

THE UNIVERSITY OF TENNESSEE  
BOARD OF TRUSTEES

MINUTES OF THE FINANCE AND ADMINISTRATION COMMITTEE

October 2, 2014  
Knoxville, Tennessee

The Finance and Administration Committee of The University of Tennessee Board of Trustees met at 3:15 p.m. EDT on Thursday, October 2, 2014, in Hollingsworth Auditorium on the campus of the Institute of Agriculture in Knoxville, Tennessee.

**I. CALL TO ORDER**

Charles C. Anderson, Chair, called the meeting to order.

**II. ROLL CALL**

Charles M. Peccolo, Treasurer and Chief Financial Officer, called the roll, and the following members of the Finance and Administration Committee were present:

Charles C. Anderson, Chair  
Joseph A. DiPietro  
J. Brian Ferguson  
John N. Foy  
Raja J. Jubran  
Sharon J. Pryse

Trustee Evans was unable to attend the meeting. Mr. Peccolo announced the presence of a quorum of the Committee. Other Trustees, administrative staff, members of the public, and representatives of the media were also present.

**III. CONSENT AGENDA**

Chair Anderson directed the Committee's attention to the Consent Agenda and called for requests to remove any items. Hearing none, the Chair called for a motion to approve the Consent Agenda, consisting of the following items:

- A. Minutes of Last Meeting
- B. FY 2014 Annual Flight Operations (Exhibit 1)

- C. Disclosure of Additional Revenue/Institutionally Funded Capital Projects, FY 2014-15 (presented for information only) (Exhibit 2)
- D. Real Property Transactions (Exhibit 3)
  - 1. 234 East Street Acquisition and Master Plan Amendment (UTHSC)
  - 2. Gulf & Ohio Railways Property Acquisition (UTK)
  - 3. 2035 Sutherland Avenue Acquisition and Master Plan Amendment (UTK)
  - 4. KUB Underground Electric Line Easement for Volleyball Practice Facility (UTK)
  - 5. KUB Gas Line Easement (UTK)
  - 6. Acquisition of Street Right-of-Way and Alley Interests from the City of Knoxville (UTK)
  - 7. 634 Old Fulton Road Acquisition (UTM)
  - 8. 779 Old Fulton Road Acquisition and Master Plan Amendment (UTM)

Trustee Pryse moved approval of the Consent Agenda. Trustee Foy seconded the motion, and it carried unanimously.

#### **IV. HR/COMPENSATION ADVISORY BOARD REPORT**

Vice President Linda Harig presented a report updating the Committee on the HR Redesign and the HR Strategic Plan (Exhibit 4, pages 1-13). Dr. Richard Brown, Chair of the Compensation Advisory Board (CAB), updated the Committee on the work of the CAB over the past year (Exhibit 4, pages 14-18).

With respect to progress in closing the market gap for compensation, Vice Chair Ferguson asked for the denominator of the current \$153 million gap. Controller Maples stated it is \$986 million for total salaries, representing a gap of approximately 15%.

Trustee Jubran then asked whether the amount the state appropriates for pensions is including in comparing University compensation to peers. CFO Peccolo responded that it is included, but any related unfunded pension liability is not included.

#### **V. TREASURER'S REPORT ON ENDOWMENT INVESTMENT PERFORMANCE**

Rip Mecherle, Executive Director of Investments, explained that the Endowment Investment Report (Exhibit 5) was provided without schedules

of investments or financial statements. The full version of the report can be supplied if requested.

The pool has crossed the line of \$1.1 billion with strong market performance and gifts since the credit pre-crisis of 2007. The CIP fiscal year distributions were then presented. Looking at fiscal year 2014, those distributions began July 1, 2013 and those calculations took into account the previous calendar end value in 2012 plus 2011 and 2010. He then presented a backward biased chart showing data feeding into each of these distributions multiple years behind the actual fiscal year presented. Additionally, in 2012 UT changed the expenses charged to the Pool by adding 50 basis points to help fund development expenses of the UT Foundation, Inc. Normalizing that, there would be \$2.5 to \$3 million added to each of the last three years, putting 2014 closer to a \$33.4 level back in line with 2010. The credit crisis drew it down in 2012 and the change of expense ratio also had an impact.

The Pool's asset allocation relative to the NACUBO universe was presented, and Mr. Mecherle reported that the Pool's 17.4% return for the year might put the University in the top quartile for fiscal year 2014. He noted the Pool had outperformed NACUBO in the last seven out of ten years. Mr. Mecherle concluded by saying the Pool had performed better than expected given the strong performance of the US Markets, to which it is underweighted.

## **VI. TREASURER'S FINANCIAL REPORT**

CFO Peccolo explained that the Treasurer's Financial Report (Exhibit 6) is a draft because the audit is still underway. We do not yet have financial statements for the three components: UT Foundation, Inc., UC Foundation, and UT Research Foundation. The final report will be published with the auditor's opinion letter as soon as it is available, around the end of the year. He noted that the University has been working with the auditors for four months, and as of yesterday there were no findings at all.

The University's assets grew over 5%, liabilities were up over 8%, and net position was up 4%. The reason the receivables decreased by \$52.4 million is partially because Foundation pledges (receivables) have moved from the University's books to the Foundation's books. Additionally, there was a more timely settlement of money between the University and the UT Foundation, Inc. which resulted in a decrease of receivables.

Bonds increased \$58.6 million because Tennessee State School Bond Authority issued additional debt for the University during the last fiscal year

to finance construction projects for revenue generated facilities (auxiliaries primarily). The deferred revenues increased due to sponsored projects funding received on the front end with the research work still to do. Most of the other categories remain constant year over year. Salaries and benefits are the bulk of the University's expenditures at almost 70%. Trustee Pryse asked if the \$1 billion expense on behalf of faculty and staff is really more than that, making the percentage gap even higher. CFO Peccolo said yes, the total with benefits is \$1.3 billion.

Trustee Wharton asked why scholarships dropped in 2014. Controller Ron Maples explained that GASB 34 and 35 require the University to reflect some scholarships as discounted against tuition revenue.

Committee members continued discussing the impact of the University unfunded pension liability on the compensation gap, and Mr. Peccolo reiterated that the unfunded pension liability was not included in the analysis that produced the compensation gap of approximately \$153 million.

#### **VII. POLICY ON THE PROCESS FOR SUBMITTING LEGISLATIVE PROPOSALS AND FUNDING REQUESTS TO THE GENERAL ASSEMBLY**

CFO Peccolo began by saying that the Policy on the Process for Submitting Legislative Proposals and Funding Requests was developed as a result of a new Public Chapter 538 passed by the General Assembly this past year. In summary, it requires the two higher education systems to follow an established process for developing operating and capital outlay budgets and presenting them to the General Assembly and requires any requests or initiatives outside the normal process to be endorsed by the chief executive officer of the unit and the University President. The proposed policy requires that any such requests or initiatives outside the normal process be advanced by the President, but requests are first submitted to the Chief Financial Officer, who will review them with the President and the campus chief executive officer.

Trustee Jubran moved that the policy titled "Process for Submitting Legislative Proposals and Funding Requests to the General Assembly" be approved as presented in the meeting materials (Exhibit 7). Trustee Pryse seconded the motion; and it carried unanimously.

#### **VIII. FY 2015-16 OPERATING BUDGET APPROPRIATIONS REQUEST FOR NON-FORMULA UNITS**

CFO Peccolo stated that each year the University has the opportunity to compile a new funding priority list for the non-formula units, which are all operations except UT Chattanooga, UT Knoxville and UT Martin. The list is submitted to THEC, which then submits both the UT and TBR lists to the Governor's office for consideration as the State develops the budget for the next year. To the extent there are new State dollars that can be appropriated to these units, the list represents how the funds will be deployed. There was approximately \$44.5 million submitted on various initiatives with one fourth of it designated toward compensation issues. The remaining is for new initiatives that include staffing, operating costs, and equipment. We remain hopeful there will be new dollars for non-formula units for this year, but at present it looks doubtful.

Trustee Pryse moved that the University's FY 2015-16 operating budget appropriations request for the non-formula units be approved as presented in the meeting materials (Exhibit 8). Trustee Jubran seconded the motion; and it carried unanimously

#### **IX. FY2015-16 CAPITAL OUTLAY AND CAPITAL MAINTENANCE PROJECTS**

CFO Peccolo advised the Committee that his team meets with campus leadership in the early spring to review their prioritized list of capital needs. The campus lists are then compiled into a single list for the President and Chancellors to review. The University's prioritized list is then submitted to THEC, which combines it with the TBR list and submits a final Capital Outlay and Capital Maintenance Projects List for the Governor to consider. This year, the capital outlay considerations were based on how the facility would impact the Complete College Tennessee Act, STEM disciplines, and ensuring equitable distribution of capital outlay. Four years ago, this administration established a matching requirement of 25% of the total project cost for the formula units and a 10% matching requirement for the non-formula units. The first six items on the Capital Outlay list have either a significant amount or all of the match in hand and total over \$300 million.

Capital Maintenance is handled similarly to the Capital Outlay process. Last year the University received \$40 million from the State, and this year the list totals around \$50 million. We have already submitted these lists to THEC due to the deadline being ahead of the Board meeting. Once the Board considers and approves, we will notify THEC of the final lists.

Trustee Pryse moved that the Capital Outlay and Capital Maintenance Funding Requests for FY 2015-16 and subsequent years be approved (Exhibit 9), with authorization to enter into contracts for design and construction for these projects within available funds. Trustee Foy seconded the motion; and it carried unanimously.

**X. FY 2015-16 REVENUE/INSTITUTIONALLY FUNDED PROJECTS**

CFO Peccolo explained that while the Revenue/Institutionally Funded Projects are included in the Governor's budget, there is no State funding involved. The University finances these projects, which are typically auxiliary related improvements or projects tied to a revenue stream. Projects totaling \$71.5 million are on the list by campus. The list is submitted to THEC, which then submits it for inclusion in the Governor's budget in its entirety.

Trustee Jubran asked if all the projects on this list were priority, and President DiPietro said they are real needs. CFO Peccolo noted there were three projects on the list that are listed as planning. Those projects will be submitted and funded by the institution, but they really apply to early design costs for items on the \$360 million list. Trustee Jubran requested confirmation that it is part of the 25% match, and CFO Peccolo confirmed.

Trustee Jubran then asked how much reserves there are for each of the campuses. CFO Peccolo responded that he would provide the information after the meeting. He noted that based on the Net Unrestricted Balance on the financial statement, the total is approximately \$400 million.

Trustee Lampley expressed concern about the Engineering Services Facility, which is badly needed for Nuclear Engineering at UT Knoxville, noting that it dropped in ranking from fourth to fifth. Dr. DiPietro explained that the timing of primary gifts for projects sometimes will affect the ranking. Dr. DiPietro also explained that financing projects through general revenue bonds is tempting because of low interest rates, but because the state budget office uses 11% as a debt service estimator, our ability to meet the debt service is compromised by the condition of the state's general revenue.

Trustee Jubran moved that the Revenue/Institutionally Funded Projects for FY 2015-16 be approved (Exhibit 10), with authorization to enter into contracts for design and construction of these projects, within available funds, and, with the approval of the President, for design and construction of other revenue/institutionally funded projects identified during the fiscal year

within available funds. Trustee Pryse seconded the motion; and it carried unanimously.

**XI. REPORT ON USE OF DIFFERENTIAL TUITION FUNDS AT UTC**

CFO Peccolo explained that the when approving the differential tuitions at Chattanooga and Knoxville, the Board requested an annual update on how the funds are being used. Beginning next year, the reports will be on the consent agenda at the Board's Fall Meeting.

CFO Peccolo presented the report on use of differential tuition funds at UTC (Exhibit 11). UTC collected \$2.2 million and spent approximately \$1.4 million. In Business, the carryover money is dedicated to program adjustments and additional faculty hires in process. Similarly, the College of Engineering and Computer Science has plans to hire two additional professional advisors. The timing of rolling out the program and collecting the differential tuition resulted in the unspent balance at the end of the year.

**XII. REPORT ON USE OF DIFFERENTIAL TUITION FUNDS AT UT KNOXVILLE**

CFO Peccolo presented the report of use of differential tuition funds at UT Knoxville (Exhibit 12), noting that UT Knoxville has collected approximately \$10 million with current expenses of \$9.8 million.

**XIII. OTHER BUSINESS**

There was no further business to come before the Committee.

**XIV. ADJOURNMENT**

There being no further business to come before the Committee, the meeting was adjourned.

Respectfully Submitted,



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Charles M. Peccolo  
Treasurer and Chief Financial Officer