

The Regents of the University of California

COMMITTEE ON FINANCE

July 22, 2015

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

Members present: Regents Davis, Gould, Island, Kieffer, Makarechian, Newsom, Ortiz Oakley, Reiss, and Ruiz; Ex officio members Lozano, Napolitano, and Varner; Advisory member Hare; Staff Advisors Acker and Richmond

In attendance: Regents Blum, Elliott, Gorman, Lansing, Oved, Pérez, Sherman, and Zettel, Regents-designate Brody and Schroeder, Faculty Representative Gilly, Secretary and Chief of Staff Shaw, General Counsel Robinson, Chief Compliance and Audit Officer Vacca, Provost Dorr, Executive Vice President and Chief Financial Officer Brostrom, Executive Vice President and Chief Operating Officer Nava, Senior Vice Presidents Henderson and Peacock, Vice Presidents Brown, Duckett, and Sakaki, Chancellors Block, Blumenthal, Hawgood, Katehi, Leland, and Wilcox, and Recording Secretary Johns

The meeting convened at 2:05 p.m. with Committee Chair Ruiz presiding.

1. APPROVAL OF MINUTES OF PREVIOUS MEETING

Upon motion duly made and seconded, the minutes of the meeting of May 21, 2015 and the minutes of the joint meeting of the Committees on Finance and Long Range Planning of May 21, 2015 were approved.

2. FISCAL YEAR 2015-16 BUDGET FOR CENTRAL AND ADMINISTRATIVE SERVICES, OFFICE OF THE PRESIDENT

The President of the University recommended that the University of California Office of the President fiscal year 2015-16 budget for Central and Administrative services be approved, as outlined in Table A below.

TABLE A

FY 2015-16 BUDGET SUMMARY OFFICE OF THE PRESIDENT (\$ millions)	TOTAL BUDGET		UNRESTRICTED BUDGET		RESTRICTED BUDGET	
	TOTAL	TOTAL	TOTAL	TOTAL	TOTAL	TOTAL
	FY 2014-15	FY 2015-16	FY 2014-15	FY 2015-16	FY 2014-15	FY 2015-16
OFFICE OF THE PRESIDENT						
Central and Administrative Services	213.13	219.13	105.55	109.21	107.58	109.92
Academic Affairs	29.09	29.40	28.09	28.40	1.01	1.00
Intellectual Property Program*	46.44	49.78	2.29	2.08	44.15	47.70
Finance	45.18	44.96	34.25	35.06	10.93	9.90
Business Operations	69.12	71.25	23.24	25.64	45.88	45.61
President's Exec. Office	3.20	3.04	2.77	2.60	0.43	0.44
Health Sciences	3.42	3.57	3.39	3.39	0.04	0.19
External Relations**	16.68	-	11.53	-	5.15	-
Governmental Relations	-	5.19	-	4.59	-	0.60
Public Affairs	-	11.96	-	7.47	-	4.49
Regents Officers	52.64	54.58	19.72	19.46	32.92	35.11
General Counsel	12.23	11.76	10.96	10.54	1.27	1.22
Secretary of the Regents	3.19	2.90	3.19	2.89	0.00	0.01
Ethics & Compliance	5.58	6.04	5.58	6.03	0.01	0.01
Investments Office	31.64	33.88	-	-	31.64	33.88
Facilities & Operational Expenses	23.08	22.40	22.57	21.90	0.51	0.51
UC Path Center	11.28	13.08	11.28	13.08	-	-
Cost of Living Adjustment	-	5.67	-	3.30	-	2.37
TOTAL	300.13	314.87	159.13	166.96	141.01	147.91
	<i>% change</i>	<i>4.9%</i>		<i>4.9%</i>		<i>4.9%</i>

* The Intellectual Property Program is the central office for management and oversight of the University's patent and licensing functions. 97% of the \$49.8 million budget represents patent revenues paid to internal and external inventors and expenses for patent applications; 3% of the budget is for oversight of the entire systemwide program. This year UC Berkeley is transferring this function to OP including its associated \$3.5M budget.

**In FY2014-15, External Relations was reorganized into two divisions: Governmental Relations and Public Affairs

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

(See discussion and action below.)

3. FISCAL YEAR 2015-16 BUDGET FOR SYSTEMWIDE ACADEMIC AND PUBLIC SERVICE PROGRAMS, OFFICE OF THE PRESIDENT

The President of the University recommended that the University of California Office of the President fiscal year 2015-16 budget for Systemwide Academic and Public Service Programs be approved, as outlined in Table A below.

TABLE A

FY 2015-16 BUDGET SUMMARY OFFICE OF THE PRESIDENT (\$ millions)	TOTAL BUDGET		UNRESTRICTED BUDGET		RESTRICTED BUDGET	
	TOTAL	TOTAL	TOTAL	TOTAL	TOTAL	TOTAL
	FY 2014-15	FY 2015-16	FY 2014-15	FY 2015-16	FY 2014-15	FY 2015-16
SYSTEMWIDE ACADEMIC & PUBLIC SERVICE PROGRAMS						
Instruction	52.18	53.07	1.84	2.39	50.34	50.68
Research	104.20	107.50	51.81	55.91	52.39	51.59
Public Service	16.69	17.22	11.69	11.31	5.00	5.91
Academic Support	48.22	48.69	23.37	23.16	24.85	25.53
Agriculture and Natural Resources	91.30	92.58	66.20	66.06	25.10	26.52
National Laboratories	3.97	4.47	-	-	3.97	4.47
Presidential Initiatives	9.85	9.85	9.85	9.85	-	-
Cost of Living Adjustment	-	6.39	-	3.60	-	2.78
TOTAL	326.40	339.76	164.75	172.28	161.65	167.48
	<i>% change</i>		<i>4.1%</i>	<i>4.6%</i>		<i>3.6%</i>

[Background material was provided 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 and Chief Operating Officer Nava presented the two agenda items for the annual budget for the Office of the President (UCOP). The UCOP budget represents two percent of the total UC budget of \$26 billion. The presentation of the budget as two separate items was a result of the past year's effort to best represent the work of UCOP. UCOP has an administrative leadership role, overseeing the mission of the University. UCOP also has a role in managing several academic and public support programs on behalf of UC. At times the functions within UCOP have been perceived as purely administrative, but in fact the academic and public support programs operated by UCOP account for a significant share of the total UCOP budget. Separating the UCOP budget into these two major categories would make the actual purposes served by UCOP more transparent.

The first of the two items was the UCOP budget for central and administrative services; this covered not only executive leadership at UCOP, but many services which are more effectively and efficiently managed at one location rather than every location. The second item, for systemwide academic and public service programs, included a number of research, instruction, academic support, and public service programs best managed at one location; more than 60 percent of the funds in this budget flow through to the campuses and Agriculture and Natural Resources (ANR) in direct support of UC's mission. In recent years the UCOP budget had been reduced significantly. In the past year UC kept the campus budget assessment flat. This assessment funds most of UCOP's unrestricted budget.

The University's budget agreement with the State has allowed UC to plan for a three percent cost of living adjustment for non-represented staff and faculty. The systemwide budget also included certain target increases aimed at achieving systemwide efficiencies and responding to campus priorities for key academic programs and initiatives. These

increases were offset to some extent by the elimination of redundancies and strategic reductions.

The UCOP budget for central and administrative services included essential services delivered on behalf of the campuses and medical centers such as retirement and benefits administration, investment management, strategic sourcing, insurance, legal services, risk management, and compliance. These services are provided centrally for the campuses in order to maximize efficiency and effectiveness. The central and administrative services budget totaled \$315 million, \$167 million in unrestricted funds and \$148 million in restricted funds. The budget was proposed to grow by \$14.7 million, over 4.9 percent. Thirty-eight percent of the budget increase was due to the cost of living adjustment, 23 percent was due to the transfer of UC Berkeley's patent administration program to UCOP, 15 percent was attributable to the Office of the Chief Investment Officer, which would be deploying a strategy in the coming year to lower external management fees, and 12 percent was attributable to the UCPath Center and its further development.

The UCOP budget for systemwide academic and public service programs encompassed key programs and initiatives and represented one percent of the University's overall budget. These programs benefit all the campuses and would otherwise have to be managed by each campus. They include the UCDC program in Washington, D.C., the UC Sacramento Program, and the Education Abroad Program. This budget included just under \$29 million for State-funded programs for research in areas such as breast cancer, tobacco, and HIV/AIDS. An increase of \$2 million for UC's Multicampus Research Programs and Initiatives (MRPI) would restore funding for these Programs, bringing MRPI funding closer to its level before the most recent fiscal crisis. Ms. Nava underscored the value of UC's investment in MRPI; for every dollar invested since 2009, the University has received a 165 percent return in subsequent federal grant awards. Public service programs provide outreach to potential future students, both from the K-12 system and from community colleges. The systemwide academic and public service program budget totaled \$340 million, \$172 million in unrestricted funds and \$168 million in restricted funds. The budget was proposed to grow by \$13 million or 4.1 percent. Forty-eight percent of the budget increase was due to the cost of living adjustment. In addition, the University anticipated an increase of \$1.3 million in grant funding from the U.S. Department of Agriculture to support ANR. UC was introducing a \$2 million initiative to focus on Latino, American Indian, and Alaskan Native doctoral enrollment.

A portion of both UCOP budgets would be funded by an assessment to the campuses. While the assessment was kept level the previous year, there would be a modest increase of 3.5 percent to the assessment in the 2015-16 fiscal year budget.

Regent Ortiz Oakley requested clarification of the difference between restricted and unrestricted revenues in the budget. He referred to the budget agreement with the State and asked how it would affect funding UC had received to increase enrollment. Ms. Nava explained that UC's restricted funds consist mainly of State General and special funds, patent royalties, tuition and fees, asset management funds, and retirement funds. Unrestricted funds come from campus assessments, the President's endowment fund, and

common funds. Chief of Staff to the Chief Financial Officer Zoanne Nelson noted that retirement funds are restricted funds, and can be spent only on retirement expenses. Another example is State funds for breast cancer research; those funds can only be used for that purpose.

Regent Ortiz Oakley asked about the sources of the restricted funds in the UCOP budget, and if there was one primary source of these restricted funds. Ms. Nelson responded that there are a number of sources. Ms. Nava added that funding for the three percent cost of living adjustment would come from campus assessments, which are primarily unrestricted funds.

Regent Ortiz Oakley asked about the relationship of this increase to the budget agreement with the Governor, and what impact it might have on funds received from the State for enrollment growth at UC. Ms. Nava recalled that the budget agreement with the State was a four-year agreement, which afforded the University the opportunity to evaluate its salary programs. Monies received from campus assessments would not affect enrollment.

In response to another question by Regent Ortiz Oakley, Ms. Nava confirmed that the cost of living increase should not affect the University's ability to increase student enrollment.

Regent Makarechian noted that the amount budgeted for facilities and operational expenses was decreasing and asked how this was possible. Ms. Nava responded that the line item for facilities and operational expenses decreased due to an expense for a President Emeritus that was no longer required.

In response to another question by Regent Makarechian, Ms. Nava confirmed that the line item for "Ethics and Compliance" in the summary chart for the central and administrative services budget included internal audit. Regent Makarechian stated that internal audit should be specifically identified in the item. Referring to the same chart, he requested clarification of the line item for UCPATH Center expenses, and asked if this expense was for employees. Ms. Nava responded in the affirmative. This expense related to operating the UCPATH Center in Riverside. The budget allocation would allow for increasing the number of employees to 84. Seventy-six were allocated in the last budget cycle. She clarified that the expense was only for employees working in Riverside at the UCPATH Center, not for employees at other campuses who were working on the UCPATH project.

Regent Makarechian referred to the employees at other campuses working on UCPATH and asked how they were accounted for in the budget. Ms. Nelson responded that those are considered project costs, which are capitalized costs, not part of the operating budget. The line item in the chart represented the operating budget for the UCPATH Center.

Regent Elliott requested clarification of the campus assessment and the increase of 3.5 percent. Ms. Nava responded that 2.3 percent of the campus assessment would cover

the cost of living increase. The remainder would cover increases in the budget for academic and public service programs.

Regent Elliott asked about the total dollar amount of the campus assessment that goes to UCOP. Ms. Nelson responded that the total amount was \$304 million, a 3.5 percent increase over the previous year. Most of the unrestricted portion of the UCOP budget is funded through the campus assessment.

Regent Makarechian asked about the rationale for transferring the management of UC Berkeley patents to UCOP. Ms. Nelson responded that managing UC patent revenues is an administrative function. In the case of UC Berkeley, employees who managed these revenues retired, and the campus decided not to continue managing these revenues itself, but asked UCOP to perform this function. UCOP manages these revenues for all other campuses but one. President Napolitano added that there would be a fuller discussion in the fall about the University's plans for management of its intellectual property and centers of innovation.

In response to a question by Regent Sherman, Ms. Nelson confirmed that these budgets included operating expenses, but not capitalized expenses.

Regent Sherman asked what those capitalized expenses were, noting that they must represent a significant number. Ms. Nava responded that the UCPath project is capitalized.

Regent Sherman asked if there was an approximate estimate of those expenses, which are often amortized in annual budgets. Executive Vice President and Chief Financial Officer Brostrom responded that to his knowledge, UCPath was the only project the University was currently capitalizing. In the past, UC had not had capitalized projects other than the debt service on buildings.

Upon motion duly made and seconded, the Committee approved the President's recommendations in items 2 and 3 above and voted to present them to the Board.

4. **UPDATE ON FINAL 2015-16 BUDGET**

[Background material was provided 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 and Chief Financial Officer Brostrom reported that the final total State budget for 2015-16 was \$167.6 billion, with \$117.5 billion of this in State General Funds, and authorized spending of \$115.4 billion. At the end of the current fiscal year, the State would have accumulated \$4.6 billion in estimated total reserves.

In spite of increased State revenues, General Fund spending increased by only about one percent. In some cases there was one-time spending for debt payments. There were State budget increases for childcare and early learning programs, Medi-Cal, Denti-Cal, and

other safety net programs. The California State University (CSU) received almost \$100 million in additional funding. UC would receive an additional \$25 million if it met an enrollment target of 5,000 additional California resident undergraduates by May 2016. Many features of the budget reflected the funding framework agreed upon by President Napolitano and Governor Brown. Mr. Brostrom stressed that this was a very constructive agreement that provides more stability for the University, and for students and their families, who would be better able to plan for their education. It would also facilitate planning by chancellors and campuses by providing more predictability in funding.

Mr. Brostrom recalled that the Governor had agreed to extend by two years the four percent base budget adjustments; over four years, this would provide a \$500 million permanent increase to UC's State appropriation. The University would receive \$436 million, mostly in one-time Proposition 2 funds, over the next three years, to address the unfunded liability of the UC Retirement Plan (UCRP). UC also received \$25 million in one-time funding for deferred maintenance. Mr. Brostrom anticipated that UC would receive some cap and trade funding to support its energy and sustainability programs. This item was removed from the State budget process and would be taken up separately in August in special legislation.

The University agreed that there would be no increase in California resident undergraduate tuition for the next two years. Beginning in 2017-18, the University would seek to peg tuition increases to the rate of inflation. There would be an increase of five percent, amounting to \$48, to the Student Services Fee beginning in 2015-16. One-third of this revenue would be directed to student financial aid. One-half of the remainder would support student mental health programs, and the other half would be used to support other student services.

The budget agreement included an increase of up to five percent in Professional Degree Supplemental Tuition (PDST) for all programs except law and nursing, and established PDST for five new professional degree programs that would begin in 2015-16. PDST for nursing programs may increase up to 20 percent. There would be no increases in law school PDST for four years. Undergraduate nonresident supplemental tuition would increase by eight percent in 2015-16 and 2016-17, and by five percent thereafter.

The State Department of Finance authorized the University to finance 15 capital outlay projects totaling nearly \$300 million. Mr. Brostrom underscored that these were not being funded by lease revenue bonds or general obligation bonds; the University was funding these projects out of a portion of its State General Fund appropriation, a relatively new mechanism approved by the State. The State had also granted UC more flexibility in how to fund these projects, such as with leasebacks and availability payments.

Regent Davis asked if the University was planning on "rebenching" or updating the allocation formula for campuses' funding if it achieved the enrollment target of 5,000 additional California resident undergraduates. Mr. Brostrom responded that the University had begun to change the process of allocating State funds among the campuses about three years earlier. The University allocates funds on a weighted student

average, so that the funding is the same for every undergraduate regardless of campus. He acknowledged that the University was still in the midst of this six-year process. A large amount of money had to be reallocated and UC was moving to a new, long-term enrollment plan.

Regent Ortiz Oakley referred to the funding for UCRP. He asked when the Regents would receive updates on progress toward UCRP goals. Mr. Brostrom responded that the University was engaged in an experience study on UCRP. UC would update mortality tables, inflation assumptions, and the discount rate. This information would be presented in the fall, as well as concepts on additional borrowing. An updated UCRP valuation would be presented at the November meeting.

Regent Ortiz Oakley asked about the rationale for using a portion of the Student Services Fee for student financial aid, rather than using it only for student support services. Mr. Brostrom responded that return to aid is a factor in all UC tuition and some fee charges. Overall, UC undergraduate tuition and fees are about \$12,000. About \$8,000 of that amount goes to the operating budget of the campus the student attends. The remaining \$4,000 goes into the return to aid pool. This is intended to ensure that the level of help is consistent across all the campuses. In the past, the Student Services Fee was used entirely for student support services. As this source of revenue grew, the University realized that some of these funds should be returned to financial aid.

Regent Reiss asked about the conditions UC must meet to receive the additional \$25 million in State funding. Mr. Brostrom responded that the University must demonstrate, either through students' Statements of Intent to Register or transfer information, that UC would enroll another 5,000 California resident undergraduates in the 2016-17 academic year. The University was still developing enrollment plans with the campuses. The University has a plan to increase enrollment by 10,000 students over three years; it remained to be seen if UC could achieve the 2016-17 target. Mr. Brostrom noted that this was an "all or nothing" condition. If UC did not reach the 5,000 student target, the Department of Finance would not place the additional \$25 million in the University's budget.

Regent Reiss asked about the likelihood of UC achieving this goal, given news media reports that the University admitted fewer undergraduates this year than the previous year. President Napolitano responded that the 5,000 student target would be difficult to achieve, in particular because only undergraduate students would count toward this number, not graduate students. The University was considering a variety of options to address this matter. She stated that this fall UC would enroll almost the same number of students as in the past year, perhaps one percent fewer. As it happened, during the last student application season the University was renegotiating the entire budget with Governor Brown. Due to the uncertainty at the time, UC held enrollment flat. News media reports about fewer undergraduate admissions were correct, but perhaps somewhat overstated.

Regent Reiss asked if it was unlikely that UC would meet the 5,000 student target. President Napolitano stated her view that it was not unlikely. There would be several options to consider, and the administration would consult with the Board on these options.

Regent Reiss asked if the Regents would receive an update in the fall on how many admitted students actually accepted UC admission. President Napolitano responded that this information would be provided at the September or November meeting. The Regents would consider the UC budget for 2016-17 at the November meeting, and that would be a good time to discuss the issue of student enrollment.

Regent Reiss expressed concern about the increases in PDST and the University's ability to attract the best students for these programs.

Regent Sherman asked if the University had the capacity to admit 5,000 additional students. Mr. Brostrom responded in the affirmative, but added that in order to enroll 10,000 additional students, campuses would require new facilities and more faculty. One advantage of the current agreement with the State is that this framework allows for multi-year planning for facilities and faculty.

In response to a question by Regent Newsom, Mr. Brostrom elucidated the difference between the Student Services Fee approved by the Regents, consistent across the campuses, and fees approved by student referenda at particular campuses, such as the Green Initiative Fund at UC Santa Barbara. Regent Newsom requested a listing, by campus, of these student services fees. Mr. Brostrom responded that this information would be provided. Regent Newsom noted that CSU had put a limit on these types of assessments. Regent Pérez remarked that the Student Success Fees at CSU were very different from the UC Student Services Fee or campus fees approved by student referenda.

Regent Makarechian underscored the fact that CSU was receiving \$97 million in additional funding with no conditions attached, while UC might receive \$25 million, with conditions. The State paid its obligation to the CSU pension but not to the UCRP. He asked about the University's long-term plan to address the State's different treatment of CSU and UC, or if the University had a plan for the following year. President Napolitano observed that there was now a four percent increase built into the University's base budget for each of the next four years. She acknowledged that UC must continue to advocate in Sacramento, highlighting UC's contributions to California in education, research, and health care. Referring to Regent Makarechian's specific question, she stated that there might not be a single plan to address this matter, but that there is a significant focus on working with the State.

Regent Makarechian reflected on the role of the general public in influencing the State to provide support for UC. He asked that the Regents be briefed on the real steps being taken to advocate for UC with the Legislature and the general public. President Napolitano responded that she viewed this as a continual campaign.

Committee Chair Ruiz stressed that UC must be better prepared for the next year's State budget process.

The meeting adjourned at 2:55 p.m.

Attest:

Secretary and Chief of Staff