MINNESOTA STATE
Board of Trustees

AGENDA ITEM SUMMARY

NAME: Finance and Facilities Committee **DATE:** October 19, 2022

TITLE: FY2023 Operating Budget Update

☐ Proposed New Policy or Amendment to Existing Policy ☐ Approvals Required by Policy ☐ Other Approvals

☐ Monitoring/Compliance ☒ Information

PRESENTERS
Bill Maki, Vice Chancellor for Finance and Facilities
Steve Ernest, System Director, Financial Planning & Analysis

PURPOSE

This item provides the Board of Trustees with an update on the Fiscal Year 2023 Annual Operating Budget for the System.

The Board approved the annual operating budget at its June 22, 2022, meeting. Based on experience to date, colleges and universities have updated their budgets for the year.

BACKGROUND INFORMATION

When the System's fiscal year 2023 Annual Operating Budget was approved in June, the operating budget assumed a 2.2 percent decline in enrollment over fiscal year 2022. Now that summer term has concluded and fall term is well underway, annual enrollment for fiscal year 2023 is projected to decrease more than 2.2 percent

Colleges and universities provide updated enrollment projections three times during the fiscal year typically in October, February, and May. Our current projections for fiscal year 2023 now show a 3.8 percent decrease in enrollment over fiscal year 2022 or a decline of 1.6 percent more than projected when fiscal year 2023 operating budgets were approved last June.

This report provides the Board with updated fiscal year 2023 budget numbers for the System, including revised projections for enrollment, revenues, and expenditures. On an all-funds basis, the October revision of the fiscal year 2023 budget has a slightly more negative outlook than the budget approved by the Board in June. Specifically:

- For the System as a whole, enrollment is lagging behind where it was projected to be in the June fiscal year 2023 budget.

- Operating revenues are projected to decline more than operating expenses after updating fiscal year 2023 enrollment projections. Operating costs are relatively unchanged over what was originally budgeted in June, however inflationary pressures continue to reduce purchasing power

- Federal COVID-19 Higher Education Emergency Relief Funds (HEERF) and the use of fund balance, which are both one-time in nature, are a slightly larger portion of the overall sources than they were in the June fiscal year 2023 budget.

BUDGETS APPROVED JUNE 22, 2022

On an all-funds basis, the fiscal year 2023 operating budget approved in June (Table 1) showed revenues 8.1 percent lower than the fiscal year 2022 budget at that time. Most of the decrease was in federal HEERF revenues illustrating the colleges and universities spend down of these one-time funds. June expenditures were also budgeted 9.4 percent lower than fiscal year 2022 which is reflective of less HEERF funding in our overall operating budget. After transfers in of HEERF dollars, the all-funds budgetary balance was projected to be a positive $11.4 million.

Table 1
Fiscal Years 2022 and 2023 All Funds Operating Budget, June 2022

$s in millions	FY2022 Current Budget	FY2023 Proposed Budget	$ Change	% Change
Sources				
General Fund	$1,657.9	$1,683.6	$25.7	1.6%
Revenue Fund	$102.5	$108.0	$5.5	5.3%
Other Funds	$302.8	$285.9	($16.9)	-5.6%
HEERF Funds	$242.2	$41.5	($200.7)	-82.9%
Sources Total	**$2,305.5**	**$2,119.0**	**($186.5)**	**-8.1%**
Expenses				
Compensation	$1,353.1	$1,366.6	$13.5	1.0%
Operating costs	$998.6	$763.0	($235.6)	-23.6%
Expenses Total	**$2,351.7**	**$2,129.6**	**($222.1)**	**-9.4%**
Budget gap	**($46.2)**	**($10.6)**		
HEERF transfer in	**$86.8**	**$22.0**		
Budget balance	**$40.6**	**$11.4**		

As illustrated in Table 2, the General Fund operating budget approved in June showed only a 1.6 percent increase in sources from the prior budget, but all of it is of a one-time nature as $50.2 million of programmed fund balance is being used to balance the budget or to support projects as specific colleges or universities. In addition, after transfers in of HEERF dollars for lost revenue, the fiscal year 2023 general fund budgetary balance was projected to be a positive $2.9 million.

Table 2
Fiscal Years 2022 and 2023 General Fund Operating Budget, June 2022

$s in millions	**FY 2022 Current Budget**	**FY 2023 Proposed Budget**	**$ Change**	**% Change**
Revenue/Sources				
State appropriation	$792.0	$789.5	($2.5)	-0.3%
Tuition	$707.1	$712.7	$5.6	0.8%
Other revenues	$140.1	$131.2	($9.2)	-6.5%
Programmed fund balance	$18.4	$50.2	$31.8	172.7%
Total budgeted	**$1,657.9**	**$1,683.6**	**$25.7**	**1.6%**
Expenses/Uses				
Compensation	$1,249.9	$1,267.1	$17.2	2.6%
Operating costs	$454.1	$435.3	($18.8)	-4.1%
Total budgeted	**$1,704.0**	**$1,702.4**	**($1.6)**	**-0.1%**
Budget gap	**($46.1)**	**($18.8)**		
HEERF transfer in	**$74.9**	**$21.7**		
Budget balance	**$28.7**	**$2.9**		

**Numbers may not add due to rounding.*

ENROLLMENT UPDATE
Enrollment continues to be a major concern for many of our colleges and universities. Since fiscal year 2011, enrollment has decreased by nearly 50,000 full year equivalent (FYE) students which equates to a 32 percent decline. During the pandemic, enrollment declined at a faster pace. Almost 30 percent or 14,449 of the 50,000 FYE decline occurred between fiscal years 2020 and 2022.

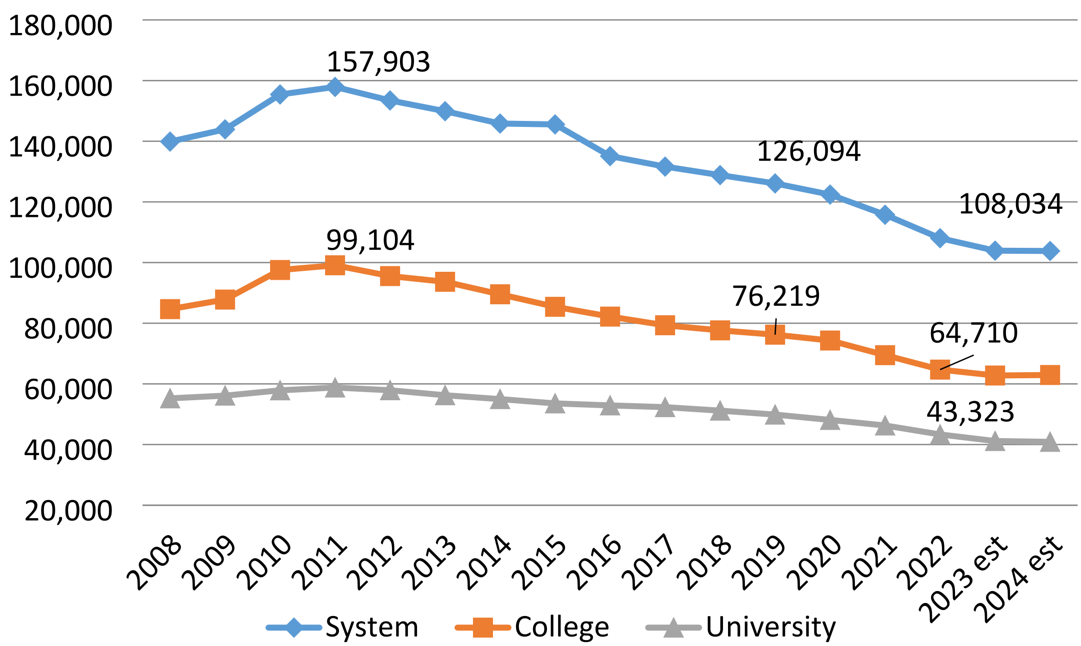
Enrollment projections for the system have weakened since the June budget was approved. Table 5 shows the system-wide enrollment change for fiscal year 2023 compared to fiscal year 2022 is now projected to be down by 3.8 percent from actual fiscal year 2022 levels compared to the 2.2 percent decline assumed when the fiscal year 2023 operating budget was approved in June. Projected college enrollment decline has gone from 2.2 percent to 3.0 percent compared to last year. Projected university enrollment decline has gone from 3.0 percent to 5.0 percent compared to last year.

Table 5
System FYE Enrollment Outlook for Fiscal Year 2023

FY2023 Compared to FY2022	June Enrollment Projections	June Enrollment FYE Projection	October Enrollment Projections	October Enrollment Projections
Colleges	-2.2%	63,430	-3.0%	62,763
Universities	-3.0%	42,039	-5.0%	41,160
System	-2.2%	105,469	-3.8%	103,923

Five of the seven universities are projecting enrollment below their June projections; over half of colleges are now projecting lower enrollment than they did in June. On the other hand, there are around ten colleges still projecting increased enrollment over fiscal year 2022 which is an improvement from the past few years. Unlike a year ago when the Delta variant of COVID-19 and the economic uncertainty involving the pandemic had a significant impact on enrollment, our continued loss of enrollment may be attributed to a strong job market where more businesses are seeking employees than the amount of people seeking employment. Potential students possibly are foregoing higher education in order to take advantage of more employment opportunities and opportunities with significant incentives businesses are using to attract new employees. In addition, demographic changes will continue to put pressure on our enrollment in the long-term.

Chart 1
Historical and Projected Enrollment for the System



Historic actual and projected enrollment by college and university is attached to this report.

REVISED FISCAL YEAR 2023 ALL FUNDS AND GENERAL FUND BUDGETS UPDATE

Fiscal Year 2023 All Funds Operating Budget

The fiscal year 2023 all funds operating budget update (Table 6) shows modest changes in revenues and expenses since June. Overall, revenue projections have decreased by $4 million from what was reported to the Board in June which is only a 0.2 percent drop. Expenses are essentially flat compared to June. Budgetary gaps grew in all funds which increased our use of programmed fund balance and reliance on HEERF funding to cover lost revenue.

Table 6
Fiscal Year 2023 All Funds Updated Operating Budget, October 2022

$s in millions	FY2023 Approved Budget	FY2023 Updated Budget	$ Change	% Change
Revenues/Sources				
General Fund	$1,683.6	$1,678.8	($4.8)	-0.3%
Revenue Fund	$108.0	$106.6	($1.4)	-1.3%
Other Funds	$285.9	$290.9	$5.0	1.7%
HEERF Funds	$41.5	$38.7	($2.8)	-6.8%
Total budgeted	**$2,119.0**	**$2,115.0**	**($4.0)**	**-0.2%**
Expenses/Uses				
Compensation	$1,366.6	$1,366.6	$0.0	0.0%
Operating costs	$763.0	$763.5	$0.4	0.1%
Total budgeted	**$2,129.6**	**$2,130.0**	**$0.4**	**0.0%**
Budget gap	**($10.6)**	**($15.0)**		
HEERF transfer in	**$22.0**	**$25.0**		
Budget balance	**$11.4**	**$10.0**		

**Numbers may not add due to rounding.*

Updated fiscal year 2023 operating budgets by college and university are attached to this report.

Fiscal Year 2023 General Fund Operating Budget

The impact of continued enrollment decline is better illustrated by the impact it has on tuition revenue in the General Fund. Since the June Board report, the additional enrollment decline at many of our colleges and universities results in a $9.6 million reduction in tuition revenue or a 1.4 percent decline. Some of the loss will be resolved by reductions in expenses. Personnel costs are anticipated to decrease by $2.3 million, but due to inflationary pressures on goods and services, our operating costs increased slightly by $1.2 million. Because the tuition loss cannot in the short-term be completely resolved by reductions in spending, colleges and universities are using more programmed fund balance and turning to HEERF funds (if they have funds remaining) to cover lost revenue due to enrollment declines (Table 7).

Table 7
Fiscal Year 2023 Updated General Fund Operating Budget, October 2022

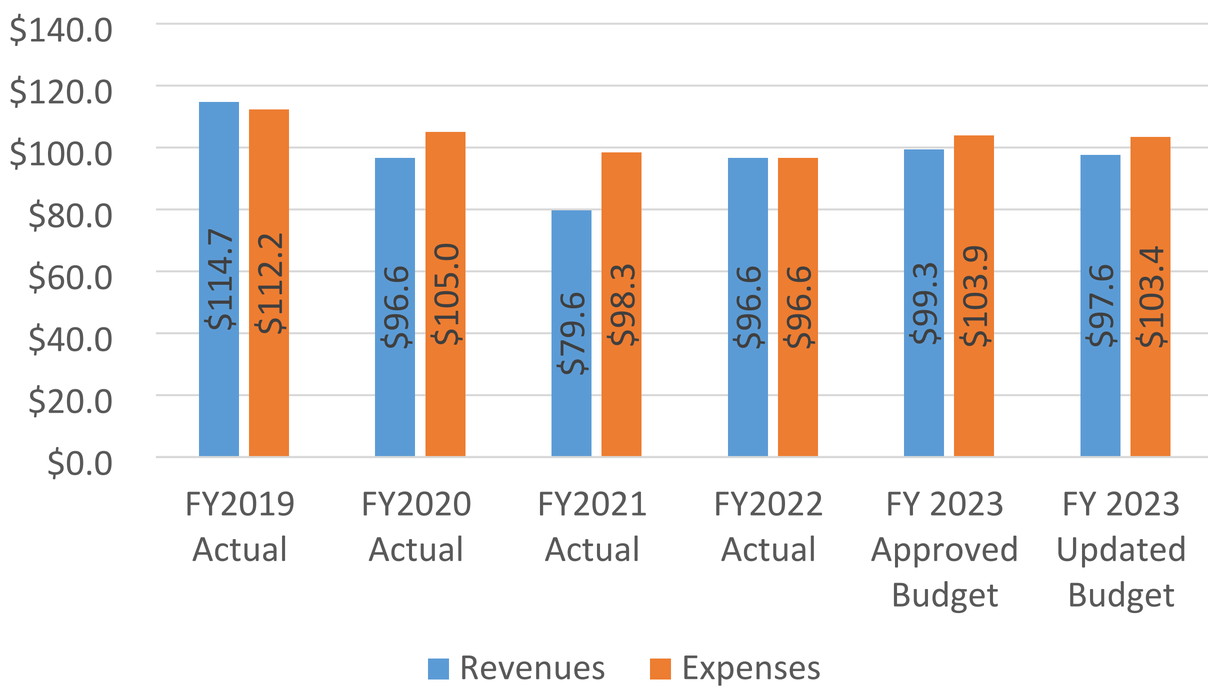
$s in millions	FY 2023 Approved Budget	FY 2023 Updated Budget	$ Change	% Change
Revenues/Sources				
State appropriation	$789.5	$789.5	$0.0	0.0%
Tuition	$712.7	$703.0	($9.6)	-1.4%
Other revenues	$131.2	$131.1	($0.1)	-0.1%
Programmed fund balance	$50.2	$55.2	$5.0	10.0%
Total budgeted	**$1,683.6**	**$1,678.8**	**($4.8)**	**-0.1%**
Expenses/Uses				
Compensation	$1,267.1	$1,264.8	($2.3)	-0.2%
Operating costs	$435.3	$436.5	$1.2	0.3%
Total budgeted	**$1,702.4**	**$1,701.3**	**($1.1)**	**-0.1%**
Budget gap	**($18.8)**	**($22.4)**		
HEERF transfer in	**$21.7**	**$24.3**		
Budget balance	**$2.9**	**$1.9**		

**Numbers may not add due to rounding.*

REVENUE FUND

In addition to providing the Board of Trustees with an overview of the Revenue Fund budget approved in June compared to changes made this fall, Chart 2 shows the Revenue Fund revenues and expenses each year since fiscal year 2019 before the significant impact resulting from the pandemic. Although the Revenue Fund has recovered slightly in fiscal years 2022 and 2023, revenue overall is $17 million less in fiscal year 2023 compared to fiscal year 2019. The gap between revenues and expenses were covered during this time period using HEERF funds and fund balance to offset lost revenue due to declining enrollments and occupancy in residential housing.

Chart 2
Revenue Fund Revenues and Expenses, Fiscal Years 2019-2022 Actual & 2023 Budgeted



The activities in the Revenue Fund include residential housing (room and board), wellness facilities, parking, and student unions. Residential Housing makes up 74 percent of overall Revenue Fund revenues. Between fiscal years 2019 and 2023, there was a reduction in residential beds used of 29 percent at the six state universities offering residential housing. While fiscal year 2022 saw a slight rebound from the low bed utilization in fiscal year 2021, fall 2022 bed utilization indicates an additional loss, bringing the estimated total loss in beds used between fiscal years 2019 and 2023 to 29 percent.

Continued reliance on one-time funding from the HEERF funds and fund balance, combined with enrollment declines has created a structural imbalance in the Revenue Fund that will need to be addressed soon in order to right size operations and become sustainable in the future.

FISCAL YEARS 2023 STRUCTURAL GAPS AND BUDGET STRATEGIES

Continued declining enrollments and the impact on tuition revenue increased the budgetary gap in the General Fund (Table 8). Although some of the $9.6 million reduction in tuition revenue resulted in adjustments made in spending, most of the gap will be covered by increasing the use of programmed fund balance and using HEERF funds (if there are remaining funds) to offset revenue loss. The budgetary gap in the Revenue Fund also grew by less than $1 million and the gap in other funds grew from a positive position in June to a $1.4 million gap in October resulting in the loss of fee revenue sensitive to enrollment changes.

Table 8
Fiscal Year 2023 Structural Budget Gaps, October 2022

$s in millions	General Fund	Revenue Fund	Other Funds
Revenue/Sources	$1,623.6	$97.6	$287.0
Expenses/Uses	$1,701.3	$103.4	$288.4
Budget gap	($77.6)	($5.7)	($1.4)
HEERF Transfer in	$24.3	$0.4	$0.3
Programmed fund balance	$55.2	$8.1	$3.9
Budget balance	$1.9	$2.8	$2.8

Using one-time funds is a way for colleges and universities to address structural imbalances in the short-term, but it is not a sustainable long-term solution. In addition to using fund balance and HEERF funds, colleges and universities continue to use a variety of ways to address enrollment loss in their day-to-day operations. Examples include:

- Adjusting the number of course offerings to reflect lower enrollment
- Delay hiring or eliminating faculty, staff, and administrative positions as they become vacant
- Using Board Early Separation Incentive (BESI) programs to right-size staffing as a result of current and past enrollment changes
- Investing in student services and student success technologies to improve the tracking and retention of current students
- Developing new programs or expanding of existing programs to meet regional needs and to help stabilize enrollment

FEDERAL COVID HEERF FUNDING

Since fiscal year 2020, colleges and universities received over $600 million of relief funding from the federal government with half of the funds given to students in the form of grants. Table 9 shows the breakdown of when HEERF funds have been spent with the majority of spending occurring during the current biennium. Many of our colleges and a few universities still have federal HEERF funds to spend with around $64 million left to use in fiscal year 2023. The $64 million reflects about 10.5 percent of the total HEERF funds that were available in the three primary rounds of funding.

When colleges and universities were initially awarded HEERF funding, late fiscal year 2022 was set as the deadline to spend those funds. Last spring, the federal government granted an extension of those funds until June 30, 2023. This extension provided significant relief to help offset challenges in spending due to supply chain issues, contractor delays, and continued revenue loss from declining enrollment. During these past four fiscal years, colleges and universities have become reliant on HEERF funding to cover additional expenses to mitigate the impact of COVID-19 on our campuses as well as to soften the impact declining enrollment has had on tuition and fee revenue. In addition, many of our students have benefitted from additional resources in the form of HEERF grants to help cover the cost of their education and/or general living expenses.

Table 9
HEERF Awards for Students Grants and Institutional Needs
(dollars in millions)

Higher Education Emergency Relief Funds (HEERF)	Actual Use FY2020-21 Biennium	Estimated Use FY2022-23 Biennium*	Total Awarded in Three Rounds of HEERF
Student Grant Awards	$92.1	$168.3	**$260.4**
Institutional Awards a) additional student grants	$10.4	$30.0	**$40.4**
b) pandemic response	$111.1	$155.0	**$306.5**
Total to Institutions	**$213.6**	**$353.3**	**$607.3**

*additional students grants are fiscal year 2022 only and will increase when fiscal year 2023 is final

The first round of HEERF funding was distributed under the CARES (Coronavirus Aid, Relief, and Economic Security Act), 50 percent or $46.7 million of the overall $93.4 million in funding was reserved to provide students with financial aid grants to help cover expenses related to the disruption of campus operations due to the pandemic. The second round CRRSAA (Coronavirus Response and Relief Supplemental Appropriations Act) and third round ARP (American Rescue Plan) provided an additional $213.7 million for student grants and $300.2 million for institutional needs.

Around half of the $600 million the federal government awarded to our colleges and universities went directly to students as grants. Guidance was developed at the system level regarding the development of a plan to distribute these grants. CRRSAA and ARP funding requirements directed institutions to prioritize students with exceptional need. These grants did not lessen the amount students would have received in financial aid. In other words, students received financial support above and beyond what they were eligible for in regular financial aid. Institutions also had the ability to utilize the institutional award for additional student grants. At least $40 million was added to the $260 million that was earmarked for student grants.

Following fiscal year 2023, HEERF funds will no longer be available to support our students and operating budgets.

CONCLUSION

Enrollment and inflationary pressures continue to cause challenges for college and university budgets. In addition, the significant amount of federal support from the HEERF funds provided our colleges, universities, and our students with additional resources to use during the pandemic. Those are one-time funds, but the majority of needs the funds supported are not one-time in nature. We must look at ways to continue to support some of the activities that came out of the pandemic by aligning to what we may seek in the fiscal years 2024-2025 biennial budget request; examples include System stabilization funds, student basic needs, and additional financial support to students. The revised fiscal year 2023 all funds operating budget illustrates continued deterioration in enrollment and ongoing structural budget issues. Long-term enrollment trends, shifting educational interests, inflation, and state support at a rate less than annual cost increases remain significant budgetary concerns.