The Regents of the University of California

COMMITTEE ON FINANCE
March 16-17, 2011

The Committee on Finance met on the above dates at UCSF–Mission Bay Community Center, San Francisco.

Members present:	Regents Blum, DeFreece, Island, Lozano, Makarechian, Schilling, and Varner; Ex officio members Gould and Yudof; Advisory members Mireles, Pelliccioni, and Simmons; Staff Advisors Herbert and Martinez
In attendance:	Regents Crane, De La Peña, Hime, Johnson, Lansing, Pattiz, Reiss, Ruiz, Torlakson, and Zettel, Regent-designate Hallett, Faculty Representative Anderson, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Chief Compliance and Audit Officer Vacca, Provost Pitts, Executive Vice Presidents Brostrom and Taylor, Senior Vice Presidents Dooley and Stobo, Vice Presidents Beckwith, Darling, Duckett, Lenz, and Sakaki, Chancellors Birgeneau, Block, Blumenthal, Desmond-Hellmann, Drake, Fox, Kang, Katehi, White, and Yang, and Recording Secretary Johns

The meeting convened at 9:35 a.m. with Committee Chair Lozano presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of January 19, 2011 were approved.

2. **UPDATE ON THE 2011-12 STATE BUDGET**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Committee Chair Lozano emphasized the difficulty of the issues faced by the University, including its mandatory costs and the unreliability of State funding. The Committee's discussions would include an examination of long-term budget options.

Executive Vice President Brostrom observed that, if the Governor's budget is passed as proposed and his proposed tax extensions are approved in a June election, State support for the University, roughly $2.5 billion, will be equal in absolute dollars to its level in the 1998-99 budget year, a time when the University served 73,000 fewer students, had one fewer campus, and far fewer programs and majors. These figures reflect a threat to the core values of the University and to its commitment to quality, access, and affordability. As the University seeks to build a sustainable long-term funding model, it has leverage over only a few variables, such as the size of enrollment, tuition, amount and sources of financial aid, and the overall academic program offerings and the faculty and staff who provide them. Mr. Brostrom recalled that the State's contribution to UC per student has declined by 57 percent in inflation-adjusted dollars since 1990, from $16,700 in 1991 to a projected $7,200 in the coming year. For the first time in UC's history, the amount the University raises from tuition and fees will exceed the amount it receives from the State. Students now bear roughly 46 percent of general fund support; 20 years previously, that share was 12 percent. The overall amount spent per student has declined by nearly 20 percent in the past 20 years. Tuition has increased as the State has disinvested in UC, and the rate of increase has not kept pace with the decline in State spending. While the price of a student's education has been increasing, the funding for providing it has declined.

Vice President Lenz reported that, while State budget negotiations were ongoing, the budget approved by the two-house Conference Committee closely followed a number of the Governor's recommendations. State spending would be reduced by $12.5 billion; General Fund tax revenues of $12 billion are assumed; there would be funding transfers of $3 billion; and $840 million is assumed in a State budget reserve. Unresolved issues for the Governor and the Legislature include public employee pension reform, establishment of a State spending cap, major changes to the California Environmental Quality Act, and reform of the State tax code.

The budget approved by the Conference Committee includes the Governor's proposed $500 million reduction in State support for UC, a redirection of $3 million from the University's base budget to fund salary increases for service worker employees represented by the American Federation of State, County and Municipal Employees (AFSCME), and $9.3 million in capital funding for equipment. Trailer bill language has been added requiring a report to the Legislature and the Governor's administration by June 1, 2011 regarding the University's recommended 2011-12 budget options, and a report on implemented budget solutions by September 1, 2012. In addition, the trailer bill language sets the University's State-supported enrollment target at almost 210,000 full-time equivalent students. The last matter has been of concern to the University, which would prefer a target number more closely reflecting actual State support.

At the request of State Senator Leno, the Legislative Analyst's Office has provided recommendations regarding budget alternatives if tax extensions are not approved by voters. These recommendations include a reduction of UC personnel costs by ten percent, a seven percent UC tuition increase in addition to that already approved for fall 2011, and a reduction in State General Fund support for UC and California State University research. The Legislature is now considering budget reductions which could cause serious concerns for UC.

Mr. Lenz then outlined State actions on Cal Grants. Cal Grant funding was included in the budget to offset the eight percent UC student fee increase approved in November 2010. The Governor's January budget proposal included $1.6 billion in financial aid grant programs and a transfer of $946 million in federal Temporary Assistance for Needy Families funds to support Cal Grants. The Legislature has reduced this fund transfer to

$285 million and has applied General Fund monies for the remainder. Mr. Lenz called attention to other actions taken regarding Cal Grants: annual income verification for Cal Grant recipients, a new student default risk index, and reporting requirements on completion and job placement rates.

The significant pressures on the 2011-12 UC budget are the proposed $500 million reduction in State funding, an increase in UC mandatory costs of $362 million, uncertainty regarding voter approval of the tax extension initiative, and the possibility of further reductions to the UC budget if the tax initiative does not succeed. Mr. Lenz emphasized the need for a long-term plan for fiscal stability.

The 2011-12 UC budget gap includes a $733.4 million reduction in State General Fund support; this represents a 22.5 percent reduction from 2007-08 levels. Mandatory costs through the current year total almost $587 million, and there are additional mandatory costs in 2011-12 of almost $267 million. While the 2011-12 budget gap would be offset by earlier fee increases, 2011-12 fee increases, and a prior year shortfall that campuses absorbed in 2010-11, Mr. Lenz anticipated a shortfall of almost $700 million.

The University has implemented various measures in the past to address budget shortfalls, and if there are further reductions to its budget, it would be forced to consider measures for 2011-12 including deferral of salary increases, furloughs, deferral of increases to the employer contribution to the UC Retirement Plan, health benefit cost reductions, debt restructuring, additional tuition increases, and enrollment reductions.

Mr. Brostrom underscored that the current budget crisis is not a single-year phenomenon. In 2008-09, the State reduced UC funding even more drastically, by over 25 percent, although this cut was tempered somewhat by one-time federal American Recovery and Reinvestment Act (ARRA) funds. Since 2008-09, campuses have responded with over 4,400 layoffs, leaving 3,700 positions unfilled or eliminated. They have considered the consolidation, restructuring, and elimination of academic and extracurricular programs. Every unit, whether administrative or academic, has been subject to reductions, although reductions have varied by campus and unit.

In the past round of budget cuts beginning in 2008-09, solutions were generated mostly by systemwide actions, such as large increases in tuition and fees, the furlough plan, and systemwide efforts in debt and asset management. In 2011-12, a greater part of the burden in filling the gap will fall to the campuses. Campus action plans are now in a preliminary phase; the form they take will depend on the outcome of the State budget and the possible June ballot. Most campuses are allocating disproportionately larger cuts to administrative units to reduce the impact on academic programs; making use of temporary financing measures to serve as a bridge and planning to implement permanent cuts over a longer period; planning to increase nonresident enrollment; deferring or freezing faculty hiring; and engaging in significant efforts to generate administrative efficiencies, such as developing shared service centers to consolidate administrative functions, participating in the Statewide Energy Partnership program to reduce energy costs, and curtailing hiring of staff, reducing travel, and other deferrals.

3. **CAMPUS PRESENTATIONS ON IMPACTS OF BUDGET CUTS**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Chancellor Blumenthal stated that the budget cuts made in the past three years and those planned for the immediate future have brought the University to the point of compromising educational quality. As a smaller campus without a medical center, the Santa Cruz campus has fewer resources and must be entrepreneurial in its choices. The campus' culture of strategic decision-making would serve it well in the current difficult circumstances.

Chancellor Blumenthal enumerated achievements by UCSC faculty and reported that, in a recent comparison with Association of American Universities (AAU) institutions, UCSC ranked fourth for citations per research paper. When compared to AAU institutions without medical schools, UCSC ranks ninth in federal research funding per faculty member. These achievements are now at risk.

Funding for core functions at UC Santa Cruz has been permanently reduced by nearly 13 percent since 2008. This reflects State budget reductions as well as increased costs. The campus has kept up with budget cuts, working closely with the UCSC division of the Academic Senate, deans, and principal officers. Despite dwindling State support, UCSC has attempted to create a multi-year budget framework to help campus leaders plan strategically.

The Santa Cruz campus has implemented cuts differentially, protecting academic programs at the expense of support units and making strategic investments to secure its future. Chancellor Blumenthal observed that, with the latest cut, the campus budget for core functions will be 21 percent smaller than four years previously, even as UCSC serves more students and manages a robust, externally funded research portfolio whose growth has outpaced the national average. He described some of the campus' cost-cutting efforts, such as restructuring of information technology services, centralization of most business and human resource functions, implementation of a decision-support system, energy efficiency, water conservation, waste diversion, and other measures.

Chancellor Blumenthal called attention to other changes at UCSC. The campus no longer provides faculty and staff child care. It has reduced spending on library collections and is losing and delaying programs of value to faculty and students. He expressed concern that, while UCSC has worked hard to ensure that students can get the courses they need and can make timely progress toward graduation, this effort may conceal the precarious state of the campus' resources. He cautioned that the campus would not be able to make new cuts strategically. Further reductions would cut to the heart of the instruction and research missions. Curricular offerings have already been reduced to the point that some gateway courses are offered only once a year.

UCSC is considering further cuts to funding for unfilled faculty positions. It has reduced 80 full-time equivalent positions in the last three years and now faces a reduction of 40 more positions, which would amount to 16 percent of its faculty positions. Chancellor Blumenthal anticipated that there will be no faculty hiring or replacements for faculty who leave or retire. Some departments do not have enough faculty to carry the curriculum and are considering suspending degree programs. Funding for teaching assistants will also be further reduced. The campus has defunded 110 teaching assistantships to date and may cut 120 more. This has affected course availability and students' educational experience.

UCSC has eliminated or reduced 316 staff positions and may cut another 150 jobs, a significant loss for a campus of this size which is already thinly resourced. All of these cuts will have repercussions for years to come and will challenge the campus' ability to meet its obligations. Even public safety operations and the internal audit and controller's offices cannot be exempted from cuts, which are making UCSC vulnerable in many ways.

UC Santa Cruz offers an intimate, college-based undergraduate experience and all the opportunities of a major research university. Its student body is more diverse and more reflective of California than ever. Forty-four percent of Santa Cruz freshmen this year will be the first in their families to earn a four-year degree. However, access to public higher education is in jeopardy in California and the nation and the University is at a crossroads.

In order to help campuses meet current budget challenges, Chancellor Blumenthal asked that the campuses be given as much flexibility as possible as they implement cuts, that the Regents do everything in their power to help the University secure multi-year budget stability, which is especially critical for the smaller campuses, and that all options be kept open. He concluded that this was a defining moment for the University and for future generations of California students.

In beginning his presentation on the impact of the fiscal crisis on UC Irvine, Chancellor Drake recalled his first formal presentation to the Regents in 1994 on admissions programs, which successfully fostered both excellence and diversity, and the threats to those programs at that time. He reflected that the University is now facing a similar threat, poised on the precipice of a negative change in quality, which, if allowed to occur, will require a generation to remedy. He praised the excellence of the UC Irvine faculty, but noted that faculty members now spend a great deal of time mitigating damage caused by cuts rather than building for the future. He described the situation of the University as one of slow decay rather than growth. Most effort is focused on protecting the educational path for students; innovation and growth are not being fostered.

Chancellor Drake presented visible examples of this kind of gradual decline. He had noticed that there was now often a long line of students waiting for financial aid counseling near his office, due to the fact that more students need financial aid, and because there are now fewer staff to assist them. Another example was that hot water had been turned off in the bathrooms on campus to save money.

The Irvine campus strives for academic excellence, research excellence, excellence in character, and excellence in leadership. Chancellor Drake drew attention to the importance of students' experiences outside formal educational situations. He recalled a formative student experience of his own when he participated in a small seminar group. UC Irvine established a freshman seminar program when Chancellor Drake came to the campus, and participants often remarked later on what a positive experience it was for them. This year the campus has cut this program due to lack of funding. Another outstanding program on campus was the Chancellor's Distinguished Fellows Series. One speaker in this series was former President Carter, who inspired UCI students to begin the Olive Tree initiative, through which participants travel to the Middle East and learn about the region. The initiative has grown and is being emulated by other institutions. The Chancellor's Distinguished Fellows Series has been cancelled because of a lack of funding.

Chancellor Drake expressed his view that the programs of excellence in the University which are now being trimmed back define the difference between an "A" and an "A plus" institution. While this difference might not be immediately perceptible to an outside observer, it results in an educational pathway for students which is less brilliant, broad, and elevated. He concluded by voicing his concern about the future of the University and his interest in efforts to ensure that the University maintains the excellence for which it has worked a century and a half.

Chancellor Birgeneau began his remarks by noting the high rankings enjoyed by UC campuses. In the Academic Ranking of World Universities by Shanghai Jiao Tong University the previous year, four UC campuses were ranked among the top 20 universities in the world. The previous week, the London *Times Higher Education* supplement presented its world university rankings; several UC campuses were judged among the best in the world, and UC Berkeley was judged to be among the six best universities in the world. While these high rankings might suggest that the University's excellence is assured well into the future, Chancellor Birgeneau cautioned that this may be illusory. He recalled that his early scientific career was spent at Bell Laboratories, where the transistor, the Unix operating system, charge-coupled devices, solid state diode lasers, and many other inventions were developed. Bell Laboratories generated numerous Nobel prizes in science and technology. Chancellor Birgeneau observed that a series of bad decisions by government, corporate leadership, and governing boards have led to the near disappearance of Bell Laboratories. What was once arguably the foremost research laboratory in the world virtually disappeared over a period of 25 years, with a palpable impact on the American economy. He emphasized that greatness must be nurtured and stated his view that the University now finds itself in a situation similar to that of Bell Laboratories in the mid-1970s.

Chancellor Birgeneau stressed that the University should not accept the $500 million budget reduction proposed by the Governor with complacency and resignation. He noted that when he came to UC Berkeley, most campus funding came from the State. The second major source of funding was the federal government, while student fees and philanthropy provided roughly equal amounts of support and came in third place. Chancellor Birgeneau anticipated that the following year, with the projected budget cuts, the campus' primary funding source will be the federal government; the second source will be student fees. The third source will be private philanthropy, while a distant fourth will be State support. UC Berkeley has evolved from a State-funded institution to a national public university.

In addition to budget reductions, the campus faces increasing health care costs, pension costs, and negotiated salary increases. The budget shortfall at UC Berkeley for fiscal year 2012 is expected to be $110 million, and the campus is now developing a multi-year strategy for addressing this shortfall, including further fee increases, increasing nonresident enrollment, growth in philanthropic support, improved financial management, and increased federal support. The campus' Operational Excellence program aims at reducing administrative expenses and achieving efficiencies. Over the next three to five years, the campus expects to reduce administrative costs by at least $75 million annually. The first stage of this effort is complete and has reduced administrative expenses by $20 million. The number of managers has been reduced from 1,450 to 1,210; nearly a quarter of these positions had salaries of $100,000 or above.

Chancellor Birgeneau cautioned that the campus does not have a model for accommodating the further reductions which may be made to the UC system if the Governor's proposed tax extensions do not succeed. UC Berkeley faculty consistently express concern about the state of the campus in the near future. Currently almost 100 Berkeley faculty members are being aggressively recruited by outside universities. Chancellor Birgeneau stated that the campus must be able to convince its faculty that it will be a great institution in five years' time; otherwise it will begin a downward spiral. At the same time, it must maintain the diversity of its student body and its commitment to access.

Chancellor Birgeneau asked that the Regents support enlightened policies on enrollment, fees, financial aid, and compensation and benefits for faculty and staff. He stated that individual campuses would need to have as much flexibility as possible, because each campus finds itself in a different competitive situation. Given sufficient flexibility, the campuses would be able to resolve their budgetary challenges and remain a great University, but the immediate challenge is extraordinary. Chancellor Birgeneau concluded by recalling the example of Bell Laboratories and warning of the effects of bad management decisions and bad public policy.

Committee Chair Lozano expressed the Regents' commitment to maintaining flexibility for the campuses, remaining attentive to key University priorities, and doing the best possible job of management in a difficult time.

Regent Varner emphasized that legislators must understand the economic impact of UC, not only for communities that neighbor the campuses, but for California and the nation.

He suggested that the University might charge for some of the public services it provides. He asked all the chancellors to consider creative ways of seeking new revenue and to present these ideas to the Regents, and stated that he would ask the Office of the President to examine and coordinate this input.

Committee Chair Lozano noted that an effort is under way to identify new revenue streams at the campus level. She asked Executive Vice President Brostrom to present this information to the Regents at a future meeting, as well as information about how the University evaluates these ideas to determine if they are feasible. Mr. Brostrom responded that there would be discussion later in the meeting about possible systemwide and campus revenue streams, and that he could provide more extensive information then. He noted a recent collaboration between UC Berkeley and a venture capital fund, Osage Partners, to commercialize technology developed on the campus. In response to Regent Varner's remarks, Mr. Brostrom stated that the Office of the President is updating a report on UC systemwide economic impact. He concurred that elected representatives in Sacramento and Washington need to be reminded of this impact.

Regent De La Peña referred to the earlier update on the 2011-12 State budget and requested clarification on the reallocation related to Cal Grant funding. Vice President Lenz explained that this was a shift in funding revenue. There would be no less funding for the Cal Grant program. A transfer of federal funds to support the Cal Grant program would free up State General Fund monies.

Regent De La Peña asked the chancellors for an estimate of how many students the University can educate with its existing resources while maintaining an outstanding quality of education. Chancellor Blumenthal responded that this was a difficult question because all the undergraduate campuses are determined to maintain their efforts to enroll large numbers of California students. In part this is because, in the face of significant budget cuts, the campuses need the cash flow that comes from student fee revenue. He stated that Regent De La Peña's question should be considered in the context of the upcoming three to five years. The campuses must consider their future direction if the current reduced budgets become the new norm. Some reduction of size to the University might be necessary to maintain stability and excellence.

In response to a remark by Regent De La Peña, Chancellor Blumenthal confirmed that the University does not receive State funding for approximately 11,000 students in the UC system, although it does collect tuition from them.

Chancellor Drake observed that the University cannot take any immediate action that will remedy an enormous reduction of $500 million in one year. The University will have to build itself back gradually from this sudden reduction and make an effort to minimize the effect. The Irvine campus has reduced student enrollment relative to its planned trajectory, but Chancellor Drake noted that enrollment reductions do not produce savings; savings would be achieved by reducing services to the same extent. Reducing a budget to a lower level is a long process that takes time, while the injury the University experiences from sudden budget cuts is immediate. He concurred with Chancellor Birgeneau that the cuts in State support being proposed were unconscionable. This would be a difficult situation for the University to manage.

Regent Pattiz emphasized the need to identify new and creative ways to raise revenue for the University and to avoid cuts. In order to maintain excellence in the face of significant budget reductions, the University must identify its strong attributes and decide what it needs to defend. It must determine the nature of the curriculum it can offer its students. He stated that the University does not have the resources to meet the expectations of all people.

Regent Island expressed concern about a possible loss of diversity, access, and affordability, which contribute to the University's quality. He urged the University to focus on core elements of quality to be protected and cautioned that decisions made at this time to reduce enrollment or to increase tuition might not seem wise or responsible in the future. While UC might be compelled to remake itself at this time, he hoped that it would not close its doors to children from working-class families and would remain mindful of the new demographics of California.

Chancellor Birgeneau stated that the University gives a great deal of consideration to alternative revenue sources. He emphasized the need for legislators to oppose cuts to UC. While private philanthropic support for the University has increased dramatically, he expressed disappointment in the level of corporate philanthropic support and suggested that more corporate support for California public universities would be necessary. Chancellor Birgeneau observed that the U.S. is one of the few nations in which the national government does not contribute directly to the operations of its great public teaching and research universities. He noted that he is developing a model of combined private, State, and federal partnership to help ensure that outstanding research universities maintain their excellence and public character; it would require action at the State and federal level. He offered to present this in more detail at a future meeting.

Regent Johnson expressed concern about the admission of nonresident students and the disadvantage this might create for resident applicants. She expressed optimism in the University's ability to weather the current challenges.

Regent Schilling expressed the view that the Regents' greatest responsibility is to maintain the quality of the institution and expressed concern that a decline in quality might occur before the University became aware of it. She asked if the campuses had statistics or tangible measures to demonstrate the threats to UC quality. She noted that there are measures such as the student-faculty ratio, but that these are relatively rough measures. Regent Schilling then observed that there are disadvantages in being a public university. The University's building costs are greater than those of its private counterparts. She stated that the Regents, administration, and senior management must develop ways to respond rapidly to issues.

Regent Crane anticipated that the State budget situation would become more difficult. He recalled that this year, the State would spend twice as much on corrections as on UC and the California State University. In addition to reduced State support, the University would face increased health care costs and unfunded benefits. He suggested that the University should look at itself as an enterprise with a customer who now provides 13 percent of its revenue but who is going away. The University must examine new means of generating revenue while adhering to its essential values.

Regent Makarechian asked for clarification of the chancellors' request for flexibility in addressing campus budget cuts. Chancellor Birgeneau responded that the campuses would like local control over fees, salaries, and financial aid. There have been no staff salary increases for three years. Campuses are part of the UC system and are committed to the system; they do not want complete autonomy, but more flexibility at the local level. Chancellor Blumenthal added that the campuses would like there to be as few constraints as possible on the use of State funds. If the State is reducing the amount it gives the University, it should not impose constraints on how these resources are spent.

Regent Makarechian observed that UC Berkeley produces as many successful entrepreneurs as Harvard and the Massachusetts Institute of Technology. He asked how UC Berkeley compares with these private universities in philanthropy by successful alumni. Chancellor Birgeneau responded that the campus is pleased with the level of philanthropic support. UCB alumni understand the situation the University is in. Last year, for the first time ever, UCB raised more private funds from successful alumni than any other U.S. university without a medical school. There has been significant progress in this area. Corporations, though, have not yet provided this level of direct operating support.

Committee Chair Lozano asked Chancellor Blumenthal if his request for flexibility referred to unrestricted funds. Chancellor Blumenthal responded in the affirmative. Constraints imposed on the campuses regarding how funds are used reduce their opportunity to provide classes for students. These decisions should be made at the campus level.

Faculty Representative Anderson referred to a chart presented earlier during the update on the 2011-12 State budget which displayed declining levels of spending per student. He noted that the total annual spending per student decreased over 20 years from $21,370 to $17,220, just under 20 percent, despite the significant fee increases. Mr. Anderson stated his view that while the State argues that UC has approximately 15,000 unfunded students, in reality, the University has 40,000 unfunded students it is trying desperately to accommodate. Campuses are accepting students for the coming fall because they cannot reduce costs quickly and they need the fee revenue. He expressed concern about students' ability to get classes they need to graduate and about a declining quality in the students' experience. An understanding of "access" as simply admitting a certain number of students is incomplete; the University must be concerned about and mindful of the quality of the student experience as it plans for the next three to five years.

Regent Ruiz pointed out that the University has accommodated student growth and enrollment in spite of reduced contributions from the State. It educates students for whom it receives no State support. He expressed his view that, under the best possible scenario, the University would experience a $500 million cut; a reduction of $1.4 billion might become a reality. He requested information on what the effect of a $1.4 billion reduction to UC would be, for presentation to legislators, the business community, and other groups. The Regents would need this information soon in order to advocate for the University. Regent Ruiz reflected that, in his view, providing access for California students is part of the University's quality and excellence. He suggested that the University should develop a more precise definition of the "excellence" for which it strives.

Chancellor Drake recalled that the University faced reductions of this magnitude two years previously. The University managed to maintain itself for a year with cost-saving measures. He cautioned that if the University repeated this strategy, it would begin to lose opportunities to retain its best faculty. He reported that UC Irvine lost five faculty in the past year who are National Academies members and he warned of gradual attrition. Faculty can see when an institution moves down from an "A plus" to an "A" level and then may choose other options. State legislators, however, may find that an "A" or even an "A minus" level is acceptable for the University. Chancellor Drake stated his view that the role of the Regents is to ensure that the University protects a high level of quality, a higher level than legislators might find satisfactory.

Regent Zettel praised efforts made to reduce expenditures at the Office of the President. She emphasized that the Regents must be spokespeople for the University and must have facts at hand to present to business and other groups, to members of the public, and for inclusion in letters to the editor to clarify UC operations for the public. She concurred that the Regents should support campuses' flexibility. She requested more information about how the campuses were addressing changes in academic programs; some under-enrolled programs which elicit less student interest might be replaced by new, multidisciplinary programs.

Regent Torlakson stated that voters and legislators understand the need for a strong educational system. He recalled that, as State Superintendent of Public Instruction, he has declared a state of financial emergency for California K-12 schools and has tried to increase public awareness of true conditions in public schools. The State collects $5 billion to $8 billion less in taxes now than it collected ten years previously. Regent Torlakson expressed his belief that California voters are willing to invest in education. He discussed the need for a ballot measure such as a tax extension to provide the approximately $8 billion needed to stabilize the educational system. He asked Regents to communicate with members of the Legislature about this issue. He suggested that the Regents could consider declaring a state of financial emergency for the University and endorsing a tax extension ballot measure. He emphasized the importance of advocacy with alumni and other groups.

Chairman Gould stressed that the University must have a realistic view of the environment it faces. He enumerated financial challenges for the State, such as health care, debt, and pension costs. He stated his belief that the Governor and legislators all understand the importance of the University for the California economy; however, the University is not the highest budget priority. The University must become more self-reliant in its operations in the future. This might require greater flexibility at the campus level.

4. **BALANCE SHEET INITIATIVES**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Executive Vice President Brostrom explained that this item concerned an effort to use the University's balance sheet to identify new revenue streams.

Chief Financial Officer Taylor noted that the balance sheet initiatives seek to use the total assets and size of the University to reduce existing costs, create new value, and to encourage administrative efficiencies by breaking down barriers to investment.

Four balance sheet initiatives are currently being carried out. The first is a target Short Term Investment Pool (STIP) / Total Return Investment Pool (TRIP) allocation. Mr. Taylor recalled that the STIP is like a checking account, used to operate the University. The TRIP holds operating monies not needed immediately, but which will be needed in future years; these funds are invested in a less conservative asset allocation than are the STIP funds. The goal of this first initiative is to transfer approximately $1 billion from the STIP into the TRIP. Because the TRIP has an asset allocation which can earn considerably more than the STIP, Mr. Taylor estimated that if this action had been taken the previous year, it would have provided $100 million in unrestricted monies; he estimated that UC would gain about $50 million to $60 million annually on average in extra investment earnings through this initiative. These unrestricted revenues would be directed to the campuses. Most of the transfers for this initiative have been completed.

The second initiative is a UC Retirement System transfer, an action item to be considered the following day by the Committee, *Authorization to Make Additional Contributions toward the University of California Retirement Plan's Annual Required Contribution (ARC) from One or Multiple Sources*. Mr. Taylor anticipated that this action would allow the University to save $5 billion over 30 years. While this action would not provide significant savings in the next few years, he characterized it as a long-term move the University should make to save money over time. It would reduce the amount of future employer contributions to the UC pension system by making contributions at this time. This action concerns legal obligations of the University, expenses it has no choice but to pay.

The third initiative concerns capital markets strategies. One strategy is to restructure UC debt for cash flow relief. Mr. Taylor compared bonds issued by the University to 15-year mortgages; this effort seeks to restructure debt so that it is more like a 30-year or long-term mortgage. This would reduce stress on the University's cash flow at a relatively low cost. Another strategy being pursued is to purchase UC debt on the open market. He reported that the University was recently able to purchase its own bonds at a significant discount to outstanding face value following some panic selling on the market; it is now reissuing them. This allows the University to lower the amount of bonds outstanding and will provide savings over time. The University has engaged broker-dealers to seek out other purchasing opportunities.

The fourth initiative is the University's strategic investment or internal loan fund. The work of the UC Commission on the Future found that some initial investment was required to realize a number of proposals for administrative savings. Using a funding pool at the Office of the President, the University has made a commitment of $50 million to the campuses in no-interest loans, payable over seven years, with no pre-payment penalty. Mr. Taylor observed that this funding overcomes the initial inertia which might prevent ideas from being realized.

In addition to the four initiatives in progress, the University is studying other initiatives for possible implementation. Mr. Brostrom explained that one such initiative in the near term would be a special endowment payout. In recent years a number of private universities have taken extraordinary payouts over a one- or two-year period as bridges during fiscal crises. A complicating factor for UC is the fact that most of its endowments are restricted; this potential action would not address the University's central funding strains. The University is seeking ways to secure more unrestricted philanthropy.

The University is considering an expenditure tax on all payouts, restricted and unrestricted. Some campuses are considering levying an assessment on STIP assets in the near term as a temporary strategy. In general, the University is examining a variety of balance sheet strategies to augment other UC fund sources.

Another initiative under consideration is an alternative risk financing program. Mr. Taylor recalled that the University has four self-insurance programs: workers' compensation, medical malpractice, personal liability, and general liability. At the moment these are stand-alone programs. The reserves for three of these programs are overfunded, while the reserves for one program are underfunded. Mr. Taylor anticipated that a proposal would be brought to the Regents at a future meeting for a captive insurer, allowing the University's insurance programs to be cross-collateralized. This would permit a lower level of reserves in stand-alone insurance programs; funds freed up could be directed to the campuses. Finally, Mr. Taylor noted that the University is actively studying the possibility of self-insurance for health benefits.

Committee Chair Lozano praised Mr. Taylor for his work in effectively leveraging the University's balance sheet. Mr. Taylor responded that, as part of its investigations, the University has examined its daily cash flow since the year 2000. He stated that, even under dire economic circumstances, the University would have sufficient cash on hand for its operating costs.

Regent Island referred to the reallocation of funds from the STIP into the TRIP. He asked about possible risk in this action. Mr. Taylor responded that the STIP is invested only in fixed income, highly liquid assets with low earnings in the current market. The TRIP is invested 70 percent in fixed income and 30 percent in equity. In recent years, the potential equity upside has produced greater earnings in the TRIP than would have been possible in the STIP. He acknowledged that equity securities have a measure of volatility, but underscored that the TRIP funds are not immediately needed. In consultation with the Office of the Treasurer, the Office of the Chief Financial Officer believes that the degree of volatility and diversification in this asset pool is safe for campus funds in the long term. Mr. Taylor noted that his office has met with representatives of each campus and has developed individualized cash flows for each campus to demonstrate what campuses could safely afford to invest in the TRIP. He stated that a desirable systemwide goal would be an 80 percent STIP / 20 percent TRIP allocation; a maximum limit has been set at 60 percent STIP / 40 percent TRIP for campuses which would like more market exposure. A fund functioning like an overdraft protection account has also been established at the Office of the President, so that in case of a downturn in the equity market, there is a pool of cash on which to draw.

Committee Chair Lozano asked if any of the proposed actions were outside the University's risk framework. Mr. Taylor responded in the negative. The asset allocations for the STIP and TRIP have already been approved by the Committee on Investments and these funds are managed by the Office of the Treasurer.

In response to a question by Regent De La Peña, Mr. Taylor noted that the allocation of funds to the STIP and TRIP has been a campus decision. This initiative aims to convince medium-sized and smaller campuses that they are underinvested in the TRIP and should move in this direction. It was his understanding that per policy, campuses determine the amounts to be invested in the two funds.

Regent De La Peña requested specific information on policy authorization for a transfer of funds from the STIP to TRIP. Mr. Taylor responded that he would provide this information. President Yudof observed that investing in equities is riskier than investing in bonds; but as a longstanding institution, the University could expect a higher return over ten, 20, or 50 years with a mix of fixed assets and equities than with fixed assets only. He commented on the proposed 80 percent STIP / 20 percent TRIP allocation, and the fact that the TRIP is invested 70 percent in fixed income. He stated his view that this is weighted conservatively toward fixed income.

Regent Blum praised the work of Mr. Taylor and Mr. Brostrom and stated his view that UC investments have been too conservative in the past.

Regent Hime asked about UC property assets that might be better utilized or sold. He stated that the University should request that the conditions for existing restricted endowments be changed to make these endowments unrestricted. Mr. Brostrom responded that the University is examining its property assets systemwide. As one example, the Office of the President has bought a building that it previously leased, resulting in savings due to low property values and low negotiated rates. The Irvine campus has also bought previously leased assets. In response to Regent Hime's second concern, Mr. Brostrom noted that the University is actively examining endowments to determine which are truly restricted and which might be managed differently.

Regent Ruiz expressed support for campus flexibility but called attention to the financial risks involved. He stressed that the University's efforts to be more efficient would require changes and noted that there might be resistance to change within the University. He asked that the Regents be informed about such resistance to change. Mr. Taylor responded that a recommendation on a common payroll and human resources system would be brought to the President in May or June. This item might come before the Regents by July and would provide an opportunity to examine how common systems with the potential for significant savings can function only with cooperation from all parties, and with a kind of centralized control which has not been traditional for the University.

Regent Makarechian noted that some campuses have greater resources than others. He asked if all the campuses' resources would be pooled and reallocated. Mr. Taylor responded that the University manages cash as if it were a pool, but exercises caution not to transfer cash from one campus to another. Mr. Brostrom responded that each campus collects its own earnings on the STIP and TRIP funds it invests. This provides flexibility for the chancellors and helps relieve the decline in central funding. These are discretionary, unrestricted monies a campus can use for general education, regardless of the source of the funds. The University does not distribute funds between campuses.

In response to a question by Regent Makarechian, Mr. Taylor confirmed that savings would be returned to the campuses in a proportionate manner.

Regent Pattiz asked how much the University might save with self-insurance for health benefits. Mr. Taylor responded that savings could potentially be in the tens of millions of dollars. He noted that this program would not be simple to implement. Detailed analysis remains to be done to demonstrate potential savings. Mr. Brostrom added that the University spends approximately $1.6 billion on employee health and welfare benefits and that it is seeking to reduce the rate of growth in its health and welfare benefits. He recalled that this year the University launched its first pooled self-insurance program for graduate students; this will be expanded to undergraduates and could lead the way for expansion to include UC employees.

Chairman Gould referred to the transfer of funds from the STIP to TRIP and asked if this action has been tested in the market or with rating agencies. Mr. Taylor responded that the University has had extensive discussions with rating agencies about this action. The University will still have a significant amount of highly liquid, fixed income instruments in the STIP and TRIP. UC's liquidity balances, a strong credit point, are not in jeopardy.

5. **UPDATE ON THE CHANGING RELATIONSHIP BETWEEN THE CAMPUSES AND THE OFFICE OF THE PRESIDENT**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Executive Vice President Brostrom briefly outlined this item, which he indicated would be discussed in greater detail at a future meeting. In order to provide high-quality services to campuses and to allow them as much flexibility as possible in fulfilling their mission of teaching, research, and public service, the University is introducing a new funding model for the Office of the President (UCOP) in the coming fiscal year. In accordance with this model, UCOP will return all core funds for operations, including $225 million in State funds, to the campuses. Campuses will retain all the revenue they generate, such as nonresident tuition, patent revenue, and indirect cost recovery funds. UCOP will be funded by a low broad-based tax on all revenues in the system. However, in the assessment of this tax on the campuses, chancellors will have complete discretion and flexibility on how the tax is met. Mr. Brostrom suggested that one way chancellors could accomplish this would be through a tax on short-term assets, in order to protect operating income.

UCOP will continue to provide – and hopes to enhance – high-quality central services, activities that achieve economies of scale, both on the administrative and academic fronts, or that provide some common benefit for the system. This will be implemented in a direct and transparent budget process, so that all stakeholders, and particularly the campuses and the Regents, can review and comment on UCOP services and their level of funding.

Mr. Brostrom expressed his belief that this measure could reduce the UCOP budget by $50 million in the coming year; this would be in addition to earlier cuts of $55 million since 2007-08. The University is also seeking to reduce other systemwide initiatives by $30 million. These actions would reduce the impact of the State cut on campuses from $500 million to approximately $420 million. Mr. Brostrom presented some caveats regarding this approach. First, many of the “cuts” were not really cuts; funding and activities which were previously mandated centrally at UCOP would now devolve to the campuses. The decisions about funding for these activities would be made by chancellors at the campus level. A second caveat was that some of the proposed actions were politically sensitive, concerning activities which have been directed from Sacramento for years or decades. The University’s position is that, at a reduced level of State funding, the State should release UC from the constraints of explicit or implicit earmarks and allow campuses to spend funds in a way that most appropriately furthers their teaching and research missions.

President Yudof observed that some functions, such as payroll and financial systems, would become more centralized. He emphasized that no activities should be centralized unless they provide cost savings or serve a common good, and stated that the University needs a coherent approach in determining which activities should be centralized and which based on campuses. The University has carried on certain activities for historical reasons, but faced with a possible $500 million reduction, it must consider what actions would best assist the campuses in maintaining their programs. In many cases it would be sensible to move activities to campuses, with funding at the chancellors' discretion. Many functions could be better performed at the local level.

Regent-designate Mireles expressed support for assigning more flexibility and control over programs to the campuses. He reported a concern communicated by students at UC Santa Cruz that a two percent tax would be levied on campus-based student fees. Mr. Brostrom responded that for existing campus-based student fees this tax cannot be levied. In the future, a campus could choose to levy this tax. Student-funded initiatives receive the same support as other campus activities. This decision will be left to the discretion of chancellors.

Regent-designate Mireles concluded that students should communicate their concerns to their chancellor and campus leadership if they do not wish a two percent tax to be levied. Mr. Brostrom responded that he believes the tax will be less than two percent.

Regent Island praised President Yudof for his willingness to relinquish central control from UCOP. He asked if there might be any adverse effects at the campus level from this undertaking. President Yudof expressed his view that great universities are not built from central system offices. Mr. Brostrom responded that the new funding model is designed to be revenue-neutral in the first year, so that no campus is disadvantaged by the implementation of this new funding stream. The future differential among campuses would depend entirely on their different growth rates. He anticipated that UCOP would not grow at the same rate as the overall enterprise; funding for UCOP and the resulting tax rates would be reexamined periodically.

Regent Island requested assurance that this change in administration of substantial funds would not cause harm to a younger campus like UC Merced or a smaller campus like UC Santa Cruz. Mr. Brostrom responded that, in his view, the smaller campuses would receive more benefit than larger campuses from this action.

The Committee recessed at 12:00 p.m.

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The Committee reconvened at 1:30 p.m. with Committee Chair Lozano presiding.

Members present: Regents Blum, DeFreece, Island, Lozano, Makarechian, Schilling, and Varner; Ex officio members Gould and Yudof; Advisory members Mireles and Simmons; Staff Advisors Herbert and Martinez

In attendance: Regents Crane, De La Peña, Hime, Johnson, Lansing, Pattiz, Reiss, Ruiz, Torlakson, and Zettel, Regent-designate Hallett, Faculty Representative Anderson, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Chief Compliance and Audit Officer Vacca, Provost Pitts, Executive Vice

Presidents Brostrom and Taylor, Senior Vice Presidents Dooley and Stobo, Vice Presidents Beckwith, Darling, Duckett, Lenz, and Sakaki, Chancellors Birgeneau, Block, Blumenthal, Desmond-Hellmann, Drake, Fox, Kang, Katehi, White, and Yang, and Recording Secretary McCarthy

6. **BUDGET OPTIONS FOR 2011 TO 2015**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Committee Chair Lozano recounted some themes of the Regents' comments during discussion of the prior items, including finding new sources of revenue, evaluating potential budgetary effects on enrollment, reaffirming UC's commitment to diversity and access, utilizing quality metrics, and increasing campuses' flexibility. She pointed out the difficulty of making budget projections, because of the interplay of complex factors. Committee Chair Lozano stated that this item's presentation would be for discussion and to obtain Regents' input; budget proposals would be presented to the Committee in May.

Executive Vice President Brostrom stated that his presentation would be rooted in UC's core values of quality, access, and affordability. While competing with the world's top universities for faculty, graduate students, and undergraduate students, the University remains accessible to all Californians, as evidenced by the fact that nearly 40 percent of UC undergraduates are Pell Grant recipients. This unique combination of excellence and accessibility distinguishes UC from both its private and public counterparts, and should guide budget discussions.

Mr. Brostrom warned that UC faces not only an immediate fiscal crisis, but also long-term threats to its financial sustainability. Core expenses will continue to increase at an accelerating pace as UC fully pays the normal cost and unfunded liabilities of its post-employment benefits. Failure to develop steady revenue streams to meet these core expenses could threaten UC's values. Mr. Brostrom displayed a slide showing the wide year-to-year variability and overall decline in State funding of UC. The absolute level of State funding in the current year is equivalent to that of 1998-99.

This volatility in funding has been passed on to students and their families through UC's tuition policies, with periods of large increases, and other periods of no increase or even decreases. In eight of the past 20 years, tuition either did not increase or actually decreased. At the other extreme, eight of the past 20 years had tuition increases of ten percent or more; four years had tuition increases of five to eight percent. Had the rate of increase been steady, it would have been approximately eight percent per year. Mr. Brostrom reiterated that finding stable revenue sources is crucial to building a sustainable funding model, and providing stability to UC's students, faculty, and staff.

Vice President Lenz explained UC's core budget expenditures. He reiterated that the State has been an unreliable partner in recent years. In the past three years, the State significantly cut UC's budget, then reinstated half the reduced amount the following year;

UC faces another severe budget reduction in 2011-12. Part of the prior reduction was mitigated by one-time American Recovery and Reinvestment Act (ARRA) funds. Student tuition revenue has helped replace the loss of State General Funds. Revenue from UC general funds, comprised of nonresident tuition and federal indirect cost recovery, has been steady over the past three years. Overall, Mr. Lenz summarized that UC's core funds for 2011-12 have increased by approximately 3.4 percent over their 2007-08 level. State funding of the University has decreased $733 million, or 22.5 percent, over the past three years.

Turning to UC's core fund cost increases, Mr. Lenz reported that enrollment costs include faculty hiring, expansion of related services, and maintenance of new facilities. UC has been able to support merit increases for faculty, but unrepresented staff have had no general salary increase in the past three years. Additionally, employer contributions to the UC Retirement Plan (UCRP) will be four percent in the current fiscal year and will rise to seven percent in the 2011-12 fiscal year. Other costs include utilities, library collections, and instructional equipment.

Mr. Lenz pointed out that growth in costs has exceeded growth in revenue, resulting in a $900 million budget gap in 2011-12. Temporary savings have been achieved through employee furloughs and debt restructuring. Costs have been temporarily avoided by deferred faculty hiring, although this has resulted in expanded class sizes since enrollment has increased. Cost savings have been accomplished over the past three years in non-instructional areas such as alternate health benefit offerings, administrative efficiencies, and layoffs.

Mr. Lenz displayed a slide demonstrating budget pressures from enrollment. In 2005-06, State funding was close to sufficient to support actual enrollment; however, since that time demand for access to the University has grown significantly, while State resources have failed to keep pace. In 2009-10, following a significant reduction in State funding, the Regents approved a four-year enrollment reduction plan with the goal of enrolling at the State-funded level. At that time, UC had 11,000 students for whom it received no State funding; that number subsequently increased to 16,500. In the current year, the State provided enough funding to reduce the number of over-enrolled students to 11,000. Given the proposed $500 million budget cut, UC would be serving 23,000 students for whom the State provides no funding.

UC could increase student enrollment by one percent annually, given the demand for access to the University; however, the University currently lacks adequate State funding or other revenue streams to support such increased enrollment. Given adequate resources, campuses could hire new faculty, expand student services, and purchase additional instructional materials. Lacking State support for increased enrollment, the University has been forced to hire part-time rather than tenure-track faculty, resulting in higher student-faculty ratios; limit course offerings, which could extend time-to-degree for students; increase class sizes; defer equipment purchases; constrain student services; and reduce maintenance of new space.

Regarding post-employment benefits, Mr. Lenz reiterated that UC's employer contributions to the UCRP will increase to seven percent, or approximately $200 million, in 2011-12, and this cost will continue to increase to ten percent in 2012-13, and will likely increase an additional two percent annually through 2015-16. Retiree health benefit costs will also increase.

Turning to compensation budget pressures, Mr. Lenz noted that there have been no general salary increases for faculty and non-represented staff for the past three years. In fact, employees face reductions in net pay because of increases in benefit costs, such as employee contributions to UCRP. Salary lags complicate recruitment and retention of staff and faculty. Mr. Lenz stated that a stable program of merit salary increases for both faculty and non-represented staff is essential.

Mr. Lenz discussed budget pressures related to capital renewal. UC has had no systemwide program of capital renewal since 2001-02, and the State eliminated any permanent funding for deferred maintenance in 2002-03. Mr. Lenz reported that capital renewal needs are expected to increase significantly over the coming decade. The University is attempting to find creative ways to address these needs, such as strategic sourcing and partnership in energy programs that provide some assistance, but these amounts fall far short of actual campus needs.

Mr. Brostrom began a discussion of longer-term budget issues by displaying a slide showing projected revenues and costs, including all mandatory costs and allowing for one percent enrollment growth as forecast in the 2008 Long Range Enrollment Plan. Without new revenue, the University faces a $2.4 billion budget gap by fiscal year 2015-16. This projected gap would consist of the nearly $900 million budget gap from 2011-12, plus costs associated with a one percent growth in enrollment, faculty merit increases, a stable three percent salary program for faculty and non-represented staff, post-employment benefit costs, other benefits, $50 million for capital renewal, and other non-salary costs such as utilities and inflation on non-labor goods. Revenue would increase slightly from higher enrollment tuition, but, nonetheless, UC would be left with a $2.4 billion budget gap by 2015-16.

The University has undertaken efficiency measures to mitigate current budget shortfalls. Mr. Brostrom pointed out that some operational improvements would both save money and improve the quality of a UC education, such as development of information technology systems that would reduce personnel effort, strategic sourcing, use of shared library collections, energy savings programs, curriculum redesign, and alternative methods of instructional delivery. On the other hand, some austerity measures would save money, but would ultimately degrade the quality of the University, such as higher student-faculty ratios, reduced graduate student enrollment, or continuation of faculty and staff salary lags. Mr. Brostrom stated that systemwide administrative efficiencies could yield $100 million in annual savings, with two-thirds of those savings accruing to UC's core fund sources. Other current cost-saving initiatives include reductions in earmarked programs, reductions at the Office of the President, and attempts to limit cost increases for employee health benefits over the upcoming five years. Collectively, these efficiency measures could save $600 million annually, or one-quarter of the projected budget gap through 2015-16.

Mr. Brostrom then discussed potential sources of new revenue, such as increasing UC's indirect cost rate, and decreasing the number of waivers to the indirect cost rate given to government and foundations. Another source of alternative revenue is increasing unrestricted philanthropy, both through increased unrestricted donations as well as utilizing models to increase the fungibility of currently restricted philanthropy. Increasing nonresident enrollment ten percent per year, resulting in an eight percent systemwide level of nonresident students by 2015-16, would result in additional revenues, as would increasing offerings and tuition levels for professional degree programs. Mr. Brostrom pointed out that, while such initiatives are extremely important and would add revenue of over $400 million annually, the University would still face a budget gap of $1.5 billion.

Mr. Brostrom drew attention to the fact that these initiatives to find new sources of revenue would be attempts only to restore lost State funding. Important quality initiatives such as improvement of UC's student-faculty ratio, reducing faculty and staff salary lags, improving support for graduate students, and obtaining additional funding for capital renewal would remain unaddressed.

UC's remaining $1.5 billion budget gap could be bridged immediately if the State paid its portion of the pension contribution, roughly $350 million annually. Despite its efforts to arrive at an agreement, the University has received no commitment from the State.

Mr. Brostrom displayed a bar graph demonstrating the levels of increased contributions from either the State or from student tuition needed to bridge the $1.5 billion budget gap. Increased State funding of 12.4 percent annually or, alternately, 18.3 percent annual tuition increases from the current time through 2015-16 would provide $1.5 billion in additional revenue. Mr. Brostrom detailed various combinations of State and student tuition that could provide $1.5 billion. For example, if the State increased its UC funding five percent annually, student fees would need to be increased 12.6 percent per year to meet the projected $1.5 billion 2015-16 budget gap.

Mr. Brostrom continued to discuss possible combined State funding and tuition scenarios that could supply the necessary $1.5 billion. If the State augments its UC funding by eight percent per year, then UC would need to increase tuition by eight percent annually. If the State makes no additional funding to UC, and UC limits tuition increases to 12 percent annually, UC would be left with a $600 million budget gap in 2015-16. If UC holds tuition flat and the State increases its UC funding by four percent, the University would suffer a $1.1 billion budget gap. An option that Mr. Brostrom considered feasible included increased State contributions of four percent annually, combined with ten percent annual tuition increases; however, it would still leave a $350 million budget gap in 2015-16.

Mr. Brostrom described alternative revenue sources to State funds and tuition. He first discussed alternatives that would provide revenue, but would diminish the quality of the

University. Increasing the student-faculty ratio by 9.1 percent, from 21 to one, to 22.9 to one, through a faculty reduction of 870 positions systemwide, would generate $100 million of savings from reduced salaries and benefits. He noted that, prior to 2007-08, the budgeted ratio was 18.7 to one.

Increasing the proportion of non-tenure track faculty to 43.5 percent from the current 33 percent, by replacing 1,100 tenure track positions with non-tenure track faculty, would save $100 million in salaries and benefits, while the size of the faculty would remain the same. Alternatively, a systemwide reduction of 1,280 staff positions would generate $100 million savings in salaries and benefits; however, Mr. Brostrom pointed out that such a staff reduction would be in addition to prior layoffs, existing unfilled open positions, and anticipated staff reductions associated with the $500 million administrative efficiencies initiative. He cautioned that consequences of these alternatives would include reduced research funding, fewer graduate students, reduced student interaction with scholars, larger class sizes, and inadequate services and oversight.

Other funding alternatives would affect access to the University by reducing enrollment opportunities for California residents. Every enrollment reduction of 10,000 students would yield $100 million in savings net of tuition loss, but these savings would not be realized for four or five years. Alternatively, every increase in enrollment of 7,700 nonresident students would yield $100 million in additional revenue; currently UC has approximately 8,600 nonresident students. Mr. Brostrom noted that current base assumptions project a one percent annual growth in nonresident students, or an additional 10,000 nonresident students over the upcoming five years, yielding $100 million in additional revenue. Adopting these enrollment alternatives would result in reduced access to the University for Californians and abrogation of the California Master Plan for Higher Education. Mr. Brostrom emphasized that these options must be viewed in the context of national and statewide studies documenting the need for a college-educated workforce in the coming years.

Mr. Brostrom next turned to funding alternatives that would affect the affordability of the University. A six percent increase in tuition and fees would generate $100 million in additional annual revenue, net of financial aid. This alternative would require higher contributions from UC's middle-class families who already feel the strain of prior tuition increases.

Another option is to reduce the University's financial aid base. UC's current commitment to financial aid is unprecedented, with 33 percent of tuition and fees allocated for return-to-aid. Reducing the financial aid base by 11 percent would generate $100 million in discretionary revenue for the campuses. Alternatively, reducing the proportion of return-to-aid from future tuition increases to 23 percent, assuming ten percent annual tuition increases, would yield $100 million over a four-year period. Mr. Brostrom cautioned that this alternative would require higher tuition contributions from needy students and their families.

Committee Chair Lozano thanked Mr. Brostrom and Mr. Lenz for describing alternatives and their trade-offs so clearly. She noted that the Committee would not solve the budget problem at the current meeting, but would seek a sense of direction for future proposals.

Regent Reiss questioned some of the assumptions used to arrive at the $1.5 billion budget gap, such as the University's ability to raise $1 billion in unencumbered funds each year. Mr. Brostrom responded that UC raised $1.3 billion in the past year, but that most of those funds were restricted. Accomplishing future fundraising goals depends on following models for converting restricted endowments into funds available for general use. He cited the example of the Hewlett Foundation Endowed Chair Challenge at UC Berkeley, the goal of which is endowment of 100 chairs funded by $2 million each, or $100,000 annually, of which $25,000 goes to the chair holder, $50,000 supports the chair holder's salary, and $25,000 goes to support of graduate students in the chair holder's department. Thus, 75 percent of the payout from what is technically a restricted endowment can actually be used to support central demand.

Regent Reiss cautioned that the assumptions underlying the budget deliberations should be made conservatively, so that future budget gaps would not be larger than anticipated. She requested suggestions from the chancellors for the creation of new revenue streams. She supported Chancellor Drake's earlier comment that every option should be on the table and reviewed in an open-minded manner. Regent Reiss enumerated the large UC employer contributions to UCRP in coming years. She expressed her opinion that, if the University is to protect its core values, every option for dealing with the budget crisis must be considered. She expressed concern that some of the largest cost drivers are not being considered for reduction. Regent Reiss stated that she does not want to preside over the institution at a time when a family with two parents who are school teachers cannot afford to send their children to UC. Regent Reiss also stated that UC may become a public university in name only, since the State abrogated its responsibilities under the Master Plan long ago. She reiterated that all options must be considered, not just seeking State funding or increases in student tuition.

Regent Blum asked if the budgetary assumptions include the possibility that the State could contribute less than $2.5 billion each year. He expressed concern about the potential for even further reductions in State support. Mr. Brostrom responded that the projections in his presentation were based on constant State funding of $2.5 billion. Committee Chair Lozano stated that Regents would be presented with an even more dire scenario based on further deterioration in State funding.

Regent Lansing agreed that the University has a major problem. The University can no longer say that the Master Plan even exists because of the State's failure to fund it. She emphasized that UC has a core value system that the Regents must protect: quality, access, and affordability. Regent Lansing urged development of entrepreneurial ideas that are innovative and "out-of-the-box." Mr. Brostrom responded that, while his current report was a conservative presentation of budgetary realities, many new ideas are being developed at the direction of President Yudof. Regent Lansing complimented the realism of the report, but stated that she looked forward to exploring innovative options for new revenue sources.

Regent Crane asked for a definition of enrollment cost. Mr. Brostrom responded that $17,000 was used for the current presentation as the average cost of enrollment, of which UC recovers a certain amount from tuition and a certain amount from the State. Regent Crane stated that he would like to receive a breakdown of the components of the $17,000 enrollment cost. Regent Crane also asked if budgetary projections assume a 7.5 percent return on investments. Mr. Brostrom responded in the affirmative.

Committee Chair Lozano agreed that enrollment costs are not clearly defined and that a clarification would be necessary for the Regents to make budgetary decisions. Mr. Lenz said that he would supply this information.

Regent Varner stated that it is clear that the Master Plan is not being followed and that the University must have an understanding of the State's level of commitment to the Master Plan. He asked if UC is working with the other segments of California higher education to renegotiate the Master Plan.

In response to a question from Regent Makarechian, Mr. Brostrom responded that the State currently does not contribute anything to UCRP. Regent Makarechian questioned the assumption that UCRP will earn 7.5 percent return on its investments. Mr. Brostrom noted that the California Public Employees' Retirement System (CalPERS) currently assumes 7.75 percent return on investments, and that 7.5 percent is a conservative estimate of return relative to assumptions of most retirement plans. Regent Makarechian cautioned that a huge shortfall would result should UCRP not make 7.5 percent returns. He asked if budget projections have been made using a lower investment return. Mr. Brostrom responded that prior analysis showed that the employer contribution could rise to over 20 percent just to pay the unfunded liability.

Regent Makarechian asked about the possibility of reducing the amount of return-to-aid funds. Mr. Brostrom replied that the return-to-aid pool would be close to $900 million in the upcoming year, based on 33 percent of new fee income, including recent tuition increases of 32 percent and eight percent. He noted that the figures in his presentation extended those calculations to 2015-16.

Regent Pattiz expressed his opinion that it is unrealistic to think that the University's core values can be maintained given current budget constraints. He stated his belief that the time has arrived when the quality of the University is pitted against values of affordability and accessibility. UC faces deficits in the billions of dollars, while trying to maintain its quality, access, and affordability, and must reassess its core values to determine what it can realistically accomplish.

Regent Pattiz recommended finding a way to exploit the University's importance to the State and private sector economy in areas such as research. A qualified sales department could be assembled to market these necessary services in order to generate additional revenue.

Regent Ruiz expressed his opinion that UC needs to generate a revenue model through strategic marketing based on needs and demands. He asked what a $500 million budget cut would mean in terms of enrollment. Specifically, he asked how many students would have to be cut from enrollment to make up $500 million. He stated that the Regents need this information in order to be able to put together a compelling argument for support for the University. Mr. Lenz responded that, based on the State's methodology of calculating funding per student, a $500 million reduction represents funding for more than 23,000 students. Regent Ruiz expressed a lack of confidence in the information currently available to the Regents about what effect projected budget cuts would have on enrollment and pointed out that the University currently accommodates 11,000 students for whom it receives no funding. He suggested that there may be a point of critical mass, at which the University would lose more students proportionally as budget cuts affect the University. He stressed that the Regents need very clear information on the effects of funding cuts on enrollment.

Regent Lozano asked Mr. Brostrom about the accuracy of his prior statement that a reduction of 10,000 students would result in $100 million in savings. Mr. Brostrom responded that these figures are accepted as a "rule of thumb," but that variables could come into play. For example, a 10,000 reduction in the number of graduate students would yield much higher savings, but would also have a greater impact on faculty and on the quality of the University.

Regent De La Peña thanked Mr. Lenz for his helpful presentation and pointed out the assumptions underlying the budget analysis, such as steady State funding of $2.5 billion annually and a 7.5 percent return on investments. He noted that figures for enrollment cost are calculated based on ratios of 22 students per instructor, rather than the prior 18.7 students per instructor. He stated that it is his understanding that, if a student-faculty ratio of 18.7 were used, the cost of educating a student would rise to $23,000. If UC loses $500 million in State funding, it would be over-enrolled by 23,000 students; however, using the lower student-faculty ratio, UC would be over-enrolled by 40,000 students. Regent De La Peña cautioned that if State funding should be reduced by an even larger $1.4 billion, UC's over-enrollment could be even greater.

Regent De La Peña also discussed return-to-aid. He noted that projections involving possible student tuition increases are based on continuing 33 percent return-to-aid. He pointed out that the University could possibly reduce further tuition increases by lowering the percentage of fees returned to aid, perhaps by ten percent.

Mr. Lenz clarified that the $1.4 billion figure referred to the proposed cut in the Governor's budget for UC, California State University (CSU), and the California Community Colleges (CCC).

Regent DeFreece expressed support for Regent De La Peña's remarks about return-to-aid and noted that return-to-aid funding affects middle class students and their families disproportionately. He pointed out that the repercussions for middle class families would be even greater if more tuition increases are enacted.

Regent DeFreece asked about the role of the Regents in supporting the possible ballot measure regarding tax extensions. He noted that a Field Poll conducted in conjunction with UC Berkeley showed that, while a majority of California voters do not support tax increases, they do support the tax extensions. In addition, the poll showed that the electorate does not support further cuts to higher education. Regent DeFreece asked if the Regents should publicly support the placement of tax extensions on the ballot.

Chairman Gould recalled that the University had supported a prior unsuccessful tax ballot measure that was the result of a bi-partisan effort. He stated his view that the University cannot take a position until a concrete proposal is brought forward. A comprehensive budget proposal should emerge from current legislative negotiations. Chairman Gould stated that the University seeks a concrete commitment to the University from the Governor and the Legislature as a part of any tax measure, and cautioned that there currently is no such clear commitment. He stated that should these efforts be successful and the matter be set for the June ballot, the Regents could have a special meeting to discuss the proposal and possible Regental support. Regent DeFreece confirmed his support for the tax extension.

Regent-designate Mireles stated that it would be helpful to have an online tool that could help students understand the complexity of the budgetary options facing the University. He expressed the opinion that students could be part of the dialogue about the budget if supplied with necessary information. Mr. Brostrom responded that development of such a tool would be very complicated.

Regent-designate Mireles asked what the total fee increase would be in the previously discussed budget scenario in which UC's funding gap would be filled completely by student tuition increases at 18.3 percent per year through 2015-16. Mr. Brostrom responded that such an annual increase over four years would almost double student tuition over its current level. Committee Chair Lozano reminded Regent-designate Mireles that these possible scenarios were extremes for the purposes of discussion.

Regent-designate Hallett agreed with prior comments that new streams of revenue must be developed, although he noted that revenue from such new sources would not be available for a number of years at best, and that the Regents must be realistic about the current budget shortfall. With regard to UC's expenditures, Regent-designate Hallett expressed his opinion that UC must examine redundancies among campuses. He cited the example of multiple campuses having similar departments and pointed out that some duplicative departments could be eliminated. Committee Chair Lozano responded that the issue of size and scope of campuses was examined by the UC Commission on the Future and would be further examined by the Regents. Faculty Representative Anderson noted that campuses have been consolidating departments, although such efforts produce economic results relatively slowly.

Mr. Anderson agreed with Mr. Lenz's prior statement that a reduction in the number of graduate students would generate more savings than a reduction in the same number of undergraduate students, since graduate students, particularly Ph.D. students, require a good deal of faculty time and therefore are expensive. On the other hand, Mr. Anderson pointed out that graduate students pay their way by teaching and play a critical role in the undergraduate instruction program. In particular, should UC increase class size, even more graduate students would become necessary for undergraduate support. In addition, graduate students pay their way by doing research. A significant reduction in the number of graduate students would decrease UC's ability to attract faculty, which would have adverse effects on the budget. Should UC's research mission be diminished, the University would receive less support from the federal government. He pointed out that UC currently receives twice as much funding from federal research grants as it receives from the State.

While Mr. Anderson acknowledged that past reports to the Regents have shown that UC's indirect cost recovery is less than the total research cost to the University, he pointed out that indirect cost recovery is largely for past expenditures. If the amount of research funding coming into the University were reduced, it would have an immediate effect on the generation of indirect cost recovery, which reimburses expenses that have already been undertaken. Mr. Anderson summarized that, while reducing the number of graduate students would appear to save money, it may actually be more damaging to the University's budget than a reduction in the number of undergraduate students would be.

Regent Hime commented that the State has not been a reliable partner in the recent past and that the University cannot depend on the State in the future. He concluded from the information in the presentation that there are basically two options for dealing with the budget gap: either increase student tuition, reduce the number of students, or some combination of both. Additionally, UC must maximize its return on the products of its research. Regent Hime expressed his opinion that the current dilemma can be reduced to fundamental questions of how much cost the student population can absorb, and to what extent the Regents are willing to reduce the size of the student body in order to maintain the quality of the University. He reiterated that the Regents cannot count on the Legislature or the taxpayers to solve this problem for the University. He advocated widespread public discussion so that information can be disseminated about the repercussions of necessary budget decisions.

Regent Blum expressed his opinion that the Regents have not done a good job of informing the people of California of the problem facing the University and of the need to raise funds. He indicated that the only realistic solution is to raise both tuition and scholarship funds, as many of UC's competitor universities have done. Regent Blum stated that the top California companies could be asked to provide unrestricted scholarship funds. UC's top competitors charge three times as much in tuition. While UC, with its 225,000 students, could not realistically match the ability of a university like

Stanford, with its 12,000 students, to provide scholarships, nonetheless Regent Blum believed that UC could raise several billion dollars. He recalled that the University of Michigan raised over $3 billion a few years prior and expressed his opinion that UC could certainly raise more than Michigan.

Regent Blum advocated dividing California companies into smaller groups for solicitation purposes. He reported that he has spoken with the Governor, who expressed support for this plan and would help encourage companies to contribute. Regent Blum stated that UC's current marketing efforts are not good enough and cited the example of UC's television station, which is largely unknown. He pointed out that California companies continuously express the need for a well-educated employee pool.

Regent Blum reiterated that the solution to the budget shortfall is to charge higher tuition, and to devise a way to provide sufficient scholarship funds to maintain accessibility. While he supported securing more funding from UC's research enterprises, Regent Blum stated that those are long-term efforts, but the $1 billion budget gap is immediate and the University must be prepared in case State support declines even further.

Regent Crane expressed agreement with the views of Regents Hime and Blum, although he would not support the option of reducing enrollment. He pointed out that the U.S. median family income has remained flat since the mid-1990s and that all income growth has been to those with college educations. He emphasized that UC must stand for enrollment possibilities for all capable students who want to attend. He would encourage more local control by the campuses, enabling them to be more creative in generating funding.

Regent Island congratulated Mr. Brostrom and his team on their presentation, which provided information necessary to begin budget discussions. Regent Island expressed his opinion that the quality of the University cannot be separated from its values of access, affordability, and providing a substantive educational experience. His greatest concern was that the Regents could fail to understand what reducing enrollment would mean to the University. A reduction in enrollment would destroy the diversity of the University, and UC would look as it did in 1970, when California was largely a Caucasian state. Regent Island emphasized that the issue of enrollment is essential to the University. UC has become the uniquely excellent institution it is precisely because of its diversity and affordability. Regent Island urged the Regents not to lose sight of this during the current budget crisis.

Regent Island also expressed his opinion that it is a mistake to think that State support for UC is gone and will never return. He stated his belief that the State's economy will improve, wiser politicians will be elected, and UC can be restored. The Regents must not take actions that would destroy the very thing they are striving to save.

Regent Island also cautioned against intruding into areas that are properly in the domain of the faculty. The faculty should decide student-teacher ratios, and proportions of tenured versus non-tenured faculty. He noted that the Regents are not professional educators and are ill-equipped to assess the consequences of those actions. Such decisions should be made at the campus level under the direction of the President. Decisions properly in the domain of the Regents are the big questions of enrollment, affordability, and access. Regent Island pointed out that, to the extent that return-to-aid is reduced, UC will enroll fewer poor people and fewer people of color. He expressed concern about students who would not be able to attend UC if tuition were increased and urged the Regents to consider the implications of the actions they might take. He expressed his hope that UC would emerge from this budget crisis an open university, with access for poor and working class people. He noted that California taxpayers have invested billions of dollars over the years to create the University of California and the Board is charged with maintaining its core values during this difficult economic period.

Regent Pattiz expressed his opinion that many proposed options would not decrease the diversity of UC. For example, Regent Blum's suggestion of increasing scholarship funds would directly assist low-income students. While he expressed support for appropriate decisions being made on the campus level, Regent Pattiz cautioned that some decisions were moved to the Regental level in the past as a result of improprieties at the campuses.

Regent Lansing noted that UC is part of a three-tiered system of higher education with CSU and the community colleges. She advocated working together to solve the budget problem, for instance by making sure that credits are transferrable, so that UC can receive more students in their junior or senior years.

President Yudof recalled that he recently spoke at UC Day in Sacramento. He noted that, while State funding may recover in the future, UC has a real crisis at the current time and cannot engage in wishful thinking. He stated that the Regents have all the significant variables in front of them and have control of all aspects of the budget, although he cautioned that exercising some options would result in disaster for the University. For example, reducing the size of the faculty by ten percent would save $100 million, but would jeopardize the quality of the University and its research program. At the savings rate of $100 million per ten percent cut in the student body, the University would have to cut 150,000 students to save $1.5 billion. Even if efficiency measures were doubled, the budget gap would still not be closed.

While he supported Regent Blum's suggestion of increasing scholarship aid through corporate gifts, President Yudof stated that gifts alone would not make up for the reduction in State spending. He invited the Regents to alter any of the assumptions of current budget projections and to assess their consequences. He cautioned that some good ideas expressed at the current meeting should be pursued, but that their budgetary impact would be some years in the future, and the budget gap must be addressed currently. He noted that the current options are extremely challenging and that the probable outcome would be a combination of proposals.

President Yudof expressed agreement with Regent Blum's comments that a higher tuition, higher aid environment may be necessary. He stated that it would be unrealistic to anticipate 18 percent annual tuition increases or a 12 percent increase in State funding; in fact, UC would be fortunate to secure $2.5 billion in State funding. He noted that the Board would have to reach a consensus, and predicted that no Regent would be entirely happy with the outcome.

President Yudof concluded by stating that there are institutions that have more diversity and more poor students than UC, but they are not great universities; there are universities that have more research and higher faculty salaries, but do not educate as many poor students or students of color as UC. He encouraged the Regents to be mindful of the unique characteristics of the University of California during their deliberations.

Chairman Gould recalled that the goal of the current meeting was to present options clearly, and noted that options would be presented to the Regents at a future meeting for both a $2 billion and a $2.5 billion level of State funding. He expressed his opinion that the Regents should be forthright with voters about the implications for the University should tax increases not be extended. He encouraged the Regents to provide feedback to President Yudof. Chairman Gould expressed support for Regent Lansing's suggestion that UC collaborate with CSU and the community colleges to shape the future of higher education. Finally, Chairman Gould expressed every confidence in the leadership of President Yudof and the Board.

The Committee recessed at 3:20 p.m.

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The Committee reconvened on March 17, 2011 at 10:00 a.m. with Committee Chair Lozano presiding.

Members present: Regents Blum, Island, Lozano, Makarechian, Schilling, and Varner; Ex officio members Gould and Yudof; Advisory members Mireles, Pelliccioni, and Simmons; Staff Advisors Herbert and Martinez

In attendance: Regents Crane, De La Peña, Hime, Johnson, Lansing, Pattiz, Reiss, Ruiz, and Zettel, Regent-designate Hallett, Faculty Representative Anderson, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Chief Compliance and Audit Officer Vacca, Provost Pitts, Executive Vice Presidents Brostrom and Taylor, Senior Vice Presidents Dooley and Stobo, Vice Presidents Beckwith, Darling, Duckett, Lenz, and Sakaki, Chancellors Block, Blumenthal, Desmond-Hellmann, Drake, Fox, Kang, Katehi, White, and Yang, and Recording Secretary Johns

7. **PROPOSED CONTINUATION OF LIFE-SAFETY FEE, BERKELEY CAMPUS**

The President recommended that the life-safety portion of the Berkeley Campus Fee continue at its current level for four years, from summer 2011 through spring 2015, with the following specifications:

A. All students enrolled at the Berkeley campus during the regular academic year be assessed a mandatory life-safety portion of the Berkeley Campus Fee of $46.00 per student per term from fall 2011 through spring 2015.

B. Students enrolled in summer 2011, summer 2012, summer 2013, and summer 2014 be assessed a mandatory life-safety portion of the Berkeley Campus Fee at $23.00 per student per enrolled summer term.

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Committee Chair Lozano briefly summarized the item.

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

8. AUTHORIZATION TO MAKE ADDITIONAL CONTRIBUTIONS TOWARD THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN'S ANNUAL REQUIRED CONTRIBUTION (ARC) FROM ONE OR MULTIPLE SOURCES

The President recommended that the Regents amend *University of California Post-Employment Benefits Recommendations* approved by the Board of Regents at the December 13, 2010 meeting as follows:

Additions shown by underscoring; deletions shown by strikethrough

The President be delegated authority and discretion to fully fund the Annual Required Contribution (ARC) for the University of California Retirement Plan (UCRP) in the following two phases. From fiscal year (FY) ~~2011~~ 2010-11 through FY 2018-19, the University would contribute to UCRP, to the extent practical, the "modified" ARC, which would include the normal cost plus interest only on the Unfunded Actuarial Accrued Liability (UAAL). Beyond FY 2018-19, the University would contribute the full ARC payment, which would include the normal cost on the pension, interest on the UAAL, and an amount that represents the annual principal contribution of the 30-year amortization of the UAAL. The President may utilize borrowing from the Short Term Investment Pool (STIP), restructuring of University debt, and other internal or external sources to fund the gap between scheduled pension contributions from the University and employees, and the required funding amount~~, as~~ described above, as follows:

A. Transfer funds from STIP to UCRP in FY2010-11 and FY2011-12 for an amount equal to the difference between the approved total UCRP contribution and modified ARC (Normal Cost plus interest only on the UAAL). The STIP transfer shall satisfy the requirements below, and not exceed a total of $2,100,000,000:

(1) The creation of an internal note receivable ("STIP Note") for the amount above, owned by STIP participants.

(2) The ability to set the repayment terms on the STIP Note, not to exceed a maximum of a 30-year amortization period.

(3) Adoption of a waiver to the STIP investment guideline's maximum of five and a half years on investments to accommodate the terms of this STIP Note.

(4) Assessment of all University fund sources making UCRP payments to include an additional amount for principal and interest payments on the STIP Note, divided proportionally based on covered compensation.

(5) For funding sources, such as federal contracts and grants, where interest payments for the STIP Note are not billable as direct program costs, campuses will be required to pay these charges using unrestricted general revenues. These fund sources may also be excluded from the STIP loan repayment if they pre-pay their portion of the modified ARC assessment in FY2010-11 and FY2011-12.

B. Obtain external financing (not to exceed $1,000,000,000) in lieu of the STIP Note if it is expected this option could be accomplished at a lower cost or is more practical for the University. The repayment of this debt shall be from the same University fund sources responsible for making payments as outlined in A. above.

C. Partially restructure the Regents' long-term debt portfolio starting in fiscal year 2010-11, in an amount not to exceed $1,000,000,000, of such long-term debt plus additional related refinancing costs.

D. The combination of the STIP transfer, debt restructuring and the portion of external financing intended to make contributions to UCRP shall not exceed $2,100,000,000.

E. To take all necessary actions related to the STIP transfer, external financing, and debt restructuring and to execute and deliver related financing documents.

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Chief Financial Officer Taylor recalled that Regent De La Peña had raised a question during the discussion on balance sheet initiatives about the transfer of funds from the Short Term Investment Pool (STIP) into the Total Return Investment Pool (TRIP). Mr. Taylor noted that in May 2008, the Committee on Finance, the Committee on Investments, and the Board authorized campuses to transfer funds from the STIP into TRIP, provided that certain liquidity conditions were met. The Office of the Treasurer provides an annual summary of TRIP asset allocation performance. The Committee on Investments monitors the TRIP and ensures that its risk metrics are appropriate.

Mr. Taylor then discussed the current item. He recalled that the Regents approved changes to the UC Retirement Plan (UCRP) and to UCRP funding strategies at a special meeting in December 2010. At that meeting, a strategy was discussed to transfer funds to the UCRP earlier than scheduled. Discussions of this strategy have continued with the campuses, medical centers, and members of the Academic Senate. The current item would authorize the President to carry out this transfer.

Mr. Taylor pointed out that the total UCRP contributions approved for fiscal year 2010-11 and fiscal year 2011-12 are below the funding policy level. The funding policy level represents the normal cost as well as an amount to amortize the unfunded liability over a 30-year period. The funding gap is substantial: the approved contributions do not cover the normal cost or even the interest on the unfunded liability. The University's current expenditure amounts are designed to restart employee and employer contributions, with a slow ramp-up to avoid a shock to operating budgets of campus departments or to employees. Mr. Taylor anticipated that this would unfortunately cause the unfunded liability of the pension system to grow more quickly, by $1 billion this year and $1 billion in the following year. Until the combined employee and employer contributions reach a level recommended by the University's actuary, the liability will grow rapidly.

The proposed action would provide the President with the means to borrow funds, internally or externally, to make the required contribution toward the normal cost for this and the following year, and to pay interest on the UCRP liability. Mr. Taylor stated that this authority to transfer $2 billion in resources into the UCRP would produce $4.9 billion in positive fiscal impact over the next 30 years.

The cost implications of the growing UCRP unfunded liability are significant. Continuing at its current rate, the unfunded liability would double in ten years. The proposed action would transfer $2.1 billion, equal to the normal cost and interest on the unfunded liability, using a variety of financing options. It would reduce the UCRP employer contribution for a period of 19 years by 1.4 percent annually, for savings of $3.7 billion, and would reduce future growth of the unfunded liability by an additional $1.2 billion. It would improve the funded status of the UCRP and lower the amount of underfunding on the University's balance sheet.

Mr. Taylor outlined three options for the asset transfer. The first was a STIP transfer structure and involved the transfer of funds from STIP to the UCRP. At the same time, an internal UC note receivable would be created between the Regents and STIP holders, with an interest rate and a 30-year amortization schedule. The note interest rate would be equivalent to the STIP interest rate. There would be no impact for the STIP holder. STIP participants would receive interest and principal payment on the notes. Campus and medical center payroll funds would be assessed a fee to pay interest and principal on the note.

The second option was external borrowing, which would involve a variable rate general corporate bond, a general bond obligation of the University. The University would issue bonds in lieu of a certain amount of the STIP transfer. Bond proceeds would be transferred to the UCRP. In the future, UC would either roll the debt or take it out with a STIP transfer. The University would benefit from the short end of the yield curve in the taxable market. The STIP interest rate is approximately 2.4 percent, while the rate for current variable rate taxable market bonds is below one percent. To the extent that UC can continue to roll such an instrument, it would produce greater savings than other funding options. The campus and medical center payroll funds would be assessed a fee to pay the interest and principal on the debt. This action would also preserve STIP liquidity.

The third option was debt restructuring. The University would restructure a portion of its debt and transfer the proceeds to the UCRP. This would allow UC to smooth its debt profile into a more level overall structure. Current fund sources would be assessed for payment. This option would push some debt service into future years.

Mr. Taylor summarized the proposed action as a transfer of assets to the UCRP using one or a combination of the options outlined.

Chairman Gould commended this proposed use of the University's balance sheet for tangible benefits and encouraged the Regents to support it. He noted that UC would continue to work with the State regarding State obligations.

Regent Varner stated his view that these were the best possible options in the current economic climate. He emphasized that it was important for the Regents to act now and to avoid putting off problems for the future. He encouraged Mr. Taylor and the administration to continue to examine every possible option and to communicate with the Board about such options.

In response to questions by Regent Makarechian, Mr. Taylor stated that he has carried on extensive discussions with rating agencies about the proposed transfer of assets from the STIP into the UCRP. The response from the agencies was positive; they viewed the University's plans to address its unfunded liability favorably. Since the economic difficulties of 2008-09, rating agencies have paid particular attention to measures of liquidity. The University demonstrated to the agencies that even after the proposed transfer, there will be more than sufficient liquidity to meet the University's operating obligations, even under dire economic scenarios.

Regent Makarechian observed that this action involved a transfer of assets and a reduction in liability. He asked about assumptions regarding the return on assets, and the fact that returns on the UCRP which are lower than the assumed 7.5 percent create additional liability. Mr. Taylor confirmed that this was correct. If the University were to change the assumed rate of return for the UCRP, the impact would be enormous. Even a change from 7.5 percent to seven percent would have a tremendous impact on the size of the unfunded liability and balance sheet ratios.

In response to another question by Regent Makarechian, Mr. Taylor noted that the rating agencies have not taken a position on the issue of assumed rate of return. They wish the

University to demonstrate that it has implemented a plan and that it has a record of being able to accomplish plans in the past. The UCRP assumed rate of 7.5 percent is average for many defined benefit plans, neither aggressive nor conservative. Mr. Taylor stated that the proposed action is sensible as long as the UCRP return is greater than the 2.5 percent rate of return on the STIP.

In response to questions by Regent De La Peña, Mr. Taylor explained that the asset allocation in the TRIP is 65 percent fixed income and 35 percent equity. In discussions with the campuses, the University presented the future target of at least 80 percent investment in the STIP and 20 percent investment in the TRIP, with a limit of 60 percent in the STIP and 40 percent in the TRIP. All campuses would have some investment in the TRIP, unless there were a concern about low liquidity. He stated that the 60/40 limit might be more conservative than policy, but explained that the University is asking campuses to stay within this range in the interest of systemwide liquidity. This limit could be reassessed in the future.

Faculty Representative Simmons reported that the Academic Senate has formally endorsed this proposal as long as UCRP assets earn more than the 2.5 percent rate of return on the STIP. Mr. Taylor stated that discussions with the Academic Senate on this matter have been productive.

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

9. **REPORT OF NEW LITIGATION**

[Background material was mailed to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

General Counsel Robinson presented his **Report of New Litigation**, shown in Attachment 1. By this reference the report is made part of the official record of the meeting.

The meeting adjourned at 10:15 a.m.

Attest:

Secretary and Chief of Staff

NEW LITIGATION AND ARBITRATION PROCEEDINGS

Report Period: 12/2/10 – 2/2/11
Regents Meeting
March 2011

Plaintiff	Location	Nature of Dispute Alleged by Plaintiff	Forum
		Employment Cases	
McDonald, Audrey	UCLAMC	Wrongful Termination	Los Angeles County Superior Court
Alekent, Angelis D.	UCLA	Violation of the Americans with Disabilities Act	Los Angeles County Superior Court
Fashola, Oluwatope	UCR	Wrongful Termination	Alameda County Superior Court
		Professional Liability Cases	
Anzaldi, Rocco	UCSFMC	Medical Malpractice	San Francisco County Superior Court
Banta, Gregory	UCIMC	Medical Malpractice	Orange County Superior Court
Berber, Darlene	UCIMC	Medical Malpractice	Orange County Superior Court
Branner, Jurline	UCSFMC	Medical Malpractice	San Francisco County Superior Court
Fletcher, Emily	UCSFMC	Medical Malpractice	San Francisco County Superior Court
Griffin, Frances	UCIMC	Medical Malpractice	Orange County Superior Court
Hammer, Michael A.	UCLAMC	Medical Malpractice	Los Angeles County Superior Court
Jackson, Raymond D., Sr.	UCSFMC	Medical Malpractice	San Francisco County Superior Court

Lorenzana, Noe (decedent), Teresa Pinckard, Saul Lorenzaza, Lorena Lorenzana and Daniel Pinckard	UCDMC	Medical Malpractice	Sacramento County Superior Court
Navarro, Briana M.	UCDMC	Medical Malpractice	Sacramento County Superior Court
North, John (decedent), Lance North	UCSFMC	Medical Malpractice, Wrongful Death	San Francisco County Superior Court
Pucci, Jacqueline Chapparo	UCSDMC	Medical Malpractice	San Diego County Superior Court
Reyes, Victoria P. (decedent), Ronald Reyes	UCIMC	Medical Malpractice, Wrongful Death	Orange County Superior Court
Rocco, Scott and Chylea	UCSDMC	Medical Malpractice	San Diego County Superior Court
Sheeline, Christopher W.	UCSFMC	Medical Malpractice	San Francisco County Superior Court
Sleppy, Jennifer	UCDMC	Medical Malpractice	Sacramento County Superior Court
Sutton, Gabriel	UCDMC	Medical Malpractice	Sacramento County Superior Court
Wiley, Clare S.	UCDMC	Medical Malpractice	Sacramento County Superior Court
Witner, Andrew	UCLAMC	Medical Malpractice	Los Angeles County Superior Court

Other Cases

Association for Information Media and Equipment and Ambrose Video Publishing, Inc. (AIME)	UCLA	Copyright Infringement	U.S. District Court, Central District of California

Ashmore, Laura; Pamelyn Ferdin; Carol Glasser; and Nicoal Sheen	UCLA	Violation of Constitutional Rights	U.S. District Court, Central District of California
CO Architects	UCLAMC	Declaratory Relief, Temporary Restraining Order, and Preliminary Injunction	Los Angeles County Superior Court
Do, James	UCSDMC	Petition for Writ of Mandate	San Diego County Superior Court
Gryphon Solutions, LLC	UCLA	Judicial Foreclosure	Los Angeles County Superior Court
Jackson, Glenda	UCB	Personal Injury - Motor Vehicle	Alameda County Superior Court
Kronos Spinal Technologies, LLC	UCIMC	Breach of Written Contract	Orange County Superior Court
Neurografix, et al.	UCLAMC	Patent Dispute	Los Angeles County Superior Court
Orozco, Teresa, et al.	UCIMC	Breach of Contract, Fraud, Violation of Statute	Orange County Superior Court
Randall-Wright, Chelsey	UCB	Injunctive and Declaratory Relief and Damages	Alameda County Superior Court
Rice, Arthur and Marcella	UCOP	To Quiet Title to Easement	Yuba County Superior Court

Public Employment Relations Board (“PERB”)
Unfair Practices Alleged by Charging Party

CUE (Coalition of University Employees) SFCE967H	UCOP	Unilateral Change, Discrimination	PERB
CUE SFCE968H	UCSF	Unilateral Change, Discrimination	PERB

UPC State EE Trades Council/UCLA Skilled Trades SFCE969H	UCLA	Unilateral Change, Discrimination	PERB
CUE SFCE970H	UCI	Unilateral Change, Discrimination	PERB
CUE SFCE971H	UCSF	Unilateral Change	PERB
CUE SFCE974H	UCSF	Unilateral Change	PERB
Roake, Michael (AFSCME, American Federation of State, County and Municipal Employees) LACE1127H	UCSD	Discrimination	PERB