

Higher Education Capital Facilities & Budgeting in Ohio



Presentation to the
Higher Education Funding Study Council
September 28, 2005
Rich Petrick
The Ohio Board of Regents

Overview



- ❖ Current status of higher education facilities
- ❖ Trends in capital funding
- ❖ Capital funding policy

Basic facts - 1



- ❖ 38 public institutions
- ❖ 62 + public campuses
- ❖ 350,000 + full-time equivalent students
- ❖ 457,000 fall headcount students
- ❖ 48,892 faculty

Basic facts - 2



❖ Ohio is not “overbuilt”

- Number of campuses relative to our population = national average.
- Square footage of space per student = national average.
- More or less at capacity.

Basic facts - 3



❖ Two types of facilities

➤ Educational & General (E&G)

- General purpose classrooms, laboratories, offices, etc.
- Construction expected to be financed by the state.

➤ Auxiliary

- Residence and dining halls, bookstores, parking garages, convocation centers, etc.
- Construction expected to be financed by user charges or other non-state revenues.

Overview



❖ Current status of higher education facilities

- Large
- Expensive
- Old

Public higher education space inventory, 2004 – All buildings

Number of owned buildings	2,391
Net assignable square feet (NASF)	69.3 million
Replacement value (construction + "soft costs")	\$23 billion
\$ per NASF	\$332

Public higher education space inventory, 2004 – E&G Buildings

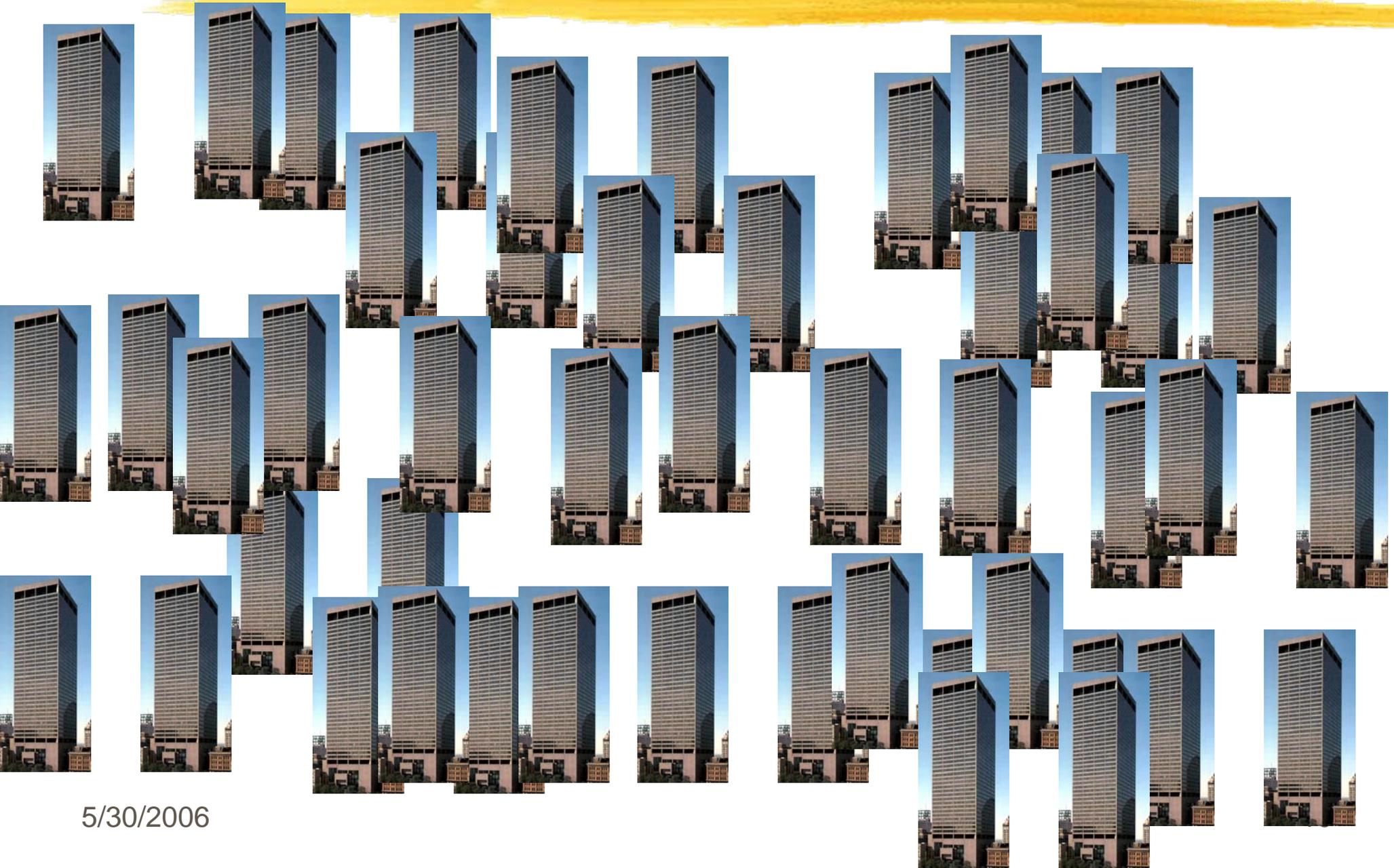
Number of owned buildings	1,836
Net assignable square feet (NASF)	56.7 million
Replacement value (construction + “soft costs”)	\$14.3 billion
\$ per NASF	\$252

How large is 56.7 million square feet of space?

The Rhodes
Office Tower has
1.2 million
square feet of
space



Ohio E&G space = 47 Rhodes Buildings



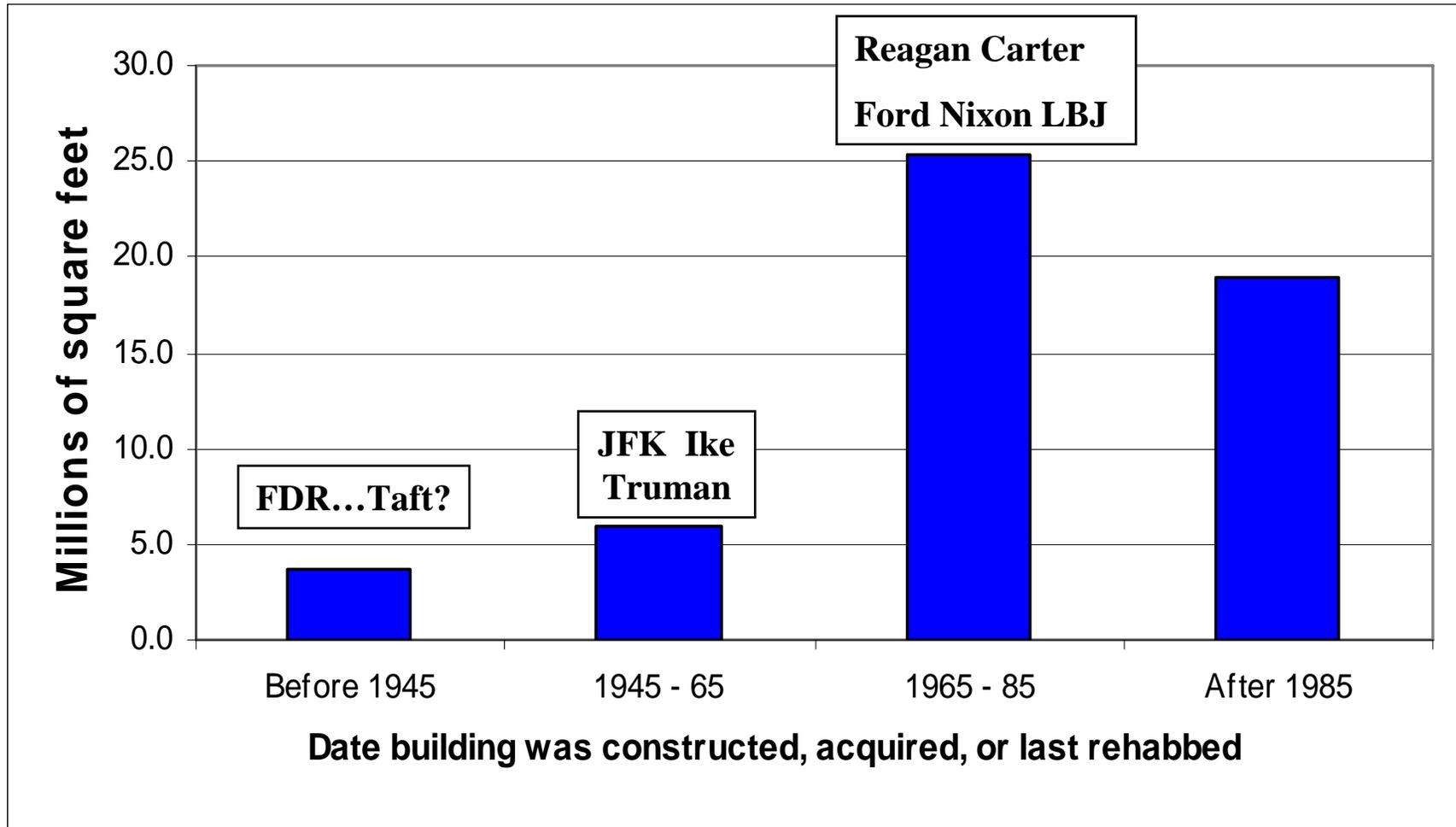
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What is “block obsolescence?”



- ❖ Simultaneous aging of a large block of facilities in a relatively short time period.
- ❖ Ohio invested heavily in the 1960s, 1970s and 1980s to accommodate the baby boom generation.
- ❖ The “bill” for many of those buildings is now coming due.

What is "block obsolescence?"



Educational and general space only; does not include auxiliaries

The condition of E&G space, & estimated cost to rehab

Condition	NASF, millions ft²	%	Estimated cost to rehab or replace
Satisfactory	19.5	34.4%	\$0 - \$248 million
Minor rehabilitation	18.4	32.5%	\$0.9 - \$1.1 billion
Rehabilitation	10.4	18.3%	\$1.1 - \$1.4 billion
Major rehabilitation	7.5	13.3%	\$1.6 - \$1.9 billion
Physically obsolete	0.9	1.6%	\$314 million
Total, all space	56.7	100.0%	\$3.9 - \$5.0 billion

Estimated annual renewal & replacement costs for E&G facilities

❖ \$14.6 billion replacement value

➤ If buildings have a 40-year useful life – state needs to provide 2.5% per year to offset depreciation.

▪ $\$14.6 \text{ billion} \times 2.5\% = \underline{\$365 \text{ million per year}}$

➤ If buildings have a 50-year useful life – state needs to provide 2.0% per year to offset depreciation.

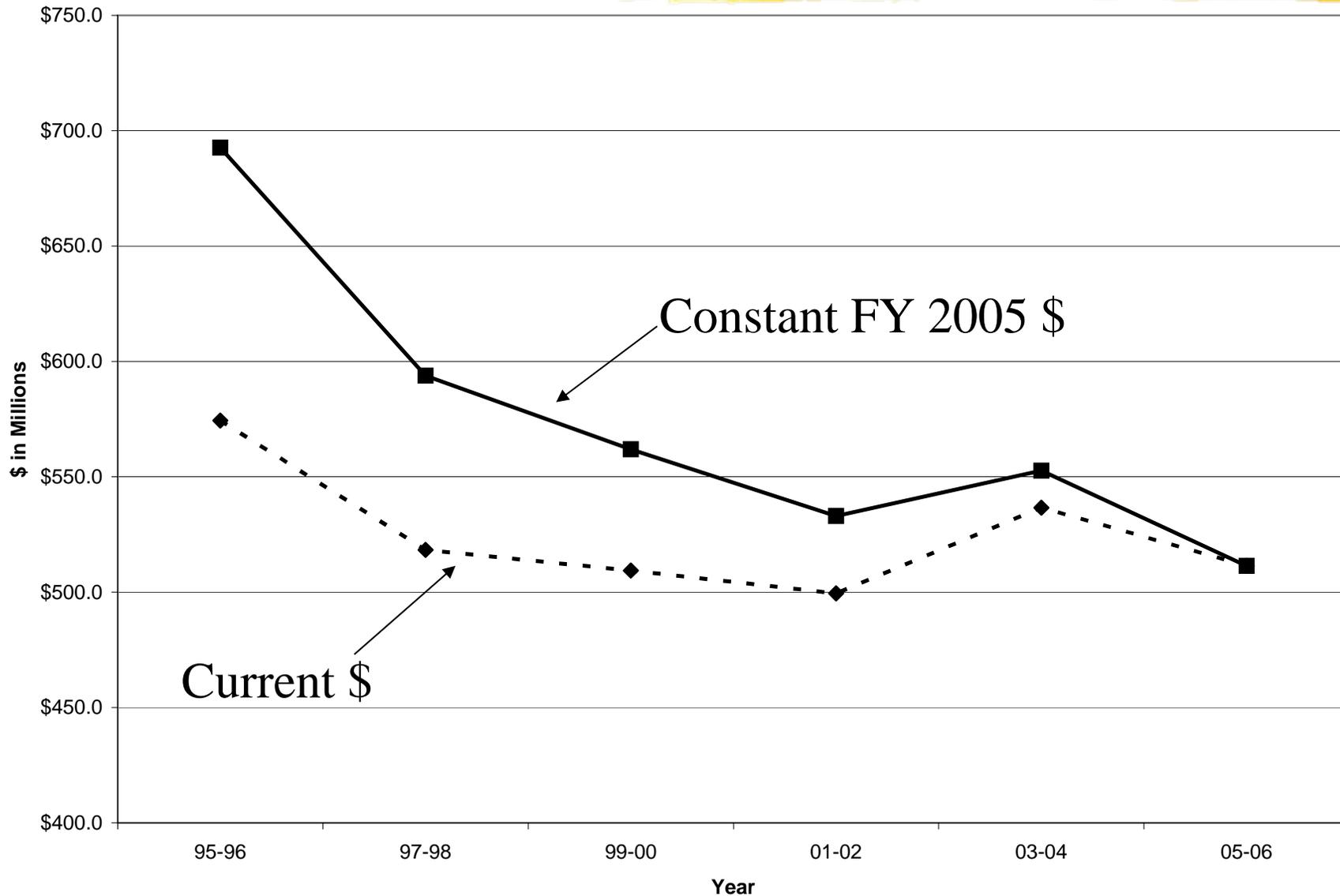
▪ $\$14.6 \text{ billion} \times 2.0\% = \underline{\$292 \text{ million per year}}$

Overview

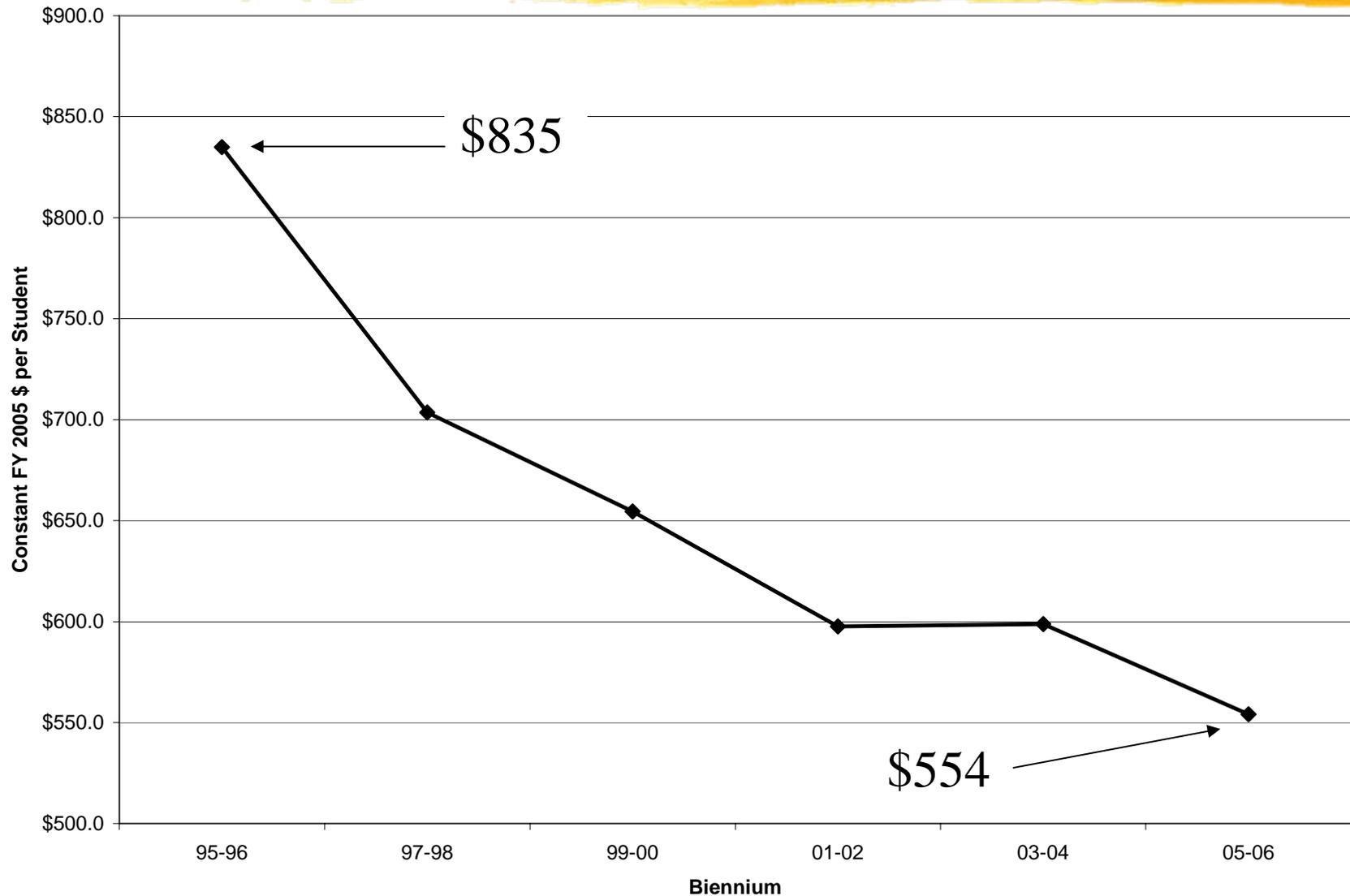


- ❖ Current status of higher education facilities
- ❖ **Trends in capital funding**
- ❖ Capital funding policy

Trend in state capital support for higher education



Trend in state capital support per headcount student – in constant FY 2005 dollars



State capital funding trends in constant FY 2005 dollars

	Total \$	\$ Per Student
95 - 96	\$693 M	\$835
05 - 06	\$511 M	\$554
Difference \$	-\$182 M	-\$281
Difference %	-26%	-34%

Constraints on state's ability to fund higher ed capital needs



❖ State Issue 1 – November 1999

- Authorized issuance of G.O. bonds for higher education and K-12
- For the first time, made K-12 eligible for state GRF-supported capital funds
- 5% debt service limitation enshrined in the Constitution
 - Economic slowdown reduces state revenues, and thereby reduces debt authority of the state

Constraints on state's ability to fund higher ed capital needs



❖ The K-12 12-Year Plan

- \$23 billion plan to renovate primary and secondary facilities
 - Includes \$10.2 billion in state commitments
- Initially anticipated use of Tobacco Settlement funds
 - But Tobacco Settlement funds used instead to balance operating budget

Constraints on state's ability to fund higher ed capital needs



❖ The K-12 12-Year Plan

- Despite reduction in available Tobacco Settlement funds, 12-year commitment and schedule is unchanged
- Funding burden shifted from Tobacco Settlement funds to state bonding
- Left less available for higher education

Recap of the problem



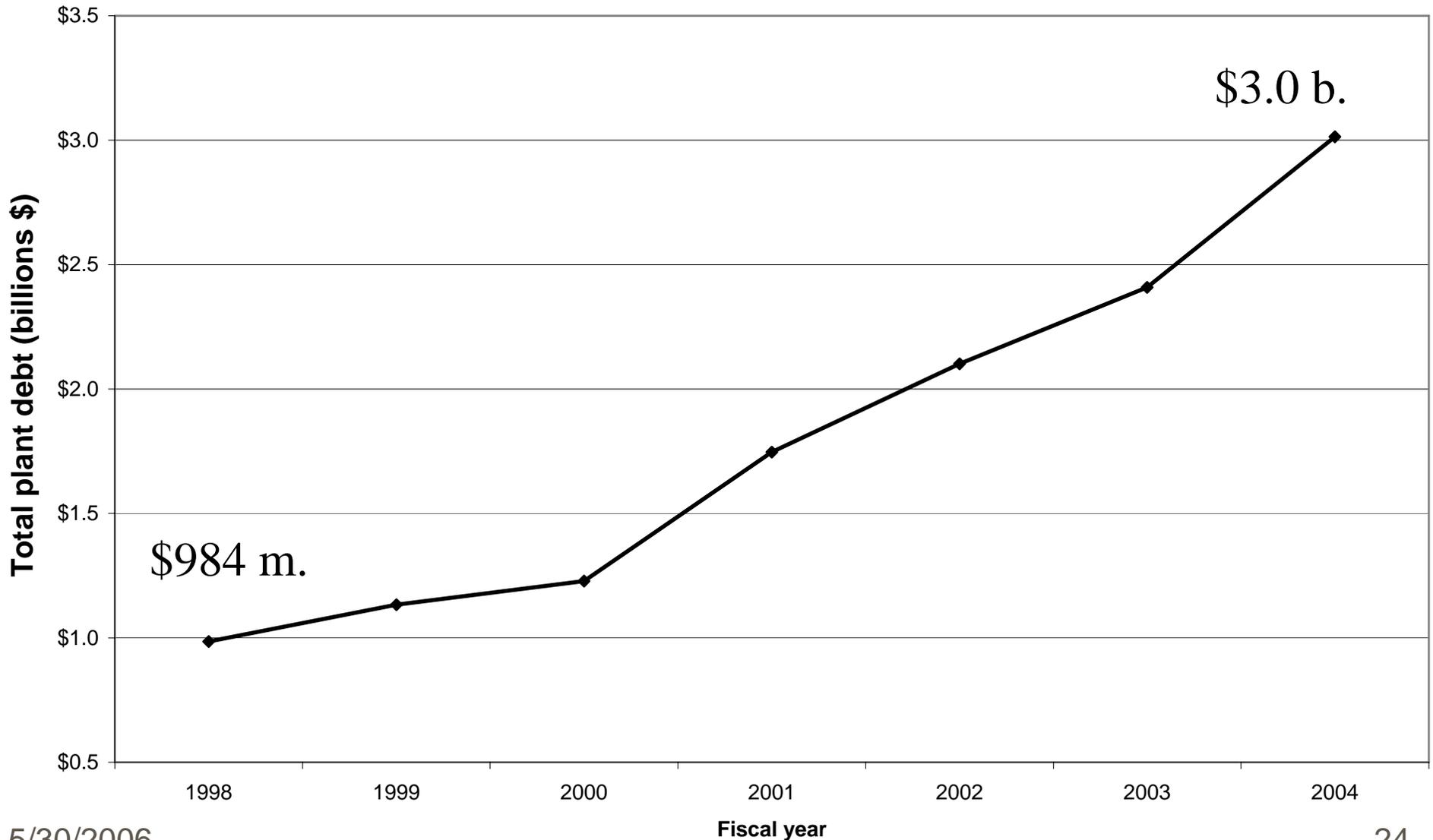
- ❖ Block obsolescence increases need for additional state capital investments
 - \$3.9 - \$5.0 billion
- ❖ Annual renewal & replacement:
 - \$292 - \$365 million
- ❖ State Issue 1, stagnant state economy, and continuing commitment to K-12 limits state capital funds for higher education
 - FY 05 – 06 capital funding = \$205 million per year

What can campuses do?



- ❖ Permit deferred maintenance to increase?
- ❖ Seek private funds?
- ❖ Use available fund balances?
- ❖ Raise student fees?
- ❖ Borrow more money?

One result: Campus debt has tripled in six years



Overview



- ❖ Current status of higher education facilities
- ❖ Trends in capital funding
- ❖ **Capital funding policy**

Overview



- ❖ **Capital funding policy**
 - **Formula funding works**

FY 03-04 and FY 05-06 state capital appropriations

Capital Line	Allocation Basis	FY 03 – 04 H.B. 675	FY 05 – 06 H.B. 16
Capital allocation	Formula	\$308.9	\$279.4
Basic renovations	Formula	\$90.0	\$77.1
Instructional equipment	Formula	\$33.0	\$28.3
Action & investment	Competitive	\$19.0	\$5.0
Non-credit job training	Competitive	\$5.9	\$0.0
Technology initiatives	Competitive	\$3.7	\$0.0
Eminent scholars	Competitive	\$2.0	\$0.9
OhioLINK	Direct grant	\$8.2	\$8.1
Supercomputer Center	Direct grant	\$8.5	\$6.8
Library depositories	Direct grant	\$0.7	\$0.0
Dark fiber	Direct grant	\$5.0	\$4.5
Total		\$485.0	\$410.1

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The pre-1996 capital funding policy



- ❖ In effect from the early 1970s through 1996
- ❖ Served Ohio during a period of enrollment growth
- ❖ Over \$4 billion in higher education bonds issued

The pre-1996 capital funding policy



❖ How did it work?

- Regents asked campuses what they needed
- Campuses responded
- Sum of requests > available state resources
- Regents and state had to ration

The pre-1996 capital funding policy



- ❖ Centralized decision making
- ❖ “Ad hoc” decision rules
- ❖ Judgment & persuasion
- ❖ Unpredictable
- ❖ Disconnect between means and ends
- ❖ Viewed as a zero-sum game

The current capital funding policy



- ❖ First proposed by the Regents in 1992
- ❖ Deliberated and refined by the “Commission to Study Higher Education Debt Service”
- ❖ Approved in 1994

The current capital funding policy



❖ Some key elements

- Campuses earn capital allocations (i.e., debt service) via a uniform agreed-upon formula
- Campuses are “charged” debt service for their decisions to spend state capital dollars
- Specific decisions to spend (or not to spend) are made by campuses – not by Regents

The current capital funding policy: allocations

- ❖ Formula earnings based on campus' share of:
 - "Activity": Credit instruction, sponsored research, and non-credit job-related training (50%)
 - Aged space (50%)
- ❖ Adjustments for:
 - Small campus factor
 - Space shortage
- ❖ Earned allocation = debt service equivalent of \$

Example of one calculation

Capital allocation example, University A

A	B	C	D	E	F	G	H	I
Activity-Based POM Earnings, FY 2004 Calculation	Small-Campus Factor	Column A times Column B	Share of Weighted Activity-Based Formula	Weighted Aged Space	Share of Wgtd Aged Space	Average of Columns D and F	Round 5 Debt Service Allocation = \$35.4 m	Round 5 Capital Approp. Equiv't
\$20.9 m	1.000	\$20.9 m	4.8%	2.2 m ft ²	5.2%	5.06%	\$1.8 M	\$18 m

Each factor is the result of separate complex calculations.

The current capital funding policy: campus spending

- ❖ Campuses are charged debt service for new capital projects
- ❖ If charge < capital allocation
 - Campus may bank the difference, or spend it on other capital-related needs, via the Capital Component
- ❖ If charge > capital allocation
 - Difference is deducted from State Share of Instruction
- ❖ If charge = capital allocation
 - It's a wash; no additional adjustment is necessary

How the capital formula works: Examples

Campus	Formula debt service allocation	Debt service cost of new capital request	Difference (Operating budget adj. for 20 years)
A	\$500,000	\$0	+\$500,000

How the capital formula works: Examples

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How the capital formula works: Examples

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B	\$500,000	\$500,000	\$0
C	\$500,000	\$1,000,000	-\$500,000

The current capital funding policy: POM \$



- ❖ Plant operations and maintenance subsidy revised:
 - From: one based on square feet of space
 - To: one based on activity (credit instruction, sponsored research, and non-credit job-related training) occurring on campus
- ❖ Old (pre-1995) square footage remains the 'floor' for POM subsidy

The current capital funding policy: conclusion

❖ “Old” Capital Policy

- Centralized
- “Ad hoc” decision rules
- Judgment & persuasion
- Unpredictable
- Disconnect between means and ends
- Viewed as a zero-sum

❖ “New” Capital Policy

- Decentralized
- Formula-based decision rules
- Empirically derived
- Predictable
- State \$ linked to state goals
- Non zero-sum

The current capital funding policy: Results



- ❖ Benefits of the new policy
 - Improved campus long-term planning
 - Improved ability to borrow funds in anticipation of future state capital moneys
 - Increased focus on operational efficiency
 - Most money used for rehabilitations, renovations, and replacements of existing facilities
 - Fewer, if any, “net new” buildings

Thank you

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Questions?