. Our report is focused on long-term solutions, not just temporary fixes.

It should be noted that the district's fiscal condition is a symptom of greater underlying problems. It is not causal but rather an outcome of other actions or inactions.

A report from early 2009 titled "Long Term Financial Plan" cited many of the same issues. Since that report was issued, the situation has worsened because of the additional decline in FTES. A primary cause of that decline was because the college had built its operations on repeated enrollments in lifelong learning that the state subsequently disallowed. However, it is not clear if there has been a corresponding decrease in expenditures in these areas. Furthermore, when the State also ended funding for non-credit courses like PFIT (physical fitness offered in private gyms in the community), MPC experienced another drastic loss in enrollment and proportional funding.

MPC does not have in place any fiscal planning or monitoring tools to aid in the important decision making regarding the college's direction. Tools such as these are required for any long-term planning to have value.

## Fiscal Operations

MPC has enjoyed staff stability in key positions related to its fiscal operations, where day-to-day transactions are managed and reporting takes place. The last three audit reports have not

identified any negative audit findings regarding the fiscal operation. The areas of weakness reside in fiscal planning, monitoring and decision making.

## Fiscal Planning and Monitoring

MPC prepares an annual budget as required by law. The budget document contains a wealth of good and useful information. While this is true, the document can be intimidating to a casual reader. Further, there is not any anticipation of events beyond the current budget year. Most organizations can survive a given bad year, but community colleges are not funded sufficiently to do so for consecutive years without some understanding of the circumstances and advance planning.

There is a structured budget development process outlined in the tentative 2015-16 budget. It seems to be centered on the college council and its ancillary committees. It is not clear from the flow chart who makes the key decisions on major budget direction. We are aware that the college council itself recognized there were some issues with the process and are working with a CBT consultant to resolve this concern.

There does not appear to be an FTES strategy in place, and further, those responsible for fiscal planning are not actively involved in FTES planning which is directly linked to budget planning.

CBT has provided a tool set of worksheets and documents to help address budget and FTES planning.

- **The first tool is a high level 3-year budget planning and modeling worksheet**

The K-12 system is required to prepare such a model. There is no such requirement for community colleges. This is the key element to sound fiscal planning. Not having this tool in place is like driving on a winding, narrow mountain road in the dark without any headlights. The 3-year model helps the district see what is ahead and how to deal with it. It does not solve problems but helps identify them; and then, as solutions are proposed, reflect the impact of those solutions.

As identified in the proposal. CBT has worked with the college to prepare a 3 year budget model using the template provided by CBT. That model is included as an appendix to this report.

What the model illustrates is how rapidly the district budget deficit grows and consumes the remaining fund balance absent any corrective action. CBT has identified a number of recommendations which help address this problem. It is not clear if the district will be able to act quickly enough to realize the benefit of those recommendations before the reserves are exhausted and at which time the budget could still be in a deficit spending pattern.

- **A sample budget narrative, along with 9 companion schedules that distill the complex issues in the budget into an easy-to-read format that help to convey the back story of the budget numbers and foster confidence in the data, its source and integrity.**

The focus of this set of documents is to provide, in just a few pages, information that will clearly demonstrate the district's fiscal condition and identify key issues. Also, by documenting the changes from the prior year's adoption budget to the new-year's budget, one can see what is different and why. Another important schedule that is included is a listing of inter-fund transfers. There have been questions raised within the district about what is really going on with these transfers and including a schedule listing those affecting the unrestricted general fund will provide some clarity on that issue.

- **CBT has provided a sample current year revenue/expenditure projection modeling tool to help fiscal staff better evaluate current year actual performance against budgeted numbers.**

The budget is only a roadmap. The actual outcome may differ, and it is important to monitor performance of the budget throughout the year. If trends are developing or anomalies occurring, this tool can help spot them earlier and provide time to take any corrective action needed. This tool should be relatively easy to implement in that the district does prepare an expenditure/revenue worksheet, but it is lacking the elements that make it useful for planning and decision making.

- **CBT has provided a sample 3-year FTES modeling spreadsheet. It helps focus attention on the impact of current FTES decisions on the next two years.**

It directs attention to key questions such as, what are the FTES targets, are there adequate resources budgeted to achieve those targets and what are the backup plans if needed?

This spreadsheet should be viewed as a companion to the 3-year budget model. FTES planning and strategies should be a major focus for administration and college leadership. In terms of implementation, action steps and monitoring success, it is important for the instructional and fiscal divisions to work together and stay in constant communication.

Enrollment management will be discussed in greater detail in a separate section of this report.

**Recommendation:** MPC should utilize the tools provided to aid in better fiscal planning and management of district resources.

**Recommendation:** Non-mandatory spending increases to the budget should be very limited until the district has shown real progress in closing the deficit and maintaining reserves sufficient to sustain the budget during this period.

**Recommendation:** FTES planning should be made the joint responsibility of the instructional and fiscal administrative staff.

**Recommendation:** Budget roles of committees and administration should be redefined to establish true responsibility and accountability. (Note: Based on work of MPC group representatives with Eva Conrad of CBT, real progress is already being made on this recommendation)

## Peer District Comparisons

Four districts were selected for comparison with MPC. There is not a direct correlation from such an analysis but rather an opportunity to see where there are similarities and dis-similarities. These are only indicators which provide an opportunity to explore why and how they exist.

The districts selected were Hartnell, Gavilan, Imperial and San Luis Obispo (Cuesta). These were chosen because they seem to have more characteristics in common with MPC than others. They are close in FTES size, located in similar geographic and demographic settings, single college districts being the primary provider of community college instruction in their general service area.

Every year, each district must report data to the state regarding the year just ended and the budget year just begun. The data format is prescribed by the State, so it is not always in the form best suited for peer-level comparisons. For instance, our focus in the review of MPC is upon the unrestricted general fund. Much of the data is a blend of the unrestricted and restricted general fund activities. The analysis is affected by the degree a district has more or fewer restricted general fund activities. Unfortunately, that is not discernable from a number of the State reports.

Further, some of the issues for which we were seeking information could only be obtained through direct inquiry of the districts themselves. Because their responses would be voluntary and require some effort on their part, we limited our questions in hopes of obtaining their assistance. We were very fortunate when we reached out to the four districts to receive affirmative responses from each.

Below we have recapped some of the responses from the districts and listed the same information for MPC. A complete table is included in another section of this report. Further, we were able to obtain some summary-level information from the State Chancellor's Office for the unrestricted general fund which is also included.

## Summary of Peer District Responses to Inquiries by CBT

(N/A indicates no useful response)

	<u>Monterey</u>	<u>Gavilan</u>	<u>Cuesta</u>	<u>Hartnell</u>	<u>Imperial</u>
Classroom Productivity (FTES per FTEF)	14.2 or 13.0*	N/A	13.31	16.93	15.78
Release Time FTEF	18	2	14.8	2.0 est	9.42
Deficit Spending	Yes	No	No	No	No
FTES Borrowing	Yes	Yes	Yes	No	Yes
Stability Anticipated	Yes	No	Yes	No	Yes
<b>2014-15 Reported FTES</b>					
Non-credit basic	397	519	78	15	36
Non-credit enhanced	128	21	165	0	15
Credit	5,984	4,724	6,833	7,179	6,814
Non-resident	173	68	175	66	54
Total FTES	6,682	5,332	7,251	7,260	6,919

\*The first number is without release time faculty and the second includes that FTEF. For MPC, the spring 2016 data shows productivity of 13.5 and 12.3.

Both Cuesta and Imperial are borrowing almost all of their summer FTES. Cuesta anticipates it will be in stability in 2016-17. Imperial did not identify a specific timeframe for entering stability.

### Observations:

- Of the districts listed above, the largest and smallest (Hartnell and Gavilan) appear to be the most stable financially. Part of the reason is related to maintaining their funded FTES. Further, Hartnell has better productivity; and almost all of its FTES is credit which means it is worth more in terms of state funding.
- Gavilan has a substantial amount of basic non-credit FTES but at the same time less release time. In fact, as noted below, Gavilan generated the largest surplus of the comparison districts for 2014-15.
- Cuesta and Imperial are not in as difficult a place as MPC but may be headed for some fiscal challenges in the near term.

- MPC utilizes more release time than any of the peer districts by a wide margin.
- MPC’s classroom productivity ranks at or near the bottom of the comparison group

The summary-level data for actual unrestricted general fund results for 2014-15 are listed below. In order to make the comparisons consistent, we used all FTES since all types produce revenue, even though the funding rates per FTES differ. Other forms of revenue are earned by each district such as lottery, non-resident tuition, rental fees, etc. Those too are available to support expenses and included in the revenue total.

Costs are not identified by FTES type, which supports the notion of measuring total real revenue, total FTES and total expenditures.

Since the transfer of funds into the general fund are not true revenues, they have been excluded. Likewise, expenditures associated with student financial aid, capital projects and transfers out (expenditures normally captured in the 7000 account series) have also been excluded. The 7000 accounts can vary widely and are not considered part of the general operation.

For MPC, 2014-15 was a break in the deficit spending trend of the prior 3 years. The budget for 2014-15 anticipated a deficit; but as a result of savings during the year, that deficit was offset. The 2015-16 budget was balanced using one-time funds, which means the 2016-17 budget will start off with that shortfall.

The 3-year budget model suggests a rapidly growing deficit due to a forecast of very little new revenue, while costs are increasing based on existing obligations.

CCSF 311 Unrestricted General Fund Summary Data 2014-15 Actual Results

	<u>Monterey</u>	<u>Gavilan</u>	<u>Cuesta</u>	<u>Hartnell</u>	<u>Imperial</u>
Total FTES	6,682	5,332	7,251	7,260	6,919
Real Revenue	\$36,585,802	\$30,175,048	\$48,465,291	\$39,828,084	\$37,293,287
(excludes transfers in)					
<b>Rev per FTES</b>	<b>\$5,475.28</b>	<b>\$5,659.24</b>	<b>\$6,683.9</b>	<b>\$5,485.96</b>	<b>\$5,389.98</b>
Expenditures	\$36,330,317	\$28,234,919	\$47,500,674	\$38,816,921	\$35,513,299
(1000-6000 accts)					
<b>Costs per FTE</b>	<b>\$5,437.04</b>	<b>\$5,295.37</b>	<b>\$6,550.91</b>	<b>\$5,346.68</b>	<b>\$5,132.72</b>
Surplus	\$255,485	\$1,940,129	\$964,617	\$1,011,163	\$1,779,988
(before transfers out)					

## Observations:

- MPC's revenue per FTES is the second lowest and its expenses are the second highest.
- MPC appears to have experienced an enrollment decline (as described on page 1) unlike the comparison districts.
- Each of the 4 comparison districts produced a much higher positive surplus than did MPC.
- Each \$100 of cost per FTES for MPC equates to \$668,000; so when comparing costs with Gavilan, for instance, MPC would need to lower expenses by \$946,000 to achieve the same cost per FTES.
- None of the other 4 districts have experienced the magnitude of decline in funded FTES as MPC.
- If you were just looking at 2014-15 in isolation, MPC does not look too far out of line with its peers. It is when the district models out its budget over several years that the impact of MPC's fiscal status comes into focus.

## Specific Matters of Note

Our report does not address every possible issue affecting the district but rather seeks to find those most needing attention and having the greatest potential for improvement and long-term benefit to the district. From our conversations with various people within the organization, many of the matters noted are understood to some degree already. In the comments and recommendations that follow, CBT is providing an external, objective view of what we see and the types of adjustments needed. Ultimately, it is up to MPC to accept, modify or reject our recommendations.

Before discussing those, we should note that we did ask about areas which often cause financial problems for community colleges:

- Long term debt—the only item of note being the retirement health benefits which we will address in this report.
- Subsidy of categorical programs from the unrestricted general fund—the district has already moved to eliminate most of these.
- Off-site centers and locations—from the information received, these do not appear to be a drain on resource but rather an opportunity for the future stability of the college.

Prior to beginning actual field work, the CBT proposal identified general areas of exploration. Once in the field, it is very often the case that the emphasis changes from that which was anticipated as information is gathered and a better understanding of the district is obtained. That is the case with MPC. Items discussed below were deemed to be most significant to the fiscal health of the district.

Based on the 3-year budget model, MPC needs to take specific steps to bring its budget back into balance. The items that follow are consistent with that goal. To the degree CBT recommendations are not accepted or actionable, other options will need to be developed.

Unless there is substantial improvement in state funding not linked to FTES production, the district must focus on cost containment and efficiencies.

### Faculty Obligation Number (FON)

MPC is a member of the South Bay Regional Public Safety JPA. To our knowledge, it is the only instructionally based joint powers agency in the state. By its very nature of being a JPA, it is distinct from Instructional Service Agreements (ISAs) which also generate state-supported FTES.

The JPA was created for the public benefit. It was intended to bring together community college districts engaged in providing public safety training in a more efficient and responsive manner.

MPC produces about 655 credit FTES through the JPA. The structure of the JPA and the way public safety training is delivered precludes the members from utilizing full-time regular faculty for FTES produced through the JPA.

MPC has approximately 6,032 credit FTES for which it is funded and upon which its FON is based. Since MPC receives almost 11% of its credit FTES through the JPA and cannot employ contract faculty, it means MPC is at a distinct disadvantage in FON compliance. The cost of FTES produced via the JPA for MPC is not inexpensive in that 60% of each apportionment dollar goes to supporting the JPA. To expend that and then be required to maintain a FON which includes the JPA generated FTES is burdensome to a small district with 11% of its credit FTES coming through the JPA.

CBT believes that the district could make a strong case to the State Chancellor's Office for an exemption or allowance that either reduces its FON or gives credit for the equivalent FON associated with the JPA. The district should not be penalized for doing a good thing.

There is some precedent for recognizing unique or unfair circumstances in funding issues related to community colleges. For instance, when colleges change the instructional calendar to have in-service days, there is a factor applied to FTES to make the district whole. The 50% law calculation allows for adjustments related to lottery revenues and capital expenditures. The way in which ISA costs are allocated was amended to fairly capture the instructional component. When the current funding model was established, a unique funding accommodation was made for very small districts. There are other examples which could be cited, but these are included to identify a basis on which such an adjustment could be made.

**Recommendation:** MPC should seek to have its FON calculation amended to account for the impact of the JPA generated FTES.

### True Funded FTES Decline

MPC has experienced true decline in funded FTES 3 out of the last 4 years. It is important to know how decline, stabilization and restoration work to really understand what this means. In



the year of decline, when a district drops below its established funded base (excluding growth), then it receives stabilization funding as if the district at least maintained its base. Call that year 0. Starting at year 1, the district **loses** all of that decline-related revenue but has years 1, 2 and 3 to gain it back. Any amount restored is added back to the district's revenue. Any FTES lost in year 0 and not restored by the end of year 3 is forever lost to the district.

The only way to gain FTES at that point is through the normal growth mechanism, which has no correlation to the amount of FTES lost. Back in the 90s, some districts experienced large true declines in FTES and had such low growth rates through the state formula that it took many years to earn their way back to the starting point.

During the restoration period, that FTES subject to recovery is only available to the affected district; so it is important to understand the implications of not being able to recover it.

#### MPC's Experience

- In 2011-12, the district lost 289 FTES valued at \$1,387,840. This was in addition to the take away from all districts imposed by the state that year, which for MPC was 587 FTES valued at \$2,603,302. Districts did have an opportunity to restore the state imposed FTES reductions, but it appears that MPC was not able to do so. Further, of the remaining 289 FTES decline, MPC was only able to restore 40. The balance expired after the 3-year window closed. The district lost the opportunity to restore the state imposed FTES (\$2,603,302) and the local decline in FTES (\$1,296,425).
- In 2012-13, there was no further decline in funded base FTES
- In 2013-14, MPC declined another 358 FTES valued at \$1,251,953 (Year 0) none of which was restored in 2014-15 (Year 1); and it is not expected that any will be restored in 2015-16 (Year 2). That leaves only one more year of opportunity before that too is forever gone.
- In 2014-15, MPC declined another 21 FTES valued at \$27,927 (Year 0)
- For 2015-16, we do not yet know what the final funded FTES numbers will be.

Given the trend, and without some new direction, it is quite possible that the district will lose the opportunity to restore any of the FTES revenue described above. That would mean that MPC has gone from a funded base of 7,682 FTES at the start of 2011-12 to an on-going base of about 6,503 FTES. This is a decline of 1,179 FTES or 15.3%. If, for example, MPC had a state approved growth rate of 1.25%, and assuming that MPC could grow back at this rate over time, it would take 12 years to get back to 7,600 FTES. One can see the very long-term implications of what some might see as a short term circumstance.

It should be noted that the district's funded FTES was as high as 8,700 in 2002-03 and over 8,500 in 2008-09 making the decline even longer and deeper. CBT has focused on the more recent events in our analysis.

**The district is faced with the reality of being a 6,500 FTES level college and the need to adjust its thinking and spending to reflect that.**

It is not clear that the decline is over. A number of actions taken by the district to shore up FTES may not be sustainable or make for a strong instructional program. One can see from the discussion above that halting the decline, while at the same time making sound longer term program decisions, is vital to the fiscal health of the district.

CBT will identify a short term FTES strategy later in this report.

### Enterprise Resource Planning (ERP) Systems

MPC utilizes the Santa Rosa system for its administrative support applications. The administration has advised us that it will no longer be supported after this year and that the college will basically be on its own. Further, it was indicated to CBT that much of data collection is prepared manually and there is not any integration of the various functional areas. There is a dearth of good and timely data which has hampered the district's ability to assess its circumstances and develop responses. Further, student and public expectations for electronic access, data and support are not being met with the current system. Shoring up the current system with patches or third party add-ons is a poor use of resources and provides no real resolution.

The district began a process in 2012 using IT specialists to evaluate and migrate to a new ERP system and is aware of the need to do so, but progress has been quite limited. It has stalled due to staff turnover but also delays as a result of the expanded involvement of the college council in administrative functions.

The district has a residual of about \$8 million in bond funds. There are more demands than there are funds which is very typical. It is not clear that the district has established funding to complete a transition to a new ERP.

**Recommendation:** MPC should make this a very high priority and firmly commit resources, bond or other one-time funds, to the completion of this transition. It is further recommended that a timeline be established and periodic reports to the board be made including any reasons for delay in meeting the timeline. The short-term FTES recommendation from CBT identifies a source of funds that could be applied to this endeavor.

**Recommendation:** The move to a new ERP is a major undertaking and can take several years to fully implement. It takes a great deal of staff time, is costly and needs a great deal of coordination. Many of those who will be responsible for making all of the individual components work do not have experience with such an implementation. MPC should consider, as it plans for this transition, the inclusion of on-site project management for some period of time from the successful vendor or a firm familiar with the vendor. This can help keep the project on schedule, avoid costly mistakes and make for a better integration of the various modules.

## Other Post-Employment Benefits (OPEB)

MPC offers post-employment health coverage to qualifying employees. This benefit has been modified from time-to-time through the negotiation process but remains in place for all new hires. While the total actuarial liability is not large compared with many other community college districts, the fact that it is an open active benefit means that the liability will never end and most likely will grow due to longevity of retirees and increasing medical costs.

The modifications mentioned above affect how employees meet the qualifications for the benefit. Further, several of the adjustments carved out groups based on hire dates so that determining qualifying status can get a bit difficult. Retirees and eligible dependents are covered in the plan.

MPC is self-insured for its health benefits which makes this issue even more complicated. Retirees over 65 have limited district paid self-assessed premiums but can pay the district the remaining calculated premium and continue to receive coverage.

The district has set aside funds in its self-insurance fund toward the unfunded portion of its actuarially calculated liability. From time to time, the district adds to this balance but not in a structured way. The funds recently have been moved into an irrevocable trust.

There are three different elements to this arrangement we will address: OPEB funding strategy, the open OPEB plan and the operation of the health plan related to retirees.

### OPEB Funding Strategy and Open OPEB Plan

Given that new employees can still qualify for the retirement health plan, the OPEB liability will never end. The 2014 actuarial report outlines a plan to fund the currently defined liability over the next 23 to 30 years. Most districts, when presented with this same type of plan, find they cannot meet the plan requirements. MPC, like many others, makes an attempt to set aside some funds toward the obligation; but this does not constitute a real plan.

What are the funds being aside intended to do?

When will the funds be applied?

For what and how will the OPEB funds be used?

Again, MPC, like many other districts, has not addressed these questions. Given the open nature of the program, answering the questions is made even harder.

**Recommendation:** The district should seek to close the program to new hires. Many districts have done so once they had a greater awareness of the financial drain on resources.

MPC is facing a number of challenges as a result of permanent loss of funded FTES. It is important to gain as much control as possible over expenditures. Obligations to retirees are oblivious to the up and down state funding cycles or the size of the district. These benefits took less of the available resources when the district was larger. The obligation to retirees must be met and, as the district becomes smaller, this obligation takes a greater percentage of district

resources. Closing the OPEB window to new hires does not change the obligation to current employees. New hires will accept employment knowing what is or isn't provided. Many public employers have made this change, including the state of California.

Once closed, there are strategies available to help the district better address the questions noted above. The plan liability will have a life cycle that can be measured and monitored. The costs will escalate more slowly and will at some point begin to decline.

Given the sizable OPEB reserve, in comparison to the total liability, if the plan were closed, there is a strategy that can help manage the rate of increase in costs from the unrestricted general fund, meaning that more of the new revenues can go toward meeting operational needs.

### Retirees and the Health Plan

Union contract language defining the conditions under which employees qualify for retirement health benefits is not easy to understand. There are various conditions and benefits available based on several key hire dates. Those hired before July 1, 1999, those hired between July 1, 1999, and June 23, 2004, and those hired after June 23, 2004. These dates trigger different levels of benefits and are linked to early retirement before age 65. Some of the differences are subtle; others a bit more substantive. It makes administering the plan more challenging and subject to error. At the time, the district and unions may well have had good intentions; but over time, as the changes were layered on top of each other, it became more complicated.

Data provided by the district regarding the health plan premiums and costs for the period of August 2014 through July 2015 indicates there were approximately 400 covered employees, retirees, and COBRA individuals. This does not include their dependents.

Out of the total 400, there were about 37 retirees under the age of 65 and 105 over the age of 65. The district assesses itself a premium for expected costs of claims, claims handling expenses and stop-loss insurance. The data indicates that active employees had a lower utilization than either of the two retiree groups. Actives were 84.07% costs versus assessed premium, retirees under 65 were 143% costs versus premium and over 65 retirees were 185% costs versus premium. The fact that retirees access the health plan more is to be expected given age-related conditions. What is important about this is that the district, in determining the self-assessed premium, is not recognizing the true cost of the retirees.

In the case of the over 65 group, this is significant because they pay the full premiums except for those retirees for whom the district pays \$125.55. It suggests that the district is in fact subsidizing this group beyond what is provided via contractual language.

Based on inquiries by CBT, it is not clear how closely the retirees' qualifying status is monitored or if premium payments are paid promptly and dependent status is confirmed.

**Recommendation:** MPC should evaluate its premium structure to better reflect the cost of retiree coverage, in particular those over age 65.

**Recommendation:** MPC should consider, in conjunction with closing the plan to new hires, smoothing out the differences between the pre-1999, 1999-2004 and post 2004 employees as means to bring clarity and simplicity to the plan. This might mean some small additional costs for the current qualifying employees; but if it is linked with the closing of the plan, may be in the best interests of all parties.

We do not propose specific actions to accomplish this since it is something that needs to be negotiated with the employee groups.

**Recommendation:** MPC should put in place procedures to monitor and confirm continued retiree qualifications for benefits, including dependents. It is further recommended that MPC have clear procedures for monitoring payment of premiums by retirees, protocols for follow up on missed payments and termination from coverage if warranted.

**Recommendation:** The district should confirm with its actuary the premium figures used in the actuarial study. Since the actual cost far exceeds the assessed premiums, it would be important to make sure the actuary is working with the best data in preparing the OPEB liability reports.

**Recommendation:** If the district is able to accomplish the above noted OPEB recommendations, then it would be further recommended that a specific analysis and true plan to address the OPEB questions posed by CBT be undertaken.

### Health Benefits and Plan

MPC is self-insured for health benefits both for active and retired employees and their dependents. This is unusual due to the small covered population. Insurance programs in the areas of health, workers compensation, property and liability are based on large numbers of participants or insured values.

MPC's model creates uncertainty and greater financial exposure when compared to more traditional health benefit programs.

As the district comes to grips with its FTES reality, gaining control over those aspects of spending having the most risk is an important strategy to consider. When evaluating options about issues that have significant financial implications, it is helpful to think in term of upside gain versus downside risk. In other words, if the reward is limited but the risk substantial, then the decision may not be the best one. On the other hand, if the reward is significant and the risk minimal, the choice is made easier. Another factor to consider in the risk/reward analysis is the district's ability to absorb a loss. If the fund balance is strong and the budget truly balanced, then the district would have a higher risk tolerance. Given its present circumstances, MPC has a low risk tolerance.

Applying this to the evaluation of health coverage options in light of the permanent financial loss due to FTES decline, the district may want to gain control over its exposure to uncontrolled costs. The present structure involves high risk and no reward in that its costs appear to be greater than others. This circumstance was also noted in the 2009 Long Term Financial Plan Report.

The district has, from time to time, pursued such options but without success. It is not clear if that was due to cost or lack of agreement with the employee unions. It is our understanding that inquiries into the health plan structure changes are again underway.

Given the inclusion of retirees in the plan and the growth in their numbers and related costs, the district's financial exposure is expanding as the district size is decreasing.

**Recommendation:** MPC, working with its unions and health plan experts, should seriously pursue changes that better define and limit the fiscal exposure and annual costs of the health benefits provided employees and retirees.

### Faculty Reassigned Time

MPC currently provides the equivalent of 18 FTE (full-time equivalent) faculty for various release time assignments. Based on total faculty regular FTEF, this equates to about 17%.

Release time serves an important purpose. It is often used for special, short-term projects. It makes sense and when the faculty expertise is relevant to the project is efficient. What happens in many districts, not just MPC, is that release time takes on a life of its own; and it is continued beyond the intended purpose, becoming institutionalized. In the case of MPC, this is even more evident due to contract language that embeds release time.

There are functions for which release time is expected and will be on-going, such as academic senate leadership, some grant activities and possibly union matters related to contract administration for grievances, negotiations, etc.

While the cost of release time is often measured based on the value of hourly replacements, there is another cost in terms of the primary role of full-time faculty in instruction and student counseling. With so much release time granted, MPC has a true detriment in its faculty ranks. The state has been working for years to increase the number of full-time faculty, and in the 2015-16 budget, allocated a sizable amount of funding for that purpose. The over application of release time assignments works against that objective and takes faculty away from their most important role.

At MPC, the hourly cost with benefits is around \$54 per hour. For a year based on a regular 15 unit load per semester that works out to roughly \$28,350 per FTE. Eighteen FTE release time would have an hourly equivalent cost of \$510,000. This is only the cost component. You cannot put a price tag on the programmatic impact of this much release time.

The faculty union contract allows for up to 7% of the faculty to be on sabbatical in any given year. It is our understanding that sabbaticals have not been granted for several years due to the district's budget problems.

If sabbaticals are granted, then that exacerbates the impact of release time, meaning the percentage of full-time faculty not in the classroom or counseling students could exceed 20% or, stated another way, 1 of every 5 faculty would not be available to students.

**Recommendation:** Release time should not be contractually guaranteed (other than for union contract administration) and should be evaluated annually based on a listing of release time needs, with approval by the college president and presentation as an informational item on a board agenda. It is assumed that the academic senate release time would be a perpetual item.

CBT understands this is a contractual matter and subject to the negotiation process. Our recommendation is focused on what is in the best interests of the institution and its students.

The division chairs are included in the counts above and detailed in the faculty union contract. CBT will speak to the administrative structural issues related to division chairs in a separate section of this report.

### Classroom Productivity

Classroom productivity is measured either in terms of weekly student contact hours (WSCH) per full-time equivalent faculty (FTEF) or by full-time equivalent students (FTES) per FTEF.

There is not a specific standard for classroom efficiency, but many districts use as a semester baseline of 525 WSCH per FTEF or 17.5 FTES per FTEF. If a district exceeds these, it is performing better and gaining efficiency. If it falls below the baseline, it makes the cost of instruction go up. The 525 is based on 5 sections, 3 contact hours and an average of 35 students per section which translates into 17.5 FTES.

Based on data provided to CBT, the district is operating around 14.2 FTES per FTEF, excluding contract and reassigned faculty. If reassigned time is included then the productivity drops to 13.0 FTES per FTEF. (However, as an added reference point, the spring, 2016 numbers were 13.5 and 12.3).

While the difference does not seem large, it is important to note this is for each full-time equivalent faculty number which is 189 without the reassigned time or 207 with it.

To simplify things, as we illustrate what the difference represents, we will use the 189 (FTEF) number and the fall, 2015 FTES per FTEF data.

Subtracting the MPC value of 14.2 FTES from the generally accepted baseline of 17.5 FTES per FTEF, the difference is 3.3 FTES. Multiplying 3.3 FTES by 189 FTEF equals 624 FTES. This is for a semester; so for the academic year, it would be twice that amount or 1,248 FTES.

The total MPC funded base FTES for 2015-16 is 6,500. As a percentage of that baseline, the 1,248 FTES is 19%. To the degree MPC can move closer to the 525 WSCH or 17.5 FTES targets, it becomes more efficient and saves costs. This can free up resources or, in the case of MPC's structural deficit, bring costs more into alignment with revenues.

Smaller colleges have fewer discretionary resources with which to work. For instance, there is a college president for a college of 6,500 FTES and there is similarly a college president for a

college of 25,000 FTES. The cost of a college president will come from revenues from 25,000 FTES or from 6,500 FTES.

There are a number of costs, like the example above, which take more resources for smaller colleges, leaving fewer discretionary funds, meaning improved productivity is very important to having a sustainable operation.

MPC has class cancellation language in its faculty union contract about minimum class sizes of 15. Apparently this means a class must not be cancelled if this number is reached. Such a rule works against the goal of greater efficiency.

**Recommendation:** MPC should adopt a goal of improving classroom productivity per semester to 525 WSCH/17.5 FTES. It is further recommended that specific benchmarks toward the goal be established and measurement of progress toward those benchmarks become part of the curriculum planning, class schedule development and job performance requirements of instructional managers.

The need to be more efficient is just one more element of coming to grips with being a smaller college. Cost containment is very necessary for the long-term financial health of the district, as evidenced by many of the CBT recommendations.

CBT has made a number of recommendations regarding enrollment management that will also help in reaching this objective.

To accomplish this may require hard decisions on which classes are offered, cancelled and when they are offered. Business as usual will not move the district forward. It is not clear that, given the current organizational structure, those decisions can or will be made.

### [CTA Contract Article 16.8: Salary Schedule Adjustments](#)

When first negotiated, the parties may have seen this methodology to increase the salary schedule as an objective way to allocate resources without having to continually negotiate compensation. They could not, however, have anticipated the most significant financial downturn ever experienced by California's community colleges. Further the internal dynamics of the district amplified the impact of the downturn through real decline in funded FTES over a period of years.

The economic factors noted above have exposed flaws in the concept and its application. It has created a circumstance whereby the district, as it tries to recover lost revenue due to declining FTES, is caused to increase the faculty salary schedules from funds that do not represent true revenue growth.

The process calls for a measurement in the change of state apportionment from what is known as P1 of the prior year to P1 of the current year. If there is an increase from one year to the next, then after specified cost items are addressed as noted in Article 16.8, the balance is applied to the various faculty salary schedules. CBT has noted the following problems related to this mechanism.



## The Use of P1 Data

P1 is an estimate and is considered soft data. It is a projection by the district of its expected FTES and by the State on what funds are anticipated to be available, most often expressed through the application of a deficit factor. There are typically 2 more valuations before the apportionment is considered final. Those are P2 which is provided in June of the current year and the final recalculation which occurs at P1 of the next year. So in simple terms, 8 months after the close of the fiscal year, the district finds out its final funding for the previous year.

There can be substantial changes from P1 to the Final.

It is our understanding that an MOU was approved in 2012 that modified this section, but we have not seen it nor do we know the exact rationale necessitating it. We have been told by the district that the MOU was temporary and no longer applicable.

There is another concern about the inclusion of all apportionment revenue. Since apportionment represents more than 92% of all unrestricted general fund revenues, the way in which Article 16.8 functions makes all increases of apportionment subject to inclusion. The remaining non-apportionment revenue increases only slightly, leaving almost no new income with which to apply to other district needs.

So while we have noted that P1 is not a good foundation, we are not suggesting that using either P2 or Recalculated Annual are appropriate either. The automatic application of new state revenues does not consider other major mitigating factors and severely limits the district's ability to respond to changing circumstances.

## Lack of Context

The methodology expressed in Article 16.8 isolates changes between two immediate points, last year and the current year. It does not take into account the longer view of related facts and circumstances. In the case of MPC, P1 data going back to the 2010-11 fiscal year reflected a computational apportionment of \$37,208,570. For 2015-16 it is expected to be \$35,187,067; yet because the change from the 2014-15 year figure of \$32,784,265 is positive, a salary schedule increase is triggered. The simplified table below helps illustrate this point.

### MPC P1 Apportionment Reports

Source: State Chancellor's Office

<u>Fiscal Year</u>	<u>2010-11</u>	<u>2014-15</u>	<u>2015-16</u>
After deficit factor	\$37,208,570	\$32,784,265	\$35,187,067

\*not all years included to simplify the illustration

Article 16.8 suggests that only the increase from 2014-15 to 2015-16 be considered, not taking into account the fact that the district is still trying to recover lost funding.

This can be further demonstrated with a scenario that, while not exactly the case, is not far from where the district finds itself now. Because of the stability/restoration process, the district could decline in year 0 receive stability funds, then in year 1 not restore but restore in year 2, Article 16.8 would only look at year 1 compared to year 2. This pattern could repeat itself a number of times so that looking 8 years out, the FTES has not changed but the salary schedule has been increased 3 times.

MPC is still trying to recover what was lost. It is not seeing real true new income. It should be noted that when revenues decline, the salary schedule is not reduced. At some point previously, the salary schedule was adjusted to reflect the increases associated with the 2010-11 revenue of \$37,208,570. As FTES declined and revenues were lost, the salary schedule was not affected.

When and if FTES is restored, the application of Article 16.8 does not take into account this reality; and with the way it is applied, salary schedule increases have been triggered during this period.

In addition to the problems with the mechanical application of the process, there is no recognition of the district's ability to pay or afford these salary adjustments. The assumption is that any new revenue flowing to the district via apportionment will have to pass through the gatekeeping of Article 16.8. The district has been deficit spending and drawing down reserves from various sources, yet that circumstance has no bearing on the application of this article.

It is unclear from where the district finds financial resources for other operational activities or compensation to other employee groups.

#### Lack of Incentive

The prescriptive nature of this article and its application provide little incentive for the district as a whole to work toward improving its financial condition. Other employee groups are left with little to negotiate over. The administration has little ability to begin new initiatives or increase the budget without first gaining approval through Article 16.8 or deficit spending.

As it stands now, the district, through the state apportionment process, still has time to restore lost FTES valued at about \$1.4 million; yet if it does so, it will not bring relief to the pattern of deficit spending but rather build in even more salary schedule enhancements that the district cannot sustain. We will address more fully below.

#### Broader Implications

In much the same way that the article is applied in a limited context there are implications on for the institution as a whole. Is a mechanism such as this in the best interests of students and the community? How are they benefited when the educational needs of those we serve are not considered? Is this really sound public policy?

Given the district's poor fiscal health and the need to take corrective action sooner rather than later, this article only adds to the challenge.

## Summary

Our comments on this topic are not an indictment of the faculty union. It was a bargained item which took agreement on the part of the district. It may have been well intended at the time but not fully understood. It was enacted at a time that did not anticipate the major changes awaiting the district.

CBT understands that it is up to the district and union to determine what action may be appropriate. From our perspective and review, it is an item that has become a barrier to the organization's ability to regain its fiscal equilibrium.

## Possible FTES Strategy

We have reviewed the District's 320 attendance reports for the last several years in an attempt to determine what the FTES strategy has been and options that may be available to the District. It does not appear that there was a real strategy based on the way in which summer FTES was applied.

CBT has identified a strategy that can accomplish more than one objective. We are, however, somewhat reluctant to fully recommend it, if it triggers an adjustment through Article 16.8. We say this because the strategy we are modeling generates funds which should be considered temporary, one step away from one-time in nature. To lock them in as salary schedule increases would not be wise and, if that was to be case, we would not recommend the strategy.

We have already discussed what permanent loss of funded FTES means to the District and how time is running out for restoration. In addition, CBT referenced the need to establish funding for the ERP migration. Our FTES strategy could address both of these points.

MPC has developed its budget based on funded FTES of 6,500. The District produces about that much on annual basis excluding the impact of summer borrowing. Summer FTES is running just over 600 per summer. Because of the summer borrowing pattern, MPC has been borrowing about 300 FTES from the next immediate summer session. For 15-16, you reported at P2 borrowing of 270 FTES from summer of 2016 leaving 330 FTES of summer 2016 to be reported in the 16-17 year. A portion of the remaining 330 FTES is not eligible for borrowing and must be reported in the 2016-17 year. The exact amount is not yet known because the 2016 summer session has not yet begun. Based on summer 2015 the additional FTES available for borrowing could be as low as 130 FTES. It could also be a bit higher.

### **Conditional Recommendation #1:**

1. For the 15-16 fiscal year, MPC borrow as much of the remaining 330 summer 2016 FTES as possible (based on recent district information the minimum would be 130 FTES) to capture funds available through restoration. The exact numbers are not yet known since there is still attendance data to be captured.

2. For the 16-17 year MPC would once again report a decline, so no summer borrowing, but receive stability funds
3. For the 17-18 MPC would be able to report the full 6,500 FTES it generates or could again begin borrowing to sustain the funding temporarily. Because this is further out on the timeline it is unclear if MPC can rebuild enrollment or end the slide in FTES.

This recommendation would produce approximately \$625,000 to \$800,000 more for 15-16 and the same amount would be there again in 16-17. Combined there could be up to \$1.6 million more than what the District has anticipated. Treating this as temporary funding, it could be put toward the implementation of the new ERP system or a resource to help address the anticipated budget deficits. Further, by employing this strategy, the district would start a new 3 year restoration period for FTES and then have more time to truly restore the lost FTES that is still in jeopardy of permanent elimination.

**Conditional Recommendation #2:**

There is a variation on Recommendation #1 that could yield better results however it is not without some risk. It has a lot to do with timing. We will explain further.

If MPC feels that in 16-17 it can produce actual FTES above the 6,500 or 6,480 as reported at P2, then applying the above noted strategy in 16-17 rather than 15-16 would be more beneficial. If MPC can only borrow 130 FTES from summer 2016 into 2015-16 and they can produce more FTES above 6500 in 2016-17, it would give them the opportunity to restore all (or more) of the available 358 FTES by choosing recommendation #2. If, however, there is a chance that the real FTES production for 16-17 could be less than 6,500, then it would be better to stay with Recommendation #1.

Because the district does not know what will happen in 16-17, the best way to approach this dilemma might be to wait until the last opportunity to re-file the 15-16 FTES report. This would give MPC some time to see the fall enrollments before making a decision. It comes down to a judgement call, but waiting awhile allows for better information upon which to act.

If the district feels confident now in terms of its 16-17 FTES and it decides to accept our recommendations regarding an FTES strategy, then it can choose now which course of action to pursue.