A FIVE-YEAR FINANCIAL PLANNING MODEL

AT LONE STAR COLLEGE, A 'LIVING DOCUMENT' OF INSTITUTIONAL FINANCES HELPS THE BOARD SET PRIORITIES AND EXPLORE 'WHAT-IF' SCENARIOS.

BY STEPHEN C. HEAD

AS A COMMUNITY COLLEGE BOARD MEMBER, FEW ISSUES ARE MORE difficult to understand fully than the finances of the institution. Board members generally have three major roles: 1) hiring the chancellor or president, 2) approving policies, and 3) overseeing and approving finances. The first two are largely process driven and involve common sense, legal issues, and community norms. Finance is a uniquely separate issue, and unless you are a CPA or you hold an MBA, reviewing finances can be a daunting task at times.

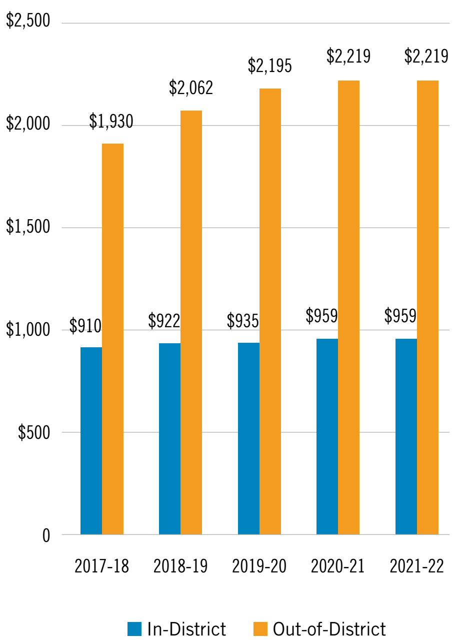
The normal scenario for budgeting and finances looks like the following: If you were a trustee in Texas, you would be one of six to nine members elected to a community college board. While you should understand spreadsheets and financial reports, it is likely that you would have limited background in the actual management of the college. The college leadership comes before the board in late spring with budget proposals for some combination of tuition and fees, as well as state and local funding dollars and miscellaneous revenues. When the board meets to review the budget, the questions focus on state appropriations, tuition and fees, local tax rates (in most cases, you are not on the board to raise taxes), pay raises, enrollment growth or decline, and miscellaneous expenditures proposed by the administration. Most board members are sensitive about "micro-managing," and while they may have legitimate questions about long-term financial consequences because they are successful in their own careers, few board members are likely to know the questions to ask. Nor would the average board member know whether the given answers are accurate.

Lone Star College, located in the north metropolitan Houston area, is one of the largest and fastest-growing

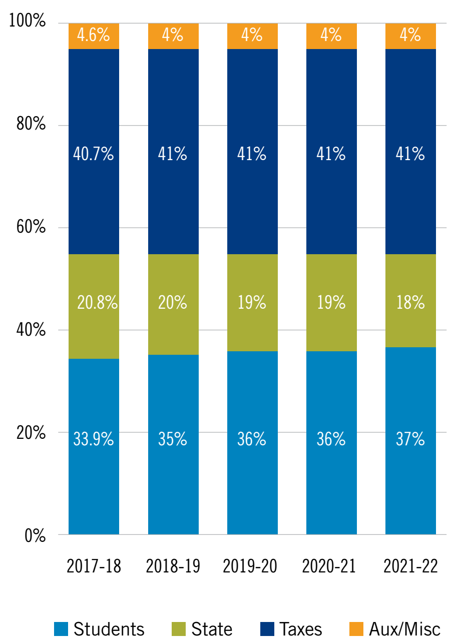
LONE STAR COLLEGE FIVE-YEAR FINANCIAL PLAN

REVENUES

TUITION/FEES FOR 12 CREDIT HOURS

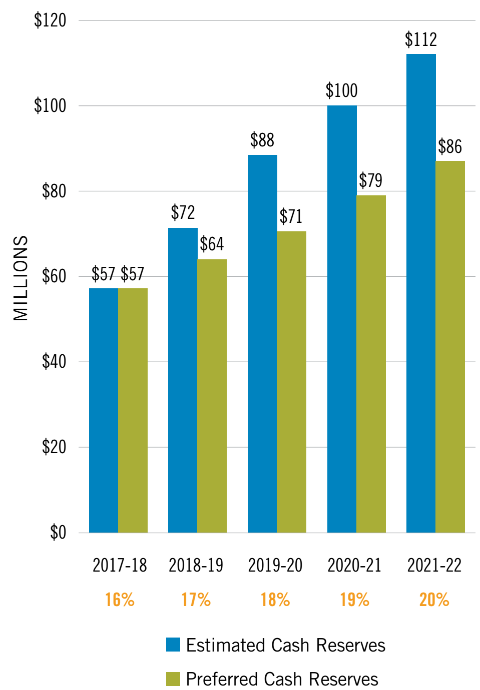


FUNDING SOURCES



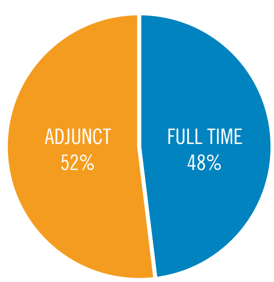
CASH RESERVES

ESTIMATED CASH RESERVES

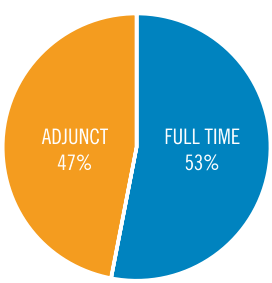


EXPENDITURES

2017-18 FACULTY TEACHING RATIO



2021-22 FACULTY TEACHING RATIO



STUDENT SUCCESS IS OUR FIRST PRIORITY, BUT WITHOUT A SOLID FINANCIAL FOUNDATION BASED ON FACTS AND LONG-TERM PLANNING, IT IS DIFFICULT TO SUSTAIN CREATIVITY, INNOVATION, AND HIGH PERFORMANCE.

community colleges in the country, featuring six comprehensive colleges and 10 centers with over 95,000 credit-earning and non-credit students each semester, an annual budget exceeding $500 million, and 7,300 employees spread over a 2,100 square mile service area. Therefore, having an in-depth knowledge of the budget is critical to the success of a high-performing institution.

When I was named chancellor in 2014, one of my key initiatives was to have discussions with the board (and college administrators) about key revenue and expense issues using a "living document" so they could see how changes in one year impacted revenue or expenses in years two, three, four, five, and beyond. For example, at Lone Star College:

- Every 1 percent increase in salaries permanently adds $1.7 million to the budget
- A 1 percent increase in the fund balance represents $3.75 million
- 5 million square feet of older facilities need repair and renovation on a planned and regular basis
- New facilities (LSC is in the midst of a $485 million bond program) mean additional costs for staffing, utilities, and supplies
- Refreshing 17,000 computers and other instructional equipment on a schedule requires planning.

Lone Star's Five-Year Plan involves several specific decisions by the board and administration. The first decision was agreement on general philosophy. Working together, we decided that students would generally pay 35 percent of the total cost of education, local taxpayers would pay 40 percent, and the state contribution — a steadily declining amount of the total budget — would be 20 percent. Grants and miscellaneous revenue account for the remainder. Those numbers could fluctuate slightly if the state reduces its contribution or if the local assessed value increases or declines. These parameters form the basis of guidance in our financial decision-making.

The second major decision on the Five-Year Plan included the selection of revenue and expense variables. Basically, we took known and projected revenues and then factored in estimates for years two, three, and beyond. These variables include compensation changes, tuition and fee rates, tax rates, state appropriations, workforce equipment, special projects, new staffing, additional faculty, and about a dozen local issues.

The Five-Year Plan has two major components (see accompanying charts). The budget overview itself is a one-page spreadsheet and details revenues and expenses over a five-year period in a clean manner. The basic formatting starts with Year 1 but allows different scenarios to be explored with the board using "what-if" analysis. If a board member asks about the possibility of pay raises in future years, the impact can be seen immediately. If another board member asks about state revenues or local tax rates, we can change those numbers and show the impact. The administration initially inputs the assumptions, but changes can occur as different scenarios evolve.

The second major component of the plan involves charts and graphs that monitor the tuition-and-fees percentage, the tax percentage, the state contribution, and a minimum 16 percent fund balance. So if we believe that the state contribution will decrease as a percentage of our operating budget (a reality), we can see how that impacts the budgeting philosophy of 35 percent student tuition and fees, 40 percent tax revenue, 20 percent state funding, and the 16 percent fund balance. Any changes in the revenue-and-expenses column have an impact on those percentages.

An auxiliary piece of the Five-Year Plan is how we distribute funds among the colleges and system office. At Lone Star College, the distribution is based on a formula allocating 40 percent to the system office (police, HR, financial aid, information technology, and other system functions) and 60 percent of new money to the colleges based on performance metrics that focus on systemwide goals and growth.

Student success is our first priority, but without a solid financial foundation based on facts and long-term planning, it is difficult to sustain creativity, innovation, and high performance. One unexpected benefit of the Five-Year Plan was that our credit rating agency — LSC is AAA rated — noted that no college they worked with had such a model. We believe the Five-Year Plan allows us to present the finances to the board, our employees, and the community in an open, transparent, and businesslike manner.

Stephen C. Head is chancellor of the Lone Star College in Texas.