The Regents of the University of California

COMMITTEE ON FINANCE
January 17, 2013

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

Members present:	Regents Blum, Gould, Island, Lozano, Mendelson, Newsom, Pérez, Stein, Varner, and Wachter; Ex officio members Brown, Lansing, and Yudof; Advisory members Flores, Powell, and Schultz; Staff Advisors Barton and Smith
In attendance:	Regents De La Peña, Kieffer, Makarechian, Pattiz, Reiss, Rubenstein, Ruiz, Schilling, Torlakson, and Zettel, Regent-designate Feingold, Faculty Representative Jacob, Secretary and Chief of Staff Kelman, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Provost Dorr, Executive Vice President Brostrom, Chief Financial Officer Taylor, Senior Vice President Stobo, Vice Presidents Duckett, Lenz, Mara, and Sakaki, Chancellors Block, Blumenthal, Conoley, Desmond-Hellmann, Drake, Katehi, Leland, and Yang, and Recording Secretary Johns

The meeting convened at 10:00 a.m. with Committee Chair Varner presiding.

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

Upon motion duly made and seconded, the minutes of the meeting of November 14-15, 2012 were approved.

2. **UPDATE ON THE 2013-14 GOVERNOR'S PROPOSED BUDGET AND 2013-14 UNIVERSITY OF CALIFORNIA BUDGET**

Committee Chair Varner expressed the Board's appreciation to the Governor for the funding for UC included in the State budget proposal.

Vice President Lenz stated that the Governor's State budget proposal provided relief for the University and recalled UC's fiscal situation over the past several years, which he described as a roller coaster ride. In October 2010, the last Schwarzenegger budget provided an increase for UC of $371 million. Governor Brown faced a $26 billion structural deficit when he took office, and this required difficult decisions, including a $500 million reduction to the University's budget in January 2011 and a further $150 million reduction in the May Revision. Due to the fact that certain State revenue assumptions were not realized, there was a third reduction of $100 million in December 2011. The University did not face any reductions in the 2012-13 fiscal year, and the University avoided another $250 million reduction thanks to the passage of Proposition

30, The Schools and Public Safety Protection Act of 2012. Nevertheless, the University faces a continuing challenge in planning for student enrollment, faculty hiring, and ongoing costs.

Mr. Lenz then outlined elements of the Governor's 2013-14 budget proposal for the University. In 2012-13, the University's base State General Fund budget was just over $2.3 billion. The 2013-14 proposed budget includes $125 million, part of an agreement to forgo any tuition increase on a one-time basis in 2012-13. He stressed that this amount did not represent additional revenue. The proposed increase in State General Funds in 2013-14 included a base budget adjustment of five percent or $125.1 million, an additional $6.4 million for annuitant health benefits, and $10.2 million to cover lease revenue costs. This would bring the 2013-14 UC operating budget to $2.6 billion, an amount which is still $600 million below the University's level of State funding in 2007-08. In addition, the portion of the University's budget funded by the State General Fund would increase by just over $200 million through a transfer of the general obligation bond debt service to the UC base budget.

The revenue assumptions and expenditure plan approved by the Regents in November 2012 were based on what the University hoped to receive from the State, other revenue assumptions, and alternative revenues. The Governor's proposed budget for 2013-14 provided a good beginning for addressing part of this expenditure plan, but the University must be creative in its approach to alternative revenues in its assumptions. Systemwide contracts and strategic sourcing would provide $20 million, and a transfer of assets from the Short Term Investment Pool to the Total Return Investment Pool would provide another $20 million. More critical still was the University's debt restructuring proposal; assistance from the Legislature would be needed to realize it. The University has engaged in discussions to address concerns that have been raised about this proposal by a number of groups – students, unions, and State officials. Mr. Lenz emphasized that Governor Brown had made education a priority in this budget proposal, whereas reductions to other parts of the State budget were not being restored. This would present a challenge for the Legislature, and the University was ready to work with the Legislature on these matters.

Executive Vice President Brostrom underscored the importance of the passage of Proposition 30, which would provide stability for the campuses to plan for additional faculty hiring and student enrollment. At the same time, the University must continue to pursue administrative efficiencies and alternative revenue streams. He recalled that the previous day, Governor Brown had remarked on the difference between the five percent State General Fund increase in the University's base budget and the 11.6 percent increase in the University's expenditure plan. Mr. Brostrom explained that in fact, including the deferred 2012-13 tuition buyout, the University's base budget was increasing by 11.2 percent. He expressed confidence that the University could produce a plan for a balanced budget that would fund most UC expenditure needs without a tuition increase, but noted that the University would need the opportunity to restructure its lease revenue debt, $80 million, in order to accomplish this. Otherwise UC could not cover its mandatory costs in the upcoming year. The University was looking forward to working closely with Governor Brown, the California Department of Finance, and the Legislature on this debt restructuring.

Mr. Brostrom recalled that the UC general fund includes State appropriations, tuition, and indirect cost recovery. In some news media reports, it was stated that this general fund had increased by 15 percent over the past five years while the budgets of other State agencies diminished. This figure of about 15 percent, or $811 million, was correct, but should be understood in context. Over the previous five years, the State reduced funding for UC by $900 million. During the same period, UC tuition revenue increased by $1.4 billion. In addition, the University had roughly $300 million in other general funds, such as nonresident tuition and indirect cost recovery. This accounted for the approximately $800 million increase.

Mr. Brostrom stressed that 60 percent of this general fund increase, or about $500 million, was returned directly to student financial aid; it did not enter the University budget. This allowed the University to maintain its commitment to low-income students. In addition, the University contributed nearly $300 million to the UC Retirement System and had an increase of $52 million in lease revenue debt service. If these expenses are taken into consideration, the University’s general fund revenues have in fact decreased over the past five years. Mr. Brostrom recalled the shortfall caused by State funding cuts together with UC’s mandatory cost increases associated with health benefits, academic merit increases, non-salary increases, and collective bargaining. Tuition covered less than 40 percent of this shortfall. At the same time, UC has increased enrollment and educates 20,000 more students now than in 2007-08. The notion that the University’s budget has increased is incomplete and does not reflect cost increases and the measures taken by the University to protect low-income students.

Mr. Brostrom then drew attention to Proposition 39, The California Clean Energy Jobs Act, another initiative approved by California voters in November 2012. This measure would provide the State with $1 billion, with $500 million of this amount dedicated to energy efficiency projects at State agencies. The University is in a good position to take on such projects, is ready to proceed with a number of them, and has discussed them with State officials. Among higher education institutions in California, UC represents the greatest share of energy usage, about 60 percent. These energy efficiency projects are very valuable to UC because they would not only decrease utility costs but would address long-term deferred maintenance concerns as well.

Regent Makarechian referred to the annual financial report for the previous year. This report showed that UC’s net worth, assets minus liabilities, had decreased from $19.7 billion to $17.8 billion, a loss of about $2 billion. If net assets continued to decrease at this rate, UC would lose its assets within eight years. Currently the University is educating 23,000 students for whom it receives no State funding. The cost of educating students was $22,000 per student in 1990; currently it is approximately $16,000 per student. In 1990, the State contributed $17,000 per student; currently the State contributes $6,000 per student. In addition, the State is not meeting its obligation to the UC Retirement Plan (UCRP). Regent Makarechian stressed that in light of these facts it was quite apparent that the University needs help from the State. Failing this, the University would lose assets and become bankrupt. Regent Makarechian asked what actions the University was taking to communicate the gravity of this situation as widely as possible. Mr. Brostrom responded that the single greatest impact on the UC balance sheet is caused by the UCRP. Because the University is not funding the normal cost of the UCRP or the interest on its unfunded liability, the unfunded liability grows every year. This accounted for the decline in the University's net assets over the past several years. He recalled that the University had taken action to counteract this trend by increasing the contributions to the UCRP. In July 2013 the University's contribution would be 12 percent and the employee contribution would be 6.5 percent. The University would still not be funding the interest on the unfunded liability, but for the first time it would be covering its normal cost. Referring to other statistics cited by Regent Makarechian, he confirmed that State funding for the University had declined by about 60 percent since 1990 on a per student basis. Tuition had increased dramatically but had not made up for this overall shortfall. In the current year, the University would receive the same amount of State funding in absolute dollars that it received in 1997-98, although UC now educates 75,000 more students. The University's plan to address the current situation has four elements: consistent and predictable support from the State, reduced administrative costs, leveraging alternative revenue sources, and moderate and predictable tuition for students.

Regent Schilling asked what stood in the way of implementation of the debt restructuring proposal, which was similar to refinancing a home mortgage from a higher to a lower interest rate, not taking on more liability or risk. Chief Financial Officer Taylor responded that the comparison with a home mortgage was accurate. He expressed confidence that the debt restructuring proposal would achieve a lower rate than currently being paid, saving $80 million annually for the next ten years. He explained that rating agencies were double-counting the debt in the State's and in UC's ratios. The debt is counted against the University, but UC has no control over how the debt is structured or paid. Mr. Lenz added that the Legislative Analyst's Office has raised the question of transparency in a situation that would arise if the University used funds from the debt restructuring for the debt service on what had formerly been State capital projects. There were no capital projects in the State budget at this point and it is not certain how UC would address its capital needs that formerly were funded either by general obligation bonds or lease revenue bonds. Another concern was expressed about the debt service costs in later years, specifically that as a result of debt restructuring, these costs might result either in an increase in tuition or in reductions to the UC budget and employee layoffs. The University has stated that the debt restructuring proposal would not result in either outcome. Mr. Lenz stated that the University once again had an opportunity to pursue this proposal, working with the Legislative Analyst's Office, students, and unions to achieve consensus.

Regent Reiss stated that the University should specify that the tuition fee buyout being discussed referred to undergraduate tuition. The University's proposed increases in revenue in 2013-14 included $20.8 million from increases in professional degree supplemental tuition. She asked that the University explore the possibility of not raising professional degree supplemental tuition. She recalled reports by chancellors that rising tuition levels in the professional degree programs were causing potential students to enroll at other institutions. She asked that the University seek to secure this $20.8 million from another source and avoid raising fees for professional degree students.

Regent Lozano stressed the importance of a predictable, moderate tuition policy that allows students and their families to plan. She asked about the projected $20 million in revenue from systemwide contracts and about how the total gains from efficiencies would be offset against increased expenditures or redirected. Mr. Taylor responded that the $20 million figure referred specifically to the effort in the coming fiscal year in the procurement arena. The University spends $4.5 billion annually systemwide on material supplies and equipment. The goal of this effort was to secure better bargains for the University. The Office of the President had spent a great deal of time during the previous nine months discussing this effort with campus procurement staff and vice chancellors. The University has hired a new chief procurement officer. The $20 million was an incremental amount.

Regent Lozano requested an estimate of the total savings under the Working Smarter initiative. Mr. Taylor responded that as of June 30, 2012 the initiative had achieved a positive fiscal impact of $287 million, a combination of savings and new revenue. He expressed confidence that this total would increase to $400 million by June 30, 2013. The University was on the right track toward the $500 million goal set for the Working Smarter initiative.

Regent Lozano noted that the hard work carried out at the campus level is not obvious when one merely examines revenues and expenditures. Mr. Taylor stated that a presentation at a future meeting would showcase campus achievements in this area.

Regent Stein thanked Governor Brown for championing Proposition 30, for the increased funding for UC in his State budget proposal, and for not reducing Cal Grant funding. He echoed Regent Reiss' concern about an increase in professional degree supplemental tuition. He asked how the University could avoid such an increase in the coming year. Referring to the University's 2013-14 budget proposal, he asked which expenditures would most likely be cancelled or altered if there were insufficient revenue. Finally, he asked about the status of the UC Riverside School of Medicine. He praised the community-based model of this promising School.

With regard to professional degree supplemental tuition, Mr. Lenz responded that the Office of the President had considered this matter very carefully, in both its policy and fiscal aspects. The highest increase proposed was for nursing programs, a 35 percent increase. He recalled that the University originally had a contractual agreement with the State to increase the number of nurses, an effort supported by Workforce Investment Act funds. In October 2012 those funds were no longer available, in the second year of a five-year agreement affecting a cohort of nursing students. There were no other funds in UC's budget to make up this difference. The University could not cancel a nursing program due to lack of funds when students have already completed the first two years of the program. In response to Regent Stein's second question, Mr. Lenz declined to comment on possible changes to UC expenditures, noting that this would be the subject of upcoming discussions, including consultation with students, faculty, and other members of the University community. In response to Regent Stein's final question, Mr. Lenz emphasized that the UCR School of Medicine remains a priority. Two pieces of legislation had been introduced to appropriate $15 million for the School, which had received its Liaison Committee on Medical Education accreditation the previous fall and would be enrolling students in fall 2013. Mr. Brostrom added that because UC had not received State funding for the School for four years, President Yudof directed the Office of the President to develop a financial plan to support the School, including a $2 million contribution from the Office of the President and a $30 million line of credit. The School has also received funding from Riverside County and other local agencies. He concurred that the School needs State support.

Regent Stein asked how the University could freeze professional degree supplemental tuition. Mr. Lenz responded that each program would have to be examined individually, with an understanding of the implications of not raising tuition levels in each case.

Regent Stein asked if it would be possible to cover the increase in professional degree supplemental tuition with University or State funds. Mr. Lenz responded that the University would need $20 million to do this.

Regent Ruiz asked about the community-based model for the UCR School of Medicine and how it differed from other UC medical schools. Mr. Brostrom responded that a medical education program already exists at UCR, with the first two years of coursework at UCR, followed by clinical work at UCLA. The UCR School of Medicine does not plan to build a new hospital for training its students but would have training take place at local hospitals. Much of the School's training would focus on primary care. The Inland Empire region has the lowest percentage of doctors per capita in California. There is a strong correlation between the location of medical training and residency and where a doctor settles. The University hopes to train doctors at UCR who will then settle and practice in the Riverside-San Bernardino area, where there is tremendous need, especially for primary care. Committee Chair Varner added that partnering with public and private hospitals in the region would not only generate cost savings but would benefit those hospitals as well.

Chairman Lansing echoed the general enthusiasm about the passage of Proposition 30, but stressed that it would not be a solution to all the challenges facing the University. It was incumbent on the Board and all UC stakeholders to seek alternative sources of revenue not dependent on the State.

Regent Pérez expressed frustration with what he described as a disjunction in the current discussion; there was an expectation of predictability for the University as an institution, but without a corresponding commitment to predictability for the constituent members of the University community. He stated that the University should reflect on the actions it takes not only for its rank and file but also for its most highly compensated employees. He noted that the decision not to make contributions to the UCRP for many years was an internal decision by UC. In purely numerical terms, debt restructuring would benefit both the University and the State, but there was a broader context. There are concerns about potential student fee increases in later years and about the implications for the UC workforce. The Legislature would evaluate the Governor's budget proposal as it evaluates all proposals, and there would be significant debate. Regent Pérez advised University representatives to be mindful of the tone of their discussions with members of the Legislature in order to achieve a desirable outcome for UC. There was great value in the passage of Proposition 30 and in the State's continued commitment to education, but there was no significant funding to make up for earlier reductions. Regent Pérez observed that the University is aware of the impact of the years of reductions on its operations, but he stressed that reductions were borne by many other sectors of California. He outlined some concerns of members of the Legislature. Over the past several years, the State had made reductions to UC of approximately $900 million and the University had increased its fee revenue by $1.4 billion. Fee increases were disproportionate to the disinvestment by the State. While actions taken by the University to address the needs of the neediest students in its return-to-aid formula were admirable, for the broad segment of middle-income students there had been no attempt to mitigate that impact. At this point it would not be sufficient merely to avoid increasing student fees, but it was necessary to address the fee increases students had endured over the past several years. This, and the problem of student debt, were problems for graduate and professional students as well as for undergraduates. He emphasized that K-12 schools and higher education were almost the only part of the State budget in the current proposal to receive any restoration of earlier reductions, a clear expression of Governor Brown's commitment. Regent Pérez expressed the Legislature's expectation that the University do no additional harm to student access to UC. He referred to the $125 million tuition buyout and stressed that this was a one-time action, not a new model. The University should not expect that it could propose a fee increase for graduate or professional students and then receive a buyout from the Legislature. The University should do nothing to undermine its commitment to affordability and accessibility.

Governor Brown noted that Proposition 30 had enjoyed strong support from unions, from the California Teachers Association, other organizations, and from individuals, even individuals who would be affected by the income tax increase. He reflected on reasons for the passage of Proposition 30. Over a four-year period, there had been many obvious cutbacks and hardships visited upon K-12 schools and many social service programs. There had been tuition increases and increases in student-teacher ratios. Public awareness of these problems had grown. The public also recognizes the growing income inequality in California and the nation. Voters were aware that the Proposition 30 income tax increase would be paid by the very wealthy, while most Californians would pay only the quarter-cent sales tax, the "people's tax."

Governor Brown observed that the salaries of California State officeholders, including his own, had been reduced by 23 percent. His own annual salary was $165,000, while former Governor Schwarzenegger's salary had been $205,000. In spite of this, there has been no lack of applicants for the governorship or other State offices. The appetite for these jobs has not diminished in spite of lower compensation, perhaps due to the "psychic income" provided by these positions. At the present time there are calls to reduce government spending on Social Security and Medicaid, programs that represent an effort to compensate for the ravages of the American market system, the global economy, and the introduction of new technologies. Thirty years earlier, the top one percent of the California population earned about 10.5 percent of the State's income; this figure had now reached 22 percent. Governor Brown cautioned that the increasing stratification of American society and fewer opportunities for advancement could result in a kind of caste system. American working people were now in a less privileged position than 30 years earlier. The current political conflicts over taxes and entitlement programs reflected the problem of providing democracy in an undemocratic environment. Without a sufficient degree of homogeneity, the social fabric would not hold together.

Governor Brown observed that no one actor in the current situation – the Governor, the Speaker of the Assembly, the President of the University, or the unions – could unilaterally alter the conditions all must function in. All must work together, since no one person or entity has sufficient leverage. He expressed his hope that all could work together to address inequalities and generate funds for common endeavors. He stated his belief that most of the activities of government are good and that cuts to government activity are not desirable. Nevertheless, fiscal discipline is not the enemy of democratic governance, but its fundamental predicate. He stressed that society must live within its means. If it fails to do so and to accommodate what are felt to be legitimate requirements, the system can and would break down. In the case of the University, instructional costs would have to be reduced without compromising quality. Students' time to degree and the graduation rate would have to be improved. He stated that a better understanding was required about the cost of undergraduate education at UC, about how student tuition revenues were spent, and about the costs of graduate instruction, research, and athletics.

Governor Brown noted that personal income in California was growing at four percent annually. In a recent paper, the economist Robert Gordon predicted that U.S. economic growth would slow to less than half its current rate due to the aging population, the global economy, and income disparities. California must prepare for a future that may not provide the same dividends. Referring to Mr. Brostrom's earlier comments on UC's $300 million contribution to the UCRP, Governor Brown stated that the State's costs for the California Public Employees' Retirement System and the California State Teachers' Retirement System amounted to billions of dollars. He enumerated other State obligations and costs.

Governor Brown emphasized that he understood concerns that are expressed about the quality of the University. He noted that in a nationwide comparison, California students have a relatively light debt load. Nevertheless, considered in the longer historical perspective of the University since its founding, UC student tuition is at an unprecedentedly high level. The University's retirement costs, like construction and security, are part of the cost of doing business. The $500 million returned to student financial aid was a direct consequence of tuition increases. The State support for the Cal Grant program over the past six to seven years had more than doubled. He stressed that current economic models in the U.S., Europe, and the State of California were broken and not functioning. In order to maintain and enhance the institution, the University's stakeholders would have to consider measures they would be uncomfortable with. Governor Brown expressed his own wish to understand better how UC costs are distributed. Topics like research and teaching loads would have to be examined.

Governor Brown remarked that during his previous tenure as Governor in the 1970s, California's spending on prisons amounted to 2.5 percent of the State General Fund. In recent years this spending had increased to 11.5 percent. He attributed this increase to a number of factors, including increasing social stratification, lack of social mobility, and the lack of a social safety net. Medi-Cal costs make up 20 percent of the State budget. All these facts reflect a social fabric that is changing and becoming frayed. The challenges facing the University are significant and require bold thinking that is not trapped in obsolete paradigms. University stakeholders must be wiser and search out different perspectives. Governor Brown stressed that the focus of attention should be moved away from the conflicts among various groups within the University – administration, unions, and students – since all these groups are a part of the institution. He emphasized the need for wisdom and understanding to bring the University through the present crisis.

Regent Island referred to the proposed increase in revenue of $23 million to be provided by nonresident supplemental tuition. He asked how many students were represented in the $23 million figure. Mr. Brostrom responded that this represented about 1,000 students in an undergraduate population of about 200,000, or 8.1 percent of the undergraduate population in the current year.

Regent Island asked if this meant that the University had admitted or proposed to admit 1,000 nonresident students rather than California students. Mr. Brostrom responded in the negative. Since 2008-09, the number of nonresident undergraduate students at UC has increased by about 7,500. The number of in-state students has grown as well, although not by the same percentage. He noted that the growth of nonresident enrollment had allowed UC to admit more California resident undergraduates.

Regent Pattiz emphasized that the University has a revenue problem. He recalled the discussion about online education that had taken place the previous day. He urged members of the UC community with concerns about the effect of online education to open their minds beyond their concerns. He anticipated that online education would be a solution to generating more revenue for the University and predicted that a free college education would be available online in the future. If UC wishes to maintain its high quality it must look to new models. In the future UC would provide a different product. At this time the University should pursue online education energetically and redouble its efforts to generate revenue in nontraditional ways. The University should not allow a situation in which it becomes an outsider, defending obsolescent traditions. A change in attitude was required as soon as possible.

Regent Newsom asked about differences between the University's budget proposal now being discussed and the UC budget approved by the Regents in November 2012. Mr. Brostrom responded that the University initially had an expenditure request close to

$600 million. This request obviously represented UC aspirations, including mandatory costs, a solid salary program, funding for the UCR School of Medicine, other enrollment growth, and a $155 million reinvestment in quality. He recalled that the University was able to take positive actions during the fiscal crisis, such as reducing administrative costs, but that other actions had been detrimental. The student-faculty ratio has increased dramatically. Campuses have frozen faculty hiring. The faculty salary gap with competitor institutions has grown. The initial budget request represented an attempt to make up for these reversals. In the coming year, the University would be able to cover its mandatory costs and make its UCRP contributions. Some of the desired reinvestments in quality would take place on a campus-by-campus basis, rather than as a systemwide commitment or initiative.

Regent Newsom asked if it was correct that, in the case that additional State General Funds of $126.5 million were not made available for UC, the University would increase student tuition and fees. Mr. Brostrom responded in the affirmative, but stressed that the University does not anticipate the need for a tuition increase for 2013-14. He underscored that the expenditure plan would not be concrete until the Legislature acts on the State budget and until the May Revision.

Regent Newsom asked when the Regents would be expected to act on the recommendations of the expenditure plan, and at what specific dates the University would have to publicly announce its plans. Mr. Brostrom responded that until the State budget is finalized, the actual UC budget for 2013-14 cannot be known. In previous years, the University has had to take action before the State budget was complete; this usually occurred at the May meeting or the July meeting, at the latest. Mr. Brostrom anticipated that there would be greater stability in the State budget process this year than in past years, and expressed the hope that the University would have a firmer sense of the budget by the March meeting.

President Yudof referred to Governor Brown’s comments and stated his view that the University works to reduce income inequality in society. The University is one of the few enterprises that in fact contributes to the dismantling of the elitist caste system that Governor Brown warned of. He noted that the University’s tuition increases could have been smaller, but that this would have reduced student access to UC. The University would continue working to decrease students’ time to degree. While many programs within the University had an institutional memory of better times in the past, President Yudof expressed his view that UC should see its current position as a starting point. He called attention to two points. First, the University has undertaken a scholarship drive with a particular focus on middle-income students, with a goal of $1 billion. The program has raised $670 million, more than two-thirds of its goal. Second, the University has carried out pension reform. The pension system has a new tier, with conditions slightly more generous than the pension reform for State employees recently approved by the Legislature. The University’s pension reform is meaningful and might reduce UC pension costs by as much as 20 percent.

Regent Kieffer observed that the University was still experiencing a shock to its system from changes in higher education and the wider world since the 1960s and the development of the California Master Plan for Higher Education, which envisioned free higher education. It is difficult to adjust to the reality of tuition and declining State support. UC tuition is now more or less in line with its public competitor institutions. The *Washington Monthly* consistently ranks UC among the top U.S. universities in social mobility, for increasing economic opportunity. Regent Kieffer observed that it is easy to react to tuition or compensation issues, although these do not always represent fundamental problems of the University.

Regent Schilling stated that it was clear to everyone that the University would not be conducting its business in the same manner in the next ten years. She stressed the importance of good leadership for achieving success. She expressed understanding for Governor Brown’s viewpoint on executive compensation, but emphasized that the University operates in an environment where people pursue career opportunities. She stated that she would regret a situation in which the University would try to save $50,000 or $100,000 for the sake of political appearances, but would be less able to recruit the very best leaders. Failing to hire the best available leaders could cost the University financially in the future. The University has been establishing a model of raising private money from donors who wish UC to have superior leadership, and who will supplement the compensation for those leaders. Regent Schilling asked the State not to criticize UC for supplementing executive compensation from private sources. She stressed that the University would need the best possible leadership in the coming years.

Governor Brown expressed agreement with Regent Schilling about the importance of leadership. He questioned the idea of taking an action for the sake of “looking good politically,” unless by political one meant this in the broadest sense of the word, which derives from the Greek *polis*, and meant the health of the community or whole society. He stressed that there was a moral issue involved, and securing private donor sources for executive compensation did not address his concern, which is that the University, an institution aimed at upward mobility for its students, might ultimately reconfirm and more deeply ingrain the trends toward greater social stratification already being experienced. If American society becomes pulled apart too far it will be very difficult to govern. The University cannot influence the global economy or the effects of technology on income distribution, but it must be mindful of these factors.

Governor Brown cited the book “The University in Ruins” by Canadian professor Bill Readings. One of Readings’ observations is that what is called academic “excellence” has no referent; it is a term internal to the university. In the same way, “quality” is a problematic term, more problematic than one might want to acknowledge. Around 1870-1880, only a minority of the instructors at Harvard and Yale had doctoral degrees. Undergraduate requirements and curricula were very different at that time, as was the relationship between undergraduate education and the professional schools. There have been many changes since then; higher education is not static. The University should maintain its basic DNA but adapt to new circumstances. Governor Brown criticized the use of rankings for universities. Rankings congeal many factors into one number. UC is a powerful university and by nature should be and is a leader.

Governor Brown urged the University to pursue online education. Referring to the context of national health care reform and possible changes in cost structure, he urged caution and expressed his concern about the development of a new medical school at the Riverside campus. He expressed his support for research, but emphasized that there is a difference between genuinely new knowledge and novelty. He provided examples of the State's need to invest in bold and farsighted new programs that would generate wealth in the future. Given the many significant concerns in California, Governor Brown stated that the University must move carefully, using its collective wisdom to make the best possible decisions.

Regent Blum recalled that the University educates about 78,000 more students than it did 25 years earlier. He stated his view that the University was better managed under the current senior leadership at the Office of the President than it had been in the past. Costs have been reduced. Some campuses have followed the lead of the Office of the President in becoming more efficient. Regent Blum suggested that attention should be paid to the problem of overhead costs rather than faculty salaries. He stressed the University's need to compete nationally for the best faculty. He recalled that for at least the past six years, UC chancellors have been underpaid by any objective measure, but have forgone an increase in salary when one was offered. During this same period, California prison guards have received salary increases. Competition for qualified prison guards cannot be more difficult than competition for qualified faculty. UC is the only university system with more than one campus in the Association of American Universities (AAU). The salaries of presidents and chancellors of AAU institutions range downward from about $1.4 million; the salaries of UC chancellors in the AAU are in the bottom of the range, between the 50th and 62nd place. The University is not competitive in this area. The salaries of chancellors and deans make up only a small percentage of the entire $22 billion UC budget. Regent Blum emphasized the danger of losing UC faculty to elite private institutions that offer higher salaries and the risk that UC would become something less than those institutions. He expressed his conviction that inequality in society can essentially only be addressed through education. From a global, international perspective, people working in the U.S. today are overpaid and undereducated. The University's role is to address the problem of education. Regent Blum expressed appreciation for Governor Brown's observations and criticisms, but cautioned that paying below-market salaries for UC's leadership would, over time, seriously undermine the quality and stature of the University.

Regent Gould stated that Governor Brown had provided UC with a remarkable opportunity, the possibility of a framework, a multi-year agreement that would provide certainty for students. He concurred with remarks made earlier by Regent Pérez and stated that the University cannot look back to budgets of past years but must move forward from its current position, with efforts in online education and possible reconsideration of how faculty resources are deployed. He acknowledged the many compelling financial issues faced by the State. In response to Governor Brown's offer, the University must provide a three-year plan with concrete, achievable goals of administrative savings, affordability, access, and excellence.

Regent Zettel asked if UC costs could be affected by changes in the teaching load for instructors. She also asked if costs could be reduced by increasing the number of years between faculty sabbatical leave periods. Chairman Lansing responded that Provost Dorr would report on the UC teaching load at the next meeting.

Regent Torlakson reported that according to a recent survey of K-12 classroom technology use, California ranks 46th or 47th among U.S. states, even though much of the relevant technology was developed in California. The K-12 system and the universities can work together to bridge the digital divide and equip middle school and high school students to be ready for digital learning. Currently there is one computer for every three students in California K-12 schools. There are significant gaps in bandwidth in different parts of the state. He urged the University to join a national effort to secure E-Rate revenues for school internet access, and to collaborate with the California State University and the California Community Colleges to help prepare middle school and high school students to excel in online learning at the university level.

Governor Brown expressed appreciation for the work done at the University to reduce administrative costs. He acknowledged the complex nature of the problems facing the University. He praised research and adaptation; adaptation not to decline but to soar. No one individual had the solution to the current situation. There was a need for collaboration, inquiry, and possibly change in design. He expressed confidence in the University's ability to find solutions.

3. **AUTHORITY TO INDEMNIFY PACIFIC GAS AND ELECTRIC COMPANY, PACIFIC FOREST AND WATERSHED LANDS STEWARDSHIP COUNCIL, BEAR YUBA LAND TRUST, AND/OR THE PACIFIC FOREST TRUST IN CERTAIN LIMITED AGREEMENTS TO BENEFIT THE DIVISION OF AGRICULTURE AND NATURAL RESOURCES AND THE BERKELEY CAMPUS**

The President recommended that:

A. The Regents authorize the President to approve the execution of agreements with the Pacific Gas & Electric Company, a California corporation (PG&E), Pacific Forest and Watershed Lands Stewardship Council, a California nonprofit public benefit corporation (SC), Bear Yuba Land Trust, a California public benefit corporation (BYLT), and/or The Pacific Forest Trust, Inc., a California nonprofit public benefit corporation (PFT), their designees and/or successors in interest pertaining to the transfer of certain properties known as Narrows Unit, Pit River Unit, and Lake Spaulding Unit (Properties) to defend, indemnify and hold harmless PG&E, SC, BYLT, and/or PFT, their designees and/or successors in interest and their members, directors, officers, agents, employees, volunteers, contractors, and heirs from and against certain costs, liabilities, penalties, damages, claims, causes of action, demands, liability, and expenses, including any award of attorneys' fees and/or costs, including from the Regents' obligation for remediation required to address hazardous substances on the Properties.

B. The President, or his designee, after consultation with General Counsel, be authorized to approve and execute any documents necessary in connection with the above.

[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 Varner briefly introduced the item.

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

4. **ANNUAL REPORT ON ENTERPRISE RISK MANAGEMENT**

[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 Risk Officer Grace Crickette explained that the philosophy of the University's enterprise risk management program is to empower students, faculty, and staff to manage risk, to consider the consequences of their actions, and to consider possible reputational, financial, and operational risks to UC. There is a great deal of data demonstrating the success of UC risk management. One key performance indicator is the cost of risk, which was over $18 per $1,000 of operating budget in 2003-04 and has now been brought down to $12.49. In 2003-04 UC changed from a traditional risk management program, managing failure, to a proactive program of preventing losses, including investing in insurance coverage. The program has achieved a cost avoidance of over $700 million for the University and has significantly reduced the number of employee injuries. The program has enjoyed successes in deferred maintenance, student life, construction, travel, and other areas of operation.

Committee Chair Varner stated that the enterprise risk management program was a good example of increasing efficiency and that its work should be better known. Regent Gould praised the work of the program.

The meeting adjourned at 12:00 p.m.

Attest:

Secretary and Chief of Staff