



**THE CITY COLLEGES OF CHICAGO
FY2003 PROPOSED BUDGET
Analysis and Recommendations**

**Prepared By;
The Civic Federation
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INTRODUCTION

The Civic Federation recently concluded an analysis of financial issues related to the City Colleges of Chicago's proposed FY2003 budget. Based upon that review and a consideration of some key issues that we believe will have an impact in the future upon the District's long-term financial condition, we would like to offer the following comments. The full text of our analysis follows this summary. The analysis includes sections on FY2003 Budget Highlights, Financial Issues and Trends, Budget Process and Management Improvements and Civic Federation Concerns and Recommendations.¹

The Civic Federation appreciates the difficult situation faced by the City Colleges and its financial management team in crafting a FY2003 budget that sustains basic programs in a time of rising costs, a sharp economic downturn and declining support from the State of Illinois.

We strongly applaud the City Colleges and its leadership team for initiating a District-wide strategic planning process. This is an excellent step toward implementing planning strategies and management improvements that will help the District better target resources at its core programs, monitor performance of its activities and be better prepared to address future financial and programmatic challenges.

The Civic Federation is also encouraged by Chancellor Watson's efforts to negotiate a change in the State's funding formula for adult education programs. We believe that the current formula, which penalizes districts that make greater efforts to fund adult education through local source revenues (i.e. tuition, property taxes, grants) by cutting state funding is illogical and counterproductive. We have expressed our concern to the Illinois Community College Board and voiced support for a restructuring of the formula that would mitigate the effects of this penalty and, in addition, provide the City Colleges with a greater degree of certainty in the funding stream from the State for its adult education programs. We understand that Chancellor Watson and other City Colleges officials are participating in a task force with ICCB to rectify the situation. Although Chancellor Watson has made a credible argument over past disparities of state funding for the City Colleges, it does not seem likely that retroactive reimbursements will be forthcoming from the State. It is our hope that the ICCB and the City Colleges can reach an equitable agreement on the funding distribution matter shortly and rectify the situation to impact current funding cycles.

While the City Colleges is making great strides to improve the management of its finances through development of a strategic planning process, the Civic Federation would expect to see more effort made in regard to the presentation of the annual budget. We believe that the City Colleges, as a public educational institution, should strive to develop a more transparent, comprehensive and user-friendly budget. As examples, the budget document should contain features such as a transmittal letter that describes in general terms the underlying document, a more detailed budget and revenue overview that includes 5 years of data, trend information about

¹ For an analysis of the City Colleges' financial condition between FY1991 and FY1999, please see Bowman, Woods. *Evaluating Local Government Financial Health: Financial Indicators for Community Colleges in Northeastern Illinois*. (Chicago: The Civic Federation, 2002), pp. 9-13.

Full-Time Equivalent (FTE) staff positions and narrative descriptions of expenditures and revenues as well as programs and departments.

Although we understand the timing pressures faced by City Colleges finance staff, we urge that in the future citizens should be given at least 10 days to review the proposed budget document before scheduling a hearing that seeks public comment and input. The current truncated time period between release of the budget and public testimony does not afford sufficient time for many interested citizens and education supporters to prepare for the public hearing.

Given the ongoing economic uncertainties, the City Colleges and most other local governments may well endure more bad fiscal news during FY2003. Thus, it is imperative that the District implement measures that can generate additional budgetary savings. We congratulate the financial management team at the City Colleges for actively working with The Civic Federation and other local governments to explore the possibility of consolidated health insurance purchasing and look forward to expeditious implementation of an agreement to achieve that goal. 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.

At this time, the Civic Federation would also like to draw the City Colleges Board's attention to recent decisions by the Illinois Property Tax Appeal Board (PTAB) that could result in potentially huge financial losses for the District and other local governments. If the decisions stand and are applied to all eligible property, the City Colleges could face a loss of as much as \$8.9 million per year (see Civic Federation report analyzing the impact of PTAB decision on Cook County local governments on our Web site). The PTAB's ruling is grounded in the wide discrepancy between law and practice in application of the Cook County classification system. As such, it is yet another problem with the antiquated Cook County property tax system that starkly illustrates the need for reform to make that system more consistent and equitable.

FY2003 BUDGET HIGHLIGHTS

The City Colleges' \$296 million FY2003 budget is balanced through by means of the following measures:

- A \$3.4 million property tax increase;
- An 11% increase in tuition and fees that will yield an additional \$4.8 million;
- The use of \$4.8 million in reserves; and
- Approximately \$1.2 million in savings realized due to renegotiation of utility contracts

It is worth noting that the City Colleges eliminated approximately 160 full and part-time positions in its FY2002 recession process after losing \$4 million in unrestricted State funding.

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.

Recent Property Tax Appeal Board Decisions: City Colleges Face Potential Annual Loss of \$8.9 Million

Recent decisions by the Illinois Property Tax Appeal Board (PTAB) could result in potentially huge losses in local government revenue and a significant tax burden shift onto homeowners. If the decisions stand and are applied to all property within the boundaries of the Chicago School District, The Civic Federation's projections indicate that the City Colleges could face a loss of \$8.9 million per year. The maximum potential loss to all governmental units in Cook County could well exceed \$500 million per year. These losses could come at a time when revenue growth is anemic due to the economic downturn.

The Illinois State Constitution requires that the highest assessment level be no more than 2.5 times the lowest assessment level. The Cook County ordinance that classifies property for taxation sets the lowest assessment level at 16% for residential property and the highest assessment level at 38% for commercial property. However, the Illinois Department of Revenue conducts studies every year claiming that residential property is actually assessed at closer to 10% of its value. Based on these studies, the PTAB has created a new level of assessment for non-residential (business and apartment) property. This new level of assessment is the result of multiplying the Department of Revenue's median residential assessment level of approximately 10% by 2.5. The result is a maximum assessment level of 25%. Therefore, a commercial property appealing its assessment to the PTAB would be assessed at 25% of its value, rather than 38% as the Cook County ordinance directs. This lower assessment level, if applied to all properties currently assessed at more than 25% of full value, would result in large refunds for commercial and industrial properties.

Unless it is addressed soon, PTAB's decision has the potential to cause a serious fiscal crisis for the City Colleges of Chicago. The Civic Federation believes that it is imperative that the District join with other local governments and the State of Illinois to address local governments' overreliance on property taxes.

State Funding Formula for Adult Education Programs

The current formula for allocating state support to community college adult education programs is based upon:

- A weighted cost per unit as determined by the unit costs of the number of certified credit hours plus an inflation factor;
- Less a district's own-source funding effort from taxes, tuition and grants;
- Plus an amount of rate support provided by the ICCB at its own discretion;
- Less a percentage deduction for Operations and Maintenance grants.

The formula is structured so that greater the degree of fiscal effort the District provides by raising taxes or tuition or accessing grant funds, the less it receives from the ICCB. The penalty for greater local effort, the two-year lag in funding and the discretion exercised by the ICCB in setting rate support all combine to create uncertainty in the City Colleges' budget for its adult education programs. In addition, when funding for adult education was shifted from the Illinois State Board of Education to the Illinois Community College Board recently, the number of dollars available to City Colleges was reduced. This issue is of great importance to the City Colleges system as adult education is the single largest program the District offers. 48% of FTE enrollment in the District in FY2002 and 53% of certified credit hours in FY2001 were in the adult education programs. This is a much higher percentage than in any other community college district in Illinois.

The Civic Federation believes that it is illogical and counterproductive to punish a District that increases its funding effort by reducing state funding by a corresponding amount. We have discussed the issue with the Illinois Community College Board and voiced our support for a restructuring of the formula that would mitigate the effects of this penalty and provide the City Colleges with a greater degree of certainty in the funding stream from the State for its adult education programs. We understand that efforts are currently underway to rectify the situation. It is our hope that the ICCB and the City Colleges can reach an equitable agreement on the matter shortly.

Appropriations and Expenditures

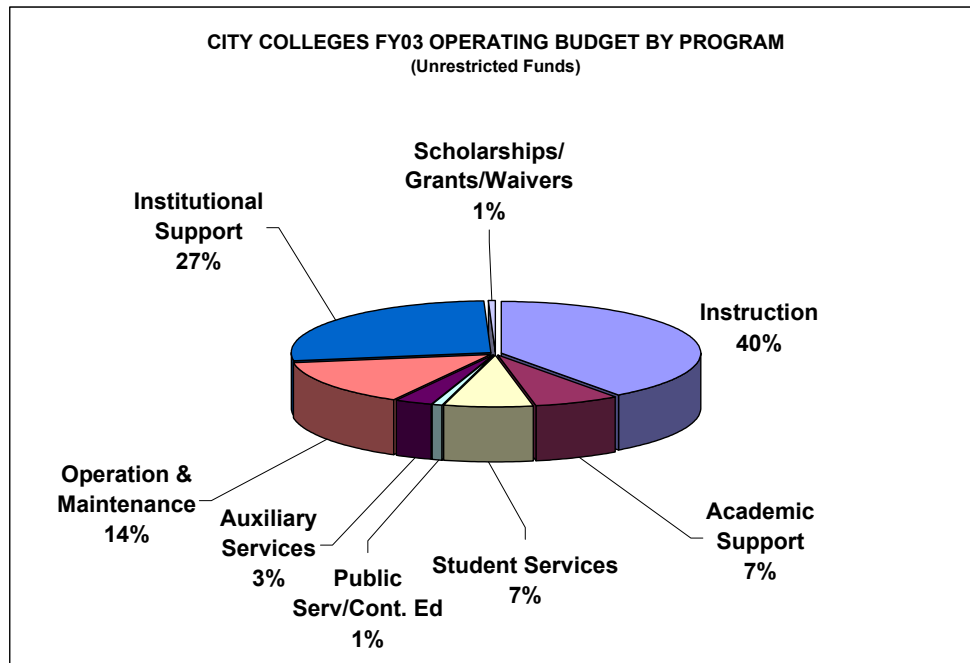
The FY2003 budget proposes a total appropriation of \$296 million. This represents a 7% decrease from the FY2002 budget of \$319 million.

The FY2003 proposed operating budget includes \$211 million from unrestricted funding sources and \$85 million from restricted funding sources such as grants awarded and grants applied for but not yet awarded. In FY2003, unrestricted fund expenditures are projected to increase by 4%, from a proposed appropriation of \$202 million last year. Restricted fund sources are expected to decrease by approximately 27%, from \$116 million to \$85 million. This is due to two factors: 1) the expiration of a number of one-time grants and 2) the loss of \$6 million from the elimination of program support grant from the state of Illinois.

The main focus of this analysis is on the City Colleges \$211 million unrestricted funds operating budget, which draws upon unrestricted sources of funding. 68% of the FY2003 unrestricted appropriations, or approximately \$144 million, are earmarked for salaries and benefits. The next largest amount, \$28 million, is proposed to fund contractual services.

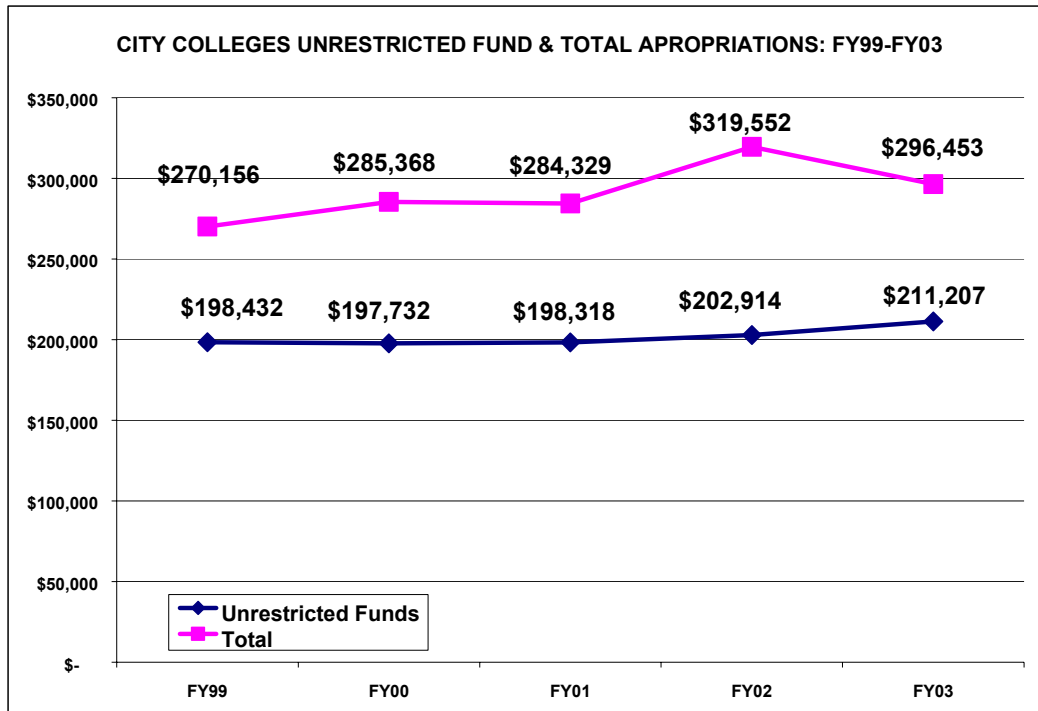
CITY COLLEGES FY03 OPERATING BUDGET BY OBJECT OF EXPENDITURE (Unrestricted Funds)		
FY2003 Appropriation by Object	Amount	% of Total
Salaries	\$ 117,299,828	55.4%
Employee Benefits	\$ 26,484,631	12.5%
Contractual Services	\$ 28,491,746	13.5%
Materials/Supplies	\$ 9,992,995	4.7%
Travel/Conference	\$ 1,549,575	0.7%
Fixed Charges	\$ 2,083,263	1.0%
Utilities	\$ 8,950,444	4.2%
Capital Outlay	\$ 955,501	0.5%
Other	\$ 15,399,399	7.3%
TOTAL	\$ 211,207,382	100.0%

Unrestricted operating expenditures by program area are presented in the next exhibit. 40% of expenditures, or \$84 million, are earmarked for instruction. The second largest amount, or \$52 million, has been proposed to fund institutional support. Operations and maintenance of the City Colleges' extensive physical plant will require 14% of the budget, or \$28 million.



5-Year Appropriation Trends

The next exhibit presents 5-year appropriation trends for the District's unrestricted operating funds and all appropriations. Unrestricted operating fund appropriations rose by 6% between FY1999 and FY2003, from \$198 million to \$211 million, while all appropriations increased by 10%. The larger increase in total appropriations was driven largely by the large increase in restricted fund revenues in FY2002. Because many of these restricted revenues were in the form of one-time grants, total appropriations decreased in FY2003.



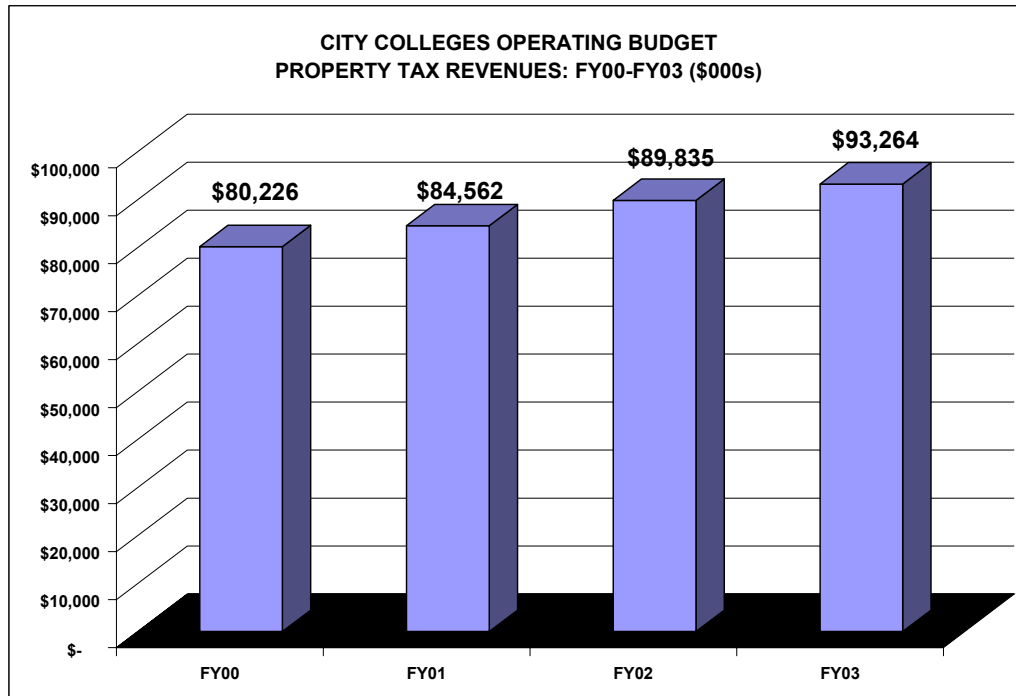
Revenue Trends

The District's own-source revenues (Property taxes, Personal Property Replacement Taxes, investment income, tuition and fees, and auxiliary and enterprise activities, are projected to increase by 3% between FY2002 and FY2003, from \$155 million to \$159 million. There will be sharp declines in investment income (down 33%, from \$3 million to \$2 million) and the PPRT (down by nearly 40%, from \$6.6 million to \$4 million). Tuition and fees will make up for much of the revenue decreases, rising by 11%. State aid, which constitutes 23% of all District revenues, is expected to decrease by nearly \$1 million. In addition to its traditional revenue sources, the City Colleges will also be drawing upon its reserves to help balance the FY2003 budget. These efforts will generate nearly \$4.8 million.

CITY COLLEGES OPERATING REVENUES: FY02 & FY03			
Sources of Unrestricted Revenues	FY02	FY03	% Change
Tuition & Fees	\$ 45,000,000	\$ 49,833,222	11%
Auxiliary/Enterprise Activities	\$ 10,424,000	\$ 10,130,295	-3%
Property Tax	\$ 89,835,000	\$ 93,264,045	4%
PPRT	\$ 6,600,000	\$ 4,000,000	-39%
Investment Income	\$ 3,000,000	\$ 2,000,000	-33%
State of Illinois	\$ 47,890,000	\$ 46,962,423	-2%
Federal Government	\$ 165,000	\$ 225,000	36%
Subtotal Revenues	\$ 202,914,000	\$ 206,414,985	2%
FY02 Surplus Carried Forward	\$ -	\$ 1,839,595	0%
FY03 Use of Fund Balance	\$ -	\$ 2,186,135	0%
FY02 Enterprise Fund Carry Forward	\$ -	\$ 766,666	0%
GRAND TOTAL	\$ 202,914,000	\$ 211,207,381	4%

Property Tax Revenues (Operating Budget)

The portion of the District's property tax levy funding its operating budget is expected to increase by 3.8% in FY2000, from \$89 million to \$93 million. Since FY2000, these revenues have increased by 16%.²



Enrollment Trends

Enrollment in the City Colleges, as measured by Full-Time Equivalent (FTE) students, declined by 9.8% between FY1998 and FY2002. This decline was recorded for every type of program, except credit programs, manufacturing technology programs and military programs. One of the most significant drops came in the large Adult Education program, which saw FTE enrollment fall by nearly 17%, from 29,406 to 24,513.

² A portion of the District's total property tax levy is levied by the City Colleges for payment of capital lease obligations to the Public Building Commission. These revenues totaled \$35 million in tax year 2000

CITY COLLEGES FTE ENROLLMENT: FY98-02						
Type	1998	1999	2000	2001	2002	1998-2002
Credit	19,201	19,459	19,094	18,551	19,649	2.3%
Pre-Credit	876	872	819	734	834	-4.8%
Continuing Education	1,899	1,704	1,538	1,463	1,457	-23.3%
Special Interest	2,449	2,638	2,460	2,246	2,174	-11.2%
Adult Education	29,406	28,457	25,138	24,564	24,513	-16.6%
Vocational Skills	2,233	2,016	1,634	1,785	1,589	-28.8%
Mfg Technology	32	53	59	62	62	93.8%
Military	1,093	1,081	1,209	1,298	1,298	18.8%
TOTAL	57,189	56,280	51,951	50,703	51,576	-9.8%

The next exhibit shows a 5-year trend for certified credit hours by funding category, from FY1997 to FY2001. The number of certified credit hours fell by 12% in that time period, mirroring the decrease in FTEs. The number of credit hours in the Baccalaureate and General Academic programs dropped by 15% and the number of credit hours in the Adult Education and ESL programs fell by 13%. These drops are significant because state funding to the City Colleges is based in part on the number of credit hours per program. However, it is important to note that the District anticipates an increase in the number of certified credit hours in FY2003. This is a positive sign and should help contribute to an improvement in the District's financial position in the future, if it is sustained and alterations are made to the adult education funding formula.

5-YEAR TREND OF CERTIFIED CREDIT HOURS BY FUNDING CATEGORY			
Funding Category	FY97	FY01	% Change
Baccalaureate & General Academic	347,990	295,807	-15%
Business & Service Occupational	57,496	49,233	-14%
Technical Occupational & Vocational	76,762	76,973	0%
Health Occupational & Vocational	66,926	55,751	-17%
Remedial Education	98,949	92,510	-7%
Adult Education/ESL	724,314	632,978	-13%
TOTAL	1,372,437	1,203,252	-12%

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. Historic trends are presented below for the City Colleges of Chicago for FY1996 through FY2001. Ratios under 10% are categorized as "Low."

As the exhibit below shows, the City Colleges of Chicago current fund balance ratio averaged 1.4% over the 5-year period analyzed, placing it in the "Low" category. However, the situation improved dramatically over the last two years analyzed. In FY2000, the fund balance rose from approximately \$118,000 to \$3 million. In FY2001, it increased to \$19 million, producing a currently fund balance ratio of 6.9%. While the FY2001 current fund balance ratio is still ranked

“Low,” the Civic Federation commends the City Colleges for substantially improving their ability to meet contingencies by substantially increasing the size of their fund balance.

In order to balance the FY2003 budget, the District proposes to use \$4.8 million in reserves. While this is an appropriate use of reserve funds, we caution the District against drawing down its reserves too deeply.

CITY COLLEGES CURRENT FUND BALANCE RATIO				
	Unreserved	Operating		
	Fund Balance	Expenditures	Ratio	Rating
FY1996	\$ 173,818	\$ 235,154,389	0.07%	Low
FY1997	\$ 214,350	\$ 242,632,403	0.09%	Low
FY1998	\$ 198,000	\$ 250,359,290	0.08%	Low
FY1999	\$ 117,944	\$ 270,379,241	0.04%	Low
FY2000	\$ 3,034,911	\$ 265,086,186	1.14%	Low
FY2001	\$ 19,203,107	\$ 278,247,017	6.90%	Low

Short and Long-Term 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, deferred revenue and termination benefits payable. In sum, it includes all liabilities except accrued salaries and wages, accrued payroll, compensated absences and long-term debt.

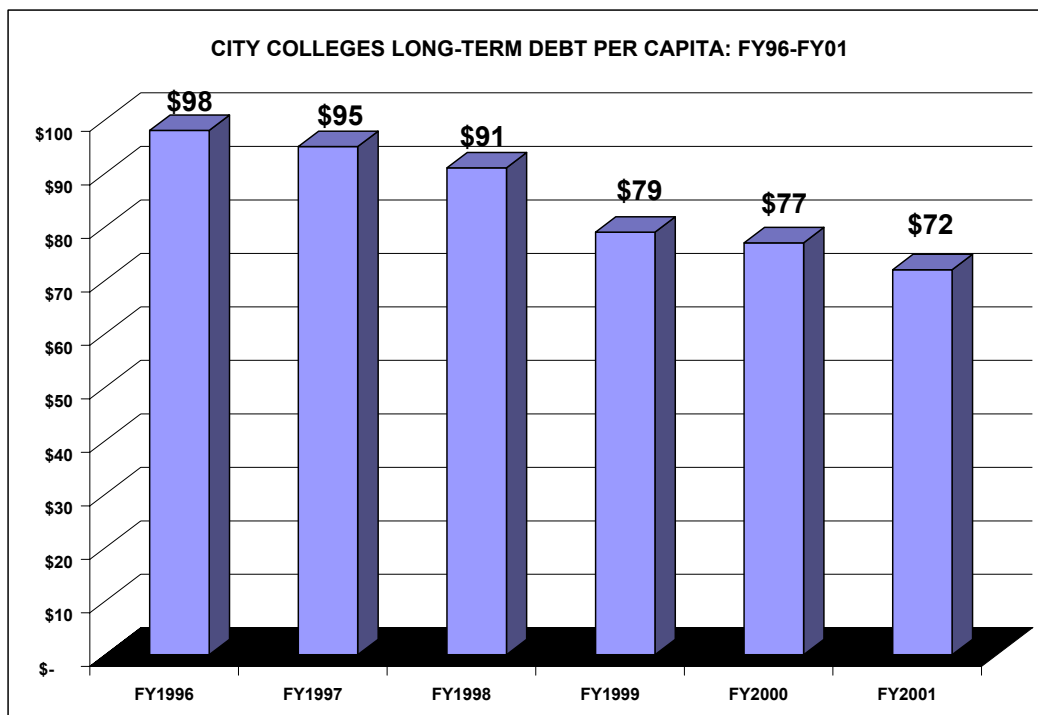
City Colleges reported a 9% increase in short-term debt between FY1996 and FY2000. This relatively modest increase is no cause for concern.

CITY COLLEGES SHORT-TERM DEBT		
Fiscal Year	Short-Term Debt	% Change
FY1996	\$ 89,017,560
FY1997	\$ 88,505,071	-1%
FY1998	\$ 89,249,381	1%
FY1999	\$ 91,244,496	2%
FY2000	\$ 95,747,230	5%
FY2001	\$ 96,637,003	1%

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.³ As the exhibit below shows, long-term debt per capita declined by 27% between FY1996 and FY2001, from \$98 to \$72. This is a positive trend.



³ 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 Civic Federation applauds Chancellor Watson and his financial management team for initiating a District-wide strategic planning process. The process will yield a strategic plan for the District focused on meeting four key goals:

- Improving the quality of all programs and services;
- Expanding services to meet the needs of all students and workforce partners;
- Increasing enrollment and retention; and
- Effectively utilizing resources and maximizing revenue opportunities.

It is our understanding that the District will utilize its strategic planning process to develop a long-term financial plan to help guide the management of the District's financial operations. Implementation of the City Colleges' new financial management information system will permit the development of long-range forecasts and a performance measurement system to better monitor actual performance of programs. It will also permit the District to better identify and allocate costs to particular programs. This is a key step in clearly identifying core versus ancillary programs and target resources at those programs central to the District's mission and goals.

The Civic Federation welcomes and strongly supports the District's efforts to develop and implement management strategies including a strategic plan, a long-term financial plan and performance measure.

CIVIC FEDERATION RECOMMENDATIONS

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

Improve Budget Format

The Civic Federation urges the City Colleges to develop a more comprehensive and user-friendly budget. We believe that the budget document should, at minimum, contain features such as a transmittal letter, a more detailed budget and revenue overview that includes 5 years of data, information about Full-Time Equivalent (FTE) staff positions and narrative descriptions of expenditures and revenues as well as programs and departments. 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.

More Time Needed for Public Review of Budget

Although we understand the timing pressures faced by City Colleges finance staff, the Civic Federation urges that in the future citizens should be given at least 10 days to review the proposed budget document before scheduling a hearing that seeks public comment and input. The current truncated time period between release of the budget and public testimony does not afford sufficient time for many interested citizens and education supporters to prepare for the public hearing.

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 into guide the development of its annual budget. This should be a component of the long-term financial planning process as it is developed and implemented.

Pursue Joint Purchasing of Health Insurance

Given the ongoing economic uncertainties, the City Colleges may well endure more bad fiscal news during FY2003. Thus, it is imperative that the City Colleges implement measures that can generate additional budgetary savings. To that point, we congratulate the financial management team at the District for actively working with The Civic Federation and other local governments to explore the possibility of consolidated health insurance purchasing and look forward to expeditious implementation of an agreement to achieve that goal. A recent Civic Federation study found that forming such an agreement consisting of the employees of the City of Chicago, Cook County, Chicago Park District, Chicago Transit Authority, the City Colleges of Chicago, the Chicago Public Schools and the Chicago Housing Authority could yield projected savings of \$40.1 million for all the governments in the first year or \$222 million over a 5-year period.⁴ Savings from an insurance pool would be very beneficial to the District's financial situation.

⁴ The Civic Federation. *Feasibility Study of Consolidated Purchasing: Chicago Public Employers. A Study Conducted by the Segal Company.* February 23, 2001.