MEMORANDUM

TO: The Finance Committee:

Mark J. Kington, Chair
A. Macdonald Caputo
The Honorable Alan A. Diamonstein
Glynn D. Key
Randal J. Kirk
Stephen P. Long, M.D.
George Keith Martin
Vincent J. Mastracco Jr.
Edward D. Miller, M.D., Ex Officio
Helen E. Dragas, Ex Officio
Daniel M. Meyers, Consulting Member

and

The Remaining Members of the Board:

Hunter E. Craig Robert D. Hardie
Allison Cryor DiNardo John L. Nau III
W. Heywood Fralin Timothy B. Robertson
Marvin W. Gilliam Jr. Jonathan B. Overdevest

FROM: Susan G. Harris

SUBJECT: Minutes of the Finance Committee Meeting on February 24, 2012

The Finance Committee of the Board of Visitors of the University of Virginia met, in Open Session, at 9:50 a.m., Friday, February 24, 2012, in the Board Room of the Rotunda; Mark J. Kington, Chair, presided. Present were A. Macdonald Caputo, The Honorable Alan A. Diamonstein, Ms. Glynn D. Key, Randal J. Kirk, Stephen P. Long, M.D., George Keith Martin, Vincent J. Mastracco Jr., Edward D. Miller, M.D., and Ms. Helen E. Dragas, Rector.

Also present were Hunter E. Craig, Ms. Allison Cryor DiNardo, W. Heywood Fralin, Marvin W. Gilliam Jr., Robert D. Hardie, John L. Nau III, Timothy B. Robertson, and Jonathan B. Overdevest.
Daniel Maxwell Meyers, the consulting member from the Council of Foundations, was also present.


The Chair asked Mr. Strine, Executive Vice President and Chief Operating Officer, to begin the meeting. Mr. Strine said he would try to keep the meetings focused on strategic priorities and that the flow of expenditures and revenues reflects those priorities.

2012-2013 Academic Division Budget Planning and Preliminary Assumptions

Mr. Strine introduced Ms. Colette Sheehy, Vice President for Management and Budget, to report on the governor’s budget, actions of the General Assembly, and updated budget assumptions to be used in the development of the 2012-2013 operating budget.

Ms. Sheehy briefly described the University’s budget amendments transmitted to the General Assembly in January, and the process on the Governor’s budget. The House has approved a budget, but the Senate has not done so.

Ms. Sheehy compared the Governor’s budget with the House and Senate versions. Crossover will occur in the following week. She focused on incremental money, pointing out that the Governor’s incentive funding concept has been met with mixed response from the legislature and some of the funds have been redirected. The enrollment growth money is based on TAG grants, and is reserved for four institutions. Financial aid money is in both House and Senate versions. There is funding for a 2% salary increase in the second year of the biennium. Interest balances on auxiliary enterprises which are held at the state, which the state has kept for two years, has been reversed so the University will receive these funds. The Senate and House reduced the Governor’s numbers for Higher Education Opportunity Act objectives, and the Senate provided some money for the Higher Education Equipment Trust Fund for research institutions.

Specific to the University, the Senate and House are staying with the same total amount as the Governor. Some initiatives in the Six Year Plan are in the House budget, including STEM degree initiatives and online programs. Also, they support a summer program for high school students to gain STEM experiences. The Senate provided some graduate financial aid. The Eminent Scholars program is eliminated entirely. The Governor’s Life Sciences Consortium is not in either legislative version of the budget. There is some capital money for the Rotunda and pre-planning money for infrastructure projects. On
compensation and benefits, the VRS rate increases, and the Senate included a bonus of 3% for next year contingent on exceeding the revenue forecast. They also acknowledge a mistake that was made in Medicaid calculations that disadvantaged the University.

For Wise, there is some money for enrollment growth and for the science consortium initiative. Capital money for dam safety and pre-planning is provided.

On motion, the committee approved the following resolution and recommended it for full Board approval:

2012-2014 BUDGET AMENDMENTS FOR THE UNIVERSITY OF VIRGINIA

WHEREAS, the three new budget amendment recommendations, Virginia Logistics Research Center, Medicaid Prospective Payment Rates, and Correction of Indirect Medical Education and Inflation Costs in Medical Center Reimbursements, represent priorities of the University and one technical correction;

RESOLVED, the Board of Visitors of the University of Virginia endorses and supports the three budget amendments to the 2012-2014 budget not previously considered; and

RESOLVED FURTHER, the Executive Vice President and Chief Operating Officer is authorized to transmit to the General Assembly the resubmitted and new proposed budget amendments requiring authorization by the Commonwealth under the University’s Management Agreement.

Report on the University’s Financial Status as of December 31, 2011

In addition to Mr. Strine and Ms. Sheehy, Ms. Yoke San Reynolds, Vice President and Chief Financial Officer, and the University of Virginia Investment Management Company’s (UVIMCO) Chief Investment Officer Larry Kochard, provided a mid-year update on the University’s financial performance.

Mr. Strine began with an overview of sources and uses of funds in the academic division and the trends going forward where the University will be more dependent on tuition revenue and less dependent on General Fund appropriations. Tuition net of financial aid is in excess of budget overall and up 6.3% over the prior year. Grants and contracts are down, financial and administrative revenue is flat, and general fund appropriations are 8.3% below what was provided last year. Mr. Strine said gifts, endowment income and auxiliary revenue are up this year. Expenses have also increased in the areas of student services, plant operations and maintenance, and financing of scholarships from sources other than tuition – last year stimulus funds supported financial aid.
On a GAAP basis, net assets are down $62.2 million due to loss of market value of investments, revenues are up 1.3% compared to the prior year, expenses are down 0.2%, and the operating margin is $21.4 million compared to $11.9 million at the same time in the prior year.

Mr. Strine turned from the mid-year financial report to an analysis of trends from 2003 until 2011. A graph on revenue streams showed volatility in investment income. Gifts showed the greatest increase. On University expenses, compensation is the biggest expense. He then showed a chart on net income which indicates that the University is about break even every year on operating net income. The real driver of the net income is the change in investment income. Patient services revenues have increased 183% from FY 2003 to FY 2011. Indigent care and contractual adjustments increased 405% over the same period of time.

Mr. Strine said tuition and fees grew 87% from 2003 to 2011. Net tuition revenue grew by 82%. Sponsored programs revenue grew 23% over the same period, with F&A recoveries growing by 40% as a result of volume growth and increases in the negotiated rate.

Mr. Strine reviewed expenses over the same period of time. The largest portion is people, with FTEs growing by 11% in the Academic Division, 21% in the Medical Center, and 32% in the College at Wise. The other big area of expense is plant operations and maintenance (O&M). Cost per square foot grew from $11.30 per square foot in 2003 to $13.70 in 2011. Most of the University’s assets are restricted or are in the ground, as in buildings. So, although net assets are increasing, they are largely in things that cannot be deployed.

Mr. Strine asked Mr. Kochard to speak about the long term pool, including the University’s endowment. Mr. Kochard explained there is a 12-member UVIMCO Board of Directors, and an investment staff, which are experienced and are responsible for the good performance.

Mr. Kochard said the trend is a big down year and a big up year over the past four and half years. Performance was up about 7% over the last calendar year, with contributors across the portfolio, particularly real estate and resources. A risk factor now is bond rates are so low that investing in bonds is locking in a negative real return. Another way to control risk is to invest in lower risk equities.

Mr. Kochard reviewed the different kinds of risk and risk management strategies. In terms of manager risk, UVIMCO has expanded operational due diligence. Market risk, the maximum possible drawdown, is compared against the policy portfolio and the risk tolerance of the institution. Liquidity risk: it is necessary to maintain liquidity to make payments to the institution, to meet capital calls and to rebalance the portfolio.
Private funds' investing was reviewed. He said they are targeting 15% of the portfolio; UVIMCO is now at about 16%. A combination of the funded and unfunded commitments is about 59%, right in the middle of peers.

Mr. Kochard mentioned the first UVIMCO annual meeting, to be held in March, which will include representatives of the University and the related foundations that invest in UVIMCO.

Mr. Strine complimented Mr. Kochard and Ms. Alimard for their assistance in educating investors to prepare for a new financial model.

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Consent Items:

Mr. Strine said there are three consent agenda items and asked for approval of them.

On motion, the committee adopted the following resolutions and recommended them to the full Board for approval:

APPROVAL TO PURCHASE 1107 WEST MAIN STREET, CHARLOTTESVILLE, VIRGINIA

WHEREAS, the Board of Visitors finds it to be in the best interest of the University of Virginia to purchase from the University of Virginia Foundation (the "Foundation") land and improvements thereon located at 1107 West Main Street, Charlottesville, Virginia (the "Property"), at a purchase price not to exceed $870,000;

RESOLVED, the Board of Visitors approves the acquisition of the Property; and

RESOLVED FURTHER, the Executive Vice President and Chief Operating Officer is authorized, on behalf of the University, to approve and execute purchase agreements and related documents, to incur reasonable and customary expenses, and to take such other actions as deemed necessary and appropriate to consummate such property acquisition; and

RESOLVED FURTHER, all prior acts performed by the Executive Vice President and Chief Operating Officer, and other officers and agents of the University, in connection with such property acquisition, are in all respects approved, ratified, and confirmed.
APPROVAL OF SIGNATORY AUTHORITY FOR MEDICAL CENTER PROCUREMENT OF CORD BLOOD PRODUCTS AND SERVICES

WHEREAS, the Medical Center Operating Board finds it to be in the best interest of the Medical Center to enter into a contract for the procurement of cord blood services and products;

RESOLVED, the Board of Visitors authorizes the Executive Vice President and Chief Operating Officer of the University to execute a multi-year contract for the procurement of cord blood services and products, based on the recommendation of the Vice President and Chief Executive Officer of the Medical Center in accordance with Medical Center procurement policy.

APPROVAL OF SCHOOL OF MEDICINE INVESTMENT IN THE FUND FOR THE FUTURE QUASI-ENDOWMENT

WHEREAS, the Board of Visitors must approve any quasi-endowment transaction of $2 million or more; and

WHEREAS, the School of Medicine received $18,044,078 from the UVa Medical Center to support its academic mission and wishes to invest $15.0 million of this money in its Fund for the Future Quasi-Endowment account; and

WHEREAS, the purpose of the transfer is to invest funds until needed to implement the Health System strategic plan approved by the Board of Visitors;

RESOLVED, the Board of Visitors authorizes the investment by the School of Medicine of $15.0 million into its Fund for the Future Quasi-Endowment account; and

RESOLVED FURTHER, any other addition to any quasi-endowment of $2 million or more will continue to require Board of Visitors’ approval.

Action Item: 2012-2013 Tuition and Fees for Special Programs

Mr. Strine recommended tuition and fees for two programs that begin their academic year in May or June. The School of Engineering and Applied Science’s Accelerated Master’s Program in Systems Engineering proposed tuition of $37,500, an increase of $1,000 (2.7%) for both Virginians and non-Virginians. The School of Continuing and Professional Studies’ Post-Baccalaureate Pre-Medical Certificate Program proposed a tuition increase of $750 (3%) for Virginians and $900 (3%) for non-Virginians, to address increasing program costs.

On motion, the committee adopted the following resolution and recommended it to the full Board for approval:
APPROVAL OF 2012-2013 TUITION AND FEES FOR CERTAIN PROGRAMS

RESOLVED, the Board of Visitors approves the tuition and fees applicable to the following programs as shown below, effective May 1, 2012, unless otherwise noted:

<table>
<thead>
<tr>
<th>Program</th>
<th>2011-12 Approved</th>
<th>Percent of Increase</th>
<th>2012-13 Proposed</th>
<th>2011-12 Approved</th>
<th>Percent of Increase</th>
<th>2012-13 Proposed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Systems Eng.</td>
<td>$36,500</td>
<td>2.7%</td>
<td>$37,500</td>
<td>$36,500</td>
<td>2.7%</td>
<td>$37,500</td>
</tr>
<tr>
<td>Post-Bac, Pre-</td>
<td>$25,000</td>
<td>3.0%</td>
<td>$25,750</td>
<td>$30,000</td>
<td>3.0%</td>
<td>$30,900</td>
</tr>
</tbody>
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The price includes the estimated 2012-2013 special session mandatory fee, books, materials, technology, group meals, and lodging.

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Action Item: Acquisition of Leasehold Improvements – Squash Facility from University of Virginia Host Properties, Inc.

The University of Virginia Foundation is working on the construction of a donor funded squash facility at the Boar's Head Sports Club for the use of UVa club teams. The proposed 33,000 gross square foot facility, valued at $12.4 million, would include:

- eight new international singles courts with seating for approximately ten spectators at each court
- 1 international show court with seating for 200-300 spectators
- 2 new North American doubles courts
- An upper viewing mezzanine
- An entry lobby and circulation
- 4 dedicated squash locker rooms (men's and women's locker rooms for both home and visiting teams)
- 1 team room/lounge
- Opportunity for an open fitness/training area
- 1 coaching office
- 1 storage room

University of Virginia Host Properties, Inc., a subsidiary of the University of Virginia Foundation, will ground lease the land on which the facility will be built and also manage operations, pursuant to a management agreement with the University.
On motion, the committee adopted the following resolution and recommended it to the full Board for approval:

APPROVAL OF ACQUISITION OF LEASEHOLD IMPROVEMENTS - SQUASH FACILITY FROM UNIVERSITY OF VIRGINIA HOST PROPERTIES, INC.

WHEREAS, the Board of Visitors desires to provide a squash facility where club teams of the University of Virginia can practice and play matches; and

WHEREAS, the most suitable location for such a facility is at the Boar's Head Sports Club on land owned by University of Virginia Host Properties, Inc. ("Host Properties"), a subsidiary of University of Virginia Foundation;

RESOLVED, the Board of Visitors approves the acquisition from Host Properties of leasehold improvements proposed to include a squash facility that is approximately 33,000 gross square feet and includes eight new international singles courts with seating for approximately ten spectators at each court, one international show court with seating for 200-300 spectators, two new North American doubles courts, an upper viewing mezzanine, an entry lobby and circulation, four dedicated squash locker rooms (men's and women's locker rooms for both home and visiting teams), one team room/lounge, the opportunity for an open fitness/training area, one coaching office and one storage room, at a cost not to exceed $12.4 million, all to be constructed in accordance with plans and specifications approved by the Executive Vice President and Chief Operating Officer; and

RESOLVED FURTHER, the Executive Vice President and Chief Operating Officer is authorized, on behalf of the University, to approve and execute all agreements and related documents, to incur reasonable and customary expenses, to approve revisions to the plans and specifications and building program, and to take such other actions as deemed necessary and appropriate to consummate such acquisition of the leasehold improvements; and

RESOLVED FURTHER, all prior acts performed by the Executive Vice President and Chief Operating Officer, and other officers and agents of the University, in connection with such acquisition of the leasehold improvements, are in all respects approved, ratified, and confirmed.

Action Item: Authorization of and Intent to Issue Tax-Exempt Debt

Mr. Strine recommended approving the authorization of and intent to issue tax-exempt debt resolution to provide bridge financing for the Athletics Fieldhouse project, not to exceed $10,000,000.
On motion, the committee adopted the following resolution and recommended it to the full Board for approval:

AUTHORIZATION OF AND INTENT TO ISSUE TAX-EXEMPT DEBT

WHEREAS, the University intends to undertake certain capital projects identified below (whether one or more, the “Projects”), and to finance the Projects through the issuance of tax-exempt debt, in the maximum principal amount stated below for each of the Projects:

ACADEMIC DIVISION

Athletics Fieldhouse — $10,000,000;

WHEREAS, the University further intends to expend funds on the Projects and to reimburse such expenditures from the proceeds of the tax-exempt debt; and

WHEREAS, to comply with the Internal Revenue Code of 1986, as amended, and Section 1.150-2 of the Income Tax Regulations (the “Regulations”), it is necessary, in order to reimburse such expenditures incurred prior to the issuance of the tax-exempt debt with the proceeds of such debt, that the University declare its official intent to make such a reimbursement of expenditures;

RESOLVED, debt may be issued for each of the Projects on a short-term basis, but only if the following conditions are met:

1. A comprehensive and detailed financial plan for each of the Projects is submitted to, and approved by, the Capital Outlay Executive Review Committee;

2. Short-term debt shall not exceed sixty (60) months in maturity; and

3. A school or unit shall remain responsible for repaying any debt obligation incurred regardless of the status of such school or unit’s Project; and

RESOLVED FURTHER, the Board of Visitors of the University of Virginia declares its intent to expend funds on the Projects and to reimburse such expenditures from the proceeds of tax-exempt debt, in accordance with the following:

1. This resolution is a declaration of official intent for purposes of Section 1.150-2 of the Regulations; and

2. The University reasonably expects to issue tax-exempt debt for each of the Projects in the maximum principal amount stated in the recitals above.
Vice President’s Remarks

Mr. Strine said the Medical Center strategies for change management are the same as those the University is going to do on the academic side. The University needs a new financial model that aligns. He said he and John Simon are working very hard to develop a coalition to implement the financial model. He said they distributed enrollment growth money this year as though the new model was in place.

He said there were two capital items to be aware of, one, the air quality in the Aquatics and Fitness Center, and the second is the partnership with the city on the Emmet and Ivy corner improvements.

Mr. Strine mentioned the report of the American Council of Trustees and Alumni (ACTA). The report asked six basic questions: what are students actually learning? How much are students paying for college? How do tuition rates compare to family income? What are the colleges spending their money on? Are freshmen returning? Are students graduating and doing so on time? He responded to each of these questions, explaining how the report did not give the full picture on many of these issues. For instance, ACTA evaluated core curriculum requirements and gave the University credit for requiring two of the seven core courses, foreign language and science, however, they did not take into consideration that many University students test out of entry level core courses, and most students graduate having taken many of the courses in the areas ACTA considers core. Many students come to the University to pursue their own intellectual interests, not to repeat courses they took in high school.

ACTA analyzed tuition increases. Mr. Strine said the University’s tuition costs have grown, but at the same time general funds have decreased. In a comparative sense, the University is spending less per in-state student from tuition and state tax funds than in 1989-90. He said net price is more important than gross price for families.

Mr. Strine addressed the question about what the University is spending money on. ACTA said it was on layers of administration. Much of the growth in administrative costs at the University has been for fundraising and alumni relations, and research administration. Annual compensation increases are also a major factor.

On the question of freshmen returning, the University has a 96% first year retention rate, which is higher than other public and private institutions in Virginia, and the six-year graduation rate is 93%.

Many committee members weighed in on these issues. Mr. Fralin said he thought it was important to educate the General Assembly on what is takes to have quality and affordability.
The Chair adjourned the Finance Committee meeting at 11:30 a.m.

SGH:lah
These minutes have been posted to the University of Virginia’s Board of Visitors website.
http://www.virginia.edu/bov/financeminutes.html