THE CITY COLLEGES OF CHICAGO
FY2004 DRAFT BUDGET
Analysis and Recommendations

Prepared By
The Civic Federation
September 23, 2003

INTRODUCTION

The Civic Federation recently concluded its analysis of the draft FY2004 budget and the associated financial issues facing the City Colleges of Chicago. Based upon that analysis we offer the following comments. We are grateful to Chairman James Tyree and to the Board of Trustees for the opportunity to comment upon the budget prior to its approval. We would also like to congratulate Chancellor Wayne Watson and his staff for their hard won successes in the previous year and to thank them for an extremely informative briefing on the City Colleges' financial and academic status. We are particularly grateful to Vice Chancellor and Chief Financial Officer Abe Eshkenazi for his assistance in obtaining answers to specific questions and for responding to requests for additional information.

The Civic Federation **supports** the passage of the City Colleges' FY2004 budget, but has concerns regarding the transparency of the budget documents available to the public. The Civic Federation's support is based on total appropriations declining by $1 million, and growth in the operating budget being limited to less than 1%. This containment of growth in appropriations is in part the result of the measures implemented after the original budget deficit of $19 million was identified in January of this year. It is also the result of a difficult decision implemented in July 2003 to reduce staffing levels by 93 vacant positions and 112 employees. Although the gross property tax levy is being increased by $5 million, which is the maximum amount allowed by property tax caps, the City Colleges of Chicago have taken aggressive steps to control expenditures and have not increased tuition costs at a time when the affordability of educational services is of great importance. The importance of balancing the budget without increasing tuition costs cannot be overstated since the current economic situation is already resulting in increased numbers of students seeking access to educational services. The strategy of maximizing non-local revenue sources has been crucial to the City Colleges' ability to accomplish its goal of providing affordable access to education. Finally, improved financial management at the City Colleges has resulted in a decline in the amount of long-term debt per capita and an increase in the fund balance of the institution.

The Civic Federation is pleased that the City Colleges successfully negotiated a change in the State's funding formula for adult education programs. In our testimony on the FY2003 budget we stated that the old formula, "penalizes districts that make greater efforts to fund adult education through local source revenues (i.e. tuition, property taxes, grants) by cutting state funding," and that such a policy was, "illogical and counterproductive." We further contacted the Illinois Community College Board to express these opinions. The successful resolution of this issue should guarantee greater stability and certainty in the City Colleges' funding from the State of Illinois.

We would also like to commend the City Colleges for responding to our calls for a long-term financial plan and an improved budget format. The Strategic Financial Plan has already enabled City Colleges to better anticipate its financial situation and take corrective actions prior to reaching a crisis. We are pleased to see that this year's budget format takes steps toward being more transparent and user-friendly than the documents provided in previous years. The inclusion of a transmittal letter, an executive summary and a narrative description of each college's accomplishments and programs help the public to better understand how and why public funds are being appropriated in the budget.

In furtherance of improving public input and recognition of the Colleges' role as an educational institution, we call on the City Colleges to continue making improvements in the budgetary process by presenting a more detailed overview of the system as a whole and providing a formal document to the public for review at least 10 days prior to the hearing. Summary information that we would recommend for inclusion in the budget consists of Full-Time Equivalent (FTE) staff positions by location over time, detailed revenue trends over time, and appropriations by location over time. The Illinois Public Community College Act requires that a tentative budget be made "conveniently available to public inspection for at least 30 days prior to final action thereon" (110 ILCS 805/3-20.1). We would recommend that the public be provided with a copy at least 10 days prior to the public hearing in order to prepare potential testimony.

There is also reason for concern regarding the way in property tax information is presented in the budget. The only information that is provided details the net property tax revenue available for unrestricted purposes (i.e. operating funds). Other local governments, including the City of Chicago and Chicago Board of Education, provide a revenue summary that distributes the total property tax levy between Operating Funds and all the other funds such as Capital and Debt Service Funds. This kind of information accounts for, and portrays to the public, the distribution of the taxing agency's entire property tax levy among various functions. The current presentation of information in the City Colleges' budget could leave the reader with the mistaken impression that only $92 million in property taxes was extended for FY2003 or that the FY2004 property tax levy is actually declining. The Cook County Clerk's Office reports that in fact the total amount of the City Colleges' most recent property tax extension was $126 million, and the gross property tax levy for FY2004 will be $131 million. Given the increase in the total levy this year of $5 million this information is crucial for a complete understanding of the budget.

The continuation of slow economic growth and unemployment with the subsequent affect on governmental revenues makes it imperative that the City Colleges continue to contain costs in the upcoming year. We are encouraged by the new initiative to explore the possibility of changes to the State's equalization funding formula. However, The Civic Federation calls on the Board of Trustees to also examine tuition costs in light of both the cost of providing services and the community's interest in maintaining affordable access to education. Given the size of the physical plant it is also necessary to do everything possible to contain maintenance and utility costs. Finally, employee benefits and wages are the largest area of expenditures for the City Colleges. We congratulate the financial management team at the City Colleges for actively working with The Civic Federation and other local governments to issue a joint Request for Proposals (RFP) to provide prescription drug benefits to employees in seven different local governments. The next step must be to explore the possibility of consolidated health insurance purchasing. A recent Civic Federation study found that forming such an agreement consisting of the employees of seven major governments in the region would yield projected savings of $40.1 million for all the governments in the first year or $222 million over a 5-year period. Savings from such an insurance pool would be very beneficial to the District's financial situation.

FY2003 BUDGET HIGHLIGHTS

The City Colleges' new Strategic Financial Plan originally projected a deficit of approximately $19 million as of January 2003. The projected deficit has been eliminated and the budget balanced through the following steps:

- $10 million in increased revenue from enrollment and a revised State funding formula:
  - $5.5 million from greater than anticipated tuition revenues;
  - $4.5 million from increased State funding for Unrestricted Credit Hours, particularly in the area of Adult Basic Education.
- $5 million from budget cuts, including but not limited to:
  - Eliminating 205 non-core positions;
  - Cutting travel expenditures by 25%.
- $4 million in reserve funds.

In addition, the City Colleges have taken a number of steps to control operating costs, including:

- 21% reduction in the overall workforce over the last five years from 8,562 to 6,716;
- Increasing average class size to 27 students or 90% of capacity;
- Freezing salary increases for non-union employees saving $800,000.

The gross property tax levy is being increased by 3.47%, from $126.8 million to $131.2 million. The portion of the levy subject to the Property Tax Extension Limitation Law ("tax caps") will increase by 4.8% or $4.3 million, from $96.1 million to $100.4 million. This includes the 2.4% allowed by tax caps plus an estimated amount allowed for new property.

FINANCIAL ISSUES AND TRENDS

This section provides summaries of key issues likely to have an impact on the City Colleges' financial situation in the forthcoming fiscal year as well as expenditure, appropriation and revenue trends.

State Funding Issues

Recent changes in the State funding formula, resulting from a successful lobbying effort by the City Colleges, should improve the financial position of the District in both the short and the long term. These changes will address funding equity issues within the different program areas and eliminate a previously existing penalty applied to Community College Districts exerting greater local effort to fund adult education programs. Additionally, the City Colleges have a plan to maximize adult education funding. That strategy leaves the maximum possible amount of instructional costs in the unrestricted budget, thereby maximizing credit hour reimbursement. This is accomplished through 1) charging the minimum allowable instructional costs (credit hours) to grants; and 2) charging the maximum allowable non-instructional costs to grants.

Another State funding issue that should be addressed in the coming year is the manner in which the State calculates its equalization grants. These grants are intended to guarantee that each Community College District has roughly the same financial means at its disposal, regardless of the property wealth available to the District for purposes of taxation. Because the formula for distributing equalization grants does not take into account the existence of the Property Tax Extension Limitation Law (PTELL or "tax caps"), it assumes that a greater amount of property wealth is available to Districts than they can actually tax without seeking approval of the voters through a referendum. Correcting this oversight in the formula would also contribute greatly to the betterment of the City Colleges' financial position without requiring increased local effort.

Appropriations and Expenditures

The FY2004 budget proposes a total appropriation of $295 million, down $1 million from the FY2003 budget of $296 million.

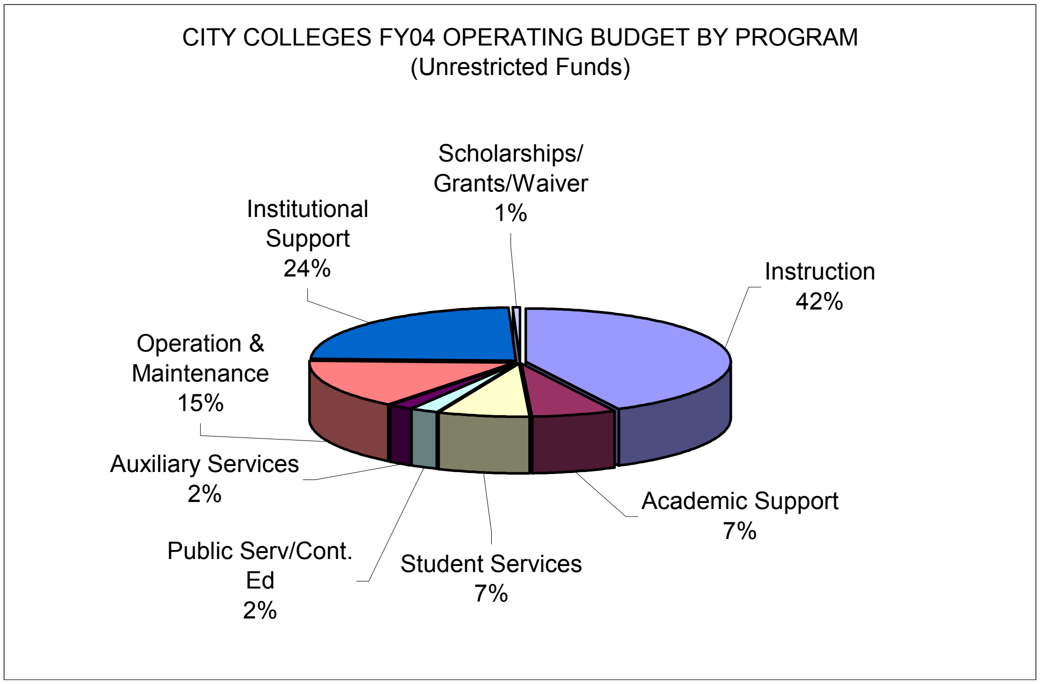
The FY2004 proposed operating budget includes $213 million from unrestricted funding sources and $81 million from restricted funding sources such as grants awarded and grants applied for but not yet awarded. In FY2004, unrestricted fund expenditures are projected to increase by 0.9%, from a proposed FY2003 appropriation of $211 million to $213 million in FY2004. Restricted fund revenues are expected to decrease 3.6% from $84 million to $81 million.

The main focus of this analysis is on the City Colleges' $213 million unrestricted funds operating budget. Seventy-two percent of the FY2004 appropriations, or approximately $153 million, is earmarked for employee salaries and benefits. The next largest amount, approximately $22 million, is proposed to fund contractual services.

CITY COLLEGES FY04 OPERATING BUDGET
BY OBJECT OF EXPENDITURE (Unrestricted Funds)

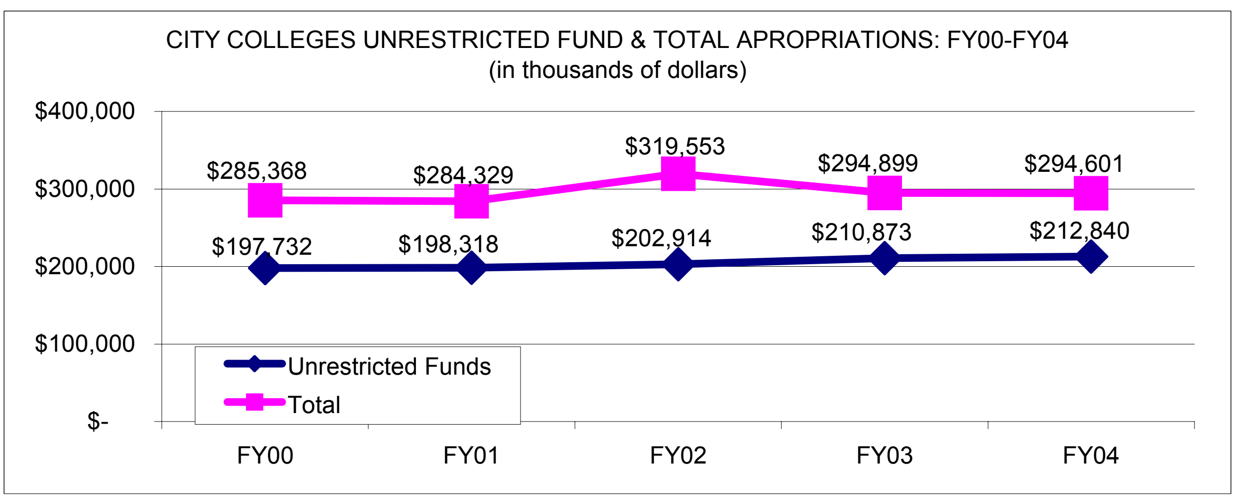
FY2004 Appropriation by Object	Amount	% of Total
Salaries	$ 122,272,125	57.5%
Employee Benefits	$ 30,775,558	14.5%
Contractual Services	$ 21,574,691	10.1%
Materials/Supplies	$ 12,389,094	5.8%
Travel/Conference	$ 1,782,359	0.8%
Fixed Charges	$ 2,161,163	1.0%
Utilities	$ 9,910,828	4.7%
Capital Outlay	$ 488,548	0.2%
Other	$ 11,485,897	5.4%
TOTAL	**$ 212,840,263**	**100.0%**

The following chart illustrates that 42% of the operating budget, or $90 million, is designated for instruction. The next largest amount, $51 million, is earmarked for institutional support. Operations and maintenance of the City Colleges' extensive physical plant will require $32 million, or 15% of the budget.



5-Year Appropriation Trends

The next exhibit presents 5-year appropriation trends for the City Colleges' unrestricted operating funds and total appropriations. Unrestricted operating fund appropriations rose 7.5% between FY2000 and FY 2004, from $198 million to $213 million, while total appropriations have risen 3.5% since FY2000. The spike of $320 million in FY2002 was due to an increase in restricted fund revenues, largely in the form of one-time grants.



While appropriations for Instruction have declined slightly, funds have been increasingly dedicated to Public Services and Scholarships. Academic Support has experienced modest growth, but Student Services and Operations & Maintenance have remained unchanged over the last five years. The largest decline in funding both in terms of dollar amounts and percentage changes has occurred in Institutional Support.

APPROPRIATIONS BY CATEGORY 5-YEAR TREND			
	FY2000	FY2004	% Change
Instruction	$ 107,225,000	$ 104,878,965	-2%
Public Services	$ 6,206,000	$ 11,242,270	81%
Academic Support	$ 18,878,000	$ 21,738,055	15%
Student Servicse	$ 19,308,000	$ 19,226,493	0%
Auxiliary/Enterprise		$ 4,133,602	
Institutional Support	$ 67,670,000	$ 57,260,669	-15%
Operation & Maintenance	$ 35,085,000	$ 35,101,876	0%
Scholarships/Fellowships	$ 30,996,000	$ 41,019,334	32%
TOTAL	**$285,368,000**	**$294,601,264**	**3%**

Personnel Trends

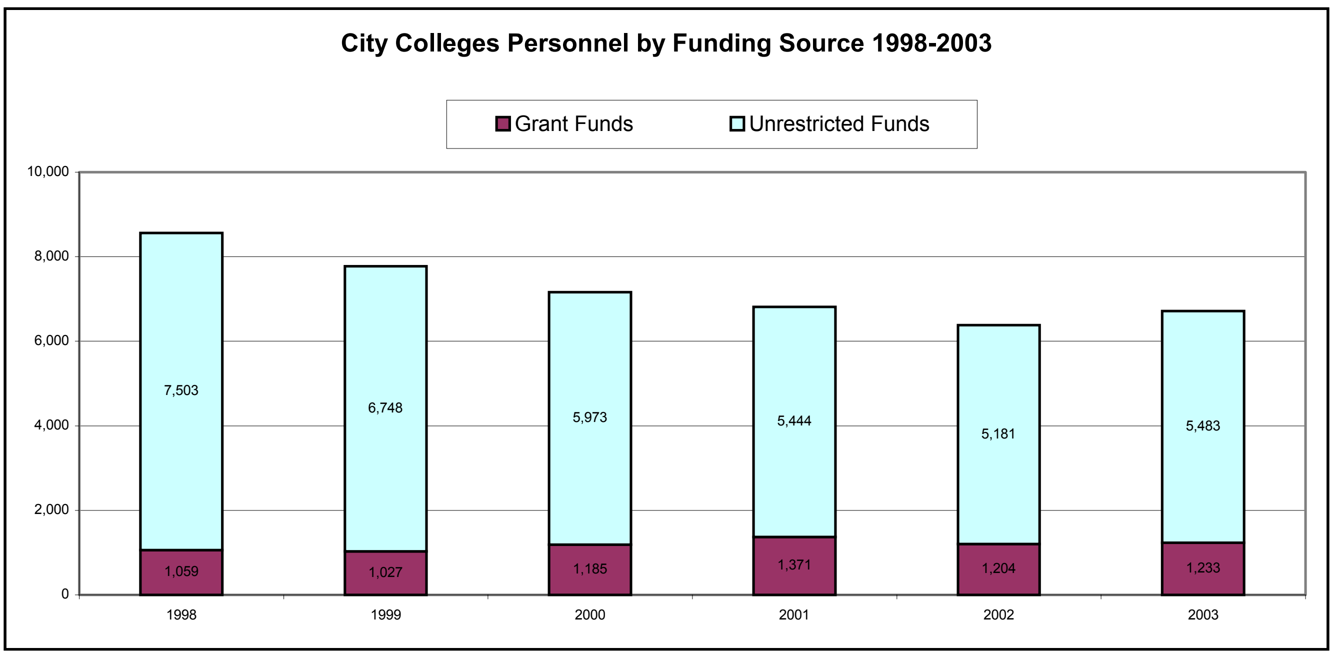
The City Colleges plan to fund 1,571.5 full-time positions in FY2004. Forty-one percent of full-time personnel are instructors, while 17.1%, or 269 positions, are in Operations & Maintenance.

CITY COLLEGES FY04 PLANNED FULL-TIME PERSONNEL BY PROGRAM (Unrestricted Funds)		
Program	Full-Time Positions	% of Total
Instruction	644.0	41.0%
Operations & Maintenance	269.0	17.1%
Institutional Support	228.9	14.6%
Student Services	207.5	13.2%
Academic Support	139.3	8.9%
Public Service/Continuing Ed.	76.0	4.8%
Auxiliary/Enterprise Activity	6.8	0.4%
TOTAL	**1,571.5**	**100%**

Over the past six years of actual data, the City Colleges have reduced the number of both full and part-time employees. Full-time staff is down by 13.8%, and part-time staff is down by 24%. Total personnel numbers have declined by 21% since 1998

CITY COLLEGES PERSONNEL 1998-2003							
	1998	**1999**	**2000**	**2001**	**2002**	**2003**	**1998-2003**
Full-Time	2,054	2,026	1,840	1,656	1,640	1,770	-13.8%
Part-Time	6,508	5,749	5,318	5,159	4,745	4,946	-24.0%
TOTAL	**8,562**	**7,775**	**7,158**	**6,815**	**6,385**	**6,716**	**-21.6%**

Over time a growing proportion of positions have been funded by grant dollars, and the number of positions funded by local tax dollars has declined. Over 2,020 positions funded by unrestricted funds in the operating budget have been eliminated.



Employee benefits represent 14.5% of the City Colleges' FY04 Operating Budget. The following exhibit provides a breakdown of the benefits costs. Over $24 million is allocated for employee health insurance.

CITY COLLEGES FY04 EXPENDITURES BY TYPE OF EMPLOYEE BENEFIT	
Benefit Type	**Amount**
Medical, Dental & Vision[1]	$ 24,088,500
Early Retirement & Termination Benefits	$ 4,750,000
Unemployment Compensation	$ 1,500,000
FICA & Medicare	$ 1,470,000
Life Insurance	$ 901,632
Disability & Workers' Compensation	$ 799,000
Pension Contribution - Grants	$ 385,524
Other Benefits	$ 28,000
Employee Contributions and Grant Reimbursements	$ (3,300,000)
TOTAL	**$ 30,622,656**

[1]Includes Health & Welfare Benefits for the Operations & Maintenance Unions

Revenue Trends

The City Colleges' own-source revenues (Property Taxes, Personal Property Replacement Taxes, investment income, tuition and fees, and auxiliary and enterprise activities) are projected to decline by 5.9% between FY2003 and FY2004, from $109.1 million to $102.7 million. Declines in investment income (down 25% from $2 million to $1.5 million) and auxiliary/enterprise revenues (down 11% from $10 million to $8.9 million) are expected, as well as no change in the PPRT. Due to higher enrollment, a 16% increase in tuition and fees collected is projected to make up for much of these revenue declines. State Aid is expected to rise very slightly, by $44,000. In addition to its traditional revenue sources, the City Colleges will draw upon $3.9 million in reserves to balance the FY2004 budget.

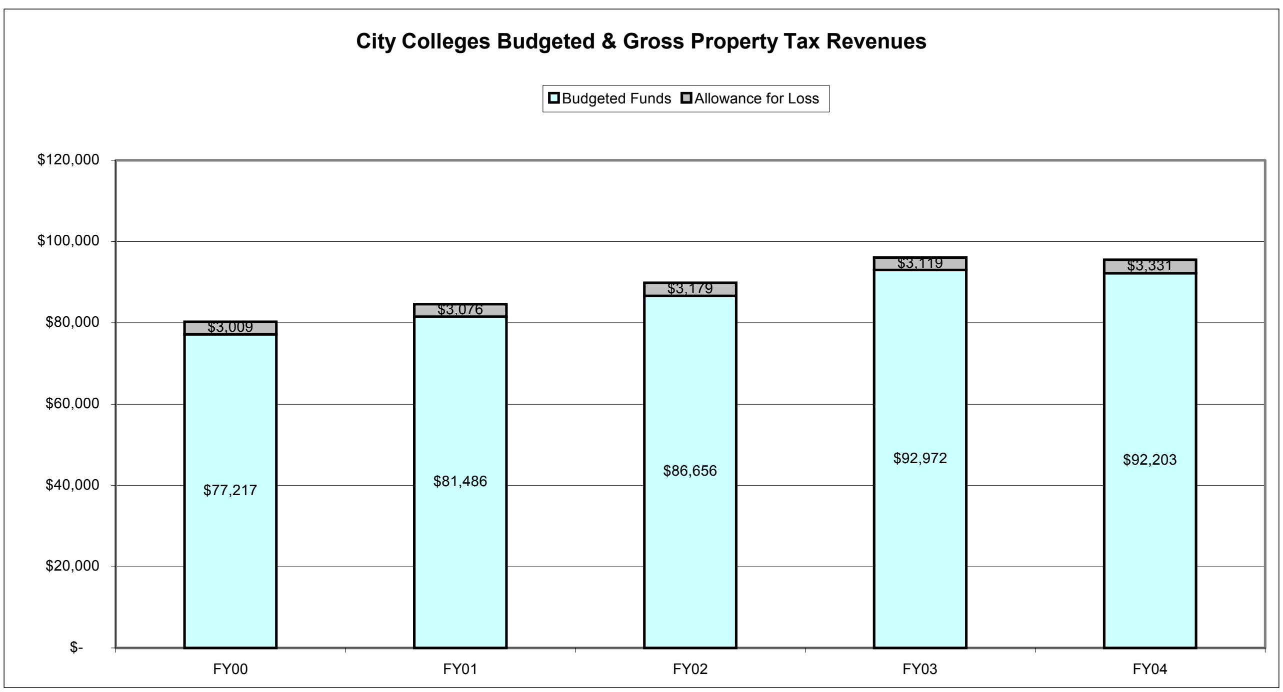
CITY COLLEGES OPERATING REVENUES: FY03 & FY04			
Sources of Unrestricted Revenues	**FY03**	**FY04**	**% Change**
Tuition & Fees	$ 49,833,222	$ 57,972,468	16%
Auxiliary/Enterprise Activities	$ 10,130,295	$ 8,992,347	-11%
Property Tax	$ 92,972,247	$ 88,227,752	-5%
PPRT	$ 4,000,000	$ 4,000,000	0%
Investment Income	$ 2,000,000	$ 1,500,000	-25%
State of Illinois	$ 46,962,423	$ 47,005,950	0%
Federal Government	$ 225,000	$ 227,501	1%
Other Sources	-	$ 1,020,000	-
Subtotal Revenues	**$ 206,123,187**	**$ 208,946,018**	**1%**
Use of Fund Balance	$ 4,749,453	$ 3,894,245	0%
GRAND TOTAL	**$ 210,872,640**	**$ 212,840,263**	**1%**

Property Tax Revenues (Operating Budget)

In FY2003 City Colleges changed the presentation of its operating budget's property tax revenues. Previously, a gross amount was included in the revenue section and a loss and cost of collection amount was included in the expenditure section. Since FY2003, the budget has included only a net revenue amount. In the FY2004 budget there is no longer a separate line item for the property taxes; instead, property tax revenue and PPRT revenue are combined under the classification of local revenues.

The budgeted portion of the City Colleges' property tax levy funding its operating budget is expected to decrease by 0.8% in FY2004, from $92.9 million to $92.2 million. Between FY2000 and FY2004 the budgeted amount of property tax revenue will increase by 19%, from $77.2 million to $92.2 million. Over this same time period the gross property tax levy, which is the amount actually requested from property taxpayers, will increase by 20%, from $80.2 million to $95.5 million.

The chart below demonstrates the difference between the budgeted amount of property tax revenues and the gross property tax levy.



Enrollment Trends

Enrollment in the City Colleges, as measured by Full-Time Equivalent (FTE) students[1], declined by 11.4% between 1999 and 2003. This decline was recorded for all programs except credit, manufacturing technology, and military. One of the most significant drops was in Vocational Skills, which has seen FTE enrollment fall nearly 33% since FY1999. Adult Education and Continuing Education enrollments have dropped 17% and 18%, respectively, since FY1999.

CITY COLLEGES FTE ENROLLMENT: FY99-03						
Type	**1999**	**2000**	**2001**	**2002**	**2003**	**1999-2003**
Credit	19,459	19,094	18,551	19,649	21,403	10.0%
Pre-Credit	872	819	734	834	830	-4.8%
Continuing Education	1,704	1,538	1,463	1,457	1,393	-18.3%
Special Interest	2,638	2,460	2,246	2,174	-	-100.0%
Adult Education	28,457	25,138	24,564	24,513	23,558	-17.2%
Vocational Skills	2,016	1,634	1,785	1,589	1,360	-32.5%
Mfg Technology	53	59	62	62	134	152.8%
Military	1,081	1,209	1,298	1,298	1,161	7.4%
TOTAL	**56,280**	**51,951**	**50,703**	**51,576**	**49,839**	**-11.4%**

The next exhibit shows a 5-year trend for certified credit hours by funding category, from FY1999 to FY2003. The number of certified credit hours fell by 7% in that time period, mirroring the decrease in FTEs. The number of credit hours in the Baccalaureate and General Academic programs rose by 10% and the number of credit hours in Business & Service Occupational rose by 12%. Credit hours in Health Occupational & Vocational, Technical Occupational & Vocational, and Adult Education/ESL have all declined, however, by 12%, 16%, and 17%, respectively.

5-YEAR TREND OF CERTIFIED CREDIT HOURS BY FUNDING CATEGORY			
Funding Category	**FY99**	**FY03**	**% Change**
Baccalaureate & General Academic	321,403	353,209	10%
Business & Service Occupational	44,087	49,430	12%
Technical Occupational & Vocational	79,965	67,018	-16%
Heath Occupational & Vocational	59,434	52,153	-12%
Remedial Education	101,023	109,449	8%
Adult Education/ESL	716,701	594,284	-17%
TOTAL	**1,322,613**	**1,225,543**	**-7%**

[1] A "Full Time Equivalent" student is equal to 30 semester hours.

Fund Balance: Current Fund Balance Ratio

The current fund balance ratio was devised by The Civic Federation to measure a government's ability to meet its financial obligations over time, long enough to convert illiquid assets to cash. It is calculated by dividing General Operating Fund expenditures (unrestricted and restricted) by the unreserved fund balances in those funds or under the provisions of GASB Statement Number 34, the unrestricted net assets. Historic trends are presented below for the City Colleges for FY1996 through FY2001. Ratios under 10% are categorized as "Low."

The City Colleges' fund balance ratio was 10.7% in FY2002, increasing from 6.9% in the previous fiscal year. Since FY1997, the fund balance ratio has increased dramatically, rising from just 0.1%. The Civic Federation commends the City Colleges' administration and financial management team for working to assure that the District has adequate reserves to deal with contingency situations.

CITY COLLEGES CURRENT FUND BALANCE RATIO				
	Unreserved Fund Balance	Operating Expenditures	Ratio	Rating
FY1997	$ 214,350	$ 242,632,403	0.1%	Low
FY1998	$ 198,000	$ 250,359,290	0.1%	Low
FY1999	$ 117,944	$ 270,379,241	0.0%	Low
FY2000	$ 3,034,911	$ 265,086,186	1.1%	Low
FY2001	$ 19,203,107	$ 278,247,017	6.9%	Low
FY2002	$ 30,144,800	$ 281,633,975	10.7%	Adequate

DEBT TRENDS

The Civic Federation has employed two measures of debt for purposes of this analysis: short-term debt trends and long-term debt per capita trends.

Short-Term Debt Trends

Short-term debt is a financial obligation that must be satisfied within one year. An increasing trend in short-term debt may be a warning sign of future financial difficulties. It is a measure of budgetary solvency, that is, a government's ability to generate enough revenue over the course of a normal budgetary period to meet its expenditures and prevent deficits

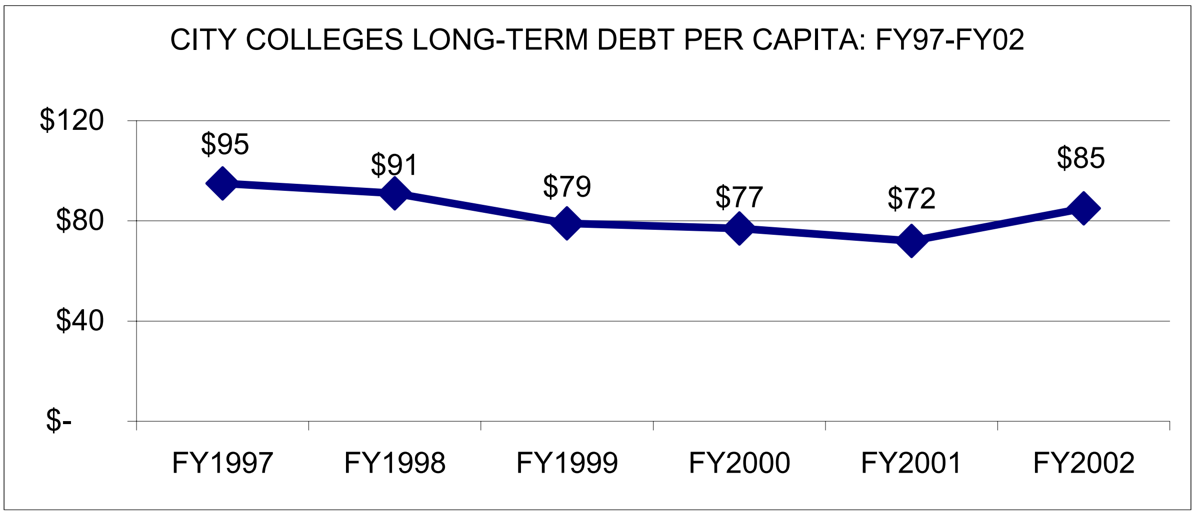
Short-term debt in the Current Funds includes obligations such as accounts payable, deferred salaries payable, deferred property tax revenue, defered revenue and termination benefits payable. In sum, it includes all liabilities except accrued salaries and wages, accrued payroll, compensated absences and long-term debt. Put another way, it includes all current liabilities less accrued payroll and the current portion of non-current liabilities.

City Colleges reported a 16% increase in short-term debt between FY1997 and FY2002, from $88 million to $102 million. Short-term debt rose from $96 million to $106 million between FY2001 and FY2002. These increases are not large and thus not a cause for concern at this time.

Long-Term Debt Per Capita

Long-term debt per capita is a measure of a government's ability to maintain its current financial policies. This long-term debt analysis takes the total liabilities in the General Long-Term Obligations Account Group and divides them by population. Any increases bear watching as a potential sign of increasing financial risk.

The City Colleges of Chicago's long-term debt includes capital lease arrangements with the Chicago Public Building Commission, 20-year revenue bonds issued to retire a prior note payable and termination benefits payable.[2] Long-term debt per capita increased by 11% between FY2001 and FY2002. However, over the six-year period between FY1997 and FY2002, long-term debt per capita declined by 11%, from $95 to $85. This is a positive long-term trend.



[2] The revenue bonds are recorded in the Comprehensive Annual Financial Report's Working Cash Fund, the amounts necessary to meet the capital lease payments are accumulated in the Retirement of Indebtedness Plant Fund and Termination Benefits payable are recorded in the Unrestricted Current Fund.

BUDGET PROCESS AND MANAGEMENT IMPROVEMENTS

This section discusses the City Colleges' strategic planning process, its major management initiative currently underway.

Strategic Planning Process

The Strategic Financial Plan (SFP) was developed in 2002 with input from a District-wide Task Force. It provides the City Colleges' the ability to project revenues and expenditures based in part upon assumptions about future enrollment and state funding. Such a device is crucial not only to the long-term financial planning of the City Colleges as a whole, but also for the individual colleges and departments in putting together accurate budget requests.

The SFP has already enabled City Colleges to better anticipate its financial situation and take corrective actions prior to reaching a crisis. In January of 2003 the SFP predicted a budget deficit of $19 million based upon enrollment trends and declining State funding. Armed with this information the City Colleges administration was able to take cost-cutting steps including the elimination of 212 non-instructional positions and a 25% reduction in travel expenditures.

CIVIC FEDERATION RECOMMENDATIONS

The Civic Federation has several recommendations regarding the City Colleges' financial situation and budget format.

Pursue Joint Purchasing of Health Insurance

We congratulate the financial management team at the City Colleges for actively working with The Civic Federation and other local governments to issue a joint Request for Proposals (RFP) to provide prescription drug benefits to employees in seven different local governments. The next step must be to explore the possibility of consolidated health insurance purchasing. A recent Civic Federation study found that forming such an agreement consisting of the employees of seven major governments in the region would yield projected savings of $40.1 million for all the governments in the first year or $222 million over a 5-year period. Savings from such an insurance pool would be very beneficial to the District's financial situation.

Provide Complete Information on Revenues

There is no information on the property tax levy provided in the draft budget. Other local governments, including the City of Chicago and Chicago Board of Education, provide a revenue summary that distributes the total property tax levy between Operating Funds and all the other funds such as Capital and Debt Service Funds. This kind of information accounts for, and portrays to the public, the distribution of the taxing agency's entire property tax levy among various functions. This information is crucial for a complete understanding of the budget.

Improve Budget Format

The Civic Federation urges the City Colleges to continue developing a more comprehensive and user-friendly budget. We believe that the budget document should, at minimum, contain features such as a more detailed budget and revenue overview that includes 5 years of data, and information about Full-Time Equivalent (FTE) staff positions. Citizens should be able to clearly understand the functions of the District and be provided an overview of its financial situation by reading the budget document.

Adopt Formal Financial Policies

The Civic Federation urges the City Colleges to consider development and adoption of formal written, publicly available financial policies to provide guidance in developing its annual budget. This should be a component of the long-term financial planning process as it is developed and implemented.