MINNESOTA STATE COLLEGES AND UNIVERSITIES
BOARD OF TRUSTEES
Agenda Item Summary Sheet

Name: Finance and Facilities Committee   **Date:** January 28, 2015

Title: System Financial Resiliency Framework

Purpose (check one):

☐ Proposed New Policy or Amendment to Existing Policy	☐ Approvals Required by Policy	☐ Other Approvals
☐ Monitoring / Compliance	☒ Information	

Brief Description:

At its June 2014 meeting, the Board of Trustees asked the Vice Chancellor of Finance and Facilities to evaluate each college and university's financial condition and ability to withstand enrollment declines. System office staff consulted with a group of campus chief financial officers (CFOs), researched measures, evaluated methodology, and analyzed data to create the "College and University Financial Resiliency" measurement instrument.

Scheduled Presenter(s):

Laura M. King, Vice Chancellor – CFO
Deb Bednarz, Director – Financial Planning and Analysis

INFORMATION ITEM
System Financial Resiliency Framework

BACKGROUND

At its June 2014 meeting, the Board of Trustees asked the Vice Chancellor of Finance and Facilities to evaluate each college and university's financial condition and ability to withstand enrollment declines. System office staff consulted with a group of campus chief financial officers (CFOs), researched measures, evaluated methodology, and analyzed data to create the "College and University Financial Resiliency" measurement instrument.

The initial resiliency design methodology was shared with the Board of Trustees at their September 2014 retreat. The finance division sought additional input from the system's CFOs, modified the framework and updated the effort with fiscal year 2014 financial and enrollment results. This report describes the revised Financial Resiliency Framework and methodology and summarizes the results of the resiliency analysis.

OVERVIEW

- Minnesota State Colleges and Universities experienced rapid enrollment growth between fiscal years 2006 and 2011. The record-setting college growth was driven in large part by the economic recession and high levels of unemployment that drove many adult learners to our colleges and universities to upgrade their skills or learn a new profession.

- Minnesota's strong economy and improved employment outlook, along with declines in the number of high school graduates and other key demographic age groups, have reversed the enrollment trend. Colleges and universities are now experiencing rates of enrollment decline that reflect national trends.

- Enrollment loss translates into lower tuition and fee revenue; colleges and universities must reduce costs and/or find alternative revenue sources to maintain financial health.

- The financial resiliency framework was designed to measure the financial condition of colleges and universities and their capacity to withstand enrollment decline or other revenue or expense shocks.

- The framework incorporates both financial and enrollment measures. The financial measures address both balance sheet condition and income statement performance. The

objective of the financial measures is to reflect both longer term financial capacity and shorter term results. The enrollment measures illustrate both absolute enrollment change and the rate or velocity of that change.

- The four financial measures include CFI, net income/loss, cash position, and change in unrestricted net assets (CUNA). Colleges and universities were scored on a scale of one to five for each measure, with one being least resilient and five most resilient.

- The four financial measures were averaged to create the financial activity composite score. This composite score, with both balance sheet and income statement measures, smooths out the impacts of short term events, and will become more meaningful as years of results are compared.

- The two enrollment measures include enrollment volatility and enrollment momentum. The two enrollment scores were averaged to create the enrollment activity composite score.

RESULTS

- The financial activity composite score is the average of the four financial measures: CFI, net income/loss, cash position, and change in unrestricted net assets.
- The average financial activity composite score was 2.9 systemwide; the median score was 3.0.
- The colleges averaged 3.0 and the universities averaged 2.4. This reflects the college's stronger CFI and net income/loss performance compared to the universities.

Financial Activity Composite Score
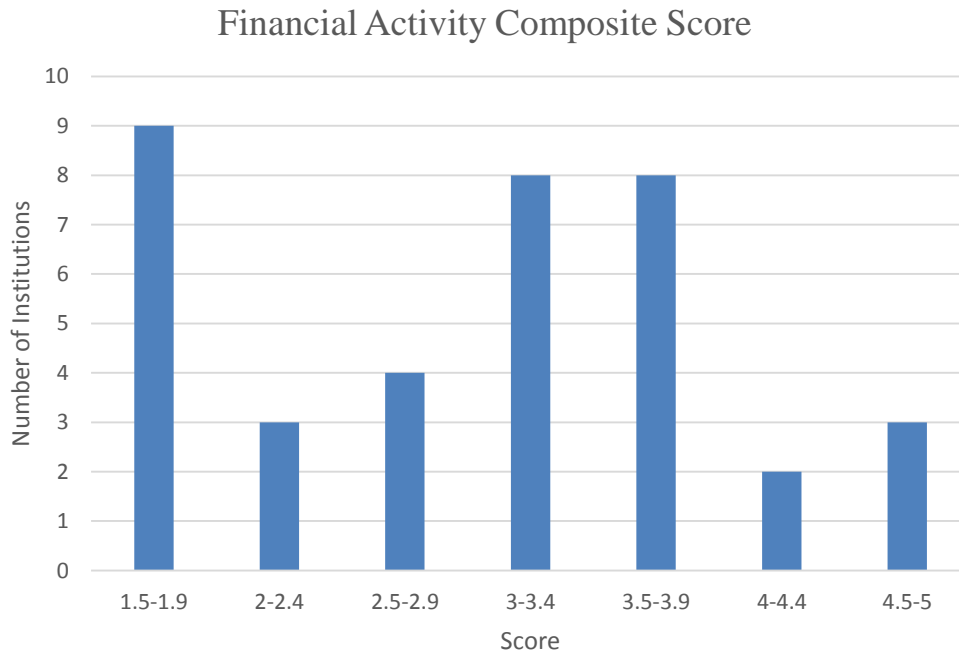
Financial Activity Composite Summary   Graph 1

- The enrollment composite score is the average of two measures: volatility and momentum.
- The average enrollment composite score was 2.8; the median score was 2.5.
- The colleges averaged 2.8 and the universities averaged 3.1.
- College enrollment was more volatile than university enrollment; colleges also scored slightly higher on the momentum measure. This aligns with observation; the colleges saw much greater enrollment increases and decreases than did the universities. However, only the universities have seen enrollment decline to 2008 levels while college enrollment remains slightly higher.
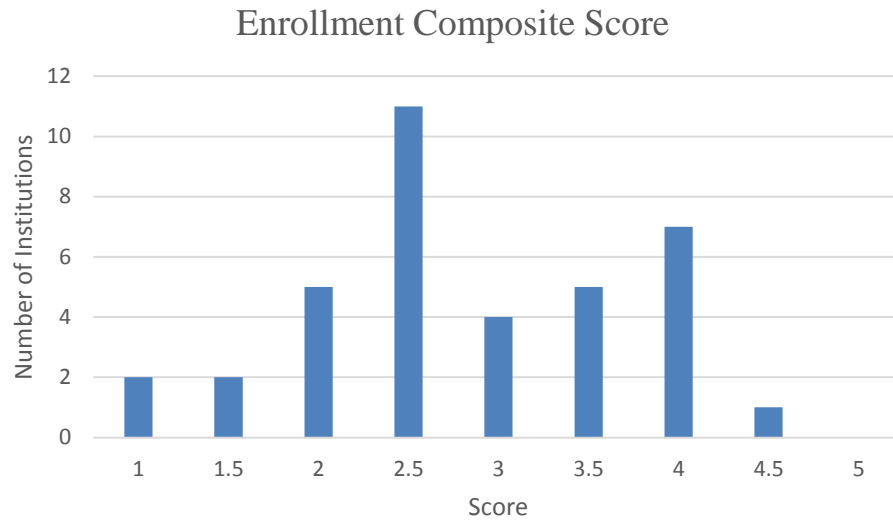
Enrollment Activity Composite Summary – Graph 2

CONCLUSIONS

- Twenty-one colleges and universities scored more than 2.9 on the financial activity composite score while sixteen colleges and universities scored 2.9 or less. The measure captures the wide variability in the 2014 performance and financial condition of our 37 colleges and universities.

- Enrollment experience is similarly divided around the 2.5 score with seventeen colleges and universities scoring above 2.5 and twenty scoring at or below 2.5. Colleges and universities with strong momentum also were more likely to experience strong volatility.

- Both colleges and universities scored higher on the cash and change in unrestricted net assets measures and lower on the CFI and net income/loss measures, an illustration of some financial capacity to absorb losses and the near term lack of structural solutions implemented.

- The financial resiliency framework has helped identify areas where the system was more resilient (cash position and net assets) and less resilient (net income/loss). It also highlighted areas where more work could be done to support resiliency (enrollment projections).

- The framework has substantially improved our ability to evaluate college and university financial condition in relation to one another. By normalizing financial data across widely divergent sized and resourced colleges and universities, we are able to identify the strengths and weaknesses in comparative terms.

- The individual measures provide clear evidence of financial condition and an opportunity for engagement and remediation actions.

- The resiliency scores correlate closely with other measures of financial health the system monitors, confirming the validity of those measures and the ability of the system to identify colleges and universities at financial risk.

- By validating our existing measures and processes, future efforts will be focused on working with colleges and universities identified as being at risk and improving their financial resiliency.

- Additional work is recommended on analyzing regional demographic projections and the resiliency results to help determine how the colleges and universities can best serve Minnesota.

- The analysis will be undertaken yearly and summary results provided to the committee and the Leadership Council.

APPENDIX

METHODOLOGY

The resiliency framework was created in consultation with the system's CFOs. It is intended to measure a college or university's financial resiliency, including its ability to withstand unexpected enrollment declines or other revenue or expense shocks. After researching and testing various measures, six measures were selected to include in the framework: four financial measures and two enrollment measures.

The financial activity composite score is a compilation of four measures designed to provide an overall measure of a college or university's financial resilience: Composite financial index (CFI), net income/loss, cash on hand, and change in unrestricted net assets.

The enrollment activity composite score is a compilation of two enrollment trend measures. Enrollment volatility and enrollment momentum which both compare enrollment changes between fiscal years 2008 and 2014. These measures are new measures and were designed to assess the enrollment characteristics of each institution that impact resiliency.

Each of the six measures are described in detail and illustrated in the next section. The reader will note that thirty-seven colleges and universities are displayed on the graphics. Each of the five colleges in the Northeast Higher Education District as well as Northwest Technical College – Bemidji are counted separately along with the thirty-one other colleges and universities.
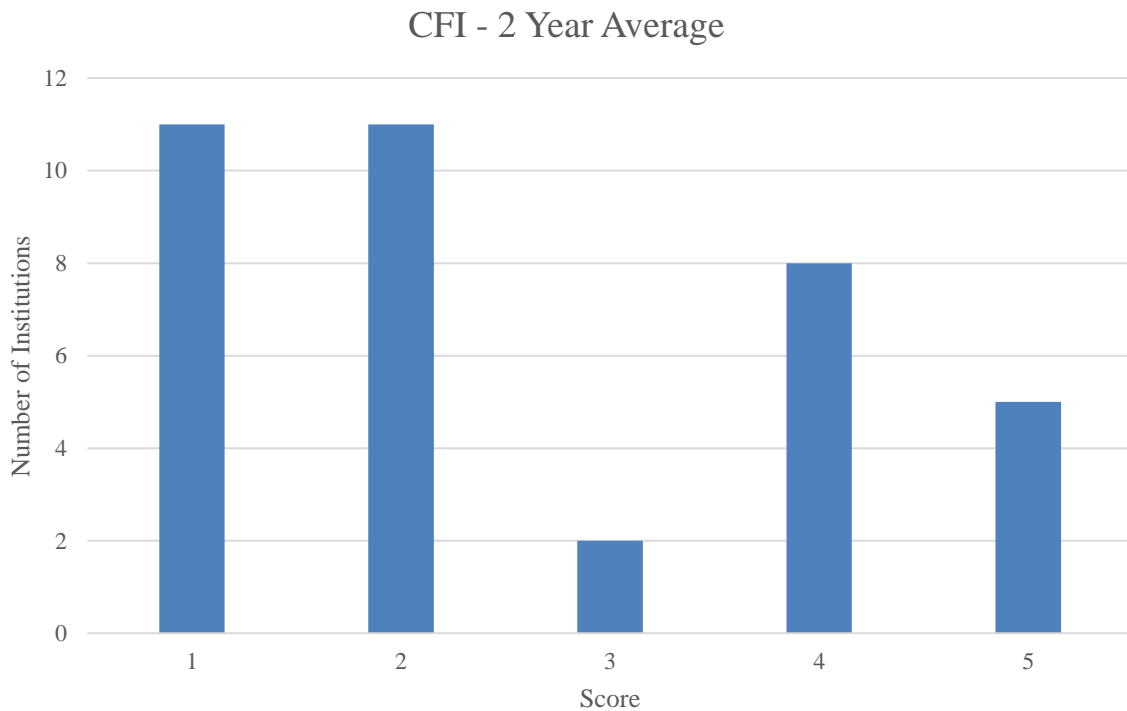
MEASURES

CFI Two Year Average

The Composite Financial Index (CFI) is a comprehensive measure of an institution's financial health. It includes four ratios: primary reserve, viability, return on net assets and operating margin. The primary reserve and viability ratios measure an institution's financial condition, the return on net asset and operating margin ratios measure an institution's annual financial performance.

The *CFI Two Year Average* calculates the average CFI for each college and university for fiscal years 2013 and 2014, the most recent data available. A two-year average is used in order to smooth some of the volatility in year to year CFI calculations.

Colleges and universities with a CFI two-year average:

- Over 4.0 received a rating of five
- Between 3.0 and 3.99 received a rating of four
- Between 2.5 and 2.99 received a rating of three
- Between 1.5 and 2.49 received a rating of two
- Less than 1.5 received a rating of one

The system's overall two-year average CFI score is 2.6; the median score was 2.0. The colleges alone averaged 2.9 and the universities averaged 1.4.

CFI - 2 Year Average


CFI Two Year Average - Graph 3

Net Income/Loss

The *Net Income/Loss* measure calculates net income/loss as a percentage of total revenue for fiscal year 2014. The measurement is calculated on the basis of full accrual accounting statements.

Colleges and universities with a net income:

- 3.0 percent or greater received a rating of five
- 2 to 2.9 percent received a rating of four
- 1 to 1.9 percent received a rating of three
- -0.9 to 0.9 percent received a rating of two
- Less than -1.0 percent received a rating of one

The system's overall net/income loss as a percentage of fiscal year revenue received a score of 1.7; the median score was 1.0. The colleges alone scored 1.9 and the universities scored 1.0.
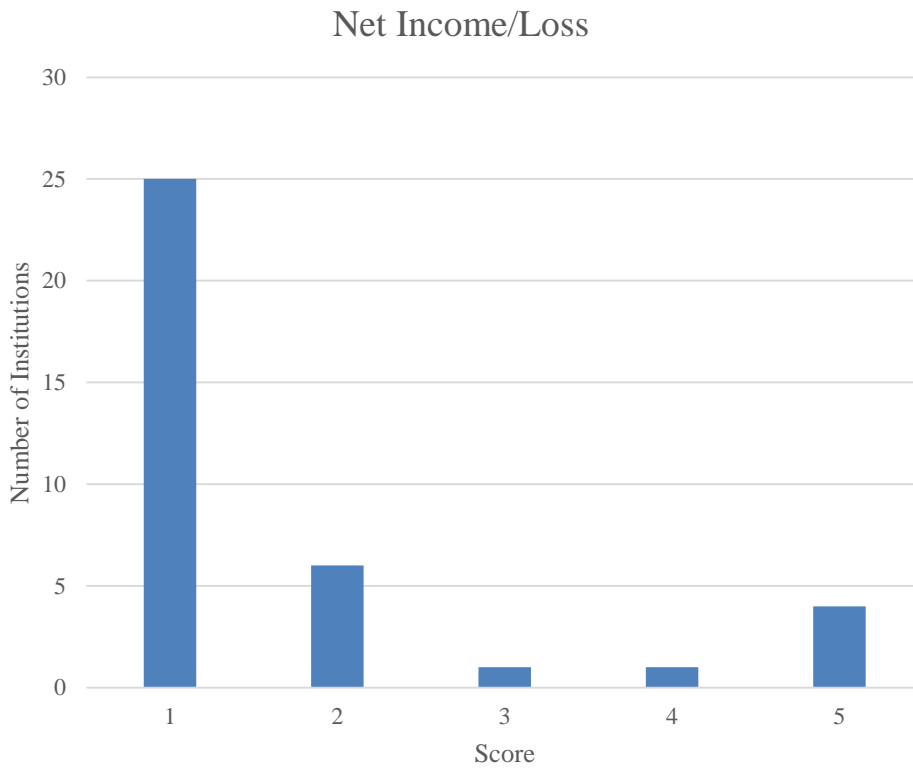
Net Income/Loss

Net Income – Graph 4

Cash Position

Strong cash balances provide colleges and universities with the resources needed to address unanticipated financial challenges, including larger than projected enrollment declines. The *Cash Position* measure calculates the general fund year-end cash balance as a percentage of new revenue, based on fiscal year 2014 data. The calculation is performed on cash basis results, not accrual basis.

Colleges and universities with a fund balance:

- Thirty percent or more of new revenue received a score of five
- Between twenty-five to twenty-nine percent received a score of four
- Between twenty to twenty-four percent received a score of three
- Between fifteen to nineteen percent received a score of two
- Less than fifteen percent received a score of one

The system's overall cash position received a score of 4.0; the median score was 5.0. The colleges alone scored 4.1 and the universities scored 3.9.
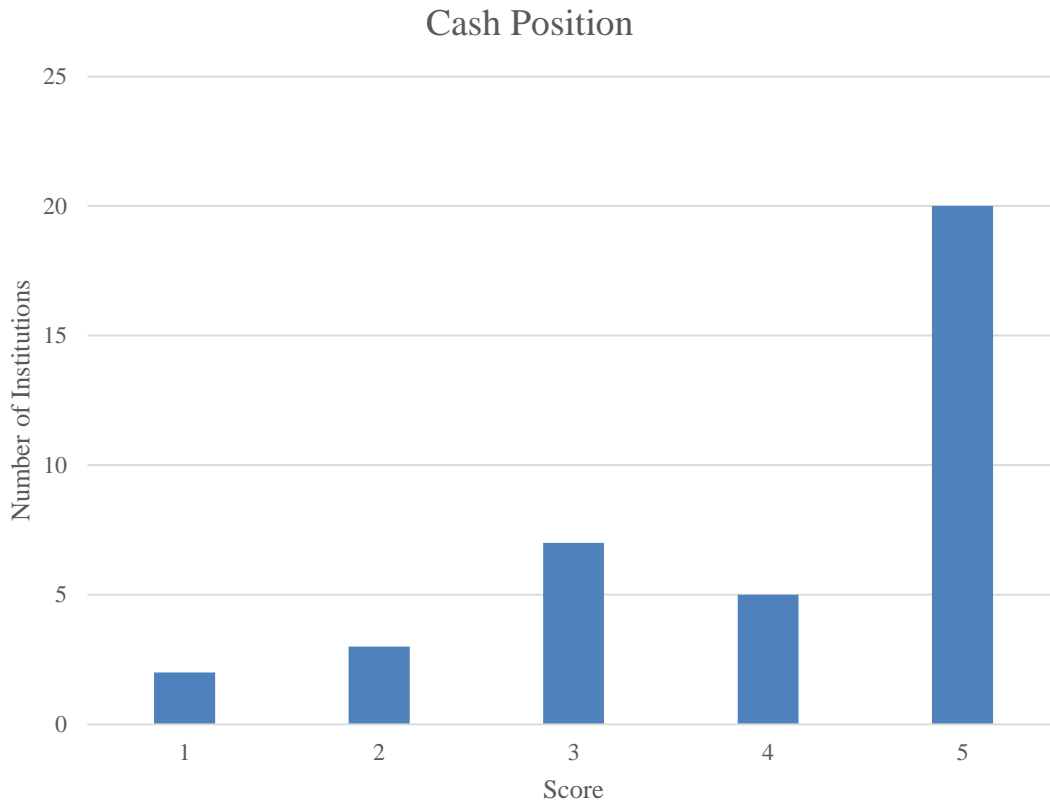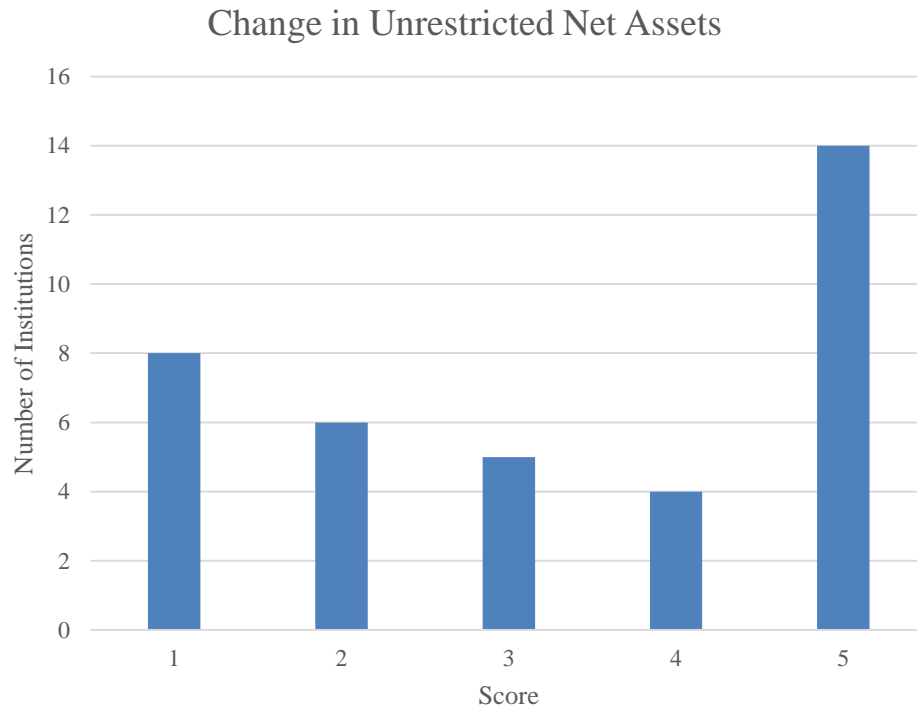

Cash Position – Graph 5

Change in Unrestricted Net Assets

Change in Unrestricted Net Assets (CUNA) is a measure of the percent change in unrestricted net assets between fiscal year 2011 and fiscal year 2014, as reported in the annual financial statements. Growth in unrestricted net assets illustrates additions to assets, rather than asset depletions and is a measure of financial health.

Unrestricted net assets with:

- Growth of more than thirty percent received a score of five
- Growth between eleven and twenty-nine percent received a score of four
- Growth between zero and ten percent received a score of three
- Decline of up to ten percent received a score of two
- Decline greater than ten percent received a score of one

The system's overall change in unrestricted net assets received a score of 3.3; the median score was 3.0. The colleges alone scored 3.3 and the universities scored 3.3.

*Change in Unrestricted Net Assets – Graph 6*

Enrollment Volatility

Enrollment Volatility measures the percent change in FYE enrollment from year-to-year for each college and university and calculates a standard deviation for a seven year period between fiscal years 2008 and 2014. The smaller the deviation over the seven year period the less volatile an institution's enrollment.

Colleges or universities with a deviation:

- Of one percent or less received a score of five
- Between two and four percent received a score of two
- Between five and seven percent received a score of three
- Between eight and nine percent received a score of two
- Over ten percent received a score of one

The system's overall enrollment volatility received a score of 3.1; the median score was 3.0. The colleges alone scored 2.9 and the universities scored 4.0.
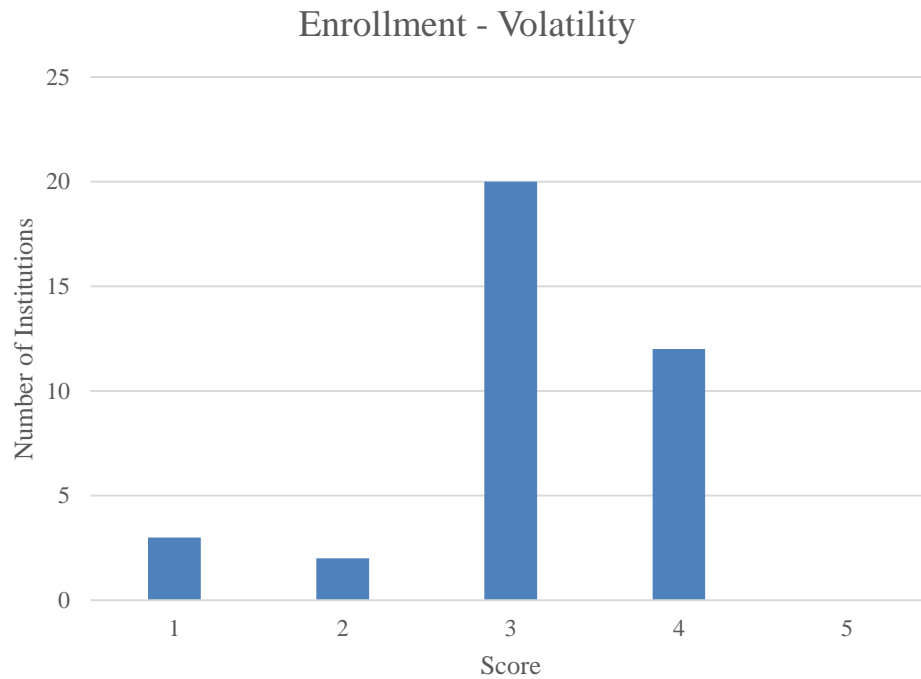

Enrollment Volatility – Graph 7

Enrollment Momentum

Enrollment Momentum measures the overall change in FYE enrollment, on a percentage basis, between fiscal years 2008 and 2014. The measure is designed to quantify how much enrollment has been recently gained or lost compared to the years of significant enrollment growth.

Colleges and universities with FYE enrollment increases:

- Ten percent or greater received a score of five
- Between eight and nine percent received a score of four
- Between five and seven percent received a score of three
- Between two and four percent received a score of two
- Less than one percent received a score of one

The system's overall enrollment momentum received a score of 2.5; the median score was 2.0. The colleges alone scored 2.6 and the universities scored 2.3.

Enrollment - Momentum
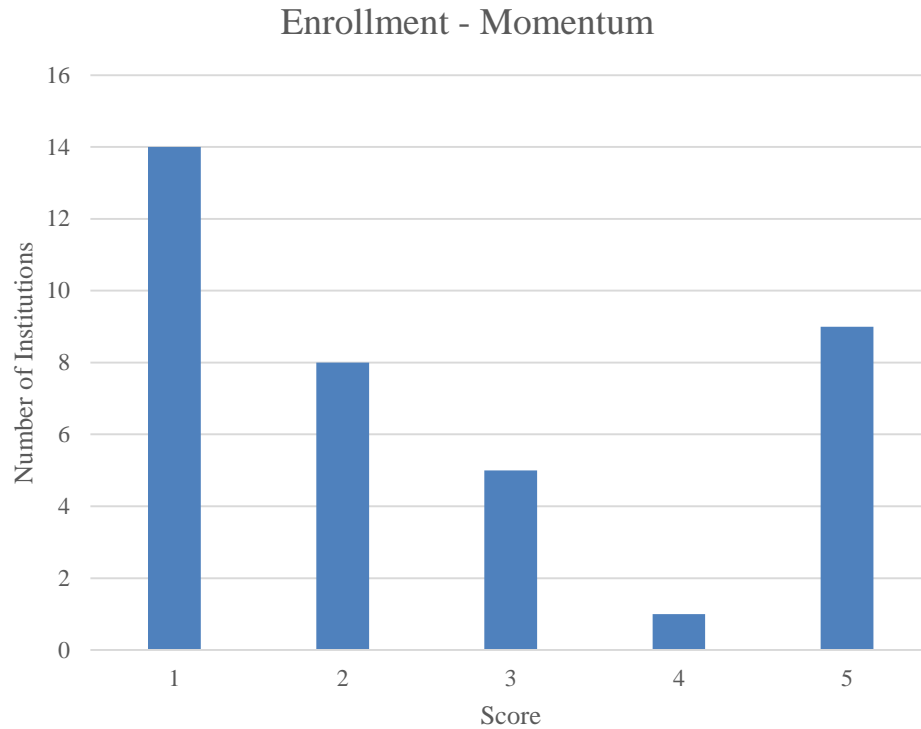
Enrollment Momentum – Graph 8

Date Presented to the Board of Trustees: January 28, 2015