HIGHER LEARNING COMMISSION

230 South LaSalle Street, Suite 7-500
Chicago, IL 60604-1411
312.263.0456 | 800.621.7440
Fax: 312.263.7462 | hlcommission.org

April 2, 2019

Interim President John Green
University of Akron
302 Buchtel Common
Akron, OH 44325-4702

Dear Interim President Green:

The interim report you submitted to our office has now been reviewed. The staff analysis of the report is attached.

On behalf of the Higher Learning Commission staff received the report on evidence of financial stability and a long-term financial plan for funding maintenance and repair of facilities. No further reports are required on this topic.

The institution's next reaffirmation of accreditation is scheduled for 2022– 2023.

For more information on the interim report process contact Lil Nakutis, Accreditation Processes Manager, at lnakutis@hlcommission.org. Your HLC staff liaison is John Marr (jmarr@hlcommission.org); (800) 621-7440 x 104.

Thank you.

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STAFF ANALYSIS OF INSTITUTIONAL REPORT
DATE: April 2, 2019
STAFF LIAISON: John Marr
REVIEWED BY: Steven Kapelke

INSTITUTION: University of Akron, Akron, OH

EXECUTIVE OFFICER: John Green, Interim President

PREVIOUS COMMISSION ACTION AND SOURCES: An interim report is required by 12/31/2018 on evidence of financial stability and a long-term financial plan for funding maintenance and repair of facilities.

This interim report derives from the Team Report of the institution's 2017 Comprehensive Evaluation. The report should document that the Institution has stabilized its on-going financial resource base funding and developed a long-term plan for funding maintenance and repair of its facilities.

REPORT PRESENTATION AND QUALITY: The University of Akron (UA) interim report consists of a clearly written narrative overview of the institution's financial situation supplemented with a wide range of supporting materials situated in the appendices. These include financial, administrative and other organizational documents. Indications are that the report is thorough and candid.

REPORT SUMMARY: The report's narrative summarizes key actions and initiatives undertaken by the University in response to the recent financial challenges triggered by significant enrollment decline and increases in tuition discounting. The narrative is not organized in sections but rather presented as a continuous document; however, the primary elements are clearly defined.

The narrative begins with a brief summary of the audit results from FY2017 and FY2018, noting that the auditors cited no material weaknesses in the FY2017 audit, though one significant deficiency was identified. The institution's Board of Trustees accepted both audits, and the University anticipated that the Ohio Auditor of Students would review and approve the audits on or about December 31, 2018

The report then describes the state of the institution's FY2018 operating budgets, which were approved by the Board of Trustees by June 2017, with the original General Fund budget projecting a deficit of $29 million. Subsequently, however, the University was able to reduce the deficit to $4 million by the end of the fiscal year, largely through more effective financial management. The current (FY2019) budget forecasts a General Fund deficit of $16.2 million, though the institution is making efforts to reduce that amount. Here the report notes that, despite "*fiscal challenges and as a result of vigilant management of our finances*," Moody's reaffirmed the institution's A1 rating and improved its outlook "*from negative to stable*;" at the same time, Fitch downgraded the University's rating to A+ but improved its outlook from negative to stable.

The report narrative goes on to describe the institution's efforts at controlling its debt portfolio through debt refinancing that resulted in the deferral of debt service payments for five years, "*while also financially satisfying a $4.5 million obligation to the UA Foundation that was scheduled to mature within a couple of years*." At the same time, according to the report, the University has decreased endowment spending and administrative rates, which will result in stronger growth in the endowment.

Here the document describes an initiative undertaken by the University designed as an incentive for faculty members that would also provide financial benefit to the institution. The Voluntary Retirement Incentive Program (VRIP), which was implemented in Spring 2018, "*attracted 48 faculty participants and resulted in the elimination of nearly $5.4 million of compensation and benefits*." This action was taken after consultation with the faculty union and subsequently approved by the University Council Budget and Finance Committee (UCCB&F) and the Board of Trustees.

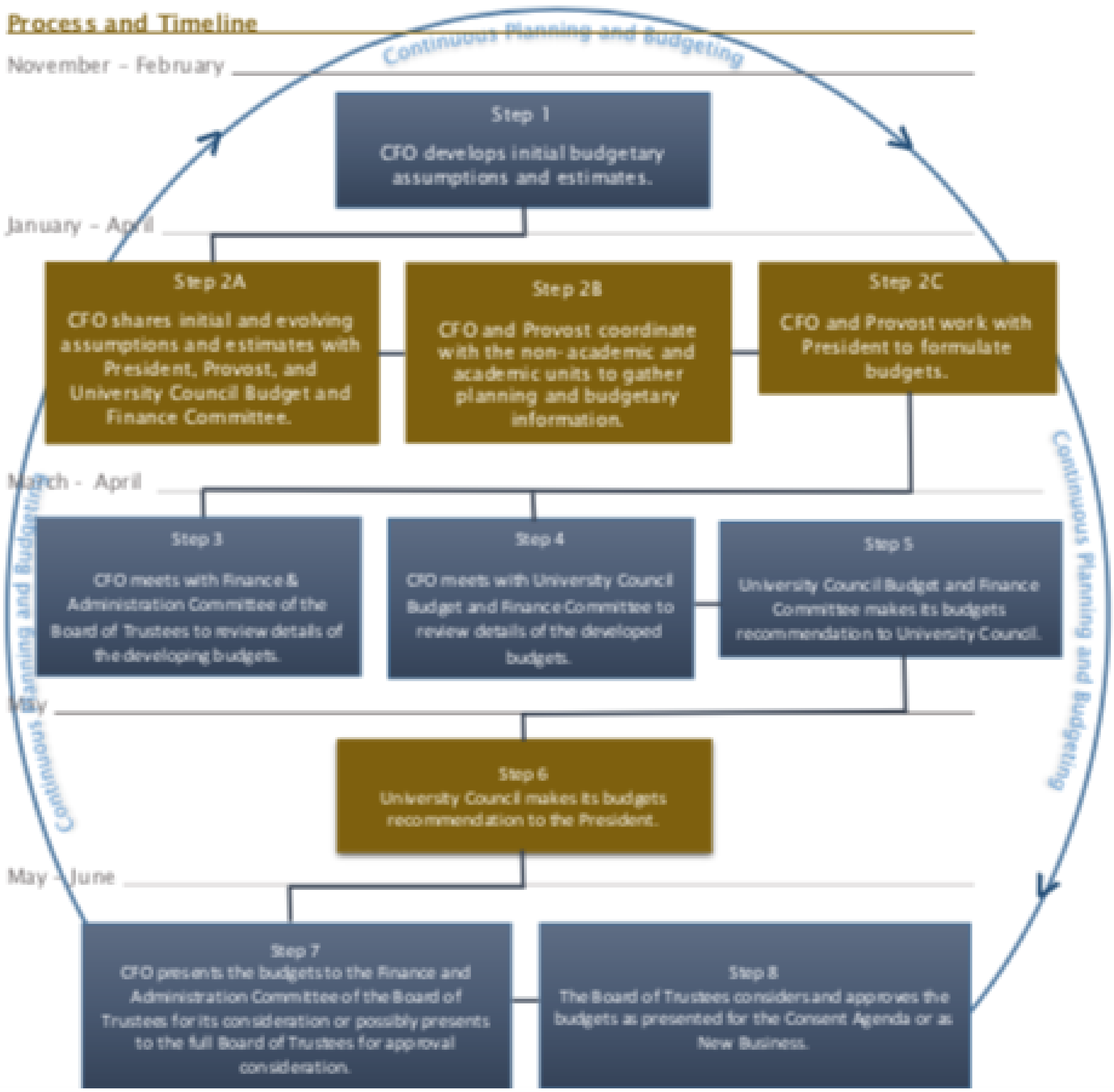
The report also provides some details pertaining to the institution's efforts at generating additional tuition income, citing for example the restoration and/or addition of athletic teams and a proposed tuition guarantee program that assures undergraduates in the same cohort fixed rates for general and instructional fees for four years. Here the document also notes "*a new undergraduate recruiting and scholarship/discount plan from our admissions and enrollment management area that will take us into the future*."

The institution acknowledges the challenge it has faced with regard to deferred maintenance, while also noting its recent progress in this area, making specific reference to an $18 million state capital appropriation "*toward reducing deferred maintenance,*" that will enable the University to continue or accelerate current efforts.

REPORT ANALYSIS: Information presented in the University of Akron interim report narrative relative to the institution's financial situation is confirmed through materials located in the extensive report appendices.

The University's financial situation is somewhat complex. UA has had to address a declining student population with its attendant drop off in tuition revenue, and has, to some extent, accomplished this goal through prudent financial management/cost control that includes debt refinancing and a faculty buyout/retirement initiative that will result in significant savings in compensation and benefits.

UA's governance infrastructure for developing and managing its budget appears sound, with appropriate input from the UCCB&F Committee, consultation with appropriate bodies such as the faculty union, and oversight by the Board of Trustees, which has final approval on annual budgets. The graphic below provides a view of the institution's budget cycle, which, according to the report, has been adhered to carefully.



With regard to the institution's current budget status, the FY2019 annual E&G ("*General Fund*") budget projects a deficit of more than $16 million as noted in the Report Summary section above, though the institution hopes to reduce that amount. Similarly, the FY2018 budget projection, which was $29 million, was ultimately reduced to $4 million. The FY2019 budget includes across-the-board compensation increases of 3%, much of which is contractually mandated through one of the University's collective bargaining agreements.

Additional positive signs include slight reductions in the endowment draw, which should enable stronger growth in the endowment, and efforts to increase student enrollment through initiatives designed to control tuition costs and through additions/reinstatements of "cost controlled" athletic programs, including men's baseball. Should these materialize as the institution anticipates, both initiatives should generate additional tuition revenue.

The institution's long-term ratings, as determined by Moody's and Fitch, show that both organizations rated UA's outlook as stable, though Fitch did downgrade its rating from AA- to A+. The Board of Trustees approved the University's audited financial statements for FY2017 and FY2018, with the FY2018 audit under final review by the State of Ohio at the time the interim report was submitted. The institution's Composite Financial Index ratios, though not stellar, have been "Above the Zone," since FY2016, as reflected in the figures below.

The University of Akron
KPMG Composite Financial Index (CFI)
Fiscal Years Ended June 30, 2010 through 2018

	2010	2011	2012	2013	2014	2015 w/o 68	2016 w/o 68	2017 w/o 68	2018 w/o 68/75
Weighted Score - Primary Reserve	0.84	1.14	1.01	0.96	1.18	1.15	1.14	1.42	1.34
Weighted Score - Net Operating Revenues	0.30	0.41	0.03	(0.23)	0.07	(0.30)	(0.03)	0.05	(0.13)
Weighted Score - Viability	0.28	0.40	0.39	0.39	0.39	0.38	0.36	0.45	0.43
Weighted Score - Return on Net Assets	0.90	0.83	0.15	(0.03)	0.51	(0.22)	0.12	0.47	0.41
KPMG CFI	2.3	2.8	1.6	1.1	2.1	1.0	1.6	2.4	2.1

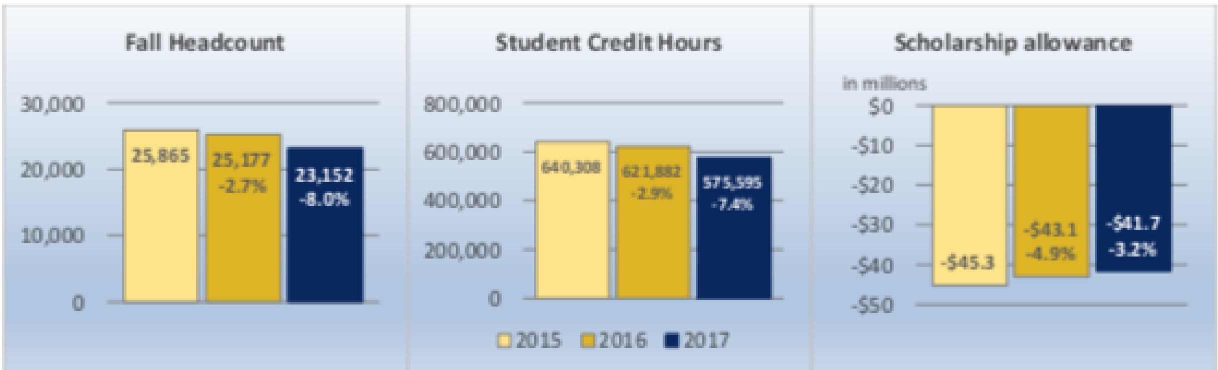
Source: Compiled from the respective years audited financial statements.

Analysis Concluding Statement: It is apparent from the materials provided in the UA interim report that the institution acknowledges the financial challenges it faces and has taken steps to address these, primarily through very prudent financial management. The two most significant of these actions, based on the evidence, are the debt reduction initiative and the Voluntary Retirement Incentive Program offered to the faculty. Some of the signature indicators of financial health are present, as noted above, including the institution's CFI ratios, its Fitch and Moody outlook, and a commitment to addressing its deferred maintenance issues. Review of the documentation provided in the appendices, such as the University Council Budget and Finance Committee In-Depth Report from November 2018, confirms the information provided in the report's narrative.

The institution's audits (audited financial statements) show that its *Total net position* increased from about \$123.4 million in FY2016 to more than \$138.2 million in FY2017. When the institution's two foundations (the UA Foundation and the UA Research

Foundation) are included in the calculations, the numbers are $179.9 million in FY2016 increasing to about $192 million in FY2017.

Despite the positive signs, however, there remains considerable work to be done if the University is to fully stabilize its financial situation. The graphic below shows two of the most salient enrollment numbers, Headcount and Student Credit Hours, both of which provide an accurate reflection of enrollment decline through Fall 2017.



The student recruitment/enrollment management initiatives identified in the interim report should, ultimately, enable the institution to stabilize its enrollments, but because these actions are in early or inchoate stages, there is no evidence at this point to show their effect. Likewise, the institution's Three Year Action Plan, one feature of which seeks to "*monetize*" various institutional facilities, such as parking and the recreation center, should generate additional revenue over time; however, no evidence of this is yet available.

Taken as a whole, the body of evidence provided by the institution in its report, indicates that it is effectively addressing one important aspect of its finances, specifically, controlling/managing costs. The University has also begun to develop means by which to generate additional revenue, though that element is still very much a work in progress.

The Higher Learning Commission will not require additional reporting on these matters; however, UA's finances will require significant ongoing attention on the part of the organization as indicated in the Staff Finding section below. The institution should assume that the HLC Peer Review Team conducting its AY2022-2023 Comprehensive Evaluation will examine carefully the University's progress with regard to stabilizing finances and student enrollment.

<u>STAFF FINDING</u>:

Note the relevant Criterion, Core Component(s) or Assumed Practice(s): <u>Core Component 5.A</u>

Statements of Analysis (check one below)
_ Evidence demonstrates adequate progress in the area of focus.
<u>X</u> Evidence demonstrates that further organizational attention is required in the area of focus.
_ Evidence demonstrates that further organizational attention and HLC follow-up are required.
_ Evidence is insufficient and a HLC focused visit is warranted.

<u>STAFF ACTION</u>: Receive the report on evidence of financial stability and a long-term financial plan for funding maintenance and repair of facilities. No further reports are required on this topic.

The institution's next reaffirmation of accreditation is scheduled for 2022– 2023.