

The Regents of the University of California

**SPECIAL COMMITTEE ON COMPENSATION  
COMMITTEE ON AUDIT**

May 17, 2006

The Special Committee on Compensation and the Committee on Audit met jointly on the above date at UCSF–Laurel Heights, San Francisco.

Members present:                    Representing the Special Committee on Compensation: Regents Dynes, Hopkinson, Juline, Marcus, Moores, Parsky, Pattiz, Schilling, and Wachter; Advisory members Coombs and Oakley  
Representing the Committee on Audit: Regents Hopkinson, Marcus, Moores, Parsky, Rominger, and Schilling; Advisory member Oakley; Expert Advisor Vining

In attendance:                    Regents Blum, Bustamante, Gould, Island, Kozberg, Lozano, Núñez, Preuss, and Rosenthal, Regents-designate Ledesma and Schreiner, Faculty Representative Brown, Secretary Trivette, General Counsel Holst, Interim Treasurer Berggren, Acting Provost Hume, Senior Vice President Darling, Vice Presidents Broome, Doby, Foley, Gomes, Gurtner, and Hershman, Chancellors Birgeneau, Bishop, Carnesale, Córdoba, Denton, Drake, Fox, Tomlinson-Keasey, Vanderhoef, and Yang, Interim Laboratory Director Miller, University Audit Reed, and Recording Secretary Bryan

The meeting convened at 9:45 a.m. with Special Committee on Compensation Chair Hopkinson presiding.

1.            **UPDATE ON COMPENSATION ISSUES AND ACTIONS TAKEN**

***Report on Internal Audit of Senior Management Group Compensation and Discussion of State Auditor’s Report; Follow-up Discussion on PricewaterhouseCoopers Audit; and President’s Proposal for Reforms in Response to Task Force on UC Compensation, Accountability, and Transparency; PricewaterhouseCoopers, State Auditor, and University Auditor Reports***

President Dynes began his report with the following statement:

Let me begin by asserting what has been driving me, my colleagues, and the Regents – that is that the University of California must be the best in the world or California will suffer enormously. The University is the gateway for young people’s lives and careers; it affects the quality of life; and it helps make California a competitive leader and drives its economy. In order to achieve excellence, it is imperative to recruit the best and brightest of staff, students, faculty, and administrators. In this, it faces competition from both public and

private universities. The University must be competitive in the context of being a public institution.

Having said that, I am driven by the Kozberg-Hertzberg task force, which stated that a sea change is necessary in the way in which the University conducts its business. I found the task force to be very insightful. Everything I say from here on in is driven by my understanding of what has to be done and the task force recommendations which make this very clear. These must be done, and we will do them. As I go through the plans that I propose to you, some of them are going to be difficult, contentious, argumentative, but we must do them.

I think it is useful to know how we got here, because it offers some guidance as to how to proceed. In order to first correct the problems and processes, we have to characterize them. Two case studies will offer a sense of the competition the University faces in recruiting people.

There are five points necessary for effecting the sea change:

- The first and perhaps most important is open communication with The Regents – something that we have not done; something that I have not done in terms of recruiting and compensation, and something that I must do and will do.
- The second is to put the mechanisms in place to assure compliance.
- The third is to ensure disclosure to The Regents in everything, and after the action, to the Legislature and the public.
- The platform for doing these things is a modern information system.
- The fifth is a culture change.

To describe the evolution as to how these innovative compensation plans came into account; in physics terms, if you apply a lot of pressure to something, it will pop out in other ways. In the past 15 to 20 years, base salary and a few other things such as home loans and vacation days were used. There was a period when the University was not recruiting heavily; when it returned to the market, it was discovered that people the University was trying to recruit were receiving many other benefits that they brought to the table. The University did not invent these; they were out there and are still out there both in public and private institutions. Over the last ten years, the private institutions have gotten richer and the public institutions have gotten poorer. These additional tools for recruitment have evolved in an attempt to bring people to California. The other ugly part of how the University got here is that housing prices in California have skyrocketed. As the *New York Times* reported recently, California has the eleven least affordable

metropolitan areas in the country. Housing is on every agenda concerning recruitment from outside of California and to new locations within California.

When I came to the Presidency, I realized I must hire five or six chancellors, laboratory directors, and senior management. In order to be successful, increasingly non-base salary techniques have become necessary. The University has lived in a thicket of outdated bureaucratic policies, conflicting policies – a situation that must be changed. Practices are dysfunctional also. The other approach taken was the notion of making people whole. It was not intended to enrich people by bringing them to the University, neither was it possible to ask people to take substantial decreases. One of the illusions that has been propagated was that the University has always managed to recruit its first choice.

My categorization of the types of findings begins with what are, in my view, the least egregious – the administrative errors. Overpayments were made because it was not recognized that some of the compensation was imputed income, W-2 forms were not issued, and recruited employees were not fully informed. Those mistakes are in the process of being repaired. The second category is exceptions to University policy. There are two kinds: the first are exceptions that were appropriate but the Regents were not informed of them; the second are those where Regental approval was required but not sought. All such past cases will be disclosed to the Regents, and mechanisms will be put in place to prevent similar oversights in the future. The third type is where policy is silent. All the types of findings are being catalogued so that they may be dealt with systematically. There were too many exceptions to programs that were approved by The Regents, including relocations, home loan programs, sabbatical benefits, separation agreements, vacation, and other unique benefits. The exceptions were authorized by senior administrators in the Office of the President and at the campuses and Department of Energy laboratories. It will be necessary to examine the delegations of authority to determine whether they have been too liberal. They were given because the market has required increased compensation for appointees, there has been a dramatic escalation of the California housing market with which the University's salary scales have not kept pace, and the University has been using outdated and ineffective working practices.

To illustrate this, I will use as an example the recruitment of Laboratory Director Chu. When he was recruited in 2004, the University was entering a competition to continue its management of the Lawrence Berkeley National Laboratory. It was the first time the University was asked to compete for the job. I determined that we needed the best person we could find, with the best vision and scientific credentials. He was a distinguished professor at Stanford and carried with him sabbatical credits. He was taking a huge risk, because there was no guarantee the University would win the contract. If the University had lost the contract, Mr. Chu would have moved to the faculty at Berkeley and would have needed his sabbatical credits to get back into the faculty mode. He was offered a \$50,000

one-time recruitment bonus, which was approved by The Regents, and an enhanced retirement benefit to make up for the fact that he was leaving a retirement plan that was calculated on his entire salary rather than the IRS limit of \$210,000. Through an error made at the Berkeley laboratory, he was enrolled in the severance pay plan. That error is being corrected. In summary, to attract a distinguished Nobel Laureate required an offer that would make him "whole." In the case of Chancellor Birgeneau, he was President of the University of Toronto, in the apex of his career. The University tried to bring him to the Berkeley campus by matching his compensation as closely as possible. The challenge of coming to Berkeley was sufficient to make him accept the job despite the fact that the University failed to make him completely whole. It takes more than base pay to bring such distinguished people from outside into the University.

My proposal is driven by the Kozberg-Hertzberg task force. In the area of compensation I did not pay enough attention. I was working very hard at recruiting and did not deal with the Regents as carefully and interactively as necessary. I relied on other people, which was a mistake. So establishing new working relations with the Regents in compensation is necessary and is being done. I talk with the Chair of the Special Committee on Compensation frequently about recruitments. The next part of the plan is to ensure compliance with the 1993 principles. There are a variety of reasons why we did not comply with those. Most of them were out of ignorance. We must put in place the mechanisms to ensure that. When we go through recruitments, the recruitment must be coordinated between business, academic affairs, Office of the General Counsel, and the controller. Nothing will go out any more until each person has a chance to examine offers to make sure they comply with not only the 1993 principles but also their spirit. Furthermore, it is important to examine the University's policies and procedures. I have formed a group of chancellors, faculty, and staff to decide how to effect this and rid the policies of contradictions.

Second, disclosure must be ensured. We have been reticent in that. This comes from an overactive secrecy plan somewhere in the University. There was a paranoia about leaking who candidates were before we were prepared. That resulted in too much secrecy and not enough disclosure. Again, I am putting the mechanisms in place so that this will not slide through any more. Disclosure to the Regents will be early, and furthermore disclosure to the Legislature and the public will be immediately upon action. We are in construction of a web site that will lay out our policies clearly and will disclose actions immediately after they are made.

All of this will be made easier by investment in a modern, comprehensive human resources information system. If anything is apparent, it is that our information systems hardly exist. Much of our inability to respond to Public Records Act requests is not because we are reluctant to, it is because we were not able to. We have information systems that are almost nineteenth century. We need an

integrated information system across the University that will make transparent information between the campuses, the Office of the President, and the laboratories. We have begun that with the design of an information system for senior management which should be in place by the fall. I hope it can be scaled up for the entire university.

Finally, the most difficult is that this requires a change in culture. The view is to work around things. It is a climate of exceptions and of trying to get away with as much as possible and disclose as little as possible. That culture simply has to change. Part of my design in changing that is to engage a group of people, including the faculty, staff, and Regents, in rewriting the policies. Looking back at the 1993 principles, they were lifted from a Tom Hayden bill and written down, so no one owned them; therefore, the compensation parts of those principles were never really effected. That must be built, and it will be the start of a change in the culture. This is the way in which we can build ourselves into leading the nation in compensation practices. What I discover is that most of our competition is engaged in the same practices that, until recently, we were. We will, as we do this, create a new climate for disclosure for public universities, and I expect the private universities will follow.

Committee Chair Hopkinson expressed appreciation for the President's comments and confirmed that she agreed with them substantially. She believed that two of the major issues confronting the Regents with relation to their interaction with the President are, first, his ability to be forthright, communicative, and cooperative. An issue that is equally important is communication with the Legislature. It is critical to the University's ongoing success. She advocated involving Regents in that effort.

Chairman Parsky asked President Dynes to expand on his statement that the intense competition for talent created an atmosphere of secrecy and paranoia about the possibility of leaks. President Dynes explained that when the University searches for a high-level position such as a chancellor, the pool of candidates consists of presidents, chancellors, vice presidents, or vice chancellors from other institutions. In many cases, if it is disclosed that they are candidates to be a chancellor at a UC campus, they will injure their ability to function in their own institution. It is typical that four or five candidates are interviewed. They need a certain level of protection or they will withdraw from the search.

Chairman Parsky believed it was critical that the Regents understand exactly what is meant when referring to this kind of culture so that steps may be taken to correct it. While he acknowledged the appropriateness of Mr. Dynes explanation, he noted that there was a set of policies that dictated that, following negotiations, the information was to be disclosed to the Regents and the public. President Dynes stated that when negotiations are completed, the 1993 principles are followed concerning the full disclosure of compensation. He commented that inside the Office of the President there has been for at least the past decade a view that those benefits that have been delegated to executives in UCOP did not have to be included in the list of compensation. He emphasized that this

view was wrong. Chairman Parsky believed that the need to be competitive in compensation does not suggest that there should be secrecy or a violation of policy once a decision is made. The Board stands ready to support the administration in maintaining the highest quality of the University, and part of doing that is being able to compensate people competitively, but the Office of the President puts the Regents on the defensive when secrecy in negotiations results in secrecy in what is being done. Mr. Dynes confirmed that the situation will not be repeated.

Chairman Parsky noted that President Dynes had indicated that he would be more forthcoming by calling a few Regents to discuss things. He believed that was not adequate. Thinking that matters are covered by calling one or two Regents is not transparency and disclosure to the public. The Board must be able to break through a culture of secrecy and a lack of transparency. Unless this becomes possible, the Regents' ability to maintain the quality of the University will be impaired. President Dynes responded that he understood this point fully. The change of the culture will be a sea change that will require the support of the Regents, the Academic Senate, the alumni, and the students.

Regent Kozberg noted that the Kozberg-Hertzberg task force's comments about the need for a sea change of culture referred to strong management and a strong sense that the University is a public trust. All mechanisms and processes need to be geared towards that. The University structure of shared governance can lead to confusion otherwise. President Dynes recalled that when eligibility was a subject of scrutiny, he had formed a group of Regents, students, faculty, administration, and outsiders that was an effective tool for developing an understanding of the problems with admissions and eligibility and how to correct them.

Regent Núñez praised President Dynes for accepting full responsibility for the problems with compensation. He noted, however, that there are people within the Office of the President who continue to believe that secrecy about benefits is appropriate and that they should not be brought to the Regents for approval. He suggested taking direct action with these people. He observed also that in being consistent with paying top, competitive wages with people in the highest positions, the University must not become an institution that generates elitism by not examining every other category of employee with the same view in mind. President Dynes noted that as both a Regent and Speaker of the Assembly, Regent Núñez could be instrumental in making the case to the Legislature and the people of California that investment in the highest quality of staff is critical to the University's success.

Regent Moores observed that there are many people in California who do not understand why the University needs to pay chancellors and senior officials their current salaries. Some faculty believe that no one in the University should be paid more than they, and some in the media take the same position. The overwhelming focus on compensation matters has consumed the Regents' time and overshadowed many other important issues for the University and the country, including the University's successful bid to manage the Los Alamos National Laboratory. There is a culture, however, of nondisclosure. He

believed that the Regents have chosen not to acknowledge that many kinds of information fail to be brought to them. Their standard of conduct has made it convenient for UCOP not to disclose information. He recalled that during his years on the Board, the Regents had never denied the Office of the President anything it wanted. He observed that, overall, compensation amounts are almost immaterial. As a function of the University's \$20 billion budget, compensation accounts for a fraction of a percent. There are huge issues facing the state. If the University of California fails, the State is in trouble. He was hopeful that, beyond a renewed commitment for transparency, the Regents would have its own staff. Now they rely on information from UCOP, which is conflicted and is not likely to put itself in a negative light. He suggested that the Regents should be somewhat embarrassed about what they have failed to do.

Regent Rosenthal believed that the Regents had not convinced themselves, the staff, the faculty, and the students of the importance of having high-caliber administrators and the necessity to pay them competitive salaries. He asked the President how he intends to present important issues to the student body, including an explanation of the need to pay competitive salaries and of why tuition has skyrocketed. The State and the Legislature must also be told about the effect of budget cuts on the University and the student body. President Dynes stated that part of the problem was the erosion of support for the University over the past twenty years. As a result, student fees had to be raised and student services reduced, and middle income families have felt the pinch. The public investment in higher education has been dwindling. Unless there is greater public awareness, that investment will continue to shrink. The Regents, faculty, students, and administration must work together to make the case to the Legislature that the legacy that was made in the 1960s and 1970s must be reinforced..

Regent Pattiz observed that serious issues have been dealt with at every Regents meeting. The public and the press – appropriate sources – have identified problems that have required Regental responses. He noted that President Dynes did not create the situation with respect to compensation. The failing was that, upon recognizing it, nothing was done about it. There is no evidence that anyone profited from the events, however. The problems were contributed to by using an outmoded culture and systems to try to accomplish things that are in the best interest of the University. He believed that the Regents had done more to fix the processes that led to the problem than had any of their predecessors.

Regent Rominger agreed that the Regents needed to do more to make the case that top administrators, faculty, and staff must be compensated fairly.

2. **REGENTS' PLAN FOR REFORMS IN RESPONSE TO THE REPORT OF THE TASK FORCE ON UC COMPENSATION, ACCOUNTABILITY, AND TRANSPARENCY**

Regents Hopkinson and Kozberg recommended that the Special Committee on Compensation recommend to The Regents the adoption of the actions shown in [Attachment 1](#) in response to the recommendations of the Task Force on UC Compensation, Accountability, and Transparency.

Committee Chair Hopkinson recalled that the Task Force on UC Compensation, Accountability, and Transparency was appointed in December 2005 by Chairman Parsky to conduct an independent review of UC's policies and practices on executive compensation and on the release of public information about compensation and related matters. The Task Force was co-chaired by Regent Kozberg and former Assembly Speaker Robert Hertzberg and included Dede Alpert, former State Senator; James Duderstadt, President Emeritus, University of Michigan; Kip Hagopian, Managing Partner, Apple Oaks Partners, LLC; Jay Harris, former Publisher of the *San Jose Mercury News* and Wallis Annenberg Chair in Journalism and Communication, Annenberg School for Communication, University of Southern California; Regent Monica Lozano, Publisher and Chief Executive Officer of *La Opinión*; James Morley, Jr., President and CEO, National Association of College and University Business Officers; and John Oakley, Chair, UC Academic Senate.

At the April 13, 2006 meeting of The Regents, the Task Force presented its report of findings and recommendations. The report focused on four areas: disclosure and transparency; governance and accountability; specific policies and practices; and competitive compensation. In order to address many of the issues identified by the Task Force, a complete rethinking of University compensation policies, practices, and procedures is required. The success of these reforms, as well as assurance that University policies and practices survive leadership changes systemwide, will depend on a new, comprehensive policy framework that must be guided by the principles of public accountability and disclosure, effective governance and oversight, individual and institutional accountability, and institutional competitiveness. It is anticipated that the conceptual basis for this new policy framework will be brought to the Regents for discussion at the July meeting, along with an implementation time line. In the longer term, in developing a new comprehensive policy framework, the University will also undertake an evaluation of all faculty and staff compensation policies and procedures, in consultation with the affected employee groups. President Dynes has appointed an Implementation Committee and workgroups composed of campus, medical center, and Office of the President personnel. The committee and workgroups have begun meeting and are poised to implement those Task Force recommendations ultimately adopted by The Regents. The attached table displays 23 recommended actions and estimated time lines for each of the Task Force recommendations.

Regent Kozberg noted that the task force deliberated how best to integrate the plan so as to educate the workforce as to the policies and ensure compliance.



Committee Chair Hopkinson and Regent Kozberg reviewed each of the recommendations proposed in the table. In general, the recommendations of the task force have pointed out some inbred problems, many of which are related to policies and procedures. The first recommendation is to create a policy framework and time frame as the first step in setting new policies and procedures. At the September meeting, a specific plan and timetable will be presented for each recommendation. The second recommendation is immediately to create an advisory committee, which is consistent with the task force recommendation. The advisory committee would be comprised of representatives from campus administration, faculty, staff, and the Office of the President, with the Chair of the Special Committee on Compensation as an ad hoc member. The group will be appointed by the President and the Committee Chair. The committee will be coordinated by the President and will report to the President and The Regents. An external consultant will be retained to help with the overall framework and individual policies and procedures. Ongoing training is a key element of all the recommendations. A consultant will be recommended to help with that task. Committee Chair Hopkinson noted that it is anticipated that the faculty will be a key player on the advisory committee.

Faculty Representative Oakley commented that the faculty had responded point by point to the task force leadership. The basic thrust of the Academic Council, acting as the executive committee of the Assembly of the Academic Senate, in endorsing point by point is to indicate that there are a number of areas where things must be revised, but the nature of the revisions is not known precisely. The faculty advocate active Senate involvement both through the role of the Faculty Representatives and through the normal channels of Senate review.

Committee Chair Hopkinson noted that the task force is focused on senior management compensation. The recommendations that are specific are more encompassing. They recognize that this step is a priority but suggest that there will be future steps involving faculty and staff compensation.

Committee on Audit Vice Chair Lozano asked that Regent Hopkinson and the chair of the task force acknowledge the sense of urgency and assure the time line for implementation addresses that urgency.

With reference to item RE-74c of the table, Regent Juline believed any family relationships of the people who are being acted upon with members of the senior management group of the University should be disclosed as part of the process. Regent Hopkinson responded that it may be considered by the group that will be working on policies and procedures.

With respect to RE-74e, Regent Hopkinson noted that an additional item will be to strengthen internal audit. No time frame has been set.

With regard to RE-74k, Regent Preuss noted that the hiring process is not one of lengthy consultation. He believed care must be taken not to come up with a policy that prevents people from being hired. Faculty Representative Oakley noted that the situation would

be helped with the installation of an up-to-date, comprehensive systemwide human resources information system that will allow the collating of information and fast-tracking exceptions when needed.

Concerning RE-74n, Chairman Parsky noted that prior to this, based on the actions taken by The Regents in November, only 32 positions, plus anyone earning over \$200,000, would have been addressed. If adopted, approximately 264 positions would be reviewed, including all elements of compensation, exceptions, variations, and definitions.

Regent Hopkinson reported that upon employment and annually thereafter, employees who are in positions at an appropriate level of decision making and authority will be required to confirm that they have read, understood, and comply with the University's statement of ethics.

With reference to RE-74s, Faculty Representative Brown reported that the faculty believe that the attractiveness of a UC position depends not just on compensation but also on having a first-class research environment, appropriate support for students, and an appropriate climate and working conditions. The faculty are concerned that all the focus on compensation is distracting attention from those important elements. Regent Hopkinson believed that RE-74t addressed those concerns.

Regent Hopkinson noted that the faculty had recommended that the Regents agree that administrative leaves should be at faculty salaries. She indicated that she was not prepared to present that action at this point.

Regent Marcus cautioned against, in trying to respond to the failings of the past, establishing new, complex, conflicting policies. The new policies must be simple and allow the administration to compete for talent, and everyone must be given a fair opportunity to adhere to them.

Upon motion duly made and seconded, the Committees approved Regents Hopkinson's and Regent Kozberg's recommendation and voted to present it to the Board.

An addendum to the item contained an additional recommendation as follows:

Regent Hopkinson recommended that the Special Committee on Compensation and the Committee on Audit recommend to The Regents the adoption of the Guidelines for Resolution of Compensation and Personnel Issues Resulting from the Findings of Audits and Management Reviews, as shown in [Attachment 2](#).

The Committees were informed that as part of the Special Committee on Compensation's responsibilities for setting compensation policy and providing necessary oversight to ensure compliance, Guidelines are being recommended to be used in addressing compensation and personnel issues that have been identified in the audits and management reviews.

The external and internal audits of UC compensation practices and other management reviews and related disclosures have resulted in numerous findings of compensation and related items that have been provided to employees through administrative oversights or errors, as exceptions to policy, or without proper approval authority. The Appendices that were distributed with item 1, above, provide all the exceptions that have been identified to date that did not have appropriate Regental approval.

The Guidelines for resolving these violations of policies are consistent with the principles presented in item 1, above. They will be used by the administration to provide recommended actions for individual compensation and personnel issues identified in the audits and management reviews, which will be brought to The Regents at future meetings for action and/or reporting, depending upon the resolution of the particular case. Associate Vice President Boyette, under the direction of Senior Vice President Darling, will coordinate a team with representatives from the Office of the General Counsel, Audit, and Financial Management that will review cases and report to The Regents at each meeting with recommended action by The Regents or progress on resolving the remainder of the cases identified in the audits and management review process. Consultation with each respective campus for each employee will occur. It is anticipated that compensation actions and/or reporting related to the remaining individuals identified to date will come to The Regents at the July and September meetings, and that the corrective actions will be reported to The Regents at coming meetings, but will be completed no later than the November meeting, when annual salary actions and related performance issues are normally discussed with the Regents.

Upon motion duly made and seconded, the Committee approved the recommendation and voted to present it to the Board.

Associate Vice President Boyette described how the policies and procedures will be reviewed and changed. The overall objective will be to redesign policies, procedures, and control mechanisms for the compensation and benefit programs. The compensation policies will be redesigned to align them with the defined pay philosophy, which will be harmonized with local needs to recruit. A governance process will be designed that recognizes the role of The Regents and segments local and systemwide decision rights. In support of any of the policies, there must be appropriate business processes and the infrastructure to support them, which includes technology to manage compensation decisions, reporting, and disclosure. Appropriate monitoring, compliance, and enforcement mechanisms will be included in the design of these new policies and processes. Priorities must be set based on the impact and the implementation issues the result from what will be a lengthy process. Appropriate tools and documentation must be created to support the governance process, which is important because the University's policies have not been clear about the rules, roles, and responsibilities for policies. The end result should meet the following criteria:

- Enables competitive, fair, and reasonable compensation and benefits;
- Compares favorably to best practices of the University's peer groups;

- Is transparent, can be monitored and enforced;
- Reflects the University's systemwide philosophy while providing appropriate autonomy to meet the needs of campuses, medical centers, and laboratories.

An effective, complete compensation and benefit governance structure for the University will require the following:

- An over-arching structure that describes guidelines and timing for an ongoing, systemwide review of policies;
- A clear set of rules, roles, and decision rights for each entity involved in making compensation policy decisions and for determining individual compensation decisions
- Business processes, technology, and systems that request, collect, and aggregate the appropriate information to enable monitoring and enforcement of systemwide guidelines;
- Involvement and agreement from the appropriate stakeholders.

A three-phased approach is recommended:

Phase I – Obtain agreement on broad approach; form advisory committee; review appropriate internal and external staffing for the project.

Phase II – Perform high-level discovery and develop policy framework and timetable; develop detailed project plans to ensure effective implementation of project

Phase III – Implement detailed project plans, perform all required analyses, and engage stakeholders to gain approval for and to execute a new governance structure.

During the data gathering phase, all variations of pay, benefits, leave, and perquisites will be reviewed. When determining stakeholders, input of representatives of the Academic Senate and the legislative and other appropriate agency representatives and other internal consultive groups will be considered carefully. A governance structure, business processes, and technology must reflect the constraints of the human resources and payroll infrastructure in existence. Some processes and/or decisions may need to be centralized, and all will require clear decision ownership and issue escalation processes. Compensation policies will need to be dealt with considering the best overall structure, while immediate action may need to be taken in order to address issues of public concern. Effective controls need technology support, and decisions involving resources to be devoted to technology improvements will need to be agreed upon. Appropriate technology reviews will need to be undertaken, including the use of third-party

technology providers or outsourcers. Timing and completion of the project will depend on timely participation during the data-gathering phase and access to key stakeholders throughout the process.

A progress report will be delivered at the July Regents meeting, at which time a policy framework and timetable will be proposed.

3. **FILING OF FORMS W-2C RELATED TO INDEPENDENT EXAMINATION OF COMPENSATION AND OTHER EMPLOYMENT ARRANGEMENTS CONDUCTED BY PRICEWATERHOUSECOOPERS, LLC**

The President recommended that the Special Committee on Compensation recommend to The Regents that, for each University of California employee identified by The Regents' external auditors as requiring a Form W-2c (Corrected Wage and Tax Statement), the University reimburse the employee for applicable tax preparation fees, interest, and penalties, if any, and any incremental taxes associated with such reimbursements, as evidenced by receipts or other documentation.

No income or employment taxes owed by the employee related to the additional income reported on the Form W-2c itself will be reimbursed by the University.

It was recalled that at the April 24, 2006 meeting of The Regents, PricewaterhouseCoopers LLP presented the findings and observations contained in its Examination of Compensation and Other Employment Arrangements of selected University of California employees for the period January 1, 1996 through December 31, 2005. Employees selected for examination generally included individuals who hold or have held one of the top 32 senior management positions or another selected position for at least six months during the period of the audit.

Among its findings and observations, PricewaterhouseCoopers identified compensation received by several employees that was omitted from their Forms W-2 in one or more years. Under regulations issued by the Internal Revenue Service, the University is required to provide these employees with a Form W-2c showing the wages that should have been reported for each year. Corrections generally fall into three categories: 1) items promised in employment offer letters that were not identified for the employee as being taxable or reported in taxable income; 2) reimbursements of taxable travel and relocation expenses that were not included in the employee's taxable income; and 3) corrections related to administrative errors in underreporting (and over reporting) of imputed income and other items of income. Employees receiving a Form W-2c must amend their personal federal and State income tax returns for any years still open under the statute of limitations. The statute of limitations is generally three years from the date a taxpayer files his or her personal income tax return. For example, the statute of limitations for a 2002 return filed on April 15, 2003 expired on April 15, 2006; thus, employees receiving a Form W-2c for 2002 or a prior year typically would not be required to amend their income tax returns unless they had waived the statute, e.g., because they are under audit by the Internal Revenue Service. Employees receiving a

W-2c for 2003 or later would be required to file amended income tax returns and might incur interest and penalties in addition to tax preparation fees. Although the three-year statute of limitations applies to income tax returns filed by most taxpayers, it does not relieve an employer of its obligation to file a Form W-2c to report unreported wages that were earned beyond the three-year statute applicable to the employee.

Upon motion duly made and seconded, the Committee approved the President's recommendation and voted to present it to the Board.

4. **POLICY ON VIOLATION OF UNIVERSITY POLICY OR LAW BY INDIVIDUALS WITH NEGOTIATED SEPARATION ARRANGEMENTS**

The President recommended that the Special Committee recommend to The Regents that the Policy on Violation of University Policy or Law by Individuals with Negotiated Separation Terms ([Attachment 3](#)) be adopted effective immediately.

General Counsel Holst recalled that recently there has been concern expressed about the provision of leave arrangements, faculty appointment terms, or other arrangements negotiated at the time of an employee's appointment in relation to questions about the employee's compliance with University policy or applicable law during employment. Such an agreement regarding separation terms negotiated by individuals at the time of their appointment to University positions is not common, but neither is it unprecedented, given the competition in the marketplace. Objections have been raised to making pre-negotiated payments in circumstances in which the employee may have violated University policy or law, or both; however, absent some qualification in the negotiated terms, typically the University will have no choice but to make the payments to which it has committed.

The proposed Policy on Violation of University Policy or Law by Individuals with Negotiated Separation Terms provides that separation terms negotiated with an individual employee prior to the time of the employee's separation from a particular position or from University employment would be subject to reduction or elimination if the University has determined that the employee has violated University policy or applicable law. The terms of the Policy would be incorporated in agreements providing for negotiated separation terms. The Policy would not affect an employee's entitlement to retirement and similar benefits that are vested under law. Any application of the Policy to a particular employee would be subject to due process applicable to the imposition of discipline for the employee's employment category. If that process resulted in a determination that there had been a violation of University policy or law, the President would determine whether the violation was serious or substantial; in such cases, the President would recommend an appropriate forfeiture or loss of separation benefits, in whole or in part. Final action would be taken by the Chairman of the Board and the Chairman of the Special Committee on Compensation, in consultation with the General Counsel.

The intention is that the proposed Policy be applied prospectively only – absent extraordinary circumstances amounting to material and intentional misrepresentation or

fraud, in which event the Regents would have the discretion to address the situation as the circumstances warrant.

Upon motion duly made and seconded the Committee approved the President's recommendation and voted to present it to the Board.

## 5. **AMENDMENT OF INTERIM POLICY ON SEPARATION AGREEMENTS**

The General Counsel recommended that the Special Committee on Compensation recommend to The Regents amendment of the Interim Policy on Separation Agreements and its renaming as the Interim Policy on Separation Agreements and Settlement of Employee Claims as set forth in [Attachment 4](#).

It was recalled that the Policy on Settlement of Claims and Litigation, adopted originally in September 1995, provides for the settlement of litigation (legal proceedings in the form of a lawsuit, arbitration proceeding, or internal or external administrative proceeding) and claims (any demand for payment which is disputed in whole or in part and is made other than through litigation). The Interim Policy on Separation Agreements, adopted at the January 2006 meeting, provided for the approval of separation agreements which are individually negotiated in some circumstances and establish terms applicable to an employee's separation from the University or transfer from one position to another. The Interim Policy resulted from the General Counsel's opinion that the Policy on Settlement of Claims and Litigation does not apply to separation agreements which typically result from an administratively initiated employment action that is not necessarily accompanied by the subsequent assertion of a claim by the separating employee; in other words, some separation agreements simply establish terms of the separation without any legal claim's being a basis for the consideration paid pursuant to the agreement.

Since some separations involve claims and others do not, and it may, under such circumstances, be difficult to evaluate the legal significance of whatever claim is asserted, a policy that treats similarly separation agreements, on the one hand, and employee claims generally (as distinguished from employee-initiated litigation), on the other, appears advisable. Under such an approach, the settlement of litigation, whether or not initiated by an employee, would be subject to an amended Policy on Settlement of Litigation and Non-Employee Claims, and separation agreements and the settlement of employee claims would be subject to an amended Policy on Separation Agreements and Settlement of Employee Claims. The proposed revisions would make all non-litigated, employment-related matters – that is, separation agreements and claim settlements whether or not related to an employee's separation, other than employee-initiated lawsuits – subject to a single policy, the Interim Policy on Separation Agreements and Settlement of Employee Claims.

Accordingly, the proposed amendments remove the settlement of employee claims from the current Policy on Settlement of Claims and Litigation and make such agreements subject to an Interim Policy on Separation Agreements and Settlement of Employee Claims that would replace the current Interim Policy on Separation Agreements. The

provisions for review and/or approval by the General Counsel, the President, and the Regents, at various monetary levels, would be unchanged. "Claims," other than employee claims, would remain subject to a renamed Policy on Settlement of Litigation and Non-Employee Claims. The definition of "claims" in that Policy would be changed to refer to "any demand for payment from an entity or individual, other than a University employee, which is disputed in whole or in part and is made other than through litigation."

The proposed amendment of the Interim Policy on Separation Agreements and Settlement of Employee Claims would include a cross-reference to Regents' Standing Order 103.7, which authorizes the President to approve severance compensation for faculty with tenure or security of employment whose resignation is deemed to be in the interest of the University. The President is required by the Standing Order to consult with the respective chancellor, and the chancellor is to consult with the appropriate advisory committee(s) of the Academic Senate. Without a cross reference, it would be unclear how to interpret the Standing Order in light of the Policy on Separation Agreements and Settlement of Employee Claims, which applies to all employees, including faculty. Accordingly, the proposed Policy on Separation Agreements and Settlement of Employee Claims includes the following language:

"With regard to faculty members with tenure or security of employment, in the event that a faculty member's resignation and severance compensation are deemed by the President to be in the best interest of the University, pursuant to Standing Order 103.7, any resulting separation or settlement agreement shall be subject to this policy, in the case of non-litigated matters, and to the Policy on Settlement of Litigation and Non-Employee claims, in the case of litigated matters."

The other substantive changes to the Interim Policy on Separation Agreements are as follows:

- The General Counsel's review and comment on employee separation agreements and employee claims is amended to require "comment on the potential legal exposure, if any."
- The amendments provide for an annual report of all separation and employee claim settlement agreements to The Regents, to include all agreements involving consideration of between \$50,000 and \$100,000. The Interim policy requires reports of agreements involving consideration of \$100,000 or more. Since the policy requires Regental approval of agreements of \$100,000 or more, the amendment will provide increased information to the Regents, rather than duplicating information already submitted. In addition, the lower, \$50,000 threshold is what is used for reports of litigated matters. The amendments also de-couple the annual report from the report on senior management compensation and the annual report on senior management outside professional activities and related compensation.



- The amendments revise the definition of “consideration” for purposes of clarity, and more precisely to distinguish what is being negotiated with the employee for purposes of the agreement – that is, the “consideration” for the agreement – from payments or benefits earned under terms and conditions of employment independent of the agreement.

Chairman Parsky reported that this action item would not affect the need for all matters relating to the approximately 264 individuals who are covered by The Regents to come to The Regents with respect to all elements of compensation going in and leaving. General Counsel reported that the first paragraph provides that all separation agreements for the specified officers, which is the group of 32, must come to The Regents regardless of the level of consideration that is involved in the separation arrangement. Chairman Parsky believed that, in light of the action that was taken with respect to those individuals who are going to come to The Regents, the policy be amended to cover all of them, so that there is no question about it. The action taken previously increased the number of individuals from 32 to approximately 264. There should be compatibility, regardless of the level of consideration. General Counsel Holst indicated he would provide wording consistent with the intent of the amended motion.

Regent Moores recalled that the media had cited a possible example of an arrangement whereby an employee, as part of a termination arrangement, was paid to do nothing for several years. He asked whether, if someone is making \$100,000 a year and as part of an exit strategy is allowed to stay in the job for a few years, that must be disclosed. General Counsel Holst responded that such an agreement would come to The Regents, and the specifics of the provisions would be included in the action. Whether it be the President or The Regents, there will be a statement of the comprehensive terms of the separation agreement so that there will be an understanding as to what is involved. Now the President will have the approval authority, subject to possible delegation to the chancellors at certain levels of his authority, but up to \$100,000 with respect to these agreements. It will be the obligation of the President’s advisors to inform him as to the consequences of the agreement. For compensation over \$100,000, The Regents will consider the specific terms.

Upon motion duly made and seconded, the Committee approved the recommendation as amended and voted to present it to the Board.

## 6. **REPORT ON SEPARATION AGREEMENTS – 2001-2005**

General Counsel Holst reported that he had developed information from a variety of campus and Office of the President sources which has identified approximately 700 separation agreements, of varying types. Some are “pure” separation agreements initiated administratively, with the objective to satisfy an administrative need to separate a particular individual from a position or from University employment. Some of those separation agreements are accompanied by legal claims. The crossover between the administrative initiative to separate a person from University employment and the responsive claim from an employee calls into action some form of legal analysis to

determine the substantiality of the claim in terms the amount of consideration to be paid. The third category is employee claim settlements resolving what are essentially employee-initiated, non-court litigation, typically grievance proceedings in the University-established process.

The meeting adjourned at 12:40 p.m.

Attest:

Secretary