THE REGENTS OF THE UNIVERSITY OF CALIFORNIA

April 24, 2006

The Regents of the University of California met on the above date at the following locations: James E. West Alumni Center, Los Angeles campus; 1130 K Street, Suite 340, Sacramento; UCSF - Mission Bay, 1675 Owens Street, Room 220, San Francisco; 777 California Avenue, Palo Alto; 111-A University Complex, San Diego campus; 700 South Flower Street, 30th Floor, Los Angeles; Konrad Adenauer Strasse 7, Frankfurt, Germany; and Gran Via de les Corts Catalanes, 668 -08010 Barcelona, Spain.

Present: Regents Blum, Dynes, Gould, Hopkinson, Island, Juline, Kozberg, Lozano, Marcus, Parsky, Pattiz, Rominger, Ruiz, and Schilling

In attendance: Regents-designate Ledesma and Schreiner, Faculty Representatives Brown and Oakley, Secretary Trivette, General Counsel Holst, Senior Vice President Darling, Vice President Broome, University Auditor Reed, and Recording Secretary Nietfeld

The meeting convened at 1:10 p.m. with Chairman Parsky presiding.

1. **READING OF NOTICE OF MEETING**

For the record, it was confirmed that notice was served in accordance with the Bylaws and Standing Orders for a Special Meeting of The Regents to receive the final audit report of PricewaterhouseCoopers.

2. **PUBLIC COMMENT**

Chairman Parsky noted that the same procedure had been followed pertaining to the release of the audit report as had been used for the report of the Task Force on Compensation, Accountability, and Transparency: the document was released to the Regents and to the public simultaneously. The public will have an opportunity to comment further at the May meeting.

Chairman Parsky explained that the public comment period permitted members of the public an opportunity to address University-related matters. The following person addressed the Regents concerning the item noted.

Report on *Examination of Compensation and Other Employment Arrangements*: *PricewaterhouseCoopers,* the Ten-Year Compensation Audit Requested by the Chairman

Ms. Mary Higgins, a member of the Coalition of University Employees, observed that there are highly-compensated individuals at the campuses who earn more than the senior executives whose salaries were examined in the report. She recalled that the report of the Task Force on Compensation, Accountability, and Transparency had suggested that for some employees higher compensation and lower benefits might be appropriate. Ms. Higgins was concerned that a 401(k) type of plan was being considered. She did not believe that the Task Force would have been able to survey University employees about their beliefs on this subject. There is also concern about how a separate retirement plan for the employees of Los Alamos National Laboratory will effect the University of California Retirement Plan.

3. **REPORT ON *EXAMINATION OF COMPENSATION AND OTHER EMPLOYMENT ARRANGEMENTS*: *PRICEWATERHOUSECOOPERS,* THE TEN-YEAR COMPENSATION AUDIT REQUESTED BY THE CHAIRMAN**

Chairman Parsky explained that he had requested a special meeting for two reasons. First, public concerns about UC senior management compensation are among the most important issues facing the University of California. Second, time is of the essence if the Regents are to restore the public's trust in the University and its compensation policies and practices. The purpose of today's meeting is to receive the findings from the PricewaterhouseCoopers (PwC) audit, which was commissioned when the compensation concerns first came to public attention last fall. The focus of this independent inquiry is the ten-year period beginning on January 1, 1996 and ending on December 31, 2005. It covers current incumbents and past holders of the top 32 senior manager positions, plus one vice chancellor whose compensation has been the focus of numerous news stories and legislative hearings. The purpose of this audit is to provide the public with full disclosure of all elements of compensation, consistent with the Principles for Review of Executive Compensation, as well as to identify failures to comply with such policy. The audit does not suggest that there was any wrongdoing on the part of the recipients of this compensation. These individuals may just now be learning that there were failures to comply with disclosure and approval policies.

Chairman Parsky recalled that the PricewaterhouseCoopers report represents the first of three audits, to be followed by the release on May 2 of the Bureau of State Audits opinion, which covers a wider group of University employees. By the May meeting, University Auditor Reed will have completed an internal audit covering the remaining members of the Senior Management Group. The internal audit will include findings on travel and entertainment expenses. Taken together, these three audits add up to one of the furthest-reaching and most rigorous inquiries ever conducted on UC compensation. They underscore the seriousness of the issue and the Regents' resolve to address the underlying problems these findings reveal.

Chairman Parsky reported that, following the presentation of the Task Force on Compensation, Accountability, and Transparency, he had asked Regent Hopkinson, in her capacity as chair of the Special Committee on Compensation, to provide a detailed plan of action, beginning immediately and continuing into the May meeting of The Regents, for possible implementation of the recommendations of the Task Force. He will ask that Regent Hopkinson include in her plan a process for The Regents to determine, on a case-by-case basis beginning at the May meeting, how people should be held accountable for policy violations and other acts deemed to be inappropriate by the independent, State, and internal auditors.

The Regents have an obligation to make their determinations with full knowledge of the facts; the process will include full explanations from President Dynes and others on the campuses and at the Office of the President who were responsible for any approvals deemed in violation of University policy or otherwise inappropriate. It is important to make sure that any disciplinary actions are warranted and appropriate to the individual circumstances. A number of factors must be weighed:

- Is the violation moot because the employee is no longer with the University or no longer receiving the benefit?

- Does the violation involve a failure to seek formal approval from The Regents for a benefit to which an employee is entitled under policy?

Chairman Parsky stressed that the conclusion should not be reached that any of the recipients of this compensation did anything wrong. He then asked the representatives of PricewaterhouseCoopers to present their report.

Ms. Peggy Arrivas explained that, as noted by Regent Parsky, PwC had performed an examination of compensation arrangements for a ten-year period for current incumbents and past holders of the top senior manager positions. The report contains factual data about what has been paid or what has been promised to certain individuals. The purpose is not to place blame but rather to report the facts. For purposes of the report, the definition of compensation is consistent with the 1993 Principles for Review of Executive Compensation. There are 64 individuals included in the report. One employee with less than six months service in an acting capacity was excluded, while personnel files were not available for three employees.

Ms. Arrivas outlined the procedures performed over the course of the audit. The auditors reviewed source data from campus payroll systems and reviewed source documentation, including records contained in personnel files, campus payroll records, W-2 forms, and

minutes of open and closed meetings of The Regents. The auditors reviewed letters sent by management to employees certifying payroll arrangements, conducted interviews, reviewed the annual reports on compensation, and evaluated adherence to University policies and procedures.

Ms. Arrivas discussed the section of the report entitled **Report of Independent Accountants**, which is an examination of compensation and other employment arrangements for certain University of California employees, as presented in the Schedule of Employee Compensation and the Schedule of Other Employment Arrangements. The University's management is responsible for these schedules, and it is the opinion of PwC that they present, in all material respects, compensation and other employment arrangements for the selected employees for the period January 1, 1996 through December 31, 2005. Ms. Arrivas noted that the Schedule of Employee Compensation includes the following elements:

- Name, Position, Tenure in Position
- Year
- Total Taxable Income
- Base Salary
- Additional Salary
- Automobile Allowance
- Bonuses, Incentives, Awards, and By-Agreement Payments
- Relocation Allowance
- Temporary Housing Allowance
- Senior Management Severance Pay Plan Distribution
- Other Severance Pay
- Terminal Vacation Pay
- Honoraria
- Taxable Moving Expenses
- Life Insurance
- Leased Automobile
- Other Non-Cash Fringe Benefits

The Schedule of Other Employment Arrangements lists other arrangements and future benefits that have been promised to these employees, many of which cannot be quantified as they have not been paid. This schedule includes the following elements:

- Travel insurance
- Home Loan Programs
- University-Provided Housing
- Senior Management Severance Pay Plan
- Separation Arrangements
- Post-Separation Employment
- Supplemental Retirement
- Specialized Health Benefits
- Sabbatical Benefits
- Supplemental Vacation

Ms. Kristen Rivera presented an overview of the **Findings and Observations** section of the report. This document was completed in the context of the examination of compensation and other employment arrangements. It is intended solely for the use of the Regents and the management of the University.

I. **Observations**

1. **Certain benefits promised or paid to selected employees were not approved by The Regents as required by Regental policies**

The auditors reviewed minutes of the open and closed sessions of The Regents and noted instances where certain elements of compensation were not brought to The Regents for approval. Specifically, management generally sought Regental approval for base salary, additional salary, and bonuses. However, management generally did not seek approval for compensation paid to individuals under programs specifically approved by The Regents nor for benefits afforded to individuals as a direct consequence of the employee's position with the University, such as an automobile allowance. Attachment 1 to the report, which contains the same information as the Schedule of Employee Compensation, highlights the elements that were approved by The Regents, while Attachment 2 highlights other employment arrangements that were approved by The Regents.

2. **Certain benefits promised or paid to selected employees were exceptions to University policies or standard practices and were not approved by The Regents**

Attachment 3 to the report contains a summary of compensation items not approved by The Regents that were exceptions to University policies or standard practices.

Chairman Parsky stressed that the intention of the audit report was full disclosure to the public of all elements of University compensation**.** Nothing suggests that any of the individuals named in Attachment 3 did anything wrong.

3. **Certain of the compensation items described above were not disclosed to the public as required by Regental policies**

There are three methods for disclosing compensation items: Open Session items, Annual Report on Compensation, and Press Release. The primary mechanism for disclosure is Regental approval in open session. The open action items did not include all elements of compensation, and, in a number of instances, compensation items were not included in the annual report.

II. **Recommendations**

PricewaterhouseCoopers recommends the following actions:

- Consider implementing a "checklist" format for documenting elements of compensation. This standard format could be used to capture all agreements during the hiring process and subsequently be used for approval and disclosure purposes;

- Review the format of the Annual Report on Compensation to ensure that all elements of compensation requiring disclosure under Regental policies are included;

- Utilize payroll data to generate or validate the accuracy and completeness of the Annual Report on Compensation;

- Review mechanisms for disclosing compensation information to the public to ensure that data is provided in accordance with internal and external requirements; and

- Perform on-going monitoring and oversight to ensure adherence to policies and procedures for Regental approval and public disclosure.

Regent Hopkinson observed that the auditors' report reinforced the conclusions reached by the Task Force on Compensation, Accountability, and Transparency. The Regents need to move fairly quickly to correct the unclear policies, uneven implementation, and lack of transparency.

Regent Blum noted that the role of the Office of the General Counsel had not been considered in the context of compensation issues. He did not believe that any President of the University could have known what the policies and procedures were for hiring and compensating executives. He described these policies as "arcane" and asked why the General Counsel had not recommended that they be updated. Employment arrangements should also be reviewed by the General Counsel's Office. The Office should issue a statement describing how it is prepared to react in the future.

Chairman Parsky commented that at the May meeting the President would be asked to offer his commentary as part of The Regents' process. He did not believe that the Regents were in a position to reach any conclusions regarding blame at this time. It is clear that there has been a total lack of compliance with Regental policies.

Regent Marcus observed that the primary focus of the report had been on process. He emphasized that no evidence had indicated that the Regents were violating principles of compensation. The fact that the University is not able to pay its faculty adequately should not be ignored in this debate.

Regent Pattiz pointed out that the focus of the report was on processes that had evolved over the years which he did not believe involved the commitment of fraud on anyone's part. The Regents need to address these issues prior to placing any blame.

Regent Kozberg commented on the fact that there had been a systemic breakdown on multiple levels. The Regents' decision making becomes questionable as a result.

General Counsel Holst observed that the recommendations from PwC appear to be in order. In response to the comments by Regent Blum, he recalled that none of the offers made to any of these individuals was submitted to or reviewed by the General Counsel's Office before they were issued to the recipients, and none of the action items was submitted to the General Counsel's Office prior to action by The Regents.

President Dynes explained that, as a result of the audit, he fully understood the changes that need to be made. A complete overall of compensation practices has been undertaken; the reports from the Bureau of State Audits and the Internal Auditor will add to these efforts. The President recalled that similar events had occurred in the early 1990s. The Regents now face the same issues. Policies and principles were put into place, but there was no system implemented to ensure that they were effective. As a further indication of the systemic lack of disclosure, Mr. Dynes revealed that the full scope of his compensation was not disclosed to The Regents upon his appointment as President, and that compensation did not conform to policy. The following steps have already been taken, following the release of the Task Force report, in order to address these problems:

- An information system is being constructed that will begin with senior management and then be expanded to the whole University.

- Ethics training for all UC employees will begin.

- A website will be established where compensation items will be accessible to the public.

- A Public Information Practices Coordinator has been appointed to oversee all public records requests. An Office of Public Records will be set up in the Office of the President.

President Dynes pledged that, in order to ensure that ethical behavior is fundamental to his administration, it will be factored into the review of performance evaluations for all senior managers. He recalled that a recent editorial in the *San Francisco Chronicle* which commented on the fact that the University had been able to offer admission to all eligible California applicants had called upon the University to resolve the compensation issues as quickly as possible so that UC may return to "...the University's central purpose: to do world-class research and to provide a stellar education to the state's highest-achieving students."

Faculty Representative Oakley noted that the audit report had drawn attention to several promised or paid benefits that had not been approved by The Regents, nor were certain exceptions to policy. Certain of the compensation items were not disclosed to the public. The report found that several types of compensation were omitted from the Annual Report on Compensation for certain individuals. Ms. Arrivas was not aware on any occasion when there had been any communication from The Regents to the administration with respect to these elements. Faculty Representative Oakley asked whether the compensation elements varied over the ten-year period covered by the report . Ms. Rivera explained that the auditors had not performed an analysis to draw that conclusion. Professor Oakley believed that placing blame excessively was inconsistent with the academic model of leadership. He urged the University to fix its institutional problems that have led to a lack of public trust and not focus on individual responsibility for institutional problems.

Chairman Parsky observed that the Regents had tended over time to rely on voluntary compliance with policy. The Regents must rethink that trust in the context of the issues that have been raised. At the May meeting consideration should be given to establishing an independent Office of Compliance, reporting directly to the Board of Regents, which would be fully staffed and headed by a Chief Compliance Officer. The role of the office would be to ensure compliance with policies established by The Regents. In addition, the Special Committee on Compensation should address all of the recommendations of the Task Force as to which should be implemented now and which should receive further consideration.

The meeting adjourned at 2:05 p.m.

Attest:

Secretary