

MEMORANDUM

TO: Capital Development Committee
Joint Budget Committee

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SUBJECT: Higher Education Cash Funded Capital Construction

DATE: February 12, 2009

Staff for the Joint Budget Committee (JBC) and Capital Development Committee (CDC) reviewed the existing legislative approval process for higher education cash funded projects to identify options for improving procedures. Two recent cash funded requests illustrated to staff ways that the current approval process may not meet the needs of the General Assembly. Also, recent changes in statutes governing the cash-funded project approval process, and testimony to both committees by higher education institutions calling for streamlining of the process, suggested to staff that changes may be necessary.

Background on the Review Process for Cash Funded Higher Education Construction

Higher education construction projects fall into two categories: 1) cash fund projects; and 2) General Fund projects. General Fund projects require an appropriation.

Cash funded projects are treated differently based on how much they cost and the source of funds. Projects under \$2.0 million may proceed without legislative review or review by the Colorado Commission on Higher Education (CCHE). Statutes do not define what constitutes a project, and so an institution could chop construction work into little pieces so that each piece is less than \$2.0 million. Pursuant to statute, cash funded projects costing less than \$2.0 million are reported annually to the General Assembly. This annual report currently includes the project title, square feet added (if any), and total cost. Frequently the project title identifies the building or buildings impacted.

Cash funded projects costing more than \$2.0 million are eligible for expedited review through the traditional S.B. 92-202 process, or through a new process established by S.B. 08-018 (Windells/Massey). The traditional S.B. 92-202 process applies to projects constructed, operated,

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and maintained from student fees, auxiliary facility funds, wholly endowed gifts and bequests, and/or research building revolving funds. Examples of projects fitting the traditional S.B. 92-202 criteria include dormitories, food service buildings, student unions, research buildings, and some athletic facilities.

For projects that meet the traditional S.B. 92-202 criteria, CCHE must review and approve or deny the facility program plan. The plan is then forwarded to the CDC and the CDC must make a recommendation to the JBC. The JBC reviews the project and submits a recommendation with written comments to CCHE. The roles of the CDC and JBC are advisory. Once the review process is complete, projects with CCHE approval may proceed without an appropriation. However, the JBC has traditionally included these projects in the next Long Bill for informational purposes.

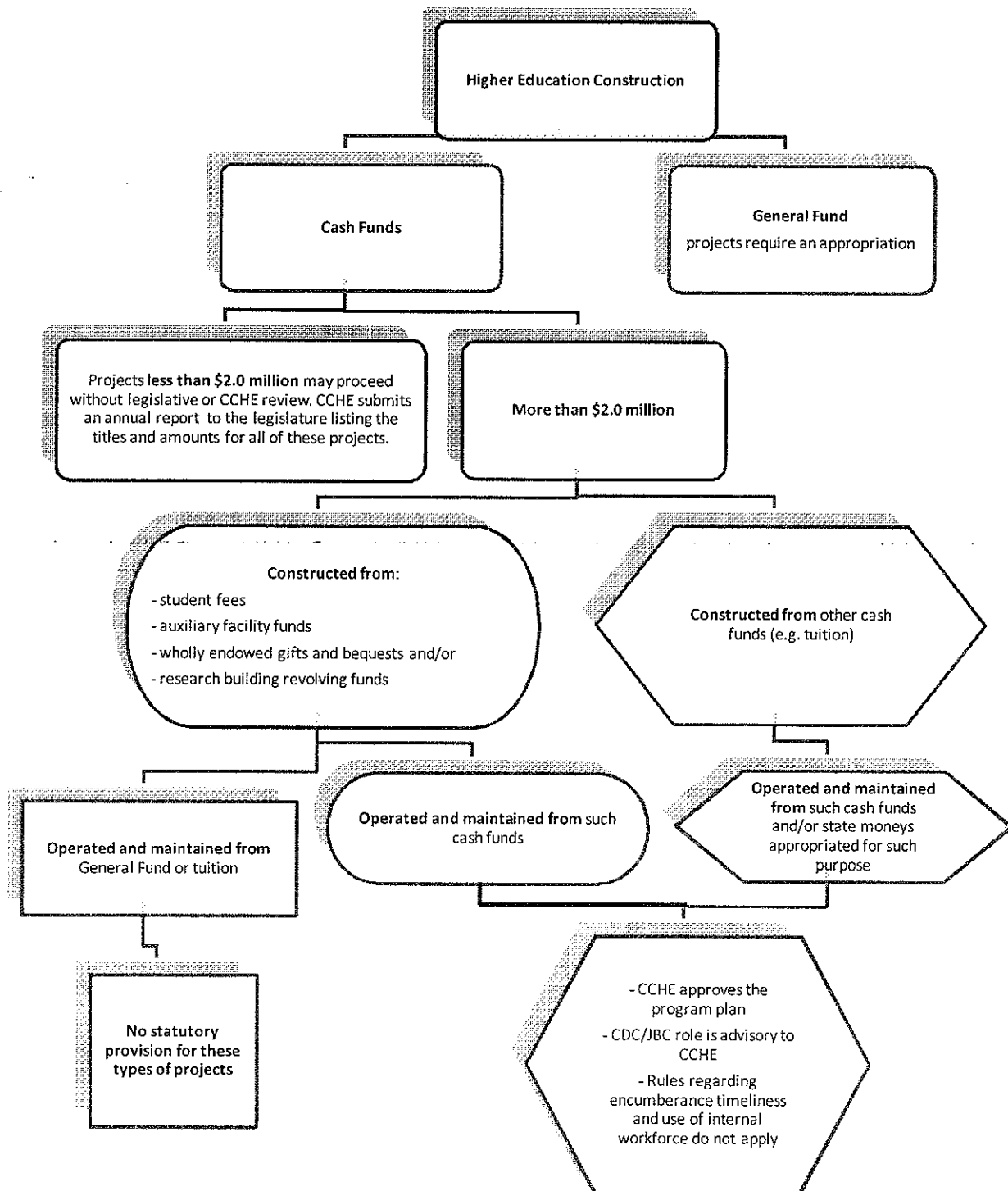
The new process created by S.B. 08-018 applies to projects constructed with cash funds other than student fees, auxiliary facility funds, wholly endowed gifts and bequests, and/or research building revolving funds. The only source of cash funds that staff can think of that would fit this criteria is tuition. Operation and maintenance costs for S.B. 08-018 projects can be paid from cash funds or the General Fund. The approval process for S.B. 08-018 projects mirrors the S.B. 92-202 process.

Some institutions have implemented special tuition charges dedicated to capital construction. The S.B. 08-018 process would allow projects associated with these special tuition charges to go through an expedited review. In addition, the S.B. 08-018 process could be applied to a much broader range of projects. Because tuition and General Fund are fungible, an institution could conceivably use the S.B. 08-018 process to seek expedited review for a project constructed using General Fund appropriated for the operating budget. An institution could start a project through the S.B. 08-018 process, and then request General Fund to complete the project, or operate and maintain the building. No construction projects have been approved through the S.B. 08-018 process to date. But, with the passage of S.B. 08-018 just about any higher education construction that doesn't require a General Fund appropriation in the first year could be started through an expedited review process with CCHE approval and advisory recommendations from the CDC and JBC.

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Problems with the Cash Funded Review Process

There is one type of project that can't proceed through either the S.B. 08-018 or S.B. 92-202 process. This would be a project constructed from student fees, auxiliary facility funds, wholly endowed gifts and bequests, and/or research building revolving funds, but operated and maintained from General Fund or tuition. Not only does this type of project fail to qualify for expedited review, current law may prohibit an appropriation for this type of project. Section 24-75-303, C.R.S. says that no capital construction project for a state-supported institution of higher education may commence unless it meets either the S.B. 92-202 or the S.B. 08-018 criteria.

The Institute for Teaching and Learning (TILT) proposed by Colorado State University at Fort Collins appears to fall into this prohibited category of capital construction. This \$13.0 million renovation and addition to convert the Music Building to a new purpose would be constructed with a \$10 per credit hour student fee, but it would be operated and maintained with General Fund and tuition. If this project were funded with a \$10 per credit hour increase in tuition, rather than a student fee, it would meet the S.B. 08-018 criteria.

The relevant portion of Section 24-75-303, C.R.S. is reproduced below:

(3) (a) No capital construction project for a state-supported institution of higher education that is estimated to require total expenditures exceeding two million dollars may be commenced unless:

(I) The project is to be constructed solely from cash funds held by the institution other than those funds specified in subparagraph (II) of this paragraph (a) and is to be operated and maintained from such cash funds or from state moneys appropriated for such purpose, or both, and the plan for the project has been approved by the Colorado commission on higher education pursuant to section 23-1-106 (10), C.R.S.; or

(II) The project is to be constructed, operated, and maintained solely from student fees, auxiliary enterprise funds, wholly endowed gifts and bequests, research building revolving funds, or a combination of such sources, and the plan has been approved by the Colorado commission on higher education in accordance with section 23-1-106 (9), C.R.S.

The Capital Development Committee recommended the TILT project for JBC approval. The JBC reviewed the project, but tabled any action pending a discussion with the CDC about legislative policies regarding cash funded higher education construction. The JBC had previously voted in the summer to have a meeting with the CDC when the session began to discuss a different cash funded

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higher education project.

In the summer the CDC and JBC were asked to approve a project that had already been started, raising questions about the purpose, value, and effectiveness of legislative oversight of cash funded higher education construction. Colorado State University at Pueblo transferred the title for five acres of land to the University's foundation. The foundation took out a short-term loan and began construction as a private entity on a new Student Housing Facility. The University requested legislative approval for the project after it had begun. Once legislative approval was provided, the University issued long-term debt to buy out the foundation's loan and transferred the property back to the University.

The University explains that there were concerns about completing the project in time for the semester, and there were delays in getting the Board of Governors to approve the project. To speed up the project, the University explored a ground lease to a private entity that would construct and then manage the housing facility. Several institutions have entered into these types of ground leases and current statutes do not require legislative approval. However, after beginning down the road to a land lease, the University and its foundation determined that the project could be constructed more cost effectively if the institution financed the project itself. The foundation offered to arrange short-term financing to begin the project in time for the semester while the University sought the necessary legislative approval.

When questioned about the legal basis for the land transfer, the University pointed to a 2003 Attorney General Opinion that found the Regents of the University of Colorado could transfer land to a private entity without consideration and without legislative approval, provided it was for a public purpose. Among many arguments, the opinion cited Article IX, Section 12 of Colorado's Constitution: "The governing boards of the state institutions of higher education, whether established by this constitution or by law, shall have the general supervision of their respective institutions and the exclusive control and direction of all funds of and appropriations to their respective institutions, unless otherwise provided by law." Through a statute, the General Assembly could choose to limit the authority of institutions to transfer property or enter ground leases, if it desires.

The JBC requested a meeting with the CDC because of these two projects, but *the JBC also heard testimony at the hearing with the Department of Higher Education that time associated with the CCHE and legislative review processes adds to the cost of construction projects.* The most detailed testimony came from the University of Colorado, which referenced a July 2007 Report to the President from the CU Capital Advisory Committee. According to the report, it takes CU an average of 32 months to get from project initiation to selecting an architect. Of this time, an average of 14 months is devoted to project approval. Much of the recommendations focused on the internal

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practices of the University, but the CCHE and legislative reviews also contribute to the time it takes to complete project approval. The following passages summarize some of the findings from the report that may be relevant in reviewing the legislative approval process:

With so many individuals, agencies, committees and boards having their say in review, each project becomes both the "property" of everyone and of no one. There is no single truly accountable and authoritative champion or steward, and the possibility of the initial concept being modified, cut back, delayed, or even rejected is very real. . .

Many of the (currently 18 to 20) individuals, agencies, commissions and boards should be removed from the process, and only those should remain which relate to the specific use of the project under consideration or its funding. This could reduce the current 32 month period covering phases 1, 2, and 3 by at least half and, under current conditions, could save as much as 10 to 15 percent in cost escalation. Early cost estimating could also be much more accurate and realistic.

Making many of the remaining reviews and approvals concurrent rather than sequential would further reduce time.

It is important to note that the average time required for approval described in the report includes both projects funded with cash funds and with General Fund, and that the report was published prior to the passage of S.B. 08-018. Statutes require "whenever possible" that the CDC and JBC complete the review of cash funded projects within 30 days after receiving the necessary information.

It is also important to note that the JBC did not debate, endorse, or refute the findings of the University of Colorado report. The JBC does not have a position on whether the legislative review process for cash funded higher education projects needs to be changed.

An Alternative Practice

Staff for the JBC and CDC discussed various options for reviewing cash projects and 202 projects. Based on current law and practice, and recent changes to Colorado law, staff identified three areas of importance to the legislature related to cash-funded projects:

- *Expedited review* -- The legislature has set up an expedited review process for 202 and cash projects to avoid project cost increases associated with waiting for legislative approval.

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- *Identification of potential impact on state funds* -- The original S.B. 92-202 process, and the expansion of the process in S.B. 08-018, preserved some legislative oversight of cash funded projects. Questions posed by CDC and JBC members suggest to staff that one of the primary concerns is the potential impact of cash funded projects on state-funded operating, construction, and maintenance costs.
- *Awareness of construction projects* -- The S.B. 92-202 process, and the expansion of the process in S.B. 08-018, ensure that the JBC and CDC are informed of construction projects costing more than \$2 million. The projects are included in the Long Bill for informational purposes for legislators outside the two committees. For projects under \$2 million, the Department of Higher Education submits an annual report pursuant to SB 01-209.

Staff recommends that the CDC and JBC consider sponsoring legislation to abbreviate the legislative review process for some cash funded higher education construction. The main components of the staff recommendation include:

- For projects where no General Fund will be required for construction, maintenance, or operating expenses, the requirement for legislative review would be eliminated;
- An expedited legislative review would be maintained for projects that require General Fund or tuition for maintenance or operating expenses; and
- The scope and purpose of the CCHE review would be defined in statute.

The staff recommendation would not eliminate the potential that an institution could start a project by transferring land to a foundation, and then ask for permission after the fact, as was the case with the CSU-Pueblo Student Housing Facility. However, the staff recommendation would significantly reduce the legislative approval process, which should reduce the reasons for an institution to consider that type of transaction.

The table below describes the staff recommendation in more detail.

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Current Practice	Alternative Practice	Comments
Projects under \$2.0 million	Same	
No legislative review, included in an annual report to the legislature	Same	As with current law, institutions could be creative in dividing construction work into many small projects under \$2.0 million each. However, it would be difficult to define "project" in statute. The staff proposal would ease approval procedures for cash funded projects, thereby reducing potential incentives for dividing construction work into many small projects.
Constructed, operated, and maintained from student fees, auxiliary facility funds, wholly endowed gifts and bequests, and/or research building revolving funds	Same	
CCHE approves the facility program plan	CCHE approves that the institution has an adequate plan for financing, maintaining, and operating the facility from sources other than the General Fund	CCHE could still consider design elements, space needs, and other items that are typically part of a facility program plan, but it would be in the context of determining whether the institution has a reasonable plan to ensure that the facility will not be a future burden on the state General Fund. This change in emphasis would reduce duplication of the work done by the governing board and architect. It would ensure that an entity outside of the governing board reviews the potential impact of the financing, operating, and maintenance plan on the General Fund. Finally, if there is strong local opposition to elements of the proposed construction work, the CCHE review may provide a more neutral forum for airing those concerns than the project review by the governing board.
CDC reviews the project and makes a recommendation to the JBC, and the JBC submits a recommendation and written comments to CCHE	The institution notifies members who represent the county where the project is located before the CCHE hearing	This eliminates the legislative review of auxiliary-funded projects, but maintains a notification requirement. It is modeled after a similar notification requirement for land and easement acquisitions by the Division of Wildlife in the Department of Natural Resources. <i>Optionally, a requirement could be added to notify the CDC and/or JBC.</i> The General Assembly does not currently approve the operating budgets of auxiliary programs, and this change would treat capital expenditures by these auxiliary programs the same way.
Once approved by CCHE, the project may proceed without a legislative appropriation	Same	
Approved projects are included in the Long Bill for informational purposes	Approved projects are included in the annual report to the legislature	The operating expenditures of auxiliary programs are not included in the Long Bill for informational purposes. This change would make the treatment of capital expenditures by auxiliary programs consistent. The information would still be available through the Department's annual report on cash-funded construction.

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Current Practice	Alternative Practice	Comments
Constructed from any source of cash funds, but funding for the operation and maintenance of the facility may include the General Fund and/or tuition	These projects would fit in the category that requires legislative review	Staff doesn't see a significant policy reason for prohibiting these types of projects, and so this solves a technical problem with the current statute by taking these types of projects out of "no man's land" and placing them in a review category. Staff recommends placing them in the category that requires legislative review because of the potential impact on the need for General Fund and tuition.
CCHE approves the facility program plan	CCHE approves that the institution has an adequate plan for financing, maintaining, and operating the facility	The logic for this change is similar to the logic for auxiliary-funded projects.
CDC reviews the project and makes a recommendation to the JBC, and the JBC submits a recommendation and written comments to CCHE	CDC reviews the project and makes a recommendation to the JBC, and the JBC approves or denies the project	Legislative review would continue for these projects to ensure that the General Assembly understands potential impacts on General Fund and tuition needs, and still supports the project. Until S.B. 08-018 passed, these projects required an appropriation, and so the proposed expedited review is still faster than the General Assembly's historic practice. To date, there have been relatively few projects meeting this criteria. There may be more requests of this nature in the future, if state capital funding continues to be limited, but staff still anticipates that the number of projects that might be slowed down by this legislative review requirement would be minimal.
Once approved by CCHE, the project may proceed without a legislative appropriation	Once approved by the JBC, the project may proceed without legislative appropriation	The decision by the JBC would be the last review of the project, rather than an advisory recommendation to CCHE.
Approved projects are included in the Long Bill for informational purposes	Same	

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Other modifications that the CDC and JBC may want to consider include:

- Require legislative review for facilities where the primary purpose is teaching
 - Current statutes and the staff recommendation designate different review procedures based solely on the source of funds, but sometimes there is little difference between student fees and tuition
 - If the primary purpose of a building is teaching, it may imply a state responsibility for operating and maintenance expenses such that the legislature should review the project
- Eliminate the CDC review of projects that will be constructed with cash funds, but funded for operating and maintenance from the General Fund and/or tuition
 - The CDC review may overlap with the review by CCHE and the governing board
 - If the purpose of the legislative review is to focus on potential General Fund and tuition impacts, the JBC may be the best entity to conduct that review
- Eliminate the CCHE review of projects
 - For projects constructed, operated, and maintained from cash funds, the CCHE review could be replaced with a statutory statement of legislative intent that these projects will not be eligible for state funding in the future and/or the tracking requirement describe in the last major bullet below
 - For projects constructed with cash funds, but operated and maintained from General Fund or tuition, the CCHE review may overlap with the CDC and JBC reviews
- Require the State Architect to track the authority used by an institution to construct a project, and whether the project is eligible for General Fund in the future based on that authority
 - Currently, institutions are on an honor system that if a facility is approved through the traditional S.B. 92-202 process, then the institution will not request General Fund for the project in a future year. There is no systematic tracking of whether a project is eligible for future General Fund appropriations, although the purpose of the building provides a clue.
 - The State Architect maintains an inventory of all state buildings and indicated that a field could be added with minimal effort to track how higher education projects were approved