MEMORANDUM

To: Timothy S. Keen, Director
Office of Budget and Management

Copies to: Regent Bruce Beeghly
E. Garrison Walters, Interim Chancellor
Tracy Najera, OBM

From: Richard L. Petrick, Vice Chancellor for Finance Richard L. Petrick

Date: June 26, 2006

Re: FY 2007-2008 Regents Supplemental Capital Recommendation

Please find attached the Board of Regents resolution approving a FY 2007-2008 supplemental capital request of $150 million, the proposed distribution of the campus share totaling $132.5 million, and a list of proposed supplemental projects by campus. Since a few campuses have yet to respond to our request for supplemental projects, the list of projects we are submitting to you is marked DRAFT. It is our intent to finalize the list by July 17th.

**Background**

As you are aware, state capital support for Ohio's public colleges and universities is distributed through a formula based on enrollments and the age of educational and general (E & G) facilities. We believe that the 1996 capital funding policy has encouraged effective and efficient use of state capital resources. The funding policy conforms to Ohio's decentralized approach to capital planning through formula-based decision rules and a predictable future stream of state capital resources. It also has promoted campus spending decisions that now allocate the vast bulk of state capital resources for the renovation of existing E & G facilities.

The 1996 capital funding policy has better rationalized the allocation of state capital resources, given campuses the ability to plan E & G projects beyond a single capital biennial period, and has provided incentives to campuses to renovate rather than add new buildings. Since 1996, campuses have used a larger and larger share of their state capital appropriations to address renewal needs. Unfortunately, a large proportion of current E & G facilities were built to accommodate the Baby Boom generation during the 1960s and 1970s. The simultaneous aging of these facilities – which is often referred to as "Block Obsolescence" – coupled with a 35% decline in constant state capital support for higher education during the 1990s, has overwhelmed the ability of campuses to completely address facility renewal needs. Figures 1 and 2 below illustrate key components of the dilemma.

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**Figure 1 – Higher Education Capital Renewal: Why the Bill Is Coming Due**

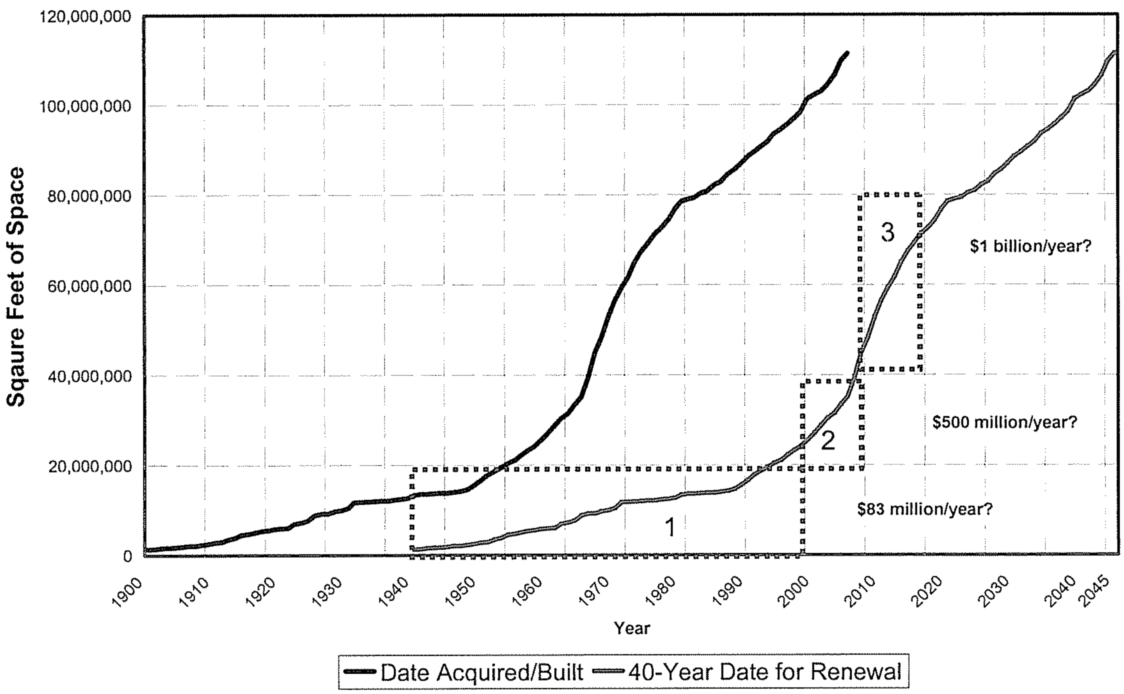
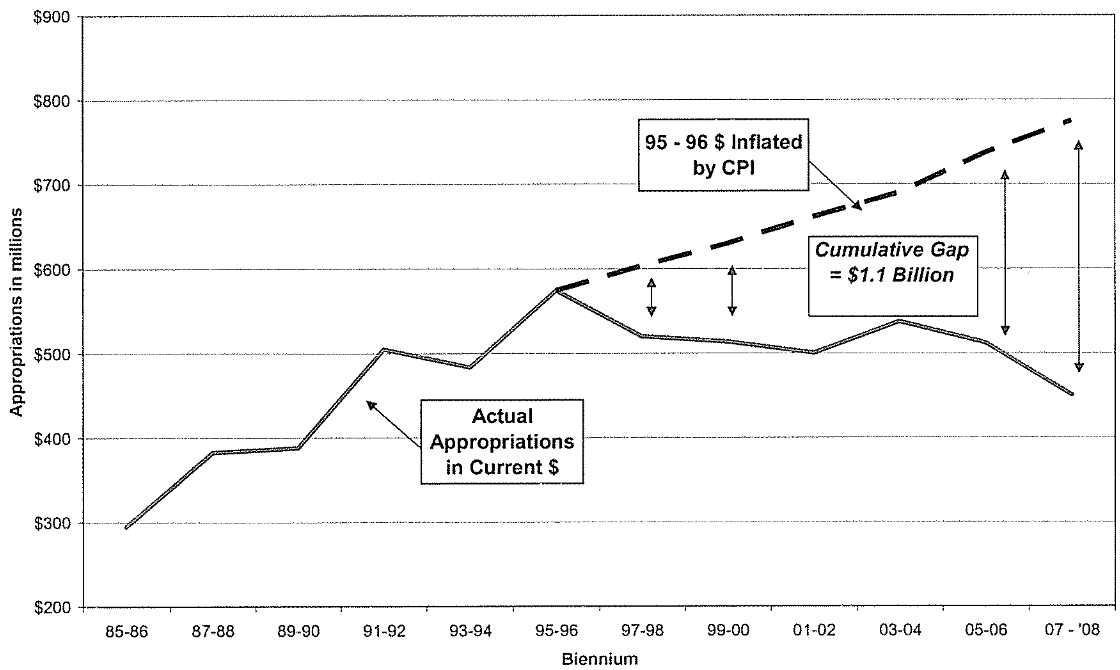



**Figure 2 – History of Higher Education Capital Appropriations**




The first data line in Figure 1 is the year a higher education facility was built or acquired. The second data line is the 40-year renewal point[1] for each facility. As noted on the chart, capital renewal needs were not that pressing prior to FY 2000 [see box labeled "1"]; however, the number of facilities reaching their renewal point over the past 6 years has increased dramatically [see the box labeled "2""]. The preliminary projected cost to renew these facilities from 2000 to 2010 is $500 million per year. From 2010 to 2020 [see box labeled "3"], we fear that the cost of facility renewal could increase to $1 billion per year.

Figure 2 illustrates the effect of the loss of state capital support for higher education in the past decade. Starting in FY 1995-1996, we project the amount of state capital funds appropriated if the amount received each biennium was inflated by CPI from the previous biennial period. When compared to the actual and expected appropriations since FY 1995-1996, the estimated cumulative gap in state capital support is $1.1 billion. This funding gap represents a significant loss of state capital resources during a time of dramatic increases in facility renewal needs at our campuses, as illustrated in Figure 1.

The Regents staff currently estimates that the cost of addressing the current capital renewal backlog for E & G facilities is between $4 and $5 billion. This amount does not include the cost of campus infrastructure or information technology needs since Regents staff does not currently have sufficient data to make reliable estimates about these two other components.

Campuses are struggling to manage facility renewal through a variety of strategies:

- Where possible and appropriate, campuses have borrowed money on their own to address critical facility needs. In fact, campus debt has more than tripled in the past five years and now exceeds $3 billion.
- At least one institution now allocates a portion of their annual operating budget to E & G facility renewal.
- Campuses continue to seek external funding from private donors and federal government grants for E & G facilities.

The supplemental request approved by the Board of Regents will provide much needed resources to help begin addressing the significant and growing backlog of E & G renewal projects at our campuses. The supplemental request also includes $10 million to support a state-wide master capital planning effort, which we think is critical to our ability to identify and help solve the capital renewal problem over the next 10 to 20 years. We are collaborating with campus representatives in this effort.

The initial structure for the state-wide capital master plan is made up of three phases:

- <u>Phase 1:</u> Development of a draft capital master plan utilizing facility data from the Higher Education Information (HEI) system.
- <u>Phase 2:</u> An independent assessment and validation of initial estimates of capital needs. Estimates will be modified based on the state-wide assessment. The final report of the Higher Education Funding Study Council (HEFSC) recommends an independent validation of E & G capital needs.
- <u>Phase 3:</u> Development of the final state-wide capital master plan. The plan is expected to include detailed facility profiles and long term funding recommendations. Also at the conclusion of Phase 3, we will have implemented one or more tools to support on-going state-wide capital

[1] The useful life of facilities varies; 40 years is used here as an average for the buildings constructed during the latter part of the 20th century.

planning.

The $10 million request will support Phase 2 and 3 of our state-wide planning effort. Without this capital support, we will be unable to conduct an independent facility assessment, as requested by the HEFSC, or develop tools to support future planning.

The balance of the supplemental request includes the following items:

- Central State University Supplemental - $4 million: Central State has identified a need of $4 million for its Center for Education & Natural Sciences project. This project, when completed, will provide a facility to house and support the CSU College of Education, Natural Sciences, and Institute for Urban Education programs.
- Supplemental Renovations – Library Depositories - $2 million: This request recognizes the continuing capital needs of five regional library depositories, which receive no other source of funding other than what they receive from the state.
- OhioLink Supplemental - $1.5 million: This increase in appropriations, matched with library funds, will enable OhioLink to buy collections of major value across a spectrum of academic disciplines from the hard sciences to humanities in journals, literature, and government documents. The acquisition of this material will make OhioLINK's current holdings even more valuable and useful.

If you have any questions regarding the list of campus projects, or other aspects of the Regents supplemental request, please feel free to contact me or James Nargang, Assistant Director, Capital Planning.

Thank you for considering this request.

Attachments (2)