



AGENDA REPORT TO EXECUTIVE COUNCIL

MEETING DATE: September 25, 2015

Item:	Capital
Author:	Carrie Passi, Managing Director Finance and Administration
Purpose of Report:	FYI REPORT to outline changes to capital process, capital plan and to illustrate how capital funds will be spend in 2015/2016

Recommendation: *For the Board to accept this agenda report as an FYI report, which outlines changes to the USC's capital spending process, changes being made to the capital approval process, changes to the capital plan and capital budget. This report will also outline how the capital funds being collected for the 2015/2016 fiscal year will be spent.*

Legislative History:

Ten-year capital plan 2011 – 2021

Capital fee referendum

Report:

Background:

When the current capital plan was created, it was meant to serve as a planning tool to determine when major renos were to be completed, what capital needs the organization required on a year to year basis and to illustrate how the capital student fee was to be allocated over the course of the ten-year plan. The plan provided for a large "front end load" of capital spending as phase one of the capital plan was to pay for the large renovation that transformed the space formerly occupied by the gyms, into Mustang Lounge. This renovation cost the USC \$7.5 million to complete of which \$3 million was paid up front and \$4.5 million was financed through Scotiabank. It was the financed piece that was to be paid over time via the student fee collected every year. This meant that of the approximate \$9 million being collected over the 10 year life span of the capital plan, \$4.5 million would go toward paying off the construction of Mustang Lounge.

The total cost of the current capital plan was approximately \$10.5 million. Given that student fee collection was only estimated at \$9 million, at the time of having the capital plan approved, the Board at the time also approved recalling \$1.5 million from reserves to cover off the shortfall from the plan. The reason that it was approved to bring in money from reserves rather than increase the student fee was because the USC had been in a position where it had been necessary to put off capital spending for so long, it was deemed unfair to tax the students beyond the original referendum approved fee until it could be determined that an increase was proven necessary.

The original capital plan provides for operational capital needs, IT organizational and departmental needs and outlines what major renovations lay on the horizon for the organization. The plan also provides for much flexibility in spending from year to year. It was not created so that there were hard and fast limits to how much could be spent in any given year but rather was put together so that if it were determined that in a given year, there were large items that needed to be added to the plan, the Board could approve such a change. The implication however of doing so is that by adding unbudgeted items to a pre-approved plan meant that you were taking money from future years with the intent to spend it today. This meant that future years would not have money or would have a significantly reduced amount to spend for capital items. In essence, the capital budget that we current have is a rolling budget in that there is a flexibility built into the plan to enable a deficit to be run in any given year, over and above the fees collected for that year, when capital needs arise that were not in the budget or when items deteriorate faster than anticipated. The nature of a rolling capital budget is that a deficit in any given year is ok, provided that it is a manageable budget and can be paid back in the next year. In other words, you can “borrow” funds from future years in order to get your capital needs taken care of this year, but it means that next year will have less capital funding available to them.

The USC experienced one year where there was close to \$1 million added to capital by an executive, who were also the Board for that year. Management took their direction from the board, just as we do now, even when the Board and the Executive were one in the same. Given that we were only collecting approximately \$750,000 in student fees for that year, coupled by the fact that the capital plan was fairly new and was meant to be in a low capital spending phase in order to pay off the loan on Mustang Lounge, these additions significantly ate into future spending within the capital plan. Further, this resulted in major spending and some major renovations being postponed as well.

The new policies being brought to the Board today, ensures more reporting to the Board on capital items, capital projects and capital updates

In order for the USC to have a capital plan that is both effective and strategic, there are many changes that need to happen.

Report:

As laid out in the Cash Flow Memo, the USC is currently in the process of redoing the capital plan. This process is a very labour intensive but the end result will provide capital renovation milestones for the organization, dollars for maintenance as well as operational capital for all departments. Each departmental manager will be responsible for; evaluating the items within the current plan and determining whether they are still required, determining their capital needs for the next 5 years and also providing a ranking of items under headings such as needs, wants, wish list. The managing directors of finance and admin as well as facilities and operations will then work with the managers to roll the 5-year projection forward so that we maintain a 10-year capital plan. These changes will help us to develop a more robust and comprehensive capital plan for the organization going forward. The managing director finance and admin will be working with the managing director facilities and operations to determine when the major renovation milestones for the organization should be and to estimate a dollar amount to be allocated to those renovations as well. Building the new capital plan in this manner ensures buy in from the departmental managers as they will be a part of building the new plan and it provides accountability within the organization as well as the capital plan will be updated annually as part of the budget process for the organization.

Two major pieces missing in the original capital plan are money set aside specifically for maintenance and administration. The new capital plan will provide definitions for the terms maintenance and administration so that it is clear what types of expenses can or cannot be budgeted under each of those. The administration definition and dollar allocation is important, as this will capture the cost of our loan with Scotia as well as administrative support costs or overhead costs associated with renovations for the organization.

The cash flow memo document outlines new capital procedures and processes that will be used by management in an effort to manage the spending on a year over year basis as well as on a 5 and 10 year snap shot basis as well.

The new purchasing policy that is for approval today is also a new tool that has emerged from the cash flow memo that will provide further structure to managing the spending within the capital new and improved capital plan. It also provides and accountability mechanism for the organization as well.

Another tool that is on the table for approval today is the Operating and Capital Budget Approval Policy and Procedure document. This further outlines how things are approved, when they get approved and who approves them. This works to clarify expectations at all levels and provides for further accountability within the organization.

Project Team:

Carrie Passi, Managing Director Finance and Administration

Jeff Armour, Managing Director Facilities and Operations

Scott Courtice, Managing Director Government Services

Sophie Helpard, USC President

Jonathan English, USC Secretary Treasurer

Cathy Clarke, USC General Manager

Financial Implications:

In terms of how the capital funds will be allocated for the current fiscal year, a summary has been provided as an attachment to this document.

In summary, the USC expects to collect \$919,483 in student fees. After capital expenditures for the year, admin fees, tenant improvement allowance for new dentist and payment is made to UWO for renovations conducted in prior year, the USC will sit with a deficit in capital spending of \$65,795.

However, this deficit will be made up (or covered off) by new money that is now in the budget due to assumption adjustments, which are detailed, in a separate document. Overall, capital spending is in check and the deficit is covered off completely without negatively impacting any approved areas of the budget.

Tenant Improvement Allowance

When the lease was signed for the new dental tenant in the lower level of the UCC, it was agreed that the USC would provide a sizeable investment into the space up front for two reasons: 1) it enabled the USC to negotiate for a higher per square foot lease rate for the duration of the lease and 2) it enabled the USC to ensure that the space was renovated properly and ensured usability and rent-ability of the space in the event that the dentist left after his lease was completed. Inherent in the investment was that the dentist would payback the amount over time into the USC operating budget. The total investment made into the dental suite was \$140,000 of capital dollars. The dentist will be paying back 100% of the investment amount to our operational budget in the first year.

Attachments:

Excel document outlining capital spending allocations for this year

Purchasing policy

Capital Backgrounder

Sign-Offs:

<i>Author:</i>	<i>Carrie Passi</i>	
<i>Financial Review:</i>	<i>Carrie Passi, Managing Director, Finance and Administration</i>	
<i>Legislative Review:</i>	<i>Scott Courtice, Managing Director, Government Services</i>	
<i>General Manager Review:</i>	<i>Cathy Clarke, General Manager</i>	

Capital Spending Reconciliation
Fiscal 2015-2016

Student Fees collected	919,483
Loan Payment	(300,000)
Dental tenant improvement allowance	(140,000)
IT software needs	(25,000)
Operational capital	(22,800)
OS bill to Western for prior year renos	(475,478)
IT hardware needs	(12,000)
Contingency	(10,000)
<u>Total deficit</u>	<u>(65,795)</u>



University Students' Council of the University of Western Ontario

PURCHASING POLICY

Effective Date

Board of Directors

OBJECTIVE

The University Students' Council purchases goods and services throughout the year that are necessary for the successful operation of the organization. This Purchasing Policy, combined with the Purchasing Administrative Regulations and Purchasing Procedures, has been created to ensure employees follow sound, efficient and standardized practices when making purchases on behalf of the corporation.

GENERAL POLICIES

The USC shall conduct its purchases in accordance with generally recognised purchasing practices including, wherever possible, the competitive process. Consistent with this the following policies shall provide the framework for all USC purchasing activities:

1. The USC will ensure that products and services are acquired such that they are of acceptable quality at the lowest available price, with consideration given for availability, urgency of demand and required service level.
2. All purchasing transactions shall ensure equal opportunity, due process and fairness to suppliers.
3. When any tendering process, including Requests for Proposal (RFP) are used, the lowest evaluated tender or price, which is the offer evaluated as striking the best balance between quality, price, urgency of demand and required service level, shall be accepted.
4. In all cases where the acquisition price exceeds \$25,000 approval of the award recommendation shall be obtained from the Board of Directors prior to purchase. For purchases of a value less than \$25,000 signing authority shall be established and delegated by the General Manager and the President.
5. For purchases that involve the acquisition of talent, such as bands, speakers, or other entertainers, the Board will be provided with an annual plan and approve an annual maximum spend on talent. The Board shall receive updates each quarter regarding progress versus the plan; any changes to the maximum spend must be approved by the Board.



University Students' Council of the University of Western Ontario

6. All USC personnel shall maintain both actual and apparent impartiality and arm's length distance in all dealings with potential suppliers of goods and services.
7. Purchases may be made without prior Board of Directors approval in an emergency situation when the lack of immediate action would jeopardize operation or equipment, disrupt critical services to students or involve the health and safety of personnel if the said purchases are approved by the General Manager and President or their designates. The Board must be made aware of all pertinent facts within one business day of the incident that required the emergency purchase.
8. Any purchase, excepting emergency purchases as described above that are not included in an approved USC budget must receive approval from the Council and/or the Board of Directors as per the procedures established within By-Law #1.
9. The General Manager and President shall maintain a set of Administrative Regulations and Procedures that establish consistent internal processes for purchasing. These processes do not require Board approval, but shall be available to Directors for their information.

Capital Backgrounder

Capital is an important piece of spending that is done at the USC. Capital is spent for many reasons but most importantly: IT hardware, IT software, renovations, operational requirements, maintenance and upkeep as well as furniture and fixtures for the organization. As one could imagine, there is a significant amount of money spent each year on capital items. As a result, the USC has a dedicated student fee to fund capital spending on an ongoing basis. In order to manage the cash coming in through fees and the ongoing capital needs, the USC also has a capital plan which serves as a guideline for expenditures.

This document outlines the current capital plan and provides recommendations for the updated capital plan and capital expenditure process going forward.

Current Situation

When the capital side of things were examined, it was determined that there had been a large amount of outlay at the front end of the plan that had been planned and there had also been a large outlay of cash for items that had not been originally included in the capital plan. Some examples of items that were completed that had not been included in the original capital plan (but were approved by Council and Board) are: moving purple store to the atrium level, splitting Info Source into Mustang Central and Western Connections, additional furniture for Mustang Lounge to make the West Lounge “useable”, purchase and creation of Kiosks, creation of clubs space and the addition of club lockers on 3rd floor, creation of intern space, second new sound system for Mustang Lounge (as it had been evidenced that one purchased when space was built could not handle concert level sound), wall of TV’s in Mustang Lounge, redo of window film on front doors of 340 suite as well as an increase in scope for Gazette renovation. The items that were planned were the original completion of mustang lounge, atrium lounge, spoke café renovation, 340 suite renovation including the new kitchen, relocation of Creative Services as well as building signage boards. It is important to note here that the relocation of the Purple Store that was referenced above occurred just one full year after the previous renovation of the Purple Store. As a result, we ended up with a newly renovated space that was left vacant. This piece was discussed with the Board at the time however, given that the Executive were the Board at the time, and that making the non-budgeted changes was in the Executive’s best interest, the decision was made to relocate the Purple Store and write off the previous renovation after just one year. It wasn’t until fiscal 2014/2015 that the USC had a wholly external Board that was separate from the Executive.

The process for capital approvals in the past has been left flexible in order to facilitate getting items completed in what is a relatively short “construction period” for the USC. A list of items that are expected to be completed is sent to Council in conjunction with the budget with a total amount that is being recommended to be spent on capital items. There is usually very little discussion on these items. Once the budget is approved, so is the total bottom line to be spent on capital. As the planning unfolds throughout the year for projects, any budget savings that we incur are generally re-directed to additional projects. This is done because: a) the new project relates to those already approved and would have to be done at some point anyhow, b) the cost of completing the project now is significantly less than it would be if

we waited to complete it and c) the project is a new ask or want from the exec that provides added service or value to students and fits within the unused money that is available for capital. The USC has never gone over budget but has added additional projects or pieces of projects without going back to Council because the money had already been approved for capital use and there were surplus funds available. As a result, we have been able to achieve more renovations within the approved spending limits each year. As you will see in the recommendations section, this is a piece that we are proposing change. The change will slow down the process but will ensure that the process is more transparent to all.

The total cash outlay stemming from capital investments, over and above the student fee collected, has been just under \$2M dollars over the past 6 years. But more specifically, the USC spend \$1M over the capital budget in one year and the remaining \$1M in overspending was done over 5 years. The implication of the \$1M in overspending in one year was that it "ate up" 2-3 years of flexible room that was inherent in the capital plan.

It is important to note here that for all of the items that were added to the capital plan, these were approved by a Board of Directors who were also the Executive. As a result, management's voice was lost during discussions of whether or not new capital items should be added to the plan. The USC has already evolved in a way that prohibits the ad hoc additions to the capital plan in that we now have an external Board of Directors.

It is also important to note that when the capital plan was developed, it was intentionally "front end loaded". This meant that the USC was going to purposely spend above and beyond what the student fee allowed for the first few years and then would intentionally spend below what the student fee allowed for the next years in order to make up the deficit. Unfortunately, because the USC did not have an external Board in those years when we should have been spending very little on renovations and just doing the bare minimum in terms of operational capital, large capital projects were added to the plan which resulted in the USC to continue to spend above what the student fee brought in each year.

As a result of the above analysis, the USC recalled \$1,500,000 back from our reserves to "top up" our operational cash supply to a level that is deemed more appropriate for the organization. As a rule of thumb, the organization likes to have \$2M in the bank to bridge us during the period where we are not receiving student fees. Given the additional capital spending detailed above along with the termination cash outlays also detailed above, in conjunction with the shortfall of fees compared to budgeted spending, the USC required the money to be recalled in order to continue regular business without having to make major changes to how the money was being spent. The calling back of the money was also approved by the Board of Directors.

Overall, without any new surprises, the USC was in a cash position that was less than ideal given the over-estimation of total number of students and our inability to confirm the number of students in time to scale back spending to match the lower revenue coming in.

Recommendations

The result of this analysis has been a number of recommendations coming forward for policy, process and procedure to gain back control of when cash is being spent so that it can be

better aligned with when cash is coming in. While some of the recommendations may not be ideal from a renovation stand point or implementation stand point, they are necessary in order to ensure that cash is spent responsibly and in line with expectations.

In terms of budget spending – it is important to note that when budget assumptions are proven to be incorrect we can always do a budget amendment however there are very few areas that can actually be changed to maintain a balanced bottom line even if revenues are lower than expected. Operational budgets are not likely to be changed for an amendment given that if revenues in operations are lower than expected, we cannot force people to come in and use our ops so there is very little room for those budgets to change. Corporate budgets are also unlikely to change dramatically given the majority of them are based on contracts – salary and benefits, occupancy, insurance, audit, legal etc cannot be changed. Office expenses and PD can be altered depending on the time of year. The major area that can be flexible in terms of pulling back in cash expenditures are the PVP budgets – however, that is clearly not the ideal situation. I include this piece in the report just as an FYI when recommending budget amendments to overcome budget assumption inaccuracies.

The following is a list of recommendations from management:

- 1. We need to encourage all managers in all departments to be cognizant of money being spent – they need to assess if they “need” to spend the money or if the spend is just a “want”.*
- 2. We will be re-assessing the capital plan this summer – we are 5 years into a 10 year plan so it is time to reassess where we are at, what needs to be done, can we afford our plan and planning how much is to be spent for each reno and timelining when those spends should occur.*
- 3. We will be scaling back renovations for the organization. We have been front end loading the capital plan spends and now it is time for it to be scaled back so that our capital finances can “catch up”. This means that we will purposely have years in the capital plan where we collect a fee of x and spend an amount less than x in total capital as a way to recoup back from the years when we front end loaded the spending and spent more than the fees collected.*
- 4. We will be reassessing the capital fee used to fund the capital plan based on the new and improved capital plan.*
- 5. We will be setting new process and procedure for capital projects – more formal process that includes scope documents that go to Board for approval. We will then use the scope document as our plan for the project – if we come in under budget that is great – we are done! Excess money goes back into the capital budget. If we require more money – we need to go back to the board for approval. We will be bringing new process and procedure forward as we develop them.*
- 6. More control over when large purchases are being made – this may mean that software and hardware are not purchased during the summer when it is slower but rather need to be purchased in August for implementation in October rather than being ready for September.*
- 7. We are looking at large cash outlays and seeing if we can reconfigure so that large payments are not made when we have little cash coming in. One example would be our*

LTC contract – we will aim to pay out the contract over 12 months rather than 9 as it is now.

- 8. We will be increasing the reporting to Board – they will now get cash flow reports quarterly in conjunction with the quarterly financial update. They will also receive capital updates quarterly as well to indicate where we are at with spending.*
- 9. We will also be looking into alternate work arrangements for staff in an effort to save some money in salaries. For example, we are examining areas that could be eligible for seasonal layoffs or shut downs at certain points in the year.*

Of course with the above recommendations, comes some implications as well.

- Renovations will be stopped for this current year and potentially for the next year as well as we “catch up” from some of the additional spending*
- The renovation process will be slowed down especially if we don’t have funding to complete renovations during the summer months*
- Capital purchases will be delayed given a new policy for the timing of purchases*
- The USC will likely pay more money out for the same product due to not being able to take advantage of efficiencies along the way*
- Politics should no longer be a part of capital recommendations*

Overall, the goal of the recommendations laid out above is to control spending within the organization in an effort to better predict cash flows have better cash management procedures that are more in line with industry best practice.

Next Steps

While there are many aspects that make the management of our cash flows and the predictability of our cash flows difficult, by implementing the recommendations above the end result will be more predictability and better ease of cash management for the organization.

Further, by enhancing the processes, policies and procedures around spending, it will remove all temptation to increase scope in capital projects on the fly and will ensure that when budget savings in projects are realized, that those funds roll back into the capital plan. From there they can then be saved to allow increased spending in the following year or they can be re-deployed to a new project in the current year if that is what the Board approves. This will allow for more transparency in how the money is being spent and will ensure that sound business cases exist for any additional work that is recommended.

And finally, a more predictive cash flow will enable the USC to be more proactive in solutions and to have time to provide educated plans for situations rather than being put in a position of having to be reactive when negative situations arise.

For the current year, the USC has a multi year budget that has been approved. That budget allows for 29,000 students as part of the revenue model. This is an assumption that we now

know needs to be adjusted to actual – the actual is closer to 28,500. As a result, the multi year budget bottom line will be impacted in a negative manner and where we had put forward a surplus in year 1 of the multi year, it will now be a deficit. This means that the USC will need to adjust spending in the current year in order to make up the now projected deficit for the year or will need to look for new revenue streams and opportunities for the organization in order to make up the deficit. We will also be looking to update any and all projections that can be adjusted that will help to make up the bottom line. At this point, with a deficit looming, we will not be looking to add any new services.

Capital Plan

The USC has made a number of solid investments into our space through capital improvements over the past 5 years. While these investments cost money, they also add intrinsic value to our space as well. The decision to make these investments at the front end of the capital plan has now caused us to have to push the next set of ‘large spends’ into the future when we have the necessary funds to afford the capital renovations. This has also caused the USC to reassess our current capital plan and look at what is in there and whether or not some of the large spends are in fact necessary at this point in time or whether they are ok to be pushed out into the future. We need to look at how the operation is doing overall – do they in fact NEED the renovation or can they comfortably wait? Will it impede their ability to bring in revenue if we don’t renovate? These are two big questions we need to evaluate as part of the capital plan redo.

As our analysis has evolved, we now know that the capital plan was flawed from the very beginning.

- 1. The original plan did not allow for contingency room. This meant that if all planned capital spending was being done, there was no room for things that came up as a surprise. This will be corrected in the new plan.*
- 2. The original plan did not consider the administrative costs associated with capital renovations to be a part of the capital plan. This will be corrected in the new plan.*
- 3. Operating capital that were included in the original plan did not require a business plan to be associated with them. They were included based on the need of the individual departments rather than the need of the organization as a whole. This is a big piece that will be corrected in the new plan.*
- 4. The fee being collected to fund the capital plan was \$25. The plan actually required a much higher figure in order to fund the capital deficit that the USC was in at the time.*
- 5. The biggest piece of the capital plan was the Mustang Lounge renovation which came in approximately \$2M dollars over budget. The USC took out a loan in the amount of \$4.5M and paid down \$1.5M towards the \$7.5M owing. The USC collected \$750k in the first year of the plan which still left the USC in a deficit position of \$750K to make up over the course of the capital plan.*

These issues will all be addressed as part of the new capital plan in addition to new capital policies, processes and procedures. However, we will still need to ensure that the new plan has an element of flexibility to it so that we are able to keep moving as best we can within our budget restrictions. We need to be able to measure the risk of doing something now versus waiting and being able to move quickly when possible and when it is in the best interest of the USC.

Overall, the USC will be putting forward recommendations to improve the processes and policies through which we spend money. We need to ensure that the size of the spend needs to be relative to the economic state of the USC, we need to be able to adjust the thinking on spending and ensure that we can "reel" it in if cash is down or projections are not on target. We also know that we need to be able to properly assess risk associated with big spends and assess the potential return on investment. In other words, if we are making a large concert spend, we need a rational Plan B that is achievable in order to ensure fiscal responsibility when moving forward with the spend.