Report of the Finance Committee

GD18-47

Board of Governors Meeting of April 25, 2019

Secretariat
845 Sherbrooke St. West, Room 313
Montreal, QC, H3A 0G4
Tel: (514) 398-3948 | Fax: (514) 398-4758

The following items arise from a meeting of the Finance Committee on April 16, 2019. They are presented to the Board of Governors for its consideration.

I. FOR ACTION BY THE BOARD OF GOVERNORS

1. Proposed McGill University Budget 2019-20 [F18-25]

Following the Committee's review of budget planning reports at its November and February meetings, members received a presentation in support of the proposed 2019-20 University budget. Members were informed that the forecasted deficit for FY2020 was $8.67M.

A presentation summarizing the highlights of the budget is attached as Appendix A.

Be it resolved that the Board of Governors, on the recommendation of the Finance Committee, approve the proposed 2019-2020 McGill University Budget, as described in Appendix A.

2. Maximum Borrowing Resolution for Fiscal Year 2020 [F18-23]

The *Ministère de l'Éducation et de l'Enseignement supérieur* (MEES) requires annual borrowing authorization limits to be confirmed by the University. The annual short-term borrowing limit authorized by the MEES is typically $300 million (for the period from June 1 to May 31). A special circumstance requires a higher limit for the remainder of the current year and all of the upcoming year. A long-term note in the amount of $172 million is scheduled to mature on May 29, 2019, and the University will be unable to repay it within a $300 million short-term borrowing limit. For this reason, Board approval is sought to increase the University's annual short-term borrowing limit for the period from May 1, 2019 until May 31, 2019, up to a maximum of $380 million. The MEES has already approved this measure, and furthermore as is standard practice, will reimburse the University for any financing charges incurred. In addition, because the University is uncertain about when and how much it will receive to reimburse the note, it requires a short-term borrowing limit of up to $400 million, from June 1, 2019 to May 31, 2020 (subject to MEES approval).

Be it resolved that the Board of Governors, on the recommendation of the Finance Committee, approve an increase to the maximum borrowing limit, from up to $300 million to up to $380 million, for the period from May 1, 2019 to May 31, 2019.

Be it further resolved that the Board of Governors approve a maximum borrowing limit of up to $400 million, for the period from June 1, 2019, to May 31, 2020.

Be it further resolved that the Board of Governors authorize the Vice-Principal (Administration and Finance) or the Associate Vice-Principal, Financial Services or the Chief Investment Officer and Treasurer to sign contracts, documents, or any instruments pertaining to these borrowings.

II. FOR THE INFORMATION OF THE BOARD OF GOVERNORS

1. Update on Financing Plan for Deferred Maintenance and IT Initiatives [F18-20]

The Finance Committee was informed of a reallocation of bond proceeds for deferred maintenance and IT initiatives. Previously, the spending allocation was set at $300 million for deferred maintenance and $100 million for IT initiatives. Moving forward, $250 million will be allocated for deferred maintenance projects, and $150 million for IT initiatives. This adjustment takes into account increased funds needed to address deferred maintenance needs in the area of IT and the availability of increased government funding for deferred maintenance in the area of construction and renovation projects.

The Committee was further informed of the following:

- With respect to construction and renovation projects:
  As of January 31, 2019, $89,628,628 from the bond has been spent on actual costs incurred for construction and renovation projects.

- With respect to IT projects:
  As of January 31, 2019, $37,345,712 from the bond has been spent on actual costs incurred for IT projects.

2. Update on the Royal Victoria Hospital Redevelopment Project

The Committee received an update on the Royal Victoria Hospital redevelopment project, including the impact of the Government of Quebec's revised funding formula for universities. The revised formula will decrease government contributions towards new infrastructure projects by the university's proportion of deregulated international students among Quebec institutions. Accordingly, government contributions to the RVH project can be expected to decrease by approximately 16%. This would result in the Quebec government's contribution to decrease from $460 to $420 million. Confirmation of funding from the Government of Quebec is not expected before the 2020-2012 provincial budget. The University's contribution to the project remains at $150 million.

3. Implementation of Recommendations from Internal Audit of Central Budget Process [F18-21]

Pursuant to a request made at the beginning of Fiscal Year 2018 by the Provost and Vice-Principal (Academic) that an internal audit of the central budget process be performed, the Committee received an update and heat map analysis of progress made on implementing the audit's recommendations. As 24 of the 27 recommendations contained in the Internal Audit report are complete, the Committee discussed implementation of the remaining items as well as continuous improvements that can be made to other processes. An update on this file is anticipated at the next meeting.

4. Budget Implementation 2018-19 Year-to-Date [F18-24]
Report on Quarterly Financial Results for Fiscal Period Ended January 31, 2019

The Committee received a quarterly report on the financial results (including a variance report) for the period ended on January 31, 2019. The report included operational highlights, and a summary of overall revenues and expenses for the period in question.

5. Annual Report on the McGill University Pension Plan [F18-24]

The Committee received the annual report on the McGill University Pension Plan for the fiscal year ended December 31, 2018, as approved by the Pension Administration Committee. Members were apprised of the pension plan fund performance and were informed that the last triennial valuation exercise performed on December 31, 2017, revealed a going concern deficit of $47.375 million (down from $78 million in December, 2015). $78M and the degree of solvency of the Pension Plan improved to 86.1% (from 81%). It was noted that the next triennial valuation exercise would be performed as at December 2020 at the latest.

6. Annual Report from General Counsel

In accordance with the terms of reference of the Committee, members received an annual report on current claims against the University. Overall, it was noted that the University's risk exposure is not significant.

END
April 2019

Budget Planning III

McGill University Budget FY2020: Summary and Highlights

Presentation to the Board of Governors on April 25, 2019

Christopher Manfredi, Provost and Vice-Principal (Academic)

McGill

FY2019 Forecast

McGill

FY2019 Year-End Forecast – Unrestricted Funds ($M)

Anticipated major budget variances for FY2019 ($M)	
FY2019 budgeted deficit	**($15.4M)**
Lower than budgeted other non-salary expenses	$25.4M
Higher than budgeted tuition & fees	$17.9M
Higher than budgeted Provincial grants	$9.2M
Higher than budgeted sales of goods & services	$7.7M
Lower than budgeted benefits expenses	$5.4M
Higher than budgeted endowment revenue (investment income)	$4.3M
Higher than budgeted Support Staff and Academic salaries & payments	($3.9M)
Higher than budgeted materials, supplies, and publications	($5.2M)
Higher than budgeted contract services	($6.1M)
Higher than budgeted building & occupancy costs	($11.6M)
Higher than budgeted Inter-Fund transfers	($18.9M)
Variations in all other revenue and expense categories	*($9.3M)*
FY2019 forecast	**($0.6M)**

FY2019 Year-End Estimates vs. Budget FY2019: Revenues

- FY2019 budget was built estimating revenues under the government's former funding policy.
- FY2019 year-end provincial grants and tuition and fees revenues are estimated using what is currently known about the government's new funding policy, outlines of which were published in July 2018 with ongoing discussions about key changes.
  - Significant one-time structural increase of operating grant in FY2019 due to implementation of a new funding grid and government grant structure.
  - Temporary grants: $4.2M for smoothing enrolment; $2.1M for supporting engineering.
- We originally coded a material cash inflow (around $7M) as a transfer into the Unrestricted Fund. The FY2019 budget reflected this expectation. However, the inflow was subsequently recoded as endowment revenue, causing both revenue and expenses to appear $7M higher than budgeted.
- Sales of goods and services are forecasted at $7.7M above budget, but only about $2M above FY2018 totals.

Side by Side Comparison of Provincial Unrestricted Revenues ($000)

Category	Budget FY2019	Year-End Estimate FY2019	Difference
Teaching Grant	301,652	333,624	31,972
Support Grant	55,047	65,575	10,528
Facilities and Buildings	58,968	61,777	2,809
Specific Grants	14,659	2,429	(12,230)
Enrolment Smoothing (new)	-	4,186	4,186
General Fixed Costs	2,432	2,809	377
Other grants (central)	7,105	(1,000)	(8,105)
Other grants (units)		2,261	2,261
Recoveries	(107,029)	(111,571)	(4,542)
Loi 100 - Productivity Cuts	(3,899)	-	3,899
FY06 Reinvestment	8,349	-	(8,349)
FY18 Additional Reinvestment	6,211	-	(6,211)
FY19 Additional Reinvestment	7,350	-	(7,350)
Total	**350,845**	**360,090**	**9,245**

FY2019 Year-End Estimates vs. Budget FY2019: Revenues (cont'd)

- FY2019 Budget based on admission and enrolment targets.
  - Fall 2018 enrolment of deregulated international students surpassed the target by 190 (Fall 2018 enrolment target of 2,248 versus actuals of 2,438).
  - FY2019 Master's and PhD new registrations surpassed the target by 196 (FY2019 admissions target of 3,057 versus actuals of 3,253).
  - Positive impact on tuition, provincial grants (only for FY2019 when it comes to deregulated students), institutional fees and sales of goods and services revenues.

FY2019 Year-End Estimates vs. Budget FY2019: Expenses

- Since FY2016, budgets have been built with the assumption that units would meet their mandated cuts and salary mass reductions ($15.0M). Units have been allowed to spread out their reductions over time. This flexibility has led to expenditures that exceed our budget.

- FY2019 year-end estimates for self-funded operating funds (non-1A funds) were originally less optimistic than budgeted, but are now more in line with past results. In particular, results and/or expectations improved in Q4 for University Advancement, the Faculty of Medicine, and Student Housing and Hospitality Services.

Looking Ahead: FY2020 – FY2024

McGill

FY2020 Strategic Priorities

- **Principal’s priorities**
- **Provost’s strategic academic plan objectives**
  - Be open to the world
  - Expand diversity
  - Lead innovation
  - Connect across disciplines and sectors
  - Connect with our communities

FY2020: Strategic Priorities – Highlights

- Over $1.5M in one-time and recurring funding for initiatives in Indigenous Studies and Education
  - Indigenous Achievement Award ($5,000 renewable admissions award given to one to three incoming Indigenous students every year).
  - Six new faculty positions under recruitment for FY2020 focusing on Indigenous health, education, language and governance.
- The Rossy Student Wellness Hub
  - New service-delivery model that integrates physical and mental healthcare and ensures that students have access to the right care at the right time.
  - $13.5M initiative funded by the Rossy Family Foundation ($4.9M) and McGill ($8.6M).
  - Annual $1.7M commitment by McGill thereafter.

FY2020: Strategic Priorities – Highlights (Cont'd)

- The Campus Médical Outaouais
  - McGill will provide the MDCM program in French in Outaouais to a number of their students.
  - Construction and hiring of educational leadership and administrative staff in progress.
  - First cohort of students to be admitted in Fall 2020.
- Student Aid
  - $34.2M in Unrestricted Funds anticipated for student aid in FY2020.
  - Continuous efforts to seek external funding for our students.
- Graduate and Postdoctoral studies
  - Over $1M for additional graduate student funding and doctoral student recruitment.

FY2020 and Beyond: Revenues

- McGill expects to maintain the enrolment goals set out in the Strategic Academic Plan:
  - Maintain undergraduate enrolment and increase graduate enrolment.
  - Maintain share of international students within undergraduate enrolment between 25%-30%.

- In FY2020, first-cycle and non-research second cycle international students will be deregulated:
  - Elimination of teaching, support, and building and grounds grants for deregulated students.
  - Tuition fees to offset the loss of these grants <u>over time</u> as we continue to adjust tuition rates for deregulated students in line with the market—a slight decrease in total revenue derived from these students expected in FY2020, with gradual increases afterward.
  - Temporary transition grant to new funding policy: $2.1M in FY2020 and $1.1M in FY2021.
  - Tuition elasticity study by major disciplines recently completed and under analysis.

FY2020 and Beyond: Expense Pressures

- Salary commitments
  - Maintain agreements and contracts
  - FY2020 salary policy estimate: **$15.0M**, including benefits
- Deferred maintenance
  - Bond issue for **$160M** in FY2016. Additional borrowing (up to $400M total) in support of capital expenditures to be repaid upon maturity.
  - Expected annual impact on the Unrestricted Fund: **$11.5M** in FY2020; **$23M/year** starting in FY2021.
- Regular maintenance to mitigate future deferred maintenance risks within budget.

FY2020 and Beyond: Expense Pressures (Cont'd)

- Working to reduce internal decisions impacting the Unrestricted Fund that are made outside the Agreement process that are nonetheless binding on the institution.

- Working to reduce authorization to carry forward surpluses in individual funds:
  - Some areas manage individual unrestricted funds for which they are authorized to retain unspent balances at the end of each fiscal year.
  - Operationally, this means that the "exceptional" fund managers have the authorization to overspend in a future year because they underspent in a past year.
  - The combined fund balances are growing, creating a future liability for the Unrestricted Fund that is not accounted for in the annual budget.

FY2020 and Beyond: Administrative and Support Staff Budget Pressures

- The administrative and support staff budget measure from FY2016 has not achieved the projected result of a reduction in salary mass. Staff levels are back to where they were prior to the Voluntary Retirement Program (VRP), as the salary mass continues to grow.
  - Although we have reduced the applicable budgets across the University, some areas have achieved a balanced budget by reducing non-salary expenditures instead of salary expenditures. Other areas have not achieved a balanced budget.
  - We are in the process of re-implementing position budgeting across the University in order to isolate differences between permanent salary budgets and total salaries for permanent employees.
  - Position control, which could be the next step, is not possible without:
    - A process that includes permanent salary budget availability as a necessity to fill a permanent position; and
    - Restrictions on the movement of permanent funds between salary and non-salary accounts; and
    - Restrictions on the use of self-financing unrestricted funds to circumvent any new process established in the first point above.

FY2020 and Beyond: Revenue Risks/Unknowns

- Success of the University in deploying its enrolment plan for Fall 2019.
- Success of the University in developing an optimal pricing strategy for tuition fees for deregulated students by program and in delivering on this strategy.
- A baseline expectation for self-financing operations, and an appropriate review mechanism if not achieved.

FY2020 and Beyond: Cost Risks/Unknowns

- Success of efforts to identify causes of increased hiring, appropriate planning to reach desired staffing levels, and application/monitoring of targeted staffing levels.
- Unprecedented capital projects, including IT investments, either in progress or in planning.
  - Estimates of total capital project costs - including cost of staff time providing significant support to capital projects and funded from operating funds.
  - Ensuring that service levels for University operations in affected units are commensurate with the salary costs that are retained in the Unrestricted Fund.
- Increases in interest rates in past two years impacts borrowing costs.
- Fluctuations in currency exchange rates; additional interest rate increases .
- Inability to spend endowment payout due to restrictions on use (e.g., research chairs, donor requirements).

Operating Budget: Past, Present and Future Outlook ($000s)

5-year outlook	FY2019 *(from Budget Book)*	FY2019(f)	FY2020(b)	FY2021(o)	FY2022(o)	FY2023(o)	FY2024(o)
Total revenues	870,863	911,510	920,002	923,887	945,023	969,275	995,983
Total expenses (1)	886,305	912,060	928,670	934,876	958,526	974,526	994,226
Annual financed surplus (deficit)	(15,442)	(550)	(8,668)	(10,989)	(13,503)	(5,251)	1,757
Financed accumulated deficit (2)		(128,989)	(137,657)	(148,645)	(162,148)	(167,399)	(165,642)
Financed accumulated deficit/Revenues (%)		14.15%	14.96%	16.09%	17.16%	17.27%	16.63%

f = forecast; **b** = budget; **o** = outlook

(1) Excluding year-end actuarial adjustments and related accrual
(2) FY2018 ending financed accumulated deficit = $128,439

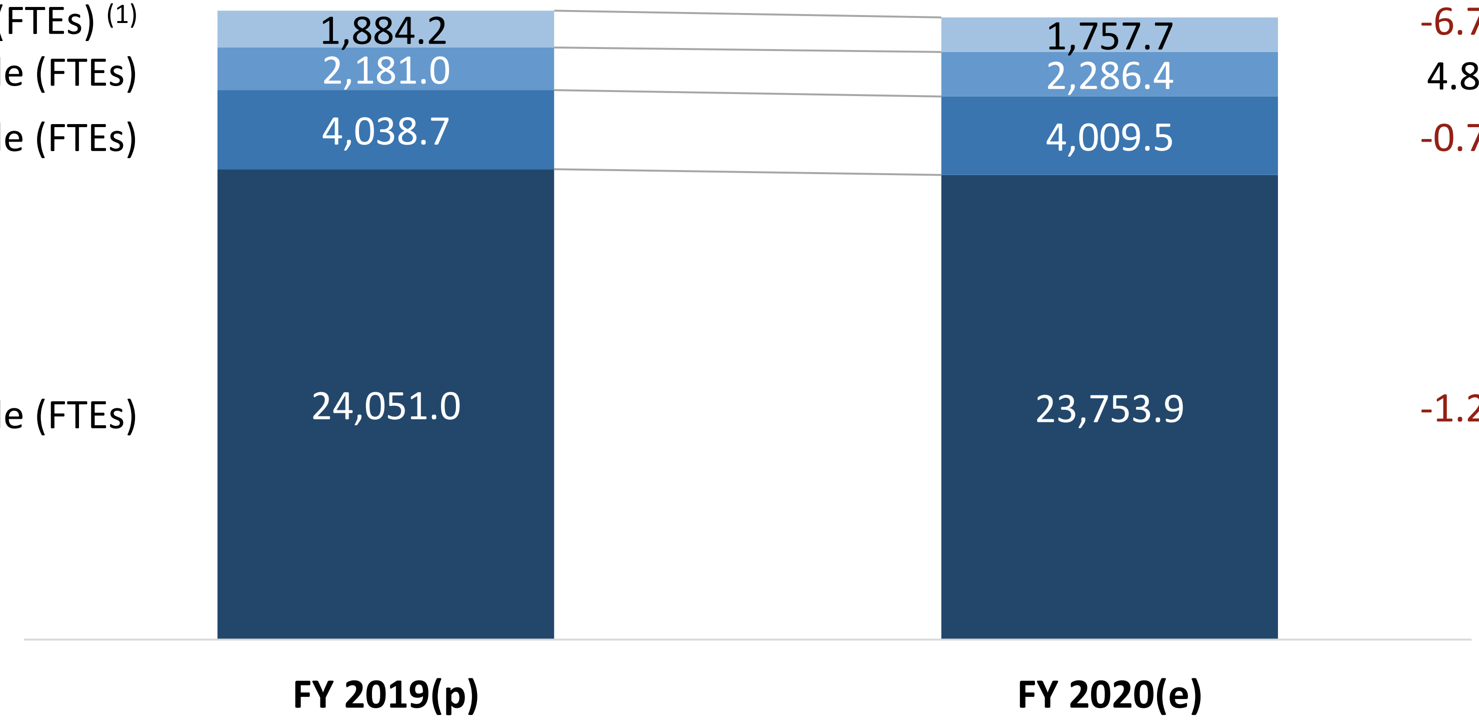
FY2020: Operating Revenue = $920.0M

($'000)	Forecast FY2019: $911,510	Budget FY2020: $920,002	% Change 0.9%
Grants - Canada	3.4%, **$30,970**	3.5%, **$32,000**	3.3%
Grants - Quebec	39.5%, **$360,090**	39.1%, **$359,822**	-0.1%
Tuition and Fees	38.4%, **$350,000**	38.9%, **$358,037**	2.3%
Sales of Goods & Services	16.2%, **$147,630**	15.9%, **$146,729**	-0.6%
Gifts & Bequests	1.0%, **$9,490**	1.1%, **$9,867**	4.0%
Endowment Revenue (Investment Income)	1.1%, **$9,840**	1.1%, **$10,053**	2.2%
Sort-Term Interest Revenue (Interest Income)	0.4%, **$3,490**	0.4%, **$3,493**	0.1%

FY2020 Key Revenue Assumptions: Student Enrolment

- Growth in PhD enrolment; slight decrease in undergraduate enrolment.

	FY 2019(p)	FY 2020(e)	% Change
Total FTEs	**32,154.92**	**31,807.53**	**-1.1%**
Med Residents (FTEs) (1)	1,884.2	1,757.7	-6.7%
3rd Cycle (FTEs)	2,181.0	2,286.4	4.8%
2nd Cycle (FTEs)	4,038.7	4,009.5	-0.7%
1st Cycle (FTEs)	24,051.0	23,753.9	-1.2%
Total weighted FTEs (2)	**99,313.7**	**99,383.5**	**0.1%**



(1) Decline in medical residents category due to approximately 100 medical fellows (headcount) being reclassified as Postdocs as of FY2020
(2) WFTEs = FTEs weighted by discipline and level, using the new CAFF weighting grid

p = projected; **e** = estimate

FY2020-FY2024 Key Revenue Assumptions: MEES Operating Grant

- Assumptions
  - Modest grant indexation (FY2020 to FY2024 – Support grant: 1% per year; Teaching grant: 1.2% per year)

- Estimated increases in regulated Quebec base tuition
  - FY2020 to FY2024: **3.6%, 2.9%, 2.0%, 2.0%, 2.0%**

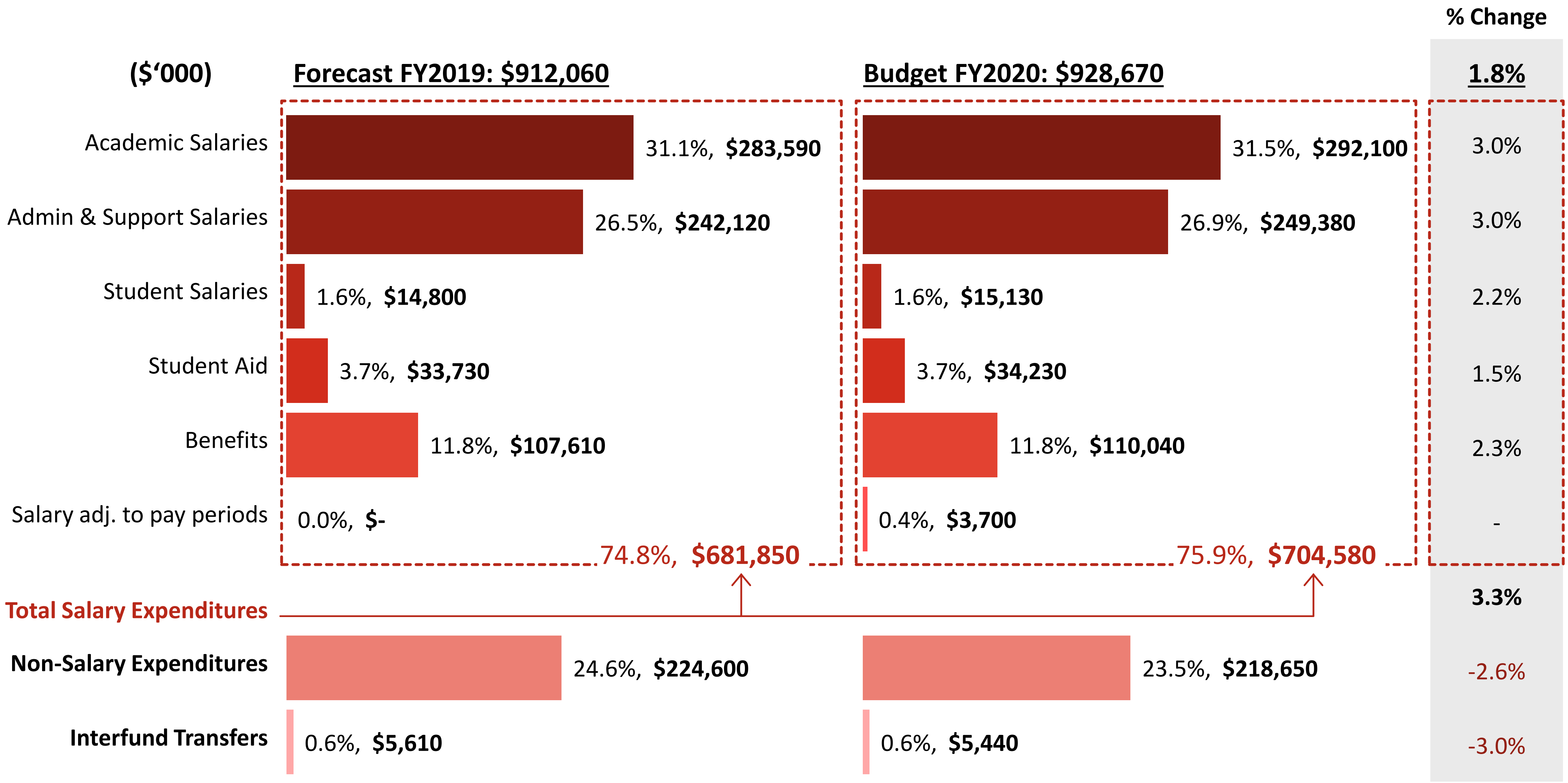
FY2020 Key Revenue Assumptions: Regulated Tuition

- Basic tuition revenues (net of student aid) = approximately **$6.2M lower** due to fewer students paying regulated tuition.
  - FY2020 increase in base tuition rate = 3.6% or $88.40/FTE ($76.58/FTE net)
  - Assumptions for subsequent years:
    - FY2021: 2.9% increase
    - FY2022 to FY2024: 2.0% per year increase
- Provincial tuition supplement recovery amount
  - International supplements = approximately **$40.9M less** to be recovered by the government in FY2020, due to fewer international students paying regulated tuition.

FY2020 Key Revenue Assumptions: Deregulated Tuition

- Increase in deregulated tuition fees for first and second cycle international students in non-research programs:
  - FY2020: 7.7% for incoming cohorts
  - FY2021 to FY2024 provisional increases for incoming cohorts:
    - Previously regulated disciplines: 10%, 11%, 12%, 13%
    - Previously deregulated disciplines: 7.7%, 7.7%, 7.7%, 5%
- Annual increases for returning students:
  - For those admitted before Fall 2019 in previously deregulated programs, tuition fees will remain constant for the normal duration of the program of study.
  - For all first or second cycle international students admitted to non-research programs in Fall 2019 or later, annual increases as a returning student will be between 3% to 5%.
- Increases for incoming cohorts will be kept at a minimum of 7.7% per year for three years, possibly adjusted upward as the market and economic indicators demand; they will be re-evaluated for FY2023 based on:
  - Ability to maintain market shares (applications, selectivity, and yields)
  - Fluctuations in currency exchange rates

FY2020: Operating Expenses = $928.7M



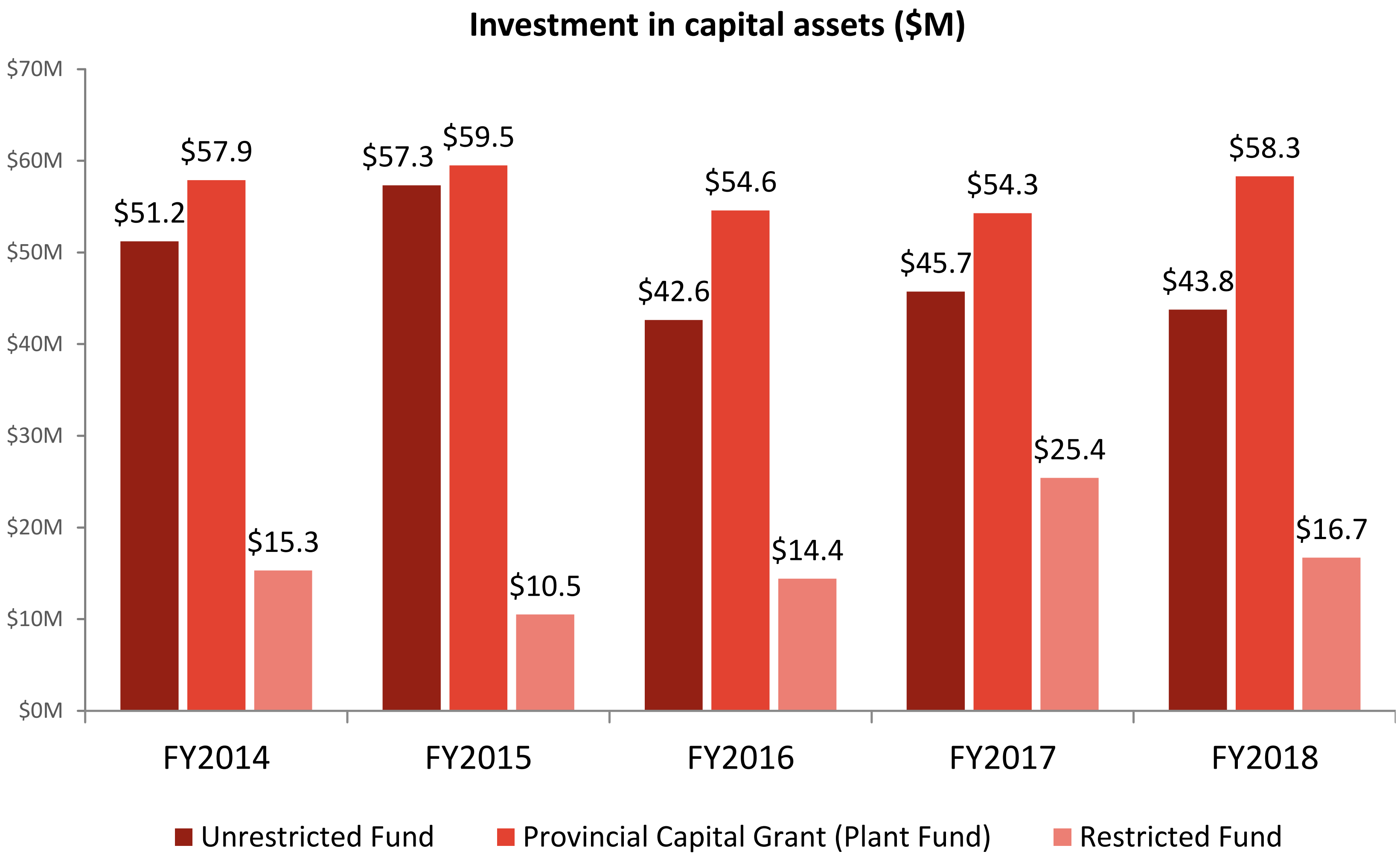
Significant One-Time and Ongoing Expenses

- Operating fund requirements for **deferred maintenance** of facilities and information technology infrastructures
  - Time-sequenced borrowing of $400M by issuance of bonds
  - Amount to be distributed between building renovations and IT projects
  - Maximum 40-year impact on operating budget
- Impact of future building projects on operating funds (constructions and maintenance costs)
  - Current Master Plan initiatives:
    - Royal Victoria Hospital
    - Powell Building
    - Fiat Lux (McLennan-Redpath Library)
    - 680/688 Sherbrooke St. West conversion
    - Wilson Hall
    - Neuro Strategic Facility Plan (Montreal Neurological Institute and Hospital)

Unrestricted Revenue Fund Capital Assets

These figures do not include:

- 1. Goods and services that do not meet government or internal capitalization requirements.
- 2. Cost of time of administrative and support staff supporting capital projects that is not recorded by project managers (e.g. most likely on IT projects – time of staff with business expertise outside ITS writing needs assessment, designing specs, performing testing and validation of new IT systems).



FY2020: MEES Capital Fund

- MEES confirmed McGill's annual capital budget for FY2019 would be based on a different distribution formula that takes into account the age of the university's infrastructure.
- Chart on the right excludes special capital grants that may be received by the University for specific projects (e.g., Wilson Hall, MacDonald-Stewart Library, RVH study, etc.)

($M)	Budget FY2018: $47.5M	Budget FY2019: $85.7M	% Change 80.4%
IT and Libraries operating envelope transfer (1)	$2.4	$2.1	-12.5%
IT Development (incl. Libraries) (1)	$1.9	$1.9	0.0%
Deferred Maintenance (new program) (2)	$15.1	$40.1	165.6%
Deferred Maintenance (current program) (2)	$10.2	$9.8	-3.9%
Redesign of existing space (réamenagement) (3)	$3.1	$4.1	32.3%
Renovations (patrimonial sites) (3)	$-	$5.1	-
Renovations (corrections) (3)	$3.5	$9.6	174.3%
Renovations (3)	$11.3	$13.0	15.0%

(1) Portfolios: IT Infrastructure & Institutional Priorities

(2) Portfolio: Physical Infrastructure

(3) Portfolios: Institutional Priorities & Student Life and Learning

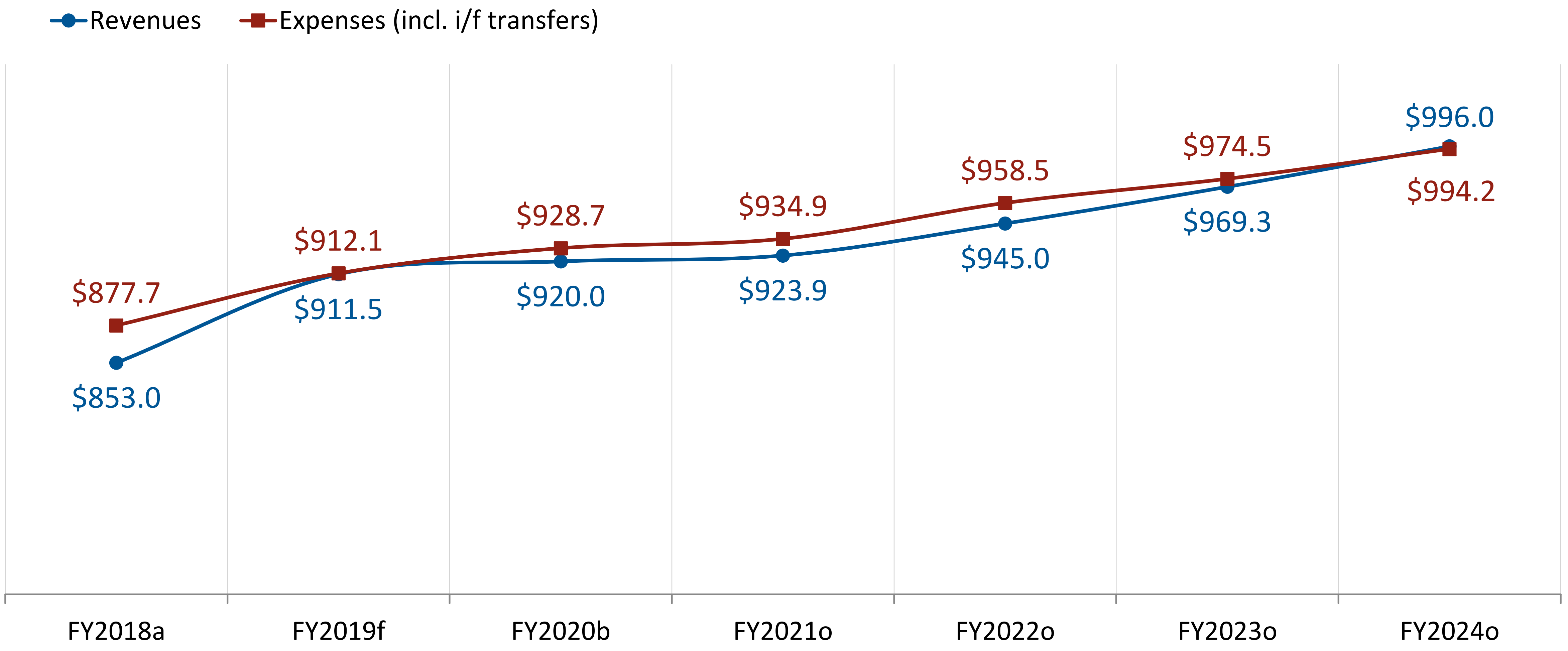
FY2020: Restricted and Endowment Funds

- **Restricted Fund**
  - Primarily composed of research grants and other special purpose revenues
  - Anticipated revenues = $415M, up from $403M forecasted for FY19

- **Endowment Fund**
  - Market value as of February 28, 2019: $1.649B (vs. $1.634B as of February 28, 2018)
  - Increased by approximately 1.5% (first 10 months of FY2019)
  - Higher interfund transfers to other funds expected in FY2019 vs. FY2018

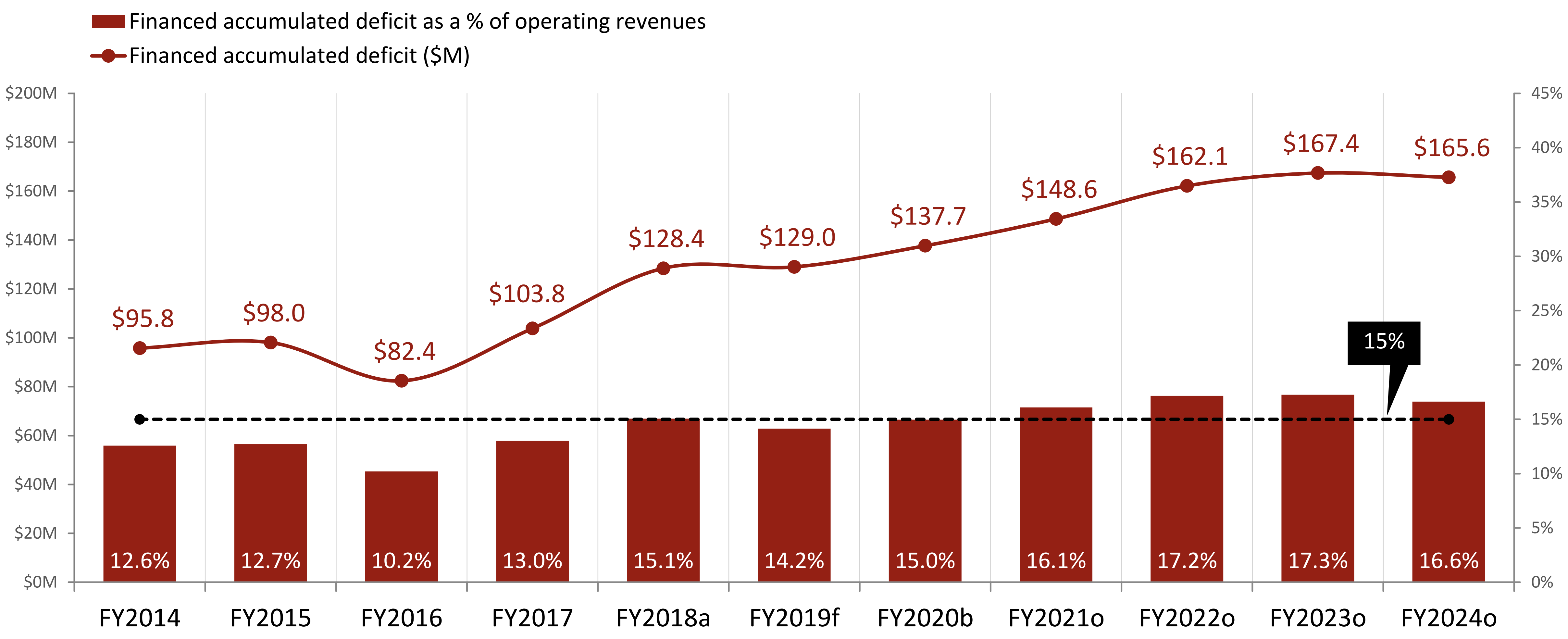
- **Philanthropic cash revenues and pledges**
  - FY2019 forecast = $115M to $135M
  - FY2020 budgeted within a corridor of between $125M to $145M

Projected Operating Revenue and Expenditure Through FY2024 ($M)



a = actual; **f** = forecast **b** = budget; **o** = outlook

Operating Fund: Financed Accumulated Deficit



a = actual; **f** = forecast **b** = budget; **o** = outlook

A Final Note

- This financial outlook informs our understanding of the resources the University has to achieve its academic mission in FY2020 and onward.
- The effectiveness of available resources in achieving the University's academic mission also depends on current internal policies (i.e., both their design and application) and on non-financial drivers.
- The University is developing Business Intelligence that enables the ability to link University resource use with achievement of the academic mission of the University:
  - Data production
  - Data governance
- The University must ensure that its staff has the required financial skills to process budget transactions correctly, technical skills to use detailed data beyond pre-formatted reports, information management skills, and ability to transfer institutional memory or know where to obtain it.

Discussion

- Questions
- Comments
- Concerns
- Suggestions