“Draft” Long-Range Financial Plan (Through FY07)
Lane Community College

SECTION I: HISTORY AND CURRENT ECONOMIC ENVIRONMENT

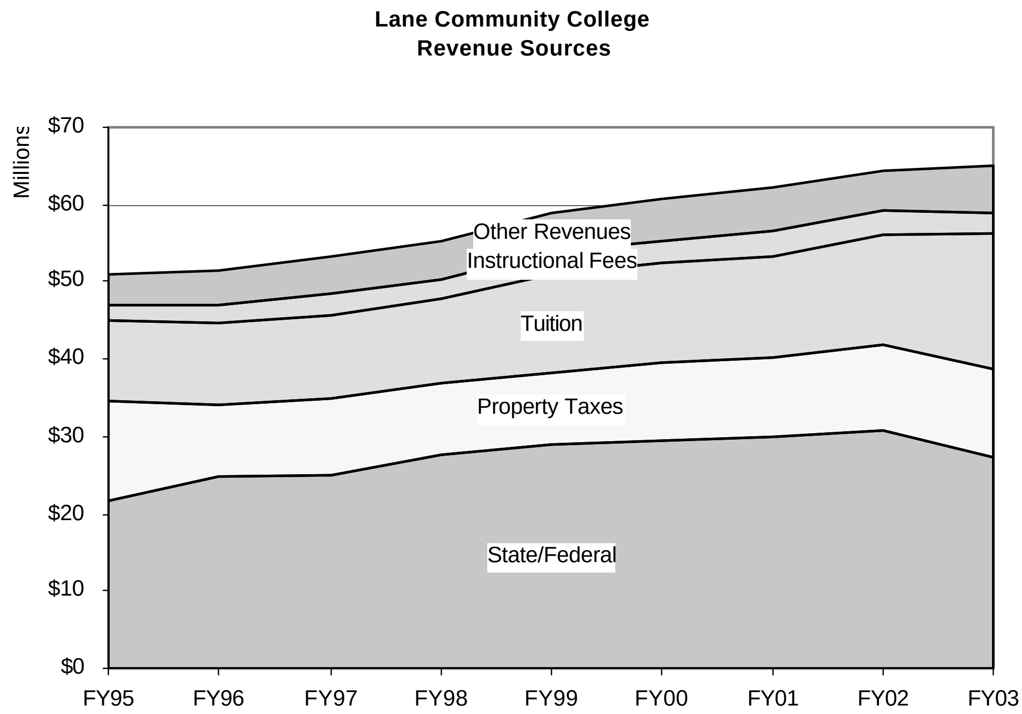
Lane Community College confronts challenges and opportunities, unique in its history, as it develops a strategic financial plan for the next three years. The economic environment is much more volatile than in 1990 when local property taxes provided 41% (versus 17% for FY 04) of our revenue. The passage of Ballot Measures 5 and 50 has made state funding our largest resource. In turn, the State of Oregon's largest revenue source, the income tax, is extremely sensitive to the economic conditions throughout the United States and larger world.

When the American economy went into recession after the financial markets' decline in 2001, Lane was immediately, adversely affected by the state's inability to sustain funding levels. To mitigate immediately necessary educational program reductions, Lane had to increase tuition paid by our students by 66% in the last three years. This substantial tuition increase has resulted in slightly reduced enrollment. Between 1996 and 2002 student FTE rose from 12,007 to 13,265, but has since declined 18% to a projected 10,880 for FY 2004. Since Lane County's population has actually grown 5.6% over the same eight year period, it appears that the college is not currently able to meet all potential learners' needs.

Lane's increasing reliance on state funding and the world economy has had other consequences. The college's share of state aid is determined by an agreed-upon community college funding formula which must balance the competing needs of: large and small community colleges; some districts growing student FTE rapidly and others not at all; some with rapidly growing local property values and others which are stagnant. As the economic characteristics and competing interests of individual community college districts change, Lane has to expect that its share of state funding will change, perhaps unexpectedly and substantially. As an employer, Lane was confronted with an unanticipated PERS liability in excess of $69 million when the financial markets rapidly declined in 2001. In long-range financial planning we need to consider strategies to address future contingencies, like the PERS liability, about which we have no present knowledge.

SECTION II: ASSUMPTIONS & PROJECTIONS

A. REVENUES



1. State Sources

   a) The projections for FY05 are based on the "new" funding distribution formula and include $10.7M allocated by the legislative emergency board for FY05. The new funding formula maintains a cap on enrollment. Base scenario projections for FY06 and FY07 are based on maintaining final revenue received from the state in FY04/FY05 plus an inflationary adjustment of 2%.

2. Local Property Taxes

   a) Property tax revenues are projected using statistical trend analysis based on historical data. The annual increase is approximately 3.5%. Property tax increases are capped by law.

3. Tuition

   a) Tuition revenues are projected based on enrollment projections developed by Institutional Research, Assessment & Planning. Tuition revenues include tuition generated by Fund IX instructional units.

   b) Base scenario projection of FY05 tuition revenue use rates adjusted for inflation using the Higher Education Price Index (HEPI) for 2003 (per Board

Policy D.110). For FY06 and beyond, future inflation adjustments use the average annual percentage increase in the HEPI since FY97.

c) $256,000 has been added to projections for differential pricing revenues in FY04. On full implementation of differential pricing in FY05, the revenues are increased to approximately $424,000. Revenues from differential pricing are increased by the same percentage as tuition increases for FY05 and beyond.

4. Instructional Fees

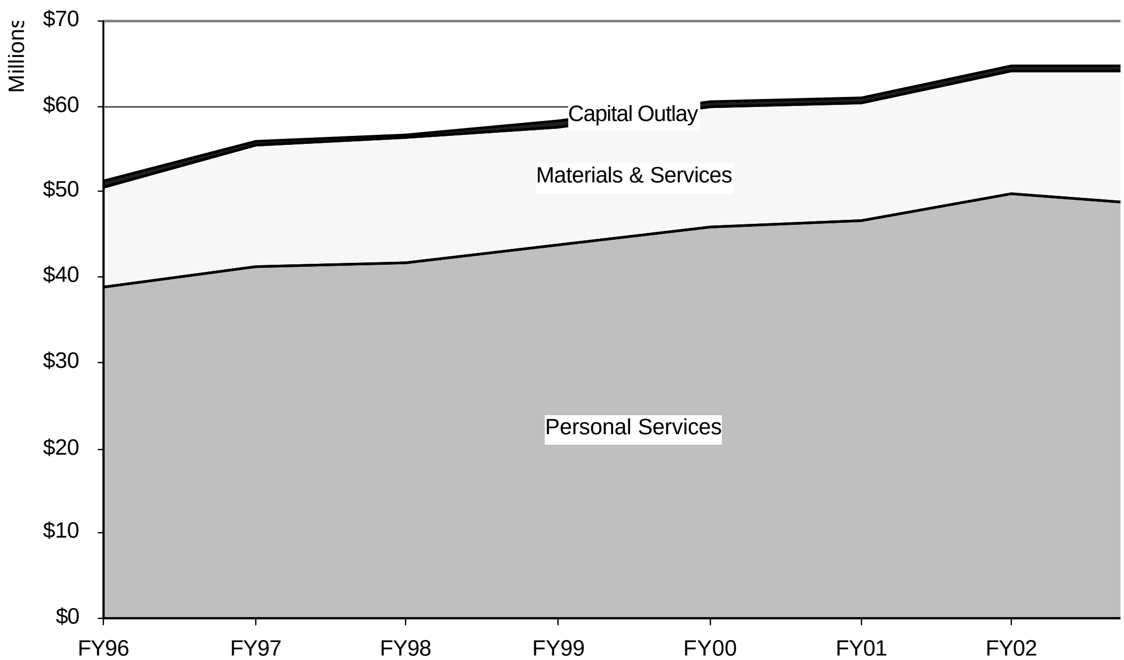
   a) Projections for instructional fees use predicted expenditures based on historical trend analysis. All instructional fees are administratively restricted revenue, i.e., fees are tied to specific direct instructional expenditures and are not available for general allocation.

5. Other Sources

   a) Other miscellaneous sources of revenue add up to approximately $6 million, $4.3 million of which is restricted for specific uses and not available for general allocation.

B. EXPENDITURES

Lane Community College
Expenditures by Object



1. Personal Services
   a) Personal Services expenditures for FY04 are based on actual position lists. Budgeted figures are used for part-time compensation projections in FY04. Personal Services expenditures for FY04 and beyond use "steps" plus estimated COLA increases each year.
   b) OPE rate is recalculated every year using projected costs of benefits. The calculated rates will vary with different scenarios based on estimated annual increase in health premium costs.

2. Materials & Services
   a) Projections use historical trend analysis to predict M&S expenditures

3. Capital Outlay
   a) Projections use historical trend analysis to predict Capital Outlay expenditures after FY04. Because spending on Capital Outlay was curtailed deliberately in FY02 and FY03, the FY04 projection for Capital Outlay has been adjusted upwards to compensate. In FY04, $200,000 recurring was added to Capital Outlay for equipment replacement. For FY05, FY06 and FY07 an additional $350,000 recurring is added each year to the projection based on needs identified in the most recent Capital Assets Replacement Forecast.

4. Contingency
   a) By Board Policy, the Unappropriated Ending Fund Balance (UEFB) is set at 3% of budgeted General Fund expenditures. According to Local Budget Law, the UEFB budgeted for the current year may not be expended except under extraordinary circumstances and therefore will be part of the total Ending Fund Balance and a resource for the ensuing year (Net Working Capital Unrestricted and part of the Beginning Fund Balance). On the projection spreadsheets, the UEFB amount is added back to the projected Ending Fund Balance as "Minimum Fund Balance (not available for appropriation)."

C. OTHER FINANCING SOURCES

1. Transfers In and Out are projected using historical trend analysis. Transfers in past years have been adjusted for one-time large transfers before the trend analysis is performed.

D. BEGINNING/ENDING FUND BALANCES (Net Working Capital)

1. The FY05 projections include $810,000 for "Deferred Maintenance Catch-up." FY06 and FY07 show $350,000 each year for maintenance catch-up. These amounts are non-recurring and will be used to fund a backlog of approximately $2.2 million. Since these are non-recurring expenditures, they are shown as an offset to the ending fund balance. In reality, these funds would be budgeted as a transfer out to Capital Projects Fund 4.
2. Projections for FY06 and FY07 include $460,000 each year to establish a Facilities

Capital Reserve Fund. These are shown as an offset to the ending fund balance (see explanation above).

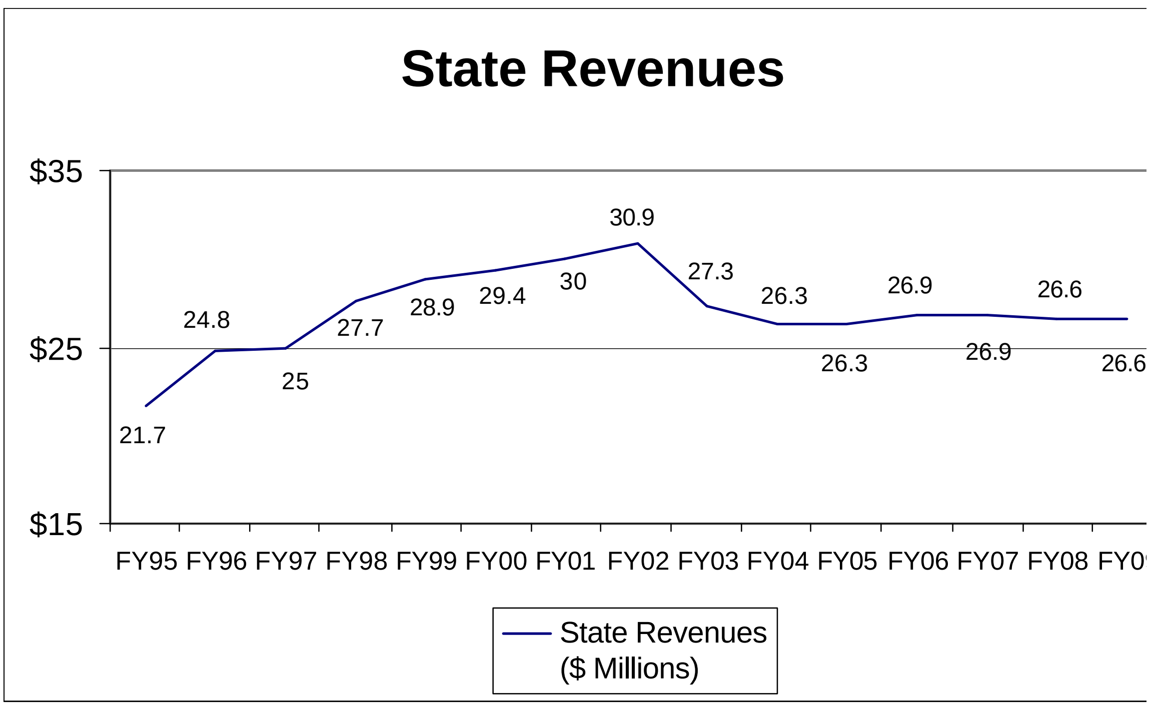
E. FUND IX-ADMINISTRATIVELY RESTRICTED

Fund IX was created in the FY03 budget to separate from the General Fund those units that rely entirely or primarily on resources other than state revenues, local property taxes and other general use revenues. For the purposes of maintaining historical trends and in order to properly monitor these units, Fund IX revenues and expenditures are included in budget projections.

SECTION III: ISSUES

State Revenues

Lane has become increasingly dependent upon state payments over the preceding 14 years. In 1990 the state provided Lane $ 8.8 million, which was 24% of Lane's total revenue. For 2004 the state is providing $26.3 million, which is 38% of Lane's current resources. While state aid has become our largest resource, it has remained relatively flat since 1997, as the following graph illustrates:



Additionally, Lane has no assurance that state aid will increase as much as inflation in the foreseeable future. The projected state revenue for years after FY 05, in the graph above, is essentially flat due to this uncertainty. However, future inflation will certainly cause expenditures to rise unless service levels are reduced. Maintenance of current service level will result in a $ 2.6 million deficit by FY 07 and increasing shortfalls thereafter.

Issues
These issues still need to be addressed in the long-range financial planning process:

1 What level of risk that state aid will increase substantially is Lane willing to accept in developing our long-range financial plan?
2 Might the state-wide allocation formula change to affect Lane adversely?
3 Will the state create an adequate "rainy day" reserve to prevent state aid reductions during the next recession?
4 At what level should Lane fund a stabilization reserve to meet potential state funding shortfalls?

Tuition rates – High student demand and increasing reliance on tuition and fees

The college's highest priority is to enable our students to have successful learning experiences. The failure of state aid since 2000 to increase sufficiently to cover Lane's increasing operating costs has negatively impacted Lane's students in the form of drastically rising tuition costs. In 1999 tuition was $ 36 per credit; but by 2004 this had risen to $ 63 per credit; a 75% increase. The college and our students face a dilemma: should large tuition increases be needed in order to maintain current program offerings.

For the past two years Lane's Board has heard from students that maintaining current service levels is their highest priority, and has acted accordingly by raising tuition. Clearly, this strategy cannot be pursued indefinitely. On the other hand, long class "waiting lists," the state "de-funding" of self-improvement classes, and the inherently high costs of professional/ technical programs, all indicate that higher tuition rates may be warranted in the future.

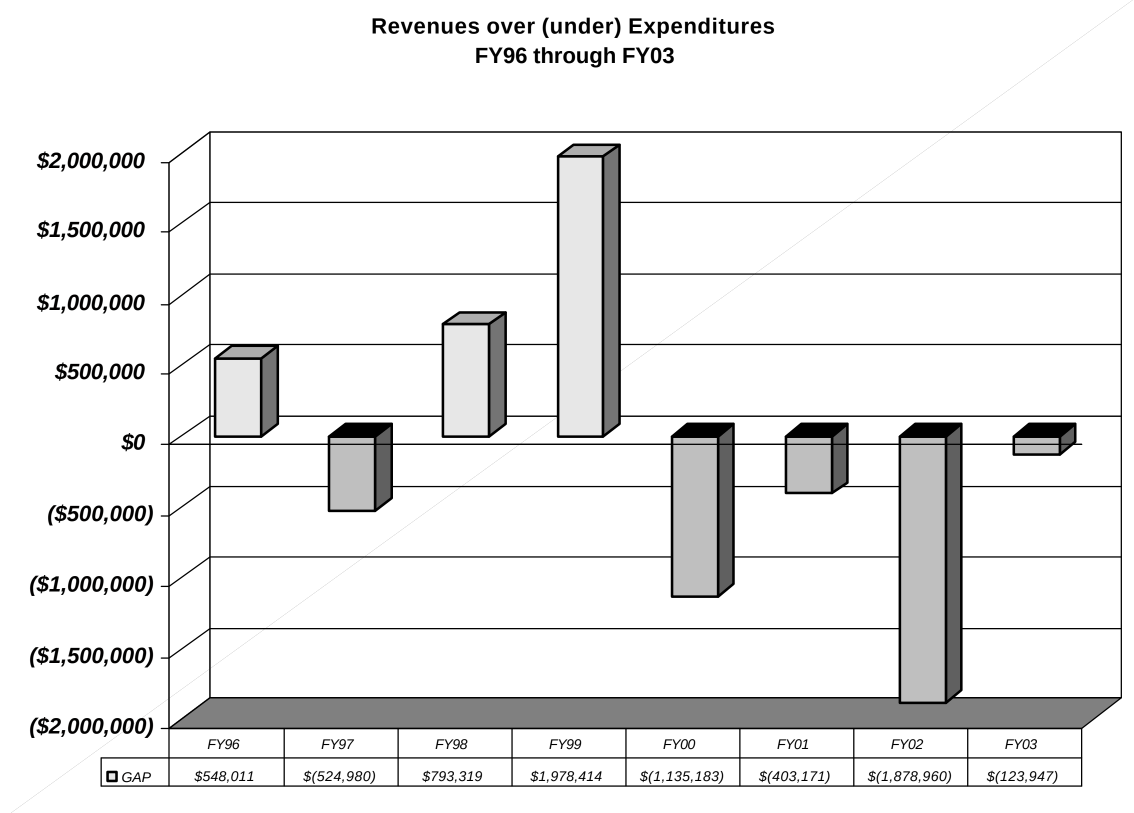
Issues:
The tuition strategies adopted in long-range financial planning will affect the size and quality of Lane's services for many years to come.

1 Should tuition rate increases in the future be limited to the rate of inflation (Board Policy), or should tuition be raised sufficiently to avoid service level reductions?
2 Should some classes/ majors be more expensive so that demand is met?

Spending down Ending Fund Balances

Long term institutional viability requires that expenditures not exceed revenues. To accomplish this end, Board Policy E.030 (Appendix 2) requires that the college maintain an unrestricted General Fund Ending Fund Balance of approximately 5% of budgeted expenditures and Board Policy E.020 (Appendix 2) specifies that 3% of general fund expenditures be budgeted as an unappropriated ending fund balance. Since FY 2000

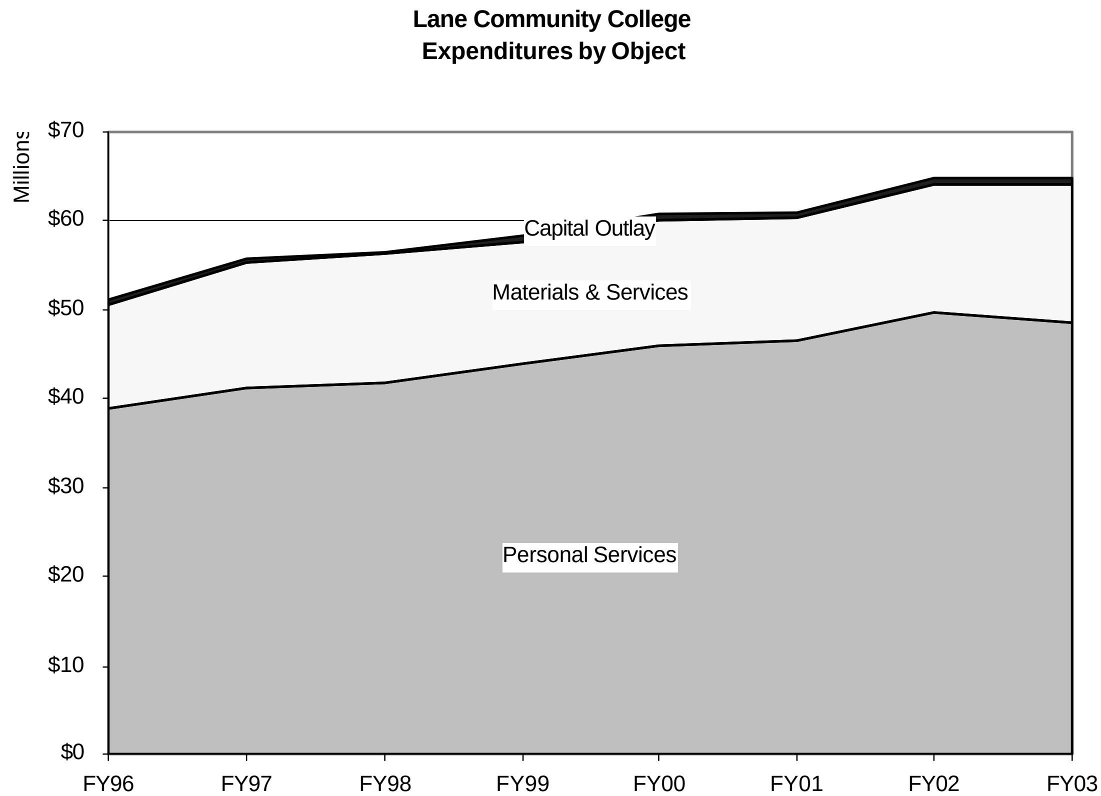
Lane’s expenditures have exceeded its revenue as shown below:



Although this spending pattern has been intentional, done to cushion the adverse impact on state aid payments caused by the economic recession, it is not sustainable. In developing future financial strategies Lane must be mindful of the impacts such strategies will have on its ending fund balance, our “resource of last resort.”

Labor intensive services

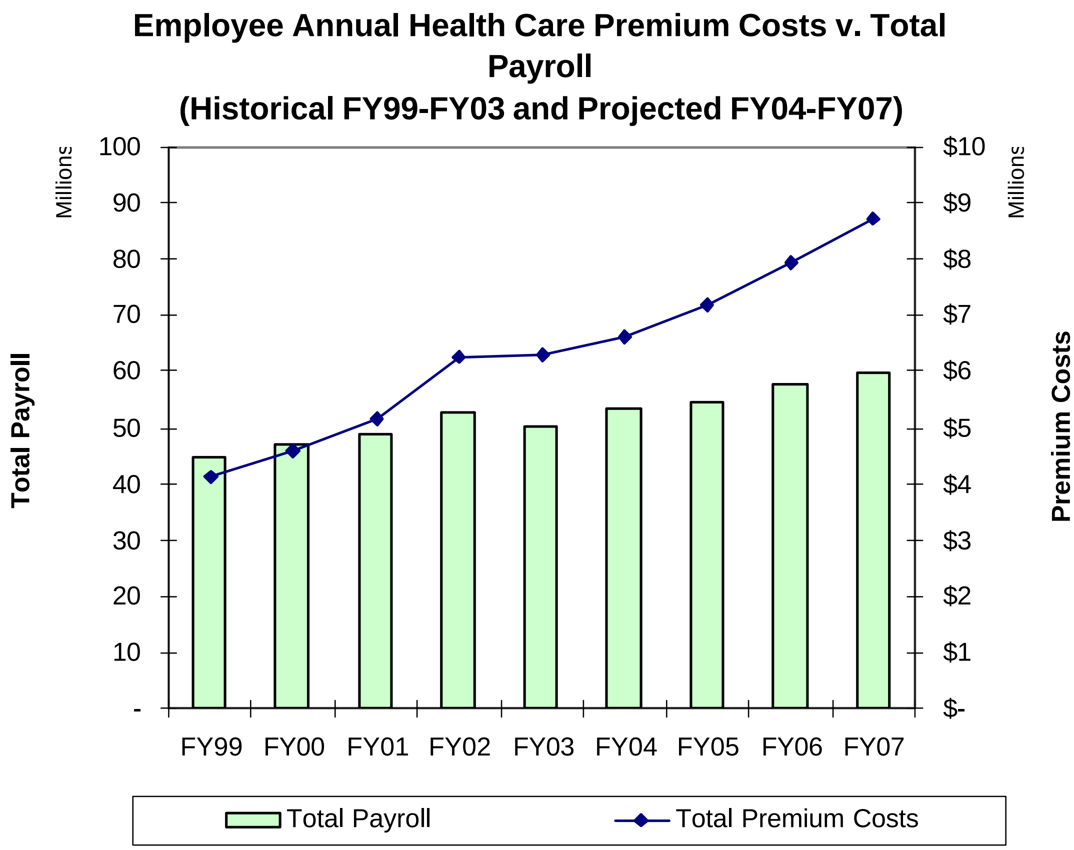
The delivery of high quality learning services is, by its very nature, a labor-intensive business. Lane’s expenditure pattern reflects this commitment, as the following graph indicates:



For FY 2004 Lane projects spending $48.5 million, out of a total budget of $74.5 million budget, on personal services and related fringe benefits. Because 2/3 of the college's financial resources are devoted to employee compensation, compensation levels must be considered a primary "driver" of rising costs. Future changes to compensation will have the largest impact on college expenditures and must be evaluated carefully to insure that they do not outpace revenue increases.

Rising costs of health care insurance for employees

Due to steep increases in the cost of medical services Lane will continue to face difficult choices in determining the level of medical insurance coverage it can afford for its employees. The Consumer Price Index indicates that medical costs have increased 47% since 1994, nearly double the rate of increase for all goods and services. During 2003 alone the CPI for medical care costs rose 6%, while overall consumer prices rose only 3.5%. The following graph portrays Lane's medical insurance historical costs and a projection of what health insurance premiums will cost the college by FY 2007 if additional cost containment measures are not taken:



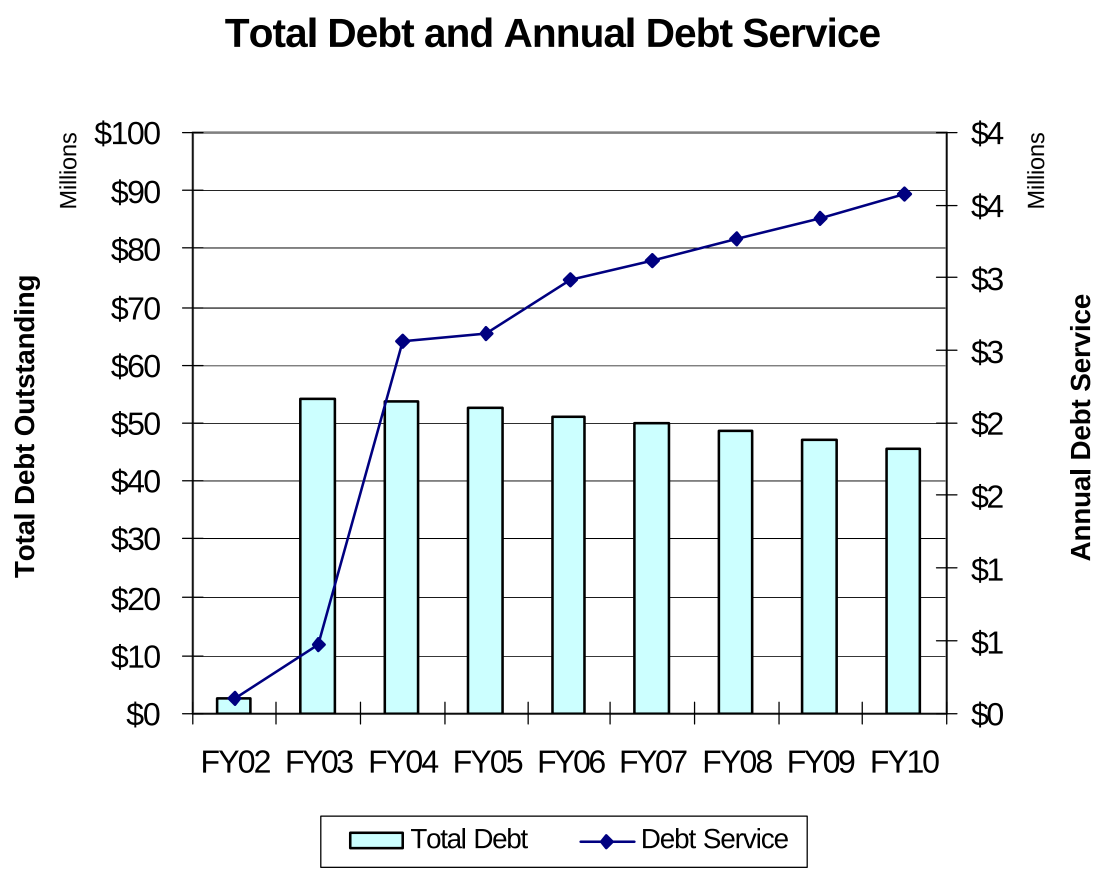
Since premium increases are currently projected to increase much faster than payroll, as the graph above illustrates, Lane must creatively devise and implement additional strategies to restrain these increases. The college has already taken steps to reduce its future rate increases: having all employees covered by the same insurance plan, requiring employees to share in the payment of the insurance premiums, a Section 125 plan, instituting the LIFE employee wellness program; and, investigating the costs/benefits of a potential on-site employee medical clinic. However, more will need to be done to prevent future medical insurance premium increases from consuming all new financial resources.

<u>Issues:</u>
These are some of the strategies that must be devised and evaluated as the college struggles with the ongoing challenge of medical insurance cost escalation.

1 Should employees bear a larger share of future health insurance premium increases?
2 If the college wants to maintain the same level of benefits, how can the costs of those benefits be contained?
3 Could an alliance with other public employers reduce costs?

PERS unfunded liability: uncertainties around recent laws

Historically high investment losses since 2000 and the unique benefit structure ("money match" provisions for Tier One employees) have combined to result in a substantial increase in PERS' Unfunded Actuarial Liability (UAL). In December 2003 Lane was informed by PERS that our share of the UAL exceeded $ 69 million - - more than the college's entire General Fund annual operating budget. This amount must be paid (in addition to current employer contributions) to PERS at an 8% interest rate over 26 years. To minimize this annual obligation, Lane issued taxable pension bonds during April 2003 at an average interest rate of 5.8%. To the extent that PERS investment earnings average more than 8% through 2028, the college will have preserved financial resources for use in the General Fund. The payments on these pension bonds must be funded annually by an increase in the college's fringe benefit (OPE) rates; an additional "overhead" cost of 5.8% for FY 2005. The long term effect of Lane's share of the PERS UAL on the college's debt and debt services requirements is represented below:



Issues: The issue of measuring and funding the PERS UAL will remain a college concern for the indefinite future. Lane's long-term financial plan will have to be adjusted periodically to take future PERS liability developments into account.

1. At what level should Lane be continuing to fund a reserve for PERS liability?
2. Will the remaining UAL be eliminated by a financial markets rise during the current economic recovery? If it is not eliminated by economic recovery, should Lane issue pension bonds at some future date for the remaining 25% of the UAL?
3. Will PERS adequately fund its loss reserves to prevent another funding crisis

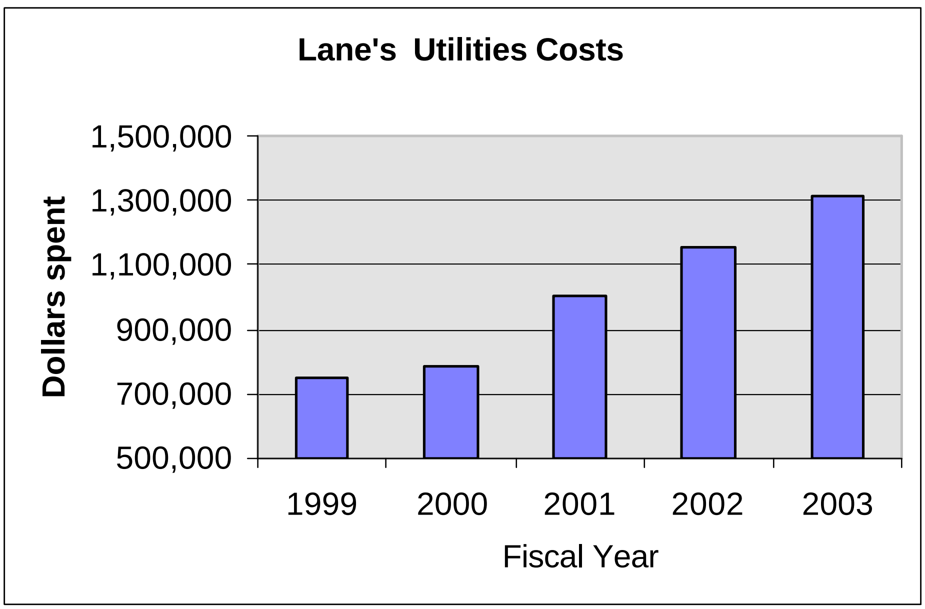
during the next recession?

4 Will current litigation between PERS and contributing employers be resolved on terms that favor employees?

5 Will the Oregon Legislature again act to dramatically affect the economic health of PERS and its contributing employers?

Rising energy costs

The college contends with increasing utilities costs for two distinctly different reasons. First, we significantly increased the square footage of facilities with the completion of new buildings which must be heated, cooled and lighted. Second, the entire Pacific Northwest has seen large energy rate increases because of California's insatiable demands and difficulties with Federal deregulation of energy prices. Lane's recent utilities expenditures trend is:



Issues: Avoiding or minimizing the impact of, unexpected, large utility rate increases will be an ongoing issue for Lane.

1 Should we become actively involved in "hedging" which is the smoothing of rates accomplished by actively trading energy futures? Should we form or join a larger alliance that actively "hedges?"

2 Should we generate a portion of our own electricity by installing photovoltaic technology or by using other alternative energy sources?

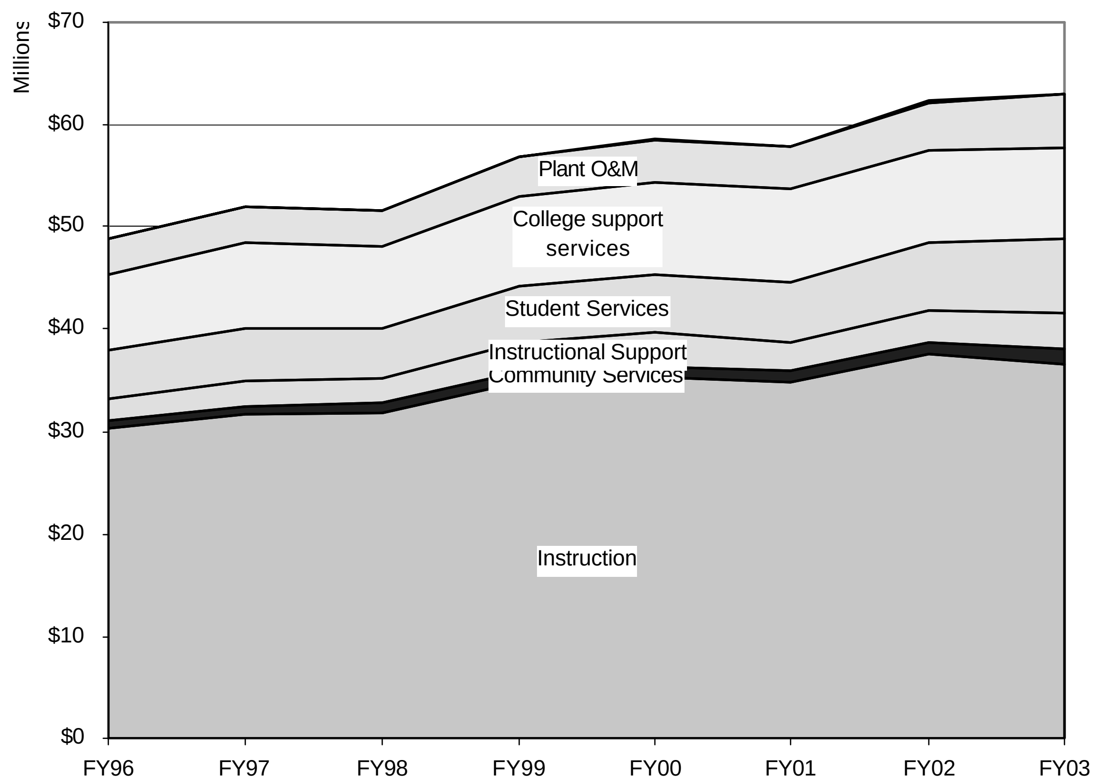
3 Should we shorten the school year or close the campus between school terms?

4 Can the college decrease its demand for electricity and natural gas?

Aging physical plant and high deferred maintenance needs

As Lane celebrates its 40^{th} anniversary in 2004, the physical condition of many college facilities is slowly deteriorating. For a variety of reasons (e.g., no tradition of funding deferred maintenance, concentrating attention and available capital outlay money on recent bond-funded construction, emergency environmental ameliorations, and devoting available resources to direct instruction since 2000), the college has not disciplined itself to adequately fund and perform the necessary major maintenance to its physical plant that will preserve a welcoming and safe learning environment for the next generation. Our recent history of expenditures (see the Plant Operations and Maintenance portion of the following graph) reveals the inadequacy of plant resources in the General Fund. For example, in FY 2003, although the college expended $5.2 million for Plant O&M, only $ .3 million of that was spent on major maintenance; and, until FY 2004, the total annual budget specifically allocated for major maintenance was only $120,000:

Lane Community College
Expenditures by Function



Issues: The Board has recognized the need to properly maintain our facilities and responded appropriately by adopting Policy E.050, Capital Reserve Funds (Appendix 2), which requires that Lane now utilize reserve funds to adequately maintain and repair college facilities according to the Major Maintenance Schedule.

1. How will this level of funding be increased and maintained at an appropriate level? Will academic programs and student services have to be reduced?
2. Should Lane submit a ballot measure to our voters to provide a portion of the funding? If so, for how much and what effect would this have on credit ratings, debt service levels and future operating budgets?

Underfunding of equipment replacement

Another result of the stagnation of state aid revenue during the current recession, has been that instructional and support services equipment has not been replaced at the end of its economic life. We have been “making do” with outdated equipment in our efforts to commit the maximum financial resources to direct instruction. The result is that Lane presently has $5.3 million of equipment in need of replacement (Appendix 3) and will have an additional need for $771,000 for FY 2005 (Appendix 4).

The college has taken steps to begin to remedy this situation. The Board has adopted Policy E.050, Capital Reserve Funds, which establishes reserve funds for equipment and facility upgrades. A desktop computer replacement program (Appendix 5), supported by new recurring Capital Outlay funds, is being implemented so that all desktop computers can be replaced regularly.

Issues: To avoid falling even further behind in equipment replacement, Lane will need to determine the appropriate funding level for Capital Reserve Funds and build this amount into its annual budget. This determination could be complex.

1. Should the Technology Fee be increased?
2. Should equipment-intensive programs assess an additional equipment replacement fee?
3. Should Lane dedicate a larger portion of its annual Carl Perkins grant to equipment acquisition?
4. What role should Lane’s Foundation and Grants Office play in pursuing equipment replacement funds?

SECTION IV: LONG-TERM STRATEGIC DIRECTIONS

Strategic Directions (see Appendix 1) for the next three to five years beginning in FY05 fall into three major categories. Two of the three categories have some long-term goals and outcomes defined, largely by direction of the Board of Education. Specific long-term goals and outcomes in all categories are being developed through the unit planning and strategic planning processes.

Transforming Students’ Lives

No long-term goals are defined for this category as yet. Short-term goals and outcomes that need funds for FY05 are described in Section VI.

Transforming the Learning Environment

1. Fully fund facilities renovation, remodeling and major maintenance
   - *Outcome: Increase capital funding for facilities to $2.7 million annually by FY09.*

2. Fully fund equipment replacement
   1 *Outcome: Increase Capital Outlay allocations to $1.3 million annually by FY08.*

Transforming the College Organization

1. Increase capacity in Human Resources
   1 *Outcome: Add Payroll Specialist (1.0 FTE) in order to be able to run twice monthly payroll without incurring overtime for staff.*

2. Several strategies relate to the Strategic Direction to "achieve and sustain financial stability." These are described in detail in the next section.

SECTION V: ACHIEVE AND SUSTAIN FINANCIAL STABILITY

1. Balance General Fund budget

1 Outcome: Ongoing (recurring) expenditures & other sources will not exceed revenues through FY07

While the FY03 ending fund balance was relatively healthy, operating expenditures have exceeded annual revenues in each of the last four years. Board Policy E.010 defines a balanced budget as one in which regular operating expenditures do not exceed annual revenues.

After two years of steep tuition increases and program reductions, FY04 is projected to end the year with revenues exceeding expenditures. However, several areas have been seriously under-funded over the last two to four years including: instructional innovation, major facilities maintenance, class sections to meet student demand, capital and computer equipment replacement, and workforce/continuing education. Complete stabilization will not occur until these problems have been addressed within available resources.

2. Stabilize tuition rates

- *Outcome: Tuition rates not to exceed inflationary adjustments through FY06.*

Lane has the highest per/credit tuition rate of community colleges in Oregon. Steep increases in tuition rates over the last two years have jeopardized the affordability of a Lane education for many students. Board Policy D.110 provides for annual tuition adjustments for inflation.

3. **Build financial stabilization fund**
    a. *Outcome: Build a reserve of $500,000 to buffer expected revenue shortfalls in the next legislative biennium.*

Board Policy E.040 provides the ability to establish a financial stabilization fund in anticipation of revenue shortfalls. Current projections show revenue shortfalls beginning with the 2005-07 Biennium indicating the need to reserve at least $500,000 over the next two fiscal years.

4. **Build capital reserves**
    1 *Outcome: Build facilities capital reserve fund to $1.2 million by FY09*
    2 *Outcome: Build equipment replacement reserve fund to $400,000 by FY09.*

    Over the last decade, Lane has depleted its capital reserves (except for construction bond funds committed to specific projects.) The college needs to build capital reserves in order to (a) provide a mechanism for funding facilities projects in years when project costs are higher than average and (b) provide funds for emergency maintenance and repairs.

    Likewise, the college has no equipment reserves. For the same reasons, the college should build equipment reserves.

    (Board Policy E.050 enables the Board to establish reserve funds for capital projects. Board Policy E.010 specifies that a balanced budget must provide adequate funds for capital needs in any given year. Reserves ensure that funds are available for emergencies and for needs in years where capital expenditures are expected to be higher than average.)

SECTION VI: STRATEGIES IN FY05 BUDGET FOR ACHIEVING LONG-TERM GOALS

All projects recommended for funding in the FY05 budget are described in detail in accompanying documents. Following are the strategies followed for the one-year period covered by the budget.

1. Limit new recurring expenditures:
    2 Fund new recurring activities through reallocation of current resources
    3 Fund new recurring activities with recurring savings or recurring new revenues created by those activities

2. Build new revenue streams

Board Policy E.010 specifies that new ongoing expenditures must be supported by recurring revenues. In order to keep Lane's current service level and/or provide additional programs and services, new revenue sources must be identified.

1. Implement second year of differential tuition program and assess ability to expand or maintain the program into FY06.
2. Build capacity in Foundation to increase fundraising
3. Revise Transportation Fee program for FY05; during FY05 develop long-range Transportation Plan for the college for FY06 and beyond
4. Continue Tuition-Based Program; assess during FY05 in order to plan changes for FY06 and beyond.
5. Assess 8% gross revenue surcharge for Food Services and Bookstore and revise as needed.

3. Use one-time (non-recurring) funds to invest in Strategic Directions with expected return on investment (in compliance with Board Policy E.060-Budgeting of Non-Recurring Resources)
    1. [List of projects, project budgets and expected returns attached]