Western Oregon UNIVERSITY

Western Oregon University Board of Trustees:
Finance & Administration Committee
Meeting No. 5 – October 13, 2016
Public Site: Werner University Center, Calapooia Room
9:00 AM – 1:00 PM

MINUTES

1) Call-to Meeting / Roll Call

In the absence of the chair, Ivan Hurtado called the meeting to order at 9:20 am.

Committee members present: Ivan Hurtado, Cec Koontz, Eric Yahnke (Vice President for Finance and Administration & CFO)

Others present: Penny Burgess (USSE), Jodi Daugherty (Eide Bailly), Reina Morgan (Assistant)

2) Chair's Welcome / Announcements

Hurtado thanked the committee for coming and asked if there were any announcements. VP Yahnke announced that Jodie Daugherty is leading the financial audit on campus and is present to update the committee on the work the auditing team is doing. Jodie shared that her team was here in July to start the process of testing federal awards and now has returned to continue with the process. Student financial aid is the biggest of the four programs they are testing. There are a lot of compliance items that need to be followed and some recent changes to those rules, but it shouldn't change much in terms of how our financial aid office actually processes things. Her team pulled information on 60 students and tests all of the financial aid that they receive. The things they look for include the student qualifying for the award, the disbursement of funds being done in accordance with the guidelines, appropriate funds being returned if a student withdraws, and the student meeting academic progress and grade requirements. The final report is due to the state on November 15th and we are on track to meet that deadline. Jodie will present the report at the January full Board meeting.

3) Approval of July 18, 2016 Draft Minutes

The approval of minutes is on hold as a result of not having quorum.

4) Discussion Items:

(a) FY16 Q4 Investment Report – Penny Burgess, CFA | Director of Treasury Management

Penny Burgess presented the fourth quarter FY 16 investment report, which includes the performance of the university's operating assets that are invested in the Public University Fund (PUF). She shared that in the materials the committee has a market commentary that provides a general discussion on the economy and market performance during the quarter. Market highlights that are underpinning investment performance include:

o British voters narrowly approving Britain's exit from the European Union. Shocked by the outcome, investors sought safety in fixed income as global markets reacted fiercely through the end of the quarter.
o The U.S. dollar climbed 7.0 percent versus the U.K. pound while declining 2 percent compared to a basket of foreign currencies.
o The Barclays U.S. Aggregate Bond Index gained 2.2 percent during the quarter; bond yields dropped to record lows overseas after the surprise outcome from the referendum in the U.K. The S&P 500 closed up 2.5 percent for the quarter, despite the price volatility during the quarter.

In regards to the University's investment returns, the PUF investments consist of an allocation to the following investment pools: the Oregon short-term fund, the Oregon intermediate-term pool, and the PUF long-term pool. The PUF investment return for the quarter was 1.0% and a positive 2.5% for the fiscal year ended June 30, 2016. The total market value of WOU's operating cash and investment deposits on June 30 was $47.5 million, equivalent to 10.3% of the total PUF balance of $463.2 million.

The Short-Term fund outperformed its benchmark for the quarter and year-to-date by 10 and 40 basis points respectively, and outperformed the 3-year benchmark return by 50 basis points. The Intermediate-Term Pool outperformed its benchmark for the quarter by 20 basis points while lagging the benchmark by 60 basis points for the fiscal year. The returns of the Long-Term pool lagged the benchmark for the quarter by 10 basis points and 140 basis points for the fiscal year.

At the beginning of the fiscal year, the State Treasury investment team believed the slow and steady growth in the U.S. economy would lead to rising short-term interest rates, creating price volatility for intermediate and longer term fixed income securities. Given this view, the portfolio manager positioned the Intermediate and Long-term pools with securities of shorter duration or maturities compared to their respective benchmarks. However, several economic events around the globe drove interest rates lower, fueling a bond market rally and resulting in the relative underperformance in the Intermediate-Term and Long-Term pools for the fiscal year.

During the quarter, the PUF administrator distributed over $198,000 of earnings to WOU.

There are some upcoming policy changes and investment strategies for the Public University Fund. The strategy changes target divestment from fossil fuel related securities and restrictions for future investment in fossil fuel related securities. The Vice Presidents for Finance and Administration from the six universities participating in the Public University Fund expressed a desire, earlier this year, to seek an investment strategy for their operating cash that would restrict investment into companies from fossil fuel related sectors such as oil, gas and coal mining.

To address the participant's request, Oregon State University in their role as the Designated University, collaborated with the Oregon State Treasury, OSU's investment advisor, PFM and the University Shared Services staff to design a portfolio strategy to incorporate fossil fuel restrictions, while maintaining a low-cost, total return strategy similar to the present PUF investment strategy. All strategy and policy changes have been reviewed and agreed upon by each participating university's Vice President for Finance and Administration. Additionally, the Oregon State Treasury and their oversight committee, the Oregon Investment Council have reviewed and approved of the investment strategy and policy changes.

At present, the three PUF investment pools do not restrict investment into fossil fuel related companies. In order to begin a divestment from fossil fuel exposure and incorporate a policy restriction, a new investment portfolio will be established by the Oregon State Treasury which I will refer to as the Fossil Fuel Free Fund. The new Fossil Fuel Free Fund will replace the investment allocations into the Oregon Intermediate-Term pool and the Long-Term pool.

The new Fossil Fuel Free Fund will combine many elements of the existing Intermediate-Term Pool and Long-Term Pool portfolios. As a result, the PUF's share of securities owned in the Intermediate-Term Pool and Long-Term Pool will be transferred into the new fossil fuel free portfolio with the exception of any existing investments in fossil fuel securities. Cash will be received in exchange for the restricted fossil fuel related securities and reinvested into securities from sectors in compliance with the policy. For the purposes of the new investment strategy, restricted fossil fuel companies are defined by the Fossil Free Indexes globally recognized list of the world's top 100 oil and gas companies and top 100 coal mining companies as measured by their calculated carbon emissions derived from reported proven reserves, also known as the Carbon Underground 200.

The liquidity portion of the investment strategy will continue to be directed into the Oregon Short-Term Fund. While the Short-Term Fund's investment policy does not restrict investment into the fossil fuel related securities and there are no expectations the policy will be amended to include such a restriction, the State Treasury investment team has recently advised, the team has no intentions of purchasing new securities from the fossil fuel related sectors. As such, the Oregon Short-Term Fund's current 1.1% allocation to fossil fuels is slated to mature over the next 18 months, eliminating the allocation by March of 2018. A quarterly compliance monitor will be established to review exposures to the companies listed on the Carbon Underground 200 list. Fossil-fuel strategy updates will also be requested during quarterly conference calls with the investment managers.

Given the PUF's total allocation to the fossil fuel sector is approximately 1.7% of invested assets, the divestment from these securities results in minor changes to the portfolio composition and overall characteristics. A conservative estimate of the gross investment yield will remain unchanged at 1.6% after divestment, generating just under $8 million dollars on an average portfolio of $512 million. One benefit from combining the Intermediate-Term Pool and

Long-Term Pool strategy into one investment portfolio is a small reduction to the investment management fees of approximately 13% or $18,000.

The investment strategy changes if approved by the Designated University's Board of Trustees, require changes to the PUF investment policy. The primary changes affect Portfolio Rules 3 through 10. Portfolio Rules 3,4 and 8 capture the investment strategy changes moving from three investment pools to two and defining the fossil fuel restriction and how it will be monitored per the Carbon Underground 200 list.

A custom benchmark to measure the performance of the new fossil fuel free portfolio strategy is defined in Portfolio Rule 10 as: 75% weighted to the Bloomberg Barclays U.S. Aggregate 3-5 year index and 25% to the Bloomberg Barclays U.S. Aggregate 5-7 year index. The 3-5 year aggregate index was the benchmark for the Oregon Intermediate-Term Pool and the 5-7 year aggregate index was the benchmark for the Long-Term Pool. To address the issues of relative portfolio underperformance associated with active management or active decisions compared to the benchmark, two portfolio rules have been modified. The allowed variance in the average modified duration or average maturities of the new portfolio's securities compared to the stated benchmark has been modified to +/- 10% from +/- 20% in Portfolio Rule 7. Secondly, the performance expectations have been modified to performing "in-line" with the stated benchmark from the current "outperform" the stated benchmark addressed in Portfolio Rule 10.

In Summary, the Public University Fund's transition to a fossil fuel free investment strategy can be easily executed, resulting in the immediate divestment of the fossil fuel related securities held in the Intermediate-Term Pool and Long-Term Pool and a gradual divestment from exposures in the Short-Term Fund with full divestment anticipated by March 2018. However, no guarantees can be made regarding future investments to fossil fuel related sectors within the Short-Term Fund.

The reinvestment of the proceeds, received from divestment, will be directed into securities with similar income and return characteristics, resulting in minor anticipated changes to the Public University Fund's income or gross portfolio yield of 1.6%. The investment policy changes reflect the strategy changes mentioned and modify the active investment management guidelines by lowering the allowed variance in average maturity of the underlying securities compared to the benchmark to +/- 10% and seek a total portfolio return in-line with the stated custom benchmark.

(b) Capital construction update

VP Yahnke shared that the opening of the new Richard Woodcock Education Center went very well. There were a lot of people in attendance, including long time alumni, Richard Woodcock, and the governor. The building was well prepared and there was a good opening ceremony. In the completion of the project there were some questions about the use of bond money for furniture. It would be nice to be able to see funding up front in the future rather than having to wait until after the fact to provide receipts to get the funding through a burdensome process. In the grant and loan agreements it states that reimbursements will be receive within two weeks but there are millions of dollars owed that have been delayed six or more weeks.
VP Yahnke also shared that the recruitment is under way for an associate director for the Physical Plant, with the hope of bringing them on board before the director retires. The selection

has been narrowed down to two candidates and references are currently being checked on one of them. They both have experience in the public sector.

We formally broke ground on the new student health building. Building permits and system development charges from the city are coming in higher than planned. VP Yahnke said he is hoping for some partnership with the city given that it is a university building and a health care facility. Koontz shared that there are currently several positions open on city council so it could be a very different council in three months than it is now.

VP Yahnke shared that he received some questions from DAS regarding OMA, ITC, and Natural Science Building projects. One question was in regards to whether they are for public or private use. Another question was about having the bond match in hand for the requests. VP Yahnke was happy to be able to respond that we do indeed have the money in hand and are ready to go. Hopefully that will help it move forward. A concern has been voiced to HECC about the big institutions outgrowing us in E&G square footage. VP Yahnke suggested perhaps only including buildings that are 10 years or older because new buildings shouldn't have repair needs. Our building inventory that was submitted doesn't currently have the new education building or the OMA building on it so VP Yahnke will be getting those added.

5) Action Items

(a) FY17 Q1 Management Report

VP Yahnke presented on the management report. At this point what was projected matches what was budgeted because we are so early on. There are still a number of budgeted positions that are vacant so we are expecting vacancy savings again this year. There are between 10 and 15 positions that are generating savings at this point, but it is too early to give a dollar amount. We have a projected fund balance of 17%. The state appropriation settle up for last year came in and there was no change to that dollar amount from what we were expecting. There are however some concerns in the FY 17 funding allocation true up summary. Those concerns are in regards to receiving less than projected in the activity based, outcomes based, and stop loss/stop gain adjustment. We received additional dollars in regional support funding due to enrollment being down and enrollment in Willamette Promise really helped us out. A major concern going forward is the stop loss/stop gain provision. It helped us out this time around, but there is a phase out period and we won't have that luxury going forward.

Tuition revenue was originally budgeted at a 5% decline in enrollment. The census date isn't until the end of the fourth week of the term so we don't currently have the final numbers. The fee remission budget is down from the prior year actual. This reduction reflects enrollment being down and an increase in rates. The amount in capital outlay was primarily for technology purchases. The transfers out was to support athletics, primarily for salaries and OPE for coaches and administrators. Expenditures and transfers out are comparable to what has been done in past years. There some increases for the incidental fee rate and we may see further variance there driven by the enrollment decline as we are trying to maintain the current service level with a smaller student base. The board members who were in attendance reviewed the management report and felt that it was acceptable. Koontz stated that had enough members been present should would've moved to recommend it to the board for approval.

(b) FY17 Initial Budget

VP Yahnke went over the FY 17 budget and pointed out several new features in the budget book. There is a new organization chart style visual that makes it easier to quickly see where the funds are allocated. For those who want to dive in deeper there are schedules that break out detail of those totals. There is also an organization chart that shows the budget oversight and development. This details out the existing process and says who gets budget worksheets and monthly budget/status reports for each department. The expectation is that the people in charge of their department's budget are involving department constituents. People will be able to easily see who in their department they should go to if they have questions about their budget or wish to know why funds were allocated a certain way. New this year there is also a history on lottery funding and the progression of the incidental fee.

We had been planning on a PERS increase of 3-3.2%. The actual increase was 5.21%.

The AIC committee is a faculty senate subcommittee that reviews proposals and makes recommendations on funding for technology and capital improvements. This past year the committee decided to only take on technology requests so they received $100k worth of funding instead of the usual $200k. The $100k for capital was transferred out and put in the capital improvement fund. The majority of that ended up being spent remodeling and sound proofing parts of Smith Music Hall. The AIC is asked to consider any and all proposals and provides us a good mechanism for seeing what is out there that needs to be funded. There is a possibility of extending the funding beyond the $200k if there is a need for it and the funding is available.

There will be a new budget committee that reviews the base budgets as well as the requests for enhancements. Koontz voiced that there will be complications due to people across campus not being familiar with budget stuff and not understand it all. You almost need a 10 hour orientation so people know what they're looking at. VP Yahnke shared that it's a modified zero based budget. It starts out with the amount from the year before and then the focus is on what they *strategically* need differently from the year before. He shared that they also look at the mix of tenure track and non-tenure track within the department. The expectation is for the budget committee to have a revised budget by July 1st. The process will change the timing of things, but shouldn't be a burden and the benefits of the new process far outweigh the challenges of moving to a new way of doing things.

Koontz shared that she feels a big point of confusion for people is regarding the fund balance. They want to know why we can't use that money and why can't carry over the money that they didn't spend the prior year. VP Yahnke shared that if a department has significant savings that they want to use there is the potential of being able to use it if they can show what they want to do with it and how it will support the mission. He also shared that at the end of the year we look at what some of the University's bigger, broader needs are and will use any extra money on those things so it is really important for departments to not overspend because it reduces what we are able to use for addressing our larger needs.

Koontz gave an example at her workplace of taking the unspent dollars and putting it into a reserve for the increasing PERS costs that they knew would be coming. If they had instead used that money to hire additional aids then that would have been an ongoing cost for future years that then would always have to be budgeted and in those years there may not be those same savings to be able to cover that expense. It is the difference of a one-time expense versus an ongoing expense. Money that is leftover one year is not guaranteed to also be leftover in future years.

Koontz suggested that VP Yahnke hold some presentations on the budget process as part of the strategic planning work that is underway. She will put together a proposal, agenda, and suggested timeline for VP Yahnke to use.

VP Yahnke provided an update on a request from HECC regarding the funding scenarios. In order to keep tuition rates at a 5% increase in year two of the biennium, an increase of 25% would be needed in the first year. This would be an increase of $818 per student. The promise cohorts would be excluded from the increase since they are locked in at their current rate. These figures assume no cuts and flat enrollment.

HECC is doing an evaluation of all of the Oregon public universities. The document on WOU is still in draft form, but will include things such as student teacher ratio, strategic initiatives, financial ratios, participation in USSE, and details about the Board and how it operates.

Earlier this fall the decision making and response teams on campus participated in a tabletop exercise where they worked through different scenarios and on October 20th WOU will be participating in the Great Shakeout. The idea will be to address it as if it is a real earthquake. If there is an earthquake or other natural disaster WOU has insurance coverage through the PURMIT. If the committee is interested our General Counsel or Public Safety director could present to them on our coverage. VP Yahnke also shared that we received a rebate on our workers' compensation insurance for the seventh year in a row.

6) Updates and Around-the-Table / Board meeting prep

Hurtado will give the committee report at the full board meeting. He will be discussing budget and the quarterly management report and providing highlights on the audit, investment report, investment policy, capital updates, and the change in funding for WOU.

7) Adjournment

The meeting was adjourned at 12:52 pm.