California State Auditor

April 2017

The University of California Office of the President

It Failed to Disclose Tens of Millions in Surplus Funds, and Its Budget Practices Are Misleading

Report 2016-130

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California State Auditor

Elaine M. Howle State Auditor
Doug Cordiner Chief Deputy

April 25, 2017 2016-130

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

At the request of the Joint Legislative Audit Committee, the California State Auditor's Office presents this audit report regarding the University of California Office of the President. Our report concludes that the Office of the President has amassed substantial reserve funds, used misleading budgeting practices, provided its employees with generous salaries and atypical benefits, and failed to satisfactorily justify its spending on systemwide initiatives. Furthermore, when we sought independent perspective from campuses about the quality and cost of the services and programs the Office of the President provides to them, the Office of the President intentionally interfered with our audit process. Auditing standards require that we disclose this interference and prohibit us from drawing valid conclusions from this portion of our work.

Specific concerns we discuss in the audit report include the following:

- The Office of the President has accumulated more than $175 million in undisclosed restricted and discretionary reserves; as of fiscal year 2015–16, it had $83 million in its restricted reserve and $92 million in its discretionary reserve.
- More than one-third of its discretionary reserve, or $32 million, came from unspent funds from the campus assessment—an annual charge that the Office of the President levies on campuses to fund the majority of its discretionary operations.
- In certain years, the Office of the President requested and received approval from the Board of Regents (regents) to increase the campus assessment even though it had not spent all of the funds it received from campuses in prior years.
- The Office of the President did not disclose the reserves it had accumulated, nor did it inform the regents of the annual *undisclosed budget* that it created to spend some of those funds. The undisclosed budget ranged from $77 million to $114 million during the four years we reviewed.
- The Office of the President was unable to provide a complete listing of the systemwide initiatives, their costs, or an assessment of their continued benefit to the university.
- While it appears that the Office of the President's administrative spending increased by 28 percent, or $80 million, from fiscal years 2012–13 through 2015–16, the Office of the President continues to lack consistent definitions of and methods for tracking the university's administrative expenses.

We found it particularly troublesome that the Office of the President intentionally interfered in our efforts to assess the types and quality of services it provides to campuses. Correspondence between the Office of the President and the campuses shows that the Office of the President inappropriately reviewed campuses' survey responses, which resulted in campuses making changes to those responses prior to submitting them to us—campus statements that were critical of the Office of the President had been removed or substantially revised, and negative ratings had been changed to be more positive.

Taken as a whole, these problems indicate that significant change is necessary to strengthen the public's trust in the University of California. To achieve this change, we believe the Legislature should increase its oversight of the Office of the President.

Respectfully submitted,

Elaine M. Howle

ELAINE M. HOWLE, CPA
State Auditor

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RESPONSE TO THE AUDIT

* Due to interference by the Office of the President, the survey responses presented in this appendix may not accurately or completely represent the campuses' perspectives.

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Summary

Results in Brief

The rising cost of higher education in the State and nationwide places an important responsibility on public universities to make fiscally prudent decisions that best serve the financially burdened students and families who help to provide for their support. Nonetheless, over the past five years, the University of California (university) Office of the President has made decisions that redirected funds away from the university's fulfillment of its role as the State's primary academic research institution and toward other priorities. Although the University of California Board of Regents (regents) delegated authority and responsibility over the administration of the university's affairs and operations to the Office of the President, it has not managed its own budget—which amounted to $747 million in fiscal year 2015–16—in a fiscally prudent or transparent way. Further, it has not ensured that its spending decisions consistently align with the needs of the university's 10 campuses, students, and other stakeholders.

Specifically, the Office of the President did not disclose to the regents that it had amassed more than $175 million in reserve funds as of fiscal year 2015–16. In each of the four years we reviewed, the Office of the President spent significantly less than it budgeted for and it asked the regents for increases in future funding based on its previous years' over-estimated budgets rather than its actual expenditures. Consequently, it accumulated significant annual budget surpluses, which it maintains in two reserves: restricted and discretionary. Furthermore, it not only failed to disclose the existence of these reserves to the regents, but it also failed to inform them of the annual undisclosed budget it created to spend the reserves. This *undisclosed budget* ranged from $77 million to $114 million in the four years we reviewed.

In effect, the Office of the President received more funds than it needed each year, and it amassed millions of dollars in reserves that it spent with little or no oversight from the regents or the public. According to the Office of the President, disclosing its reserves was unnecessary because the regents had approved the spending in previous years' budgets. Further, its budget director stated that the Office of the President can use the discretionary reserve to fund any program or project at the Office of the President or the campuses. However, this practice contradicts the intent of a regents' 2006 policy prohibiting the Office of the President from spending any funds until the regents approve its annual budget each year. Had the regents known about the Office of the President's reserves, they could have potentially requested that the Office of the President use at least some of the funds to better meet the

Audit Highlights . . .

Our audit of the University of California Office of the President's budget and staffing processes revealed the following:

» *The Office of the President did not disclose to the University of California Board of Regents, the Legislature, and the public $175 million in budget reserve funds.*

- *It spent significantly less than it budgeted for and asked for increases based on its previous years' over-estimated budgets rather than its actual expenditures.*
- *It created an undisclosed budget to spend the reserve funds; the budget ranged from $77 million to $114 million during a four-year period.*
- *The reserve included $32 million in unspent funds it received from an annual charge levied on the campuses—funds that campuses could have spent on students.*

» *The Office of the President's executive and administrative salaries are significantly higher than comparable state employee salaries.*

» *During a five-year period, the Office of the President spent at least $21.6 million on employee benefits some of which are atypical to the public sector, such as supplemental retirement contributions.*

» *The Office of the President has failed to satisfactorily justify its spending on systemwide initiatives, and it does not evaluate these programs' continued priority or cost.*

continued on next page . . .

- *Both Office of the President and campus administrative spending increased and annual budget and staffing levels for the Office of the President are higher than administrations at other comparable public universities.*
- *Auditing standards prohibited us from drawing conclusions from some of our work because the Office of the President intentionally interfered with our audit process.*
  - *It inappropriately screened the campuses' survey responses before campuses submitted the surveys to us.*
  - *Campus statements that were initially critical of the Office of the President had been revised and quality ratings shifted to be more positive.*
- *Significant reforms are necessary to strengthen the public's trust in the Office of the President.*

campuses' and students' needs. Further, even though the Office of the President stated that expenditures from its undisclosed budget went through a rigorous approval process, it could not demonstrate adequate approval for 82 percent, or $34 million, of the planned expenditures we reviewed from its undisclosed budget in fiscal year 2015–16. With no evidence of proper approval, the majority of the undisclosed budget was unnecessarily at risk for misuse.

The Office of the President's budgeting practices are also of concern because its disclosed discretionary budget is almost entirely funded by an annual charge, called the campus assessment, that it levies on the campuses. The Office of the President allows campuses to pay this assessment using any funding source, and campuses paid about a third of the $288 million fiscal year 2015–16 assessment—up to $106 million—using their portion of the money from the State's General Fund. Over the past five years, the Office of the President has underspent the revenue it received from the campus assessment by $32 million, and as a result, a significant portion of the Office of the President's discretionary reserve consists of funds the campuses could have retained and spent for other purposes. Moreover, the Office of the President increased the campus assessment in two of the four years we reviewed, a decision we find problematic given that it consistently failed to spend all of the revenue it received from the campuses. We believe the Office of the President might be able to refund *at least* $38 million of its uncommitted reserve funds to campuses.

Furthermore, because the Office of the President provides so little information about its budget—and the information it does provide is sometimes misleading—the regents and Legislature are likely to find it difficult, if not impossible to understand its operations. In fact, we found the Office of the President made inaccurate and unsubstantiated claims about its budget during regents meetings, such as claiming the Office of the President is not funded using state money even though campuses use money from the State's General Fund to pay for the campus assessment. The Office of the President's inability to substantiate its public claims is due to its lack of strong, consistent budgeting processes, which would help to provide transparency and accountability. For example, since 2013 its annual budget process has not included a formal avenue for soliciting input from the campuses regarding its planned spending decisions. We identified a number of best practices that the Office of the President should immediately implement, including eliminating its undisclosed budget and using its actual expenditures as a basis to establish its future budgets. Implementing these practices would not only increase transparency but would also shed light on opportunities that the Office of the President has to reevaluate its financial decisions and reduce its spending.

The Office of the President might also be able to realize significant savings by adjusting the generous compensation it pays its staff. For example, the 10 executives in the Office of the President whose compensation we analyzed were paid a total of $3.7 million in fiscal year 2014–15—over $700,000 more than the combined salaries of their highest paid state employee counterparts. In one example, the Office of the President paid the senior vice president for government relations a salary that was $130,000 greater than the salaries of the top three highest-paid state employees in comparable positions. In defense of its salaries, the Office of the President asserted that the higher education environment necessitates higher pay for its staff. Although this argument may have merit for certain executive employees, it has little merit for administrative staff such as financial analysts who perform similar duties irrespective of the entities for which they work. Nonetheless, we found that the Office of the President paid individuals annual salary rates for the 10 administrative positions we reviewed that were $2.5 million more than the maximum annual salary ranges for comparable state employees. The Office of the President uses salary survey data that come almost entirely from private sector companies and higher education institutions to determine its base salary levels, which typically pay their staff more than public entities.

Further, the Office of the President spent at least $21.6 million from fiscal years 2011–12 through 2015–16 on generous employee benefits, many of which are atypical of those public sector employees receive. For example, in addition to its regular retirement plan, the Office of the President also offers its executives a retirement savings account, into which the Office of the President contributes up to 5 percent of the executives' salaries. These contributions totaled $2.5 million over the past five years. The Office of the President also spent more than $2 million for its staff's business meetings and entertainment expenses over the past five years—a benefit that the State does not offer to its employees except in limited circumstances. Moreover, the Office of the President lacks sufficient policies to ensure that the cost of certain employee benefits is contained. For example, when its employees travel, the Office of the President recommends but does not require that its staff book hotels that do not exceed 200 percent of the federal per diem rate.

The Office of the President's spending decisions are not limited to its internal operations; rather, it is also responsible for deciding how to spend funds on behalf of the university as a whole. Specifically, half of its budget presented to the regents is related to *systemwide initiatives*—a term that the Office of the President uses to describe programs that benefit the entire university system. Examples of these initiatives include academic and research programs such as the University of California Observatories, the University of California Washington Center, and

the Breast Cancer Research Program. Although many systemwide initiatives undoubtedly provide a benefit to the public and to students, the choice to fund them may come at the expense of the university's priority of access and affordability for California undergraduates. Moreover, when we attempted to quantify the costs of its systemwide initiatives, we found that the Office of the President was unable to provide a complete listing of the systemwide initiatives it administers or their cost. Additionally, it has budgeted funds for systemwide initiatives that it did not include as part of the systemwide initiatives section of the budget it presented to the regents, such as $910,000 in fiscal year 2015–16 designated for three separate initiatives: advocacy communication, sustainability, and administrative funds that it uses to reimburse campus officials for purchases they make on the university's behalf. Even though some of the programs that the Office of the President has designated as systemwide initiatives benefit the university as a whole, the Office of the President does not regularly evaluate these initiatives' continued priority, benefit, cost, or intent.

The importance of justifying its spending decisions is amplified by the fact that the Office of the President's administrative costs increased from fiscal years 2012–13 through 2015–16. Specifically, the Office of the President's administrative spending increased by 28 percent, or $80 million, while campus administrative costs increased by 26 percent over the same time period. Furthermore, the Office of the President's budget and staffing levels exceed those of the central administration at comparable university systems, such as the University of Texas. The Office of the President explained that this may be because it provides services to its campuses and employees that other universities do not, such as the management costs associated with the university's retirement program. To support that assertion, we expected that the Office of the President would have established a consistent definition for and method of tracking its and the university's administrative costs; however, it has not done so. Lacking these, we question whether the Office of the President can adequately justify either its or the university system's administrative expenses.

Finally, the Office of the President's actions during this audit have caused us to question whether it will make a genuine effort to change. This conclusion is based on the fact that it intentionally interfered with our audit process, which hindered our ability in addressing certain aspects of our audit objectives. Specifically, we administered two surveys to the campuses seeking their perspectives on issues such as the quality of the Office of the President's services and programs. However, correspondence between the Office of the President and the campuses shows that the Office of the President inappropriately reviewed the campuses' survey responses and that campuses subsequently made changes before submitting them to us. Specifically, when we compared

the campuses' original survey responses sent to the Office of the President to the later versions of their responses that they eventually sent us, we found that the campus statements that were initially critical of the Office of the President had been removed or significantly revised and that the surveys' quality ratings had been shifted to be more positive. Because the Office of the President inappropriately inserted itself into the survey process, auditing standards prohibit us from drawing conclusions based on the survey results. As a result, the Office of the President missed an opportunity to receive feedback from its key stakeholders, and it demonstrated an unwillingness to receive constructive feedback.

As a result of the nature and number of the concerns we identified in the course of this audit, we believe that significant reforms are necessary to ensure that the Office of the President makes prudent decisions that reflect the interests of those that it serves. Specifically, the Legislature should directly appropriate funds to the Office of the President that eliminates the need for levying an assessment on campuses. This change would increase the Office of the President's accountability by requiring it to justify both its budget levels and fiscal decisions, such as the level of compensation it provides for its staff. Additionally, we believe that the Legislature should, from the funds appropriated, require the regents to contract with an independent third party that can assist the regents in monitoring a three-year corrective action plan focused on addressing the many issues we identify in this report. This plan, which we summarize in Figure 19 on page 91 of this report, would help to ensure the Office of the President's accountability and transparency and give campuses a better ability to plan for expenses that should benefit them.

Selected Recommendations

To determine the amount of money that it can reallocate to campuses and to ensure that it publicly presents comprehensive and accurate budget information, the Office of the President should do the following:

- Implement best practices for budgeting, including using its actual expenditures to inform its future budgets rather than using the budget amounts from its previous year and eliminating the use of an undisclosed budget.
- Develop a reserve policy that governs how large its reserves should be and the purposes for which those reserves can be used.
- Implement policies to ensure that it approves and justifies all its budget expenditures.

- Reallocate to the campuses any identified savings or excess revenues.

To ensure that its staffing costs align with the needs of campuses and other stakeholders, the Office of the President should do the following:

- Develop and implement a method for weighing comparable public and private sector pay data when establishing salaries for all positions.
- Set targets for any needed reductions to salary amounts using the results from its public and private sector pay comparisons and adjust its salaries accordingly.

To ensure that its expenditures for systemwide initiatives represent the university's priorities, the Office of the President should do the following:

- Develop and use a clear definition of systemwide initiatives to ensure consistency in future budgets.
- Develop a comprehensive list of systemwide initiatives and presidential initiatives, including their purpose and actual cost, and present this list to the regents for review.

To ensure the Office of the President's ongoing accountability, the Legislature should directly appropriate funds for the Office of the President's operations.

Agency Comments

The Office of the President disagreed with a key conclusion of our report—that it has failed to disclose millions in surplus funds. However, in its response the Office of the President did not provide evidence that refuted our conclusion. The Office of the President also stated that it intends to implement many of our recommendations; however, its conduct during this audit—namely interfering with our audit process—casts doubt on whether it will follow through on its intentions.

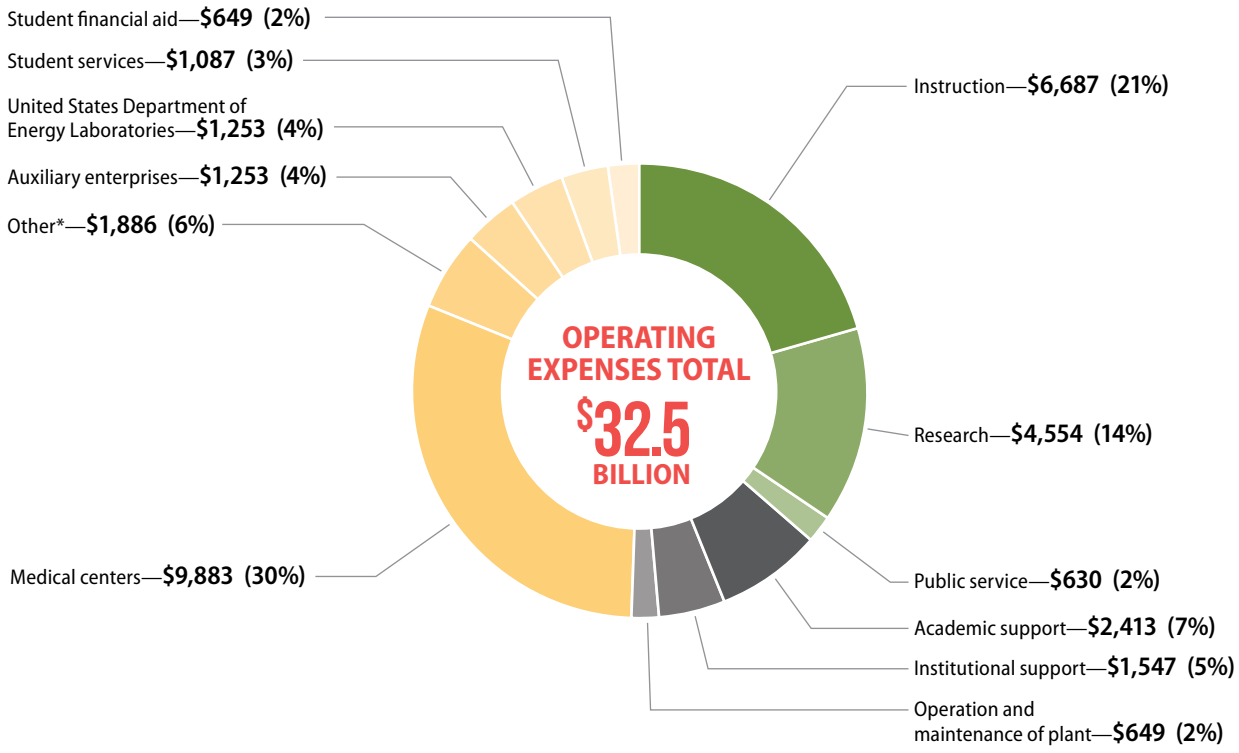
Due to the nature and number of concerns we identified in the course of this audit, we concluded that significant reforms are necessary to ensure the Office of the President makes prudent decisions that reflect the interests of those it serves. Beginning on page 121 we provide our perspective on the Office of the President's response to our report.

Introduction

Background

The Legislature founded the University of California (university) in 1868 as a public, state-supported, land-grant institution. It currently consists of 10 campuses, five medical centers, and its headquarters—the Office of the President. It is also involved in the management of three national laboratories. The university's mission is to serve society as a center for higher learning through teaching, research, and public service; and the university states in its accountability reports that access and affordability for California undergraduate students is among its highest priorities. As Figure 1 shows, out of the total of $32.5 billion in operating expenses for fiscal year 2015–16, the university spent about $6.7 billion (21 percent) on instruction, $4.6 billion (14 percent) on research, and $630 million (2 percent) on public service. Most of the remainder of its spending related to the operation of its medical centers, national laboratories, other auxiliary enterprises, and to its provision of administrative support and student services.

Figure 1
The University of California Had Operating Expenses of $32.5 Billion
Fiscal Year 2015–16
(in Millions)



Source: University of California's fiscal year 2015–16 annual financial report (unaudited *Facts in Brief* from the management discussion and analysis).

* These expenses primarily represent depreciation and noncash amortization.

Overseen by a Board of Regents, the University Is Constitutionally Autonomous

The California Constitution establishes the university as a public trust to be administered by the University of California Board of Regents (regents), an independent governing board with full powers of organization and government subject to limited legislative controls. The text box shows the composition of this governing board. Through orders and bylaws, the regents establish basic policies that guide the overall direction of the university. They also appoint the president to administer the university's affairs and operations, and they regularly review and approve the university's policies, financial affairs, tuition, and fees. The regents' committee on finance reviews the Office of the President's annual budget and recommends approval to the full board of regents, typically in July of each year. In addition, a body of university faculty representatives called the Academic Senate has responsibilities that include approving courses and determining the requirements for student admission.

University of California Board of Regents

The governing board comprises 26 members:

- With approval of the California State Senate, the Governor appoints 18 members.
- Seven individuals serve as ex officio members, including the Governor, the speaker of the assembly, and the president of the University of California.
- The Board of Regents appoints one student member.

Source: University of California Board of Regents.

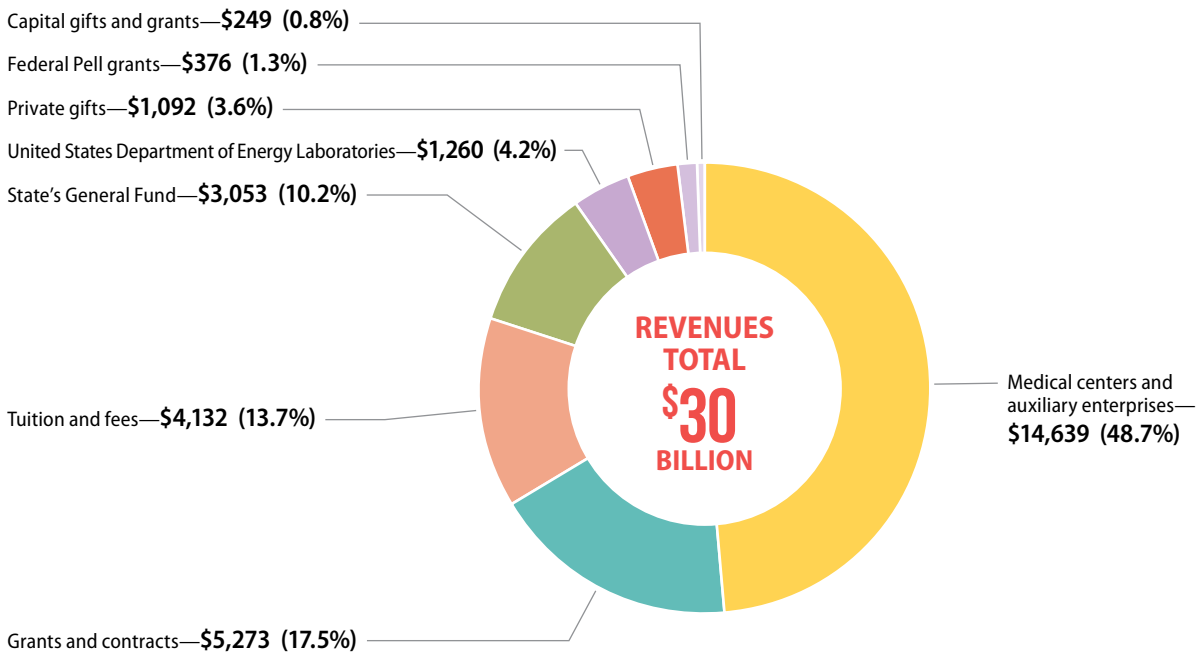
The university is subject to legislative oversight only in limited circumstances. California courts have stated that the broad powers the state constitution confers upon the university provide it general immunity from legislative regulation. However, the Legislature can specify provisions that the university must meet before it can spend state appropriations. As Figure 2 shows, appropriations from the State's General Fund constituted 10.2 percent of the $30 billion the university received in total revenue in fiscal year 2015–16. Although state appropriations as a percentage of the university's total revenues have been in decline over the last decade, this $3 billion is second only to tuition and fee revenues in terms of discretionary revenue because much of the university's remaining revenue is restricted either by grant and contract provisions or by commitments to its medical centers, laboratories, and auxiliary enterprises.

The Office of the President Provides Central Administrative Services and Manages Systemwide Initiatives on Behalf of Campuses

As the systemwide headquarters of the university, the university's Office of the President, which employed 1,667 staff in fiscal year 2015–16, serves two distinct functions for campuses: it provides certain central administrative services, and it manages systemwide initiatives that benefit multiple campuses. Examples of central administrative services include reporting at regents meetings, managing the university's retirement programs, and developing the

university's budget. The Office of the President asserted in its *Budget for Current Operations* that the centralization of these administrative services creates efficiencies by eliminating the need for campuses to individually provide them. Examples of systemwide initiatives—which the university sometimes refers to as *systemwide programs*—include the university's Education Abroad Program and online education platform. These initiatives are available to university students across multiple campuses.

Figure 2
The University of California Had Revenues of $30 Billion
Fiscal Year 2015–16
(in Millions)



Source: The University of California's fiscal year 2015–16 annual financial report (unaudited *Facts in Brief* from the management discussion and analysis).

The Office of the President also has a third role, referred to as *Office of the President Operations*. Essentially, this function encompasses a number of administrative tasks that the Office of the President performs to support its staff. These tasks include overseeing human resources, providing information technology assistance, and preparing and administering its own budget. To administer its day-to-day operations and serve the campuses, the Office of the President has organized its staff into 11 divisions. As an example,

the chief operating officer's division oversees the Office of the President's operations as well as information technology services and human resource services for the entire university system.

The Individual Campuses Conduct Additional Administrative Activities

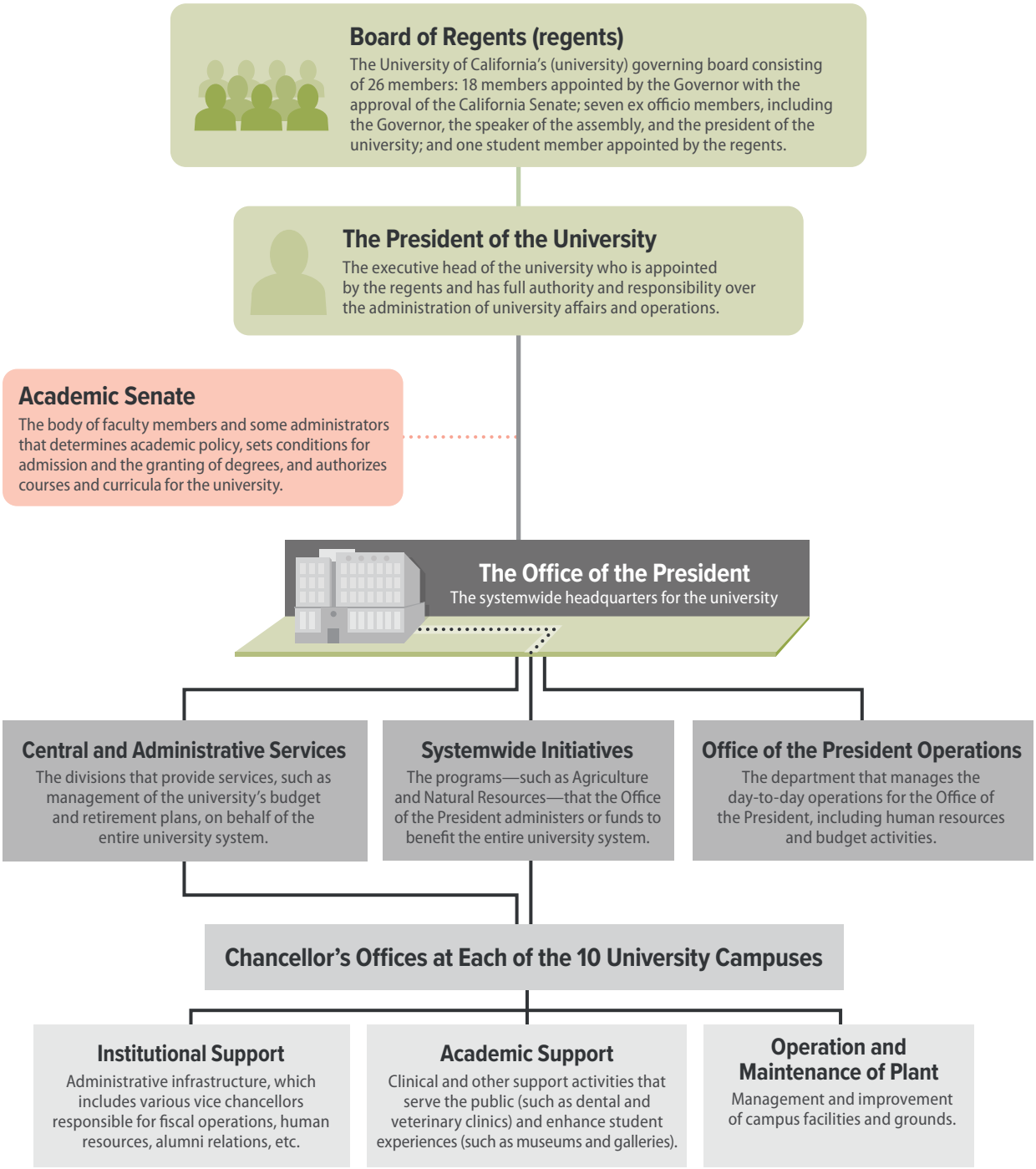
Although the Office of the President manages certain administrative functions centrally, the individual campuses also conduct administrative activities. Figure 3 shows the university's levels of administration. Each campus has a chancellor's office, which—with the support of various vice chancellors, provosts, and deans—oversees three broad categories of administration: institutional support, academic support, and operation and maintenance of plant (operations).

The university adopted these categories as a result of the uniform accounting structuring it uses, which is prescribed by the National Association of College and University Business Officers (NACUBO), a membership organization representing a variety of colleges and universities across the country. The NACUBO uniform accounting structure helps ensure accounting consistency among the university's campuses and also allows for standardized reporting of financial information from institutions of higher education nationwide. Despite its benefits, however, the NACUBO uniform accounting structure has some limitations. Specifically, it does not clearly define what should constitute a university's administrative costs, as we discuss in Chapter 3. As a result, accurately determining each campus's administrative costs is difficult, if not impossible.

To Pay for Its Discretionary Activities, the Office of the President Levies an Annual Financial Assessment on All University Campuses

To support its operations, the Office of the President requires campuses to pay an annual assessment that constitutes the majority of the Office of the President's discretionary revenue. The origin of the assessment is the Office of the President's 2011 *Funding Streams Initiative*, which aimed to simplify the university's financial activities, improve transparency, and create incentives for campuses to increase their revenues. Before the Funding Streams Initiative, the Office of the President collected campus revenues such as tuition and student fees, pooled that money with the annual state appropriation, and redistributed these funds to the campuses and itself. Under the Funding Streams Initiative, campuses generally keep their own revenues, and the Office of the President only distributes the state appropriation. However, the campuses must each pay an assessment that is intended to approximate its use of the systemwide services the Office of the President provides.

Figure 3
The University of California Has Multiple Levels of Administration



Source: California State Auditor's analysis of University of California governing documents and organizational charts.
Note: This graphic excludes administration of the university's medical centers and the Department of Energy laboratories.

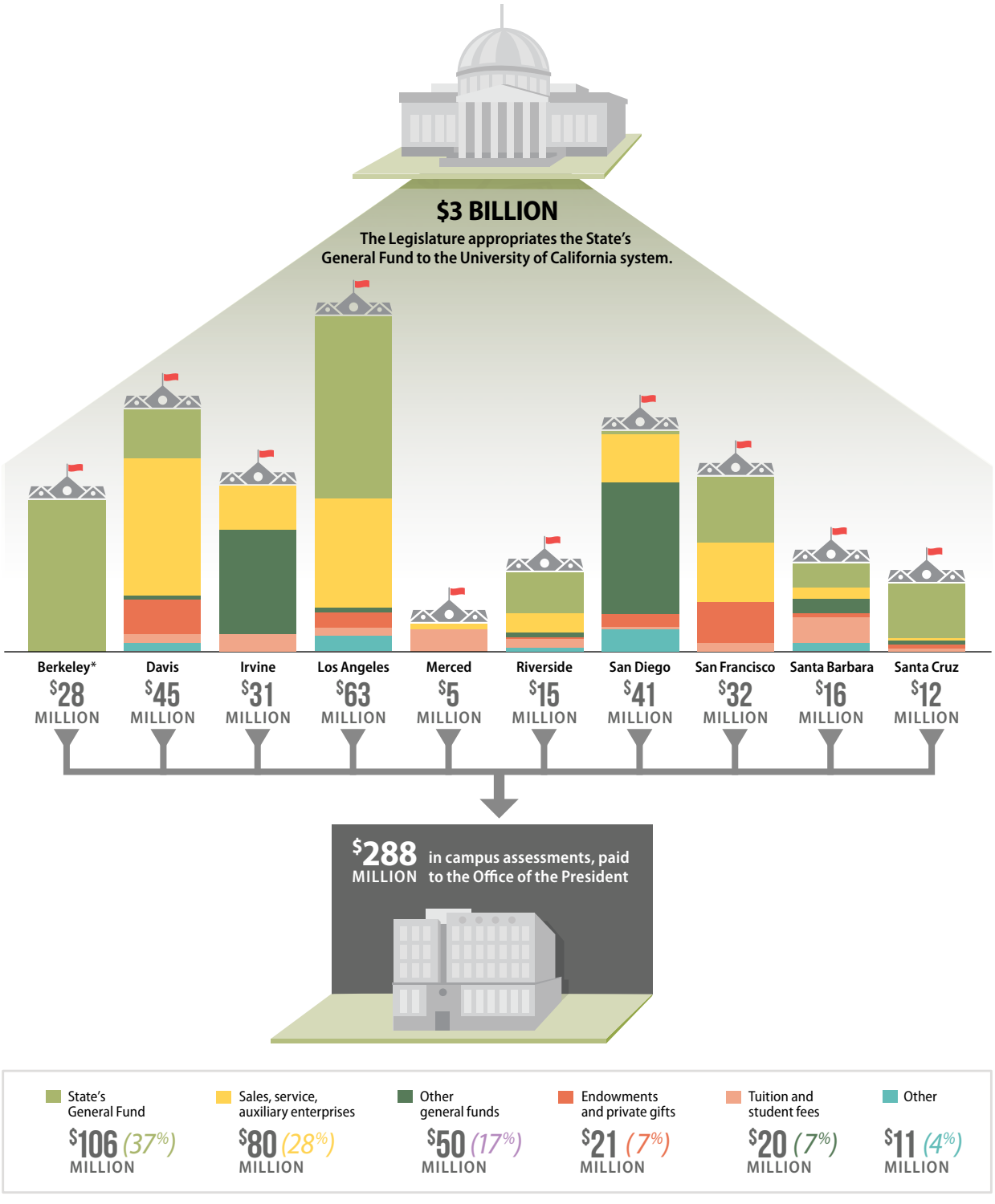
The Office of the President determines the assessment amount each campus must pay by first determining the total amount it needs to collect to support its operations and then multiplying this total by a particular percentage for each campus. The Office of the President determines the percentage it will use to calculate the amount each campus must pay by using three equally weighted factors:

- Total expenditures: The campus's percentage of the university's total campus expenditures.
- Total number of employees: The campus's percentage of the university's total number of employees.
- Total number of students: The campus's percentage of the university's total number of students.

Because the Office of the President gives campuses discretion to choose what sources they will use to pay the annual assessment, campuses may use a number of revenue sources for this purpose, including their allocations from the State's General Fund. As Figure 4 shows, the Legislature provided—and the Office of the President allocated to the campuses—about $3 billion from the State's General Fund in fiscal year 2015–16. The Los Angeles campus chose to pay the majority of its $63 million fiscal year 2015–16 assessment with its share of this appropriation, while the Davis campus paid its $45 million assessment with a mix of revenue from the State's General Fund, tuition and student fees, endowments and private gifts, and sales and service income. In total, the Office of the President collected $288 million in assessments from the campuses in fiscal year 2015–16, of which up to 37 percent—about $106 million—was paid using the State's General Fund appropriation.

The Office of the President uses the campus assessment to pay for its discretionary activities, which include its administrative services and the systemwide services and programs that it provides as the headquarters of the university. As Figure 5 on page 14 demonstrates, the campus assessment funded roughly 90 percent of the Office of the President's discretionary activities, which totaled $322 million in fiscal year 2015–16; and the remaining funds came from the university president's endowment and two smaller funds. In contrast, the Office of the President budgeted $316 million for restricted activities in the fiscal year 2015–16 budget it presented to the regents. It funds some of these activities using restricted sources such as grants that have corresponding conditions—grant funds may only be used for the grant's purposes—in order to receive the revenue. For example, the Office of the President receives funds from a tobacco tax that are to be used only to administer a breast cancer research program.

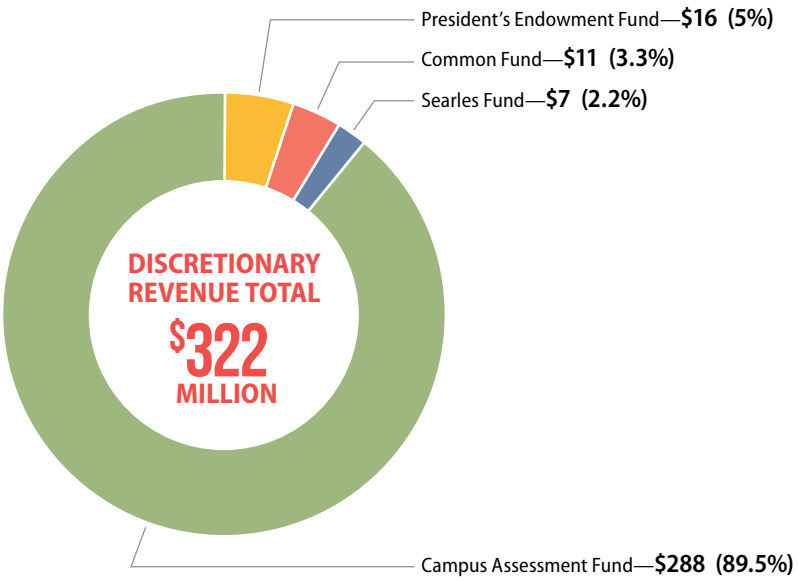
Figure 4
In Fiscal Year 2015–16, Campuses Paid the Office of the President $288 Million From Many Funding Sources



Source: California State Auditor's analysis of financial information provided by campuses for fiscal year 2015–16.

* The Berkeley campus pays its assessment from a fund that the university's account manager guidelines define as State General Funds. However, the Berkeley campus confirmed that although this fund contains mostly State General Funds, it also contains amounts from other sources, amounts which the Berkeley campus did not specify. Thus, the Berkeley campus paid up to $28 million of its fiscal year 2015–16 campus assessment with State General Funds.

Figure 5
The Campus Assessment Comprised 90 Percent of the Office of the President's Actual Discretionary Revenue in Fiscal Year 2015–16 (in Millions)



Source: California State Auditor's analysis of actual revenue data provided by the Office of the President.

Note 1: This figure does not include revenue sources that accounted for less than 1 percent of Office of the President's total discretionary revenue.

Note 2: Although the total campus assessment was $304 million in fiscal year 2015–16, the Office of the President received $288 million because campuses retained the remaining $16 million to pay for systemwide initiatives.

The Board of Regents Recently Approved a Student Tuition Increase

As numerous media outlets have reported, university students, stakeholders, and lawmakers have criticized the regents' recent decision to increase student tuition. Specifically, between academic years 2006–07 and 2011–12, the university nearly doubled resident tuition, from $6,141 to $12,192 per year. After keeping resident tuition relatively steady for the last five years, the president recommended a 2.7 percent increase in tuition and fees for academic year 2017–18, which the regents approved in January 2017. Some stakeholders have criticized this decision because they believe that the Office of the President has not done enough to cut administrative costs. The Public Policy Institute of California (PPIC) published a survey of California residents in December 2016, and the results echo these concerns. Specifically, when asked how to improve California's higher

Results of Higher Education Survey

Question: To significantly improve California's public higher education system, which of the following do you agree with most?

- Use funds more wisely and increase state funding: 49 percent.
- Use funds more wisely: 36 percent.
- Increase state funding: 13 percent.
- Don't know: 3 percent.

Source: *Californians and Higher Education*, Public Policy Institute of California, December 2016.

education system, 85 percent of survey respondents indicated that higher education should use its funds more wisely. As the text box on the previous page shows, the majority of these individuals coupled spending wisely with increasing state funding.

As we discuss in Chapter 1, the portion of its budget that the Office of the President discloses to the regents for approval increased by nearly $100 million (about 17 percent) from fiscal years 2012–13 through 2015–16. Given that the campuses fund many of the Office of the President's activities through the annual assessment, this significant budget increase has likely contributed to the university's need to raise student tuition. The remainder of this report examines the Office of the President's budget, including its budget preparation and approval process, as well as the university's personnel costs.

Scope and Methodology

The Joint Legislative Audit Committee (Audit Committee) directed the California State Auditor to conduct an audit of the Office of the President's budget and staffing processes. The analysis the audit committee approved contained nine separate objectives. We list the objectives and the methods we used to address them in Table 1.

Table 1
Audit Objectives and the Methods Used to Address Them

	AUDIT OBJECTIVE	METHOD
1	Review and evaluate the laws, rules, and regulations significant to the audit objectives.	Reviewed relevant laws, regulations, and other background materials applicable to the Office of the President's budget and staffing levels.
2	Identify the number and cost of the Office of the President staff—and any other costs related to its administrative functions—over at least the past five fiscal years. Obtain and assess the methods that the Office of the President uses to determine its budget and staffing levels. Determine what factors have influenced its budget and staffing levels over at least the past five fiscal years.	• Obtained and analyzed staffing data from fiscal years 2010–11 through 2015–16. • Assessed employee staffing costs such as pensions and travel expenses. • Interviewed Office of the President staff regarding its processes for developing its annual budget and staffing levels. • Obtained and analyzed the Office of the President's budget and expenditures from fiscal years 2012–13 through 2015–16. The Office of the President implemented its budget development system in fiscal year 2012–13. Before it implemented this system, the Office of the President tracked its budget on spreadsheets it did not retain. • Tested a selection of undisclosed budget expenditures to determine whether Office of the President management approved them.
3	Identify whether any organizational restructuring has taken place at the Office of the President over at least the past five fiscal years. Assess how these changes affected its budget and funding structure and whether these changes have met the goals of the restructuring, such as budget transparency and simplifying the overall funding structure.	• Identified two organizational restructurings—the Funding Streams Initiative, which the Office of the President implemented in fiscal year 2011–12, and an internal reorganization that it implemented in fiscal year 2014–15. • Determined the goals of the organizational restructurings and assessed the Office of the President's status in meeting those goals. • Assessed the impact these two restructurings had on staffing levels, the Office of the President's budget, and its funding.

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	AUDIT OBJECTIVE	METHOD
4	Assess the methods that the Office of the President uses to determine the budget and staffing levels for systemwide initiatives. Determine whether budget and staffing decisions for systemwide initiatives affect other areas of its budget and staffing levels.	• Requested a list of systemwide and presidential initiatives and compiled the total number of initiatives from this list and other sources such as University of California Board of Regents (regents) minutes, interviews, and the Office of the President's budget data. We had to estimate the total number and cost of initiatives because the Office of the President does not systematically track them. • Interviewed Office of the President staff regarding the steps it has taken to develop a workforce plan. • Assessed separately the budget and staffing levels for two systemwide initiatives: Agriculture and Natural Resources (ANR) and the Education Abroad Program (EAP). The EAP's budget became part of the Office of the President's budget in fiscal year 2014–15, while ANR was included in the Office of the President's budget for the entire audit period. Both ANR and EAP track their budgets separately from the Office of the President, present budget to actual comparisons, and maintain strategic plans. ANR budgets expenditures from the campus assessment. In the report, we describe ANR's best practices because of their applicability to the Office of the President's practices. Note that we base our text and recommendations on the Office of the President's processes and not the separate processes for these initiatives, unless otherwise noted.
5	Review a selection of position descriptions, job duty statements, and salaries over at least the past five fiscal years to assess whether the number of staff employed at the Office of the President, and their respective cost, is justified. Review the reasonableness, in terms of cost and need, of the services that the Office of the President provides to the campuses.	• Analyzed staffing data to see changes in the number of staff and staff salaries since fiscal year 2010–11. Note that staffing analyses exclude the Agriculture and Natural Resources employees unless otherwise noted. • Selected 10 executive level staff positions and compared them to comparable state and California State University (CSU) executives. • Selected 10 administrative staff positions and compared them to comparable state and CSU employees. • Assessed the Office of the President's process for establishing salaries. • Interviewed Office of the President staff regarding the steps it has taken to develop a workforce plan. • Sent two surveys to each of the University of California's (university) 10 campuses. The first survey asked campuses whether they used Office of the President services and programs. Next, the survey asked the campuses to rate the quality of those services and programs. The second survey asked campuses about the annual assessment they pay the Office of the President and whether the amount of the assessment was justified. However, because of the Office of the President's interference in our survey, audit standards prohibit us from using this work to inform findings or conclusions.
6	For a selection of university campuses, to the extent possible, over at least the past five fiscal years, determine the following for each: (a) The total cost and staffing levels related to administrative activities. (b) Whether there is a correlation between changes in campus administrative activities, including budget and staffing levels, with changes in the Office of the President's administrative activities. (c) If applicable, the number and type of administrative functions that are duplicative of the Office of the President's functions, and the cost of those duplicative functions at the campus and the Office of the President.	• Interviewed staff at the Berkeley, San Diego, and Santa Cruz campuses regarding how they define and track administrative activities. • Consulted the National Association of College and University Business Officers to define *administrative costs*. • Compared administrative costs at the 10 campuses to the Office of the President. • Intended to use survey results to interview campus staff about potentially duplicative services. However, because of the Office of the President's interference in our survey, audit standards prohibit us from using this work to inform findings or conclusions. • Compared staffing levels at the 10 campuses to those at the Office of the President.
7	Assess whether the oversight provided by the Office of the President ensures that campuses spend funds in accordance with legislative, statewide, and/or university priorities.	• Interviewed campus and Office of the President staff regarding oversight of campus spending. • Reviewed administrative expenditures reported by campuses. • Obtained information from campuses that showed the fund sources they used to pay the campus assessment. • Reviewed budget allocation letters the Office of the President sent to campuses. These letters contain general guidelines for how campuses should spend their funds; however, the Office of the President asserted that campuses can generally spend their unrestricted fund sources as they see fit.

	AUDIT OBJECTIVE	METHOD
8	To the extent possible, compare administrative costs and functions at the Office of the President with those of comparable public universities.	Analyzed the Office of the President's budget and staffing data, and used publicly available information to compare the cost of central administration offices at other higher education institutions.
9	Review and assess any other issues that are significant to the audit.	• Interviewed the Office of the President's independent financial auditors. • Assessed the budget information the Office of the President provides to the regents, the Legislature, and the public. • Reviewed government and higher education budgeting best practices.

Sources: California State Auditor's analysis of state law, planning documents, and information and documentation identified in the column titled *Method*.

Assessment of Data Reliability

In performing this audit, we obtained electronic data files extracted from the information systems listed in Table 2. The U.S. Government Accountability Office, whose standards we are statutorily required to follow, requires us to assess the sufficiency and appropriateness of computer-processed information that we use to support findings, conclusions, or recommendations. Table 2 describes the analyses we conducted using data from these information systems, our methods for testing, and the results of our assessments. Although these determinations may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.

Table 2
Methods Used to Assess Data Reliability

INFORMATION SYSTEM	PURPOSE	METHOD AND RESULT	CONCLUSION
University of California Office of the President's Corporate Data Warehouse and Decision Support System Employee appointment and earnings history for fiscal years 2010–11 through 2015–16	To determine the number of Office of the President employees, their positions, and their earnings.	We performed data-set verification and electronic testing of key data elements and did not identify any significant issues. To gain some additional assurance, we compared the total number of full-time equivalent employees in the data to the total number of employees the Office of the President reports on its public website and found no material differences. However, we did not perform full accuracy and completeness testing of these data because they are from partially paperless systems, and thus, not all hard-copy documentation was available for review. Alternatively, following U.S. Government Accountability Office guidelines, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews.	Undetermined reliability for this audit purpose. Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.

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INFORMATION SYSTEM	PURPOSE	METHOD AND RESULT	CONCLUSION
IBM Cognos TM1 Budget Development System The Office of the President's budgeted and actual expenditure data for fiscal years 2012–13 through 2015–16	To determine the Office of the President's total expenditures, and to compare budget allocations to actual expenditures.	We performed data-set verification procedures and electronic testing of key data elements and did not identify any significant issues. We did not perform accuracy and completeness testing on these data because the system is a paperless system. Alternatively, following U.S. Government Accountability Office guidelines, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews. To gain some assurance over the budget allocation data, we compared the total amount of the disclosed budget for each fiscal year to the Office of the President's restated budget total presented to the Board of Regents and found some immaterial differences in the total budget amounts. To gain some assurance over the expenditures data, we reconciled expenditures data for one fiscal year from the budget development system with expenditures reported through the University of California's (university) corporate financial reporting system, which is used to prepare the university's audited financial statements, and found some immaterial differences. However, some systemwide expenditures were reported at the same location as the Office of the President's expenditures in the university's corporate financial reporting system, creating some difficulties in distinguishing between the Office of the President's expenditures and systemwide expenditures. We discuss this issue in Chapter 1.	Undetermined reliability for these audit purposes. Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.
University of California, Los Angeles' Financial System The Office of the President's general ledger transaction data for its unrestricted funds for fiscal years 2011–12 through 2015–16	To make a selection of financial transactions from the Office of the President's general ledger. To determine expenditures related to selected travel expense claims. To determine the amount of meal expenses paid for by the Office of the President's campus assessment fund.	We did not perform accuracy and completeness testing on these data because the system is a paperless system. Alternatively, following U.S. Government Accountability Office guidelines, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost-prohibitive, we did not conduct these reviews. To gain some assurance over the accuracy of the financial system, we judgmentally selected 21 high-dollar value transactions and found that the selected transaction values matched to the amounts in source documentation.	Undetermined reliability for these audit purposes. Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.
University of California Office of the President's Corporate Financial Reporting System	To determine the amount of ending fund balances for funds used in the Office of the President's budget for fiscal years 2011–12 through 2015–16.	We performed data-set verification procedures and electronic testing of key data elements and did not identify any significant issues. We did not perform accuracy and completeness testing on these data because the system is a paperless system. Alternatively, following U.S. Government Accountability Office guidelines, we could have reviewed the adequacy of selected system controls that include general and application controls. However, because it was cost prohibitive, we did not conduct these reviews. We have some assurance over the data because it was extracted from the same information system used to prepare the University of California's audited financial statements.	Undetermined reliability for these audit purposes. Although this determination may affect the precision of the numbers we present, there is sufficient evidence in total to support our audit findings, conclusions, and recommendations.

Sources: California State Auditor's analysis of various documents, interviews, and data obtained from the university.

Chapter 1

THE OFFICE OF THE PRESIDENT DID NOT DISCLOSE $175 MILLION IN BUDGET SURPLUSES, AND IT LACKS SAFEGUARDS TO ENSURE ACCOUNTABILITY OVER ITS SPENDING

Chapter Summary

The budget for the University of California (university) Office of the President has grown without adequate justification. In fact, in each of the past four fiscal years, the Office of the President presented an annual budget to the University of California Board of Regents (regents) for approval that significantly overstated the amount of funds it required. Further, the Office of the President did not disclose to its stakeholders—including the regents—that it had amassed $175 million in budget surpluses as a result of its inflated budgets. By reducing the size of its budgets to better reflect its actual spending, the Office of the President could have reduced the assessment it annually levied on campuses for its services, allowing the campuses to instead spend those funds for the benefit of students. The Office of the President has itself acknowledged the campuses' need for such additional funding: it cited chronic state underfunding when it asked the regents to approve an increase in student tuition and fees in 2017.

The Office of the President has further hindered the ability of the regents and its other stakeholders to fully understand or make informed decisions about its budget and finances by issuing high-level budget reports that do not adequately account for its operations. As a result of these convoluted and misleading budgets, the Office of the President has received little meaningful oversight of its finances, increasing the risk that its spending decisions may not fully reflect the university's priorities, such as access and affordability for California undergraduate students. We recommend that the Office of the President adopt the best practices typical of government and higher education entities to ensure that its budget provides accurate and transparent information about its spending decisions to its stakeholders, including the regents, the campuses, the Legislature, the students, and the public.

The Office of the President's Budgets Are Misleading and Do Not Disclose Its Significant Budget Surpluses

For each of the past four years, the Office of the President requested that the regents approve budgets that significantly exceeded the amounts it was likely to spend. The Office of the President's budget surpluses accumulated in two reserves—restricted and discretionary. We define these as well as other key budget terms we use throughout this chapter

in Table 3. The Office of the President did not disclose the existence of these two reserves, which totaled about $175 million as of June 30, 2016, to the regents, the Legislature, or the public. Further, it did not disclose the annual budgets it created to spend these funds. In fact, its poor tracking and oversight of the expenditures it made from its reserves put the funds at risk for wasteful spending. Our analysis suggests the Office of the President could use from $38 to $175 million from its fiscal year 2015–16 reserves for other university priorities, depending on the results of a review of its funds and commitments.

Table 3
Key Budget Terms

Campus assessment	A charge the Office of the President annually levies against campuses to pay for the Office of the President's services and administration.
Carryforward expenditures	Expenditures made in the current fiscal year from funding that was approved in a prior fiscal year.
Decision memos	Documents used by the Office of the President's staff to request discretionary funds for unanticipated or one-time project expenses.
Disclosed budget	The planned spending that the Office of the President presents to the Regents of the University of California (regents). The Office of the President views spending in this budget as ongoing and internally refers to this budget as its *permanent budget*.
Discretionary funds	Unrestricted funds that the Office of the President can generally use for any purpose.
Discretionary reserve	Reserves from discretionary budget surpluses that the Office of the President annually sweeps for distribution to other budgetary priorities. Discretionary reserves can be used to fund any program or project at the Office of the President or at the campuses.
Pass-through funds	Funds, such as research grants, that the Office of the President receives and then sends to campuses or external organizations.
Restricted funds	Funds that are generally subject to limitations of use, such as state funds that can only be used for research; however, the Office of the President internally places restrictions on some funds, such as its systemwide administrative cost recovery fund. The Office of the President may also remove some restrictions on funds, as it did with the Searles Fund.
Restricted reserve	Reserve from restricted budget surpluses, which are generally subject to limitations of use.
Undisclosed budget	The planned spending that the Office of the President does not present to the regents. The Office of the President spends these funds for what it asserts are unanticipated expenses, one-time projects, or carryforwards, and internally refers to this budget as its *temporary budget*.

Sources: California State Auditor's analysis of Office of the President budget documentation and interviews with the Office of the President's budget director.

The Office of the President Did Not Inform Its Stakeholders About Its $175 Million in Budget Surpluses

The Office of the President maintains two budgets: a budget it presents to the regents each year for approval, which we refer to as the *disclosed budget*, and a budget it does not present to the regents or other stakeholders, which we refer to as the *undisclosed budget,* as shown in

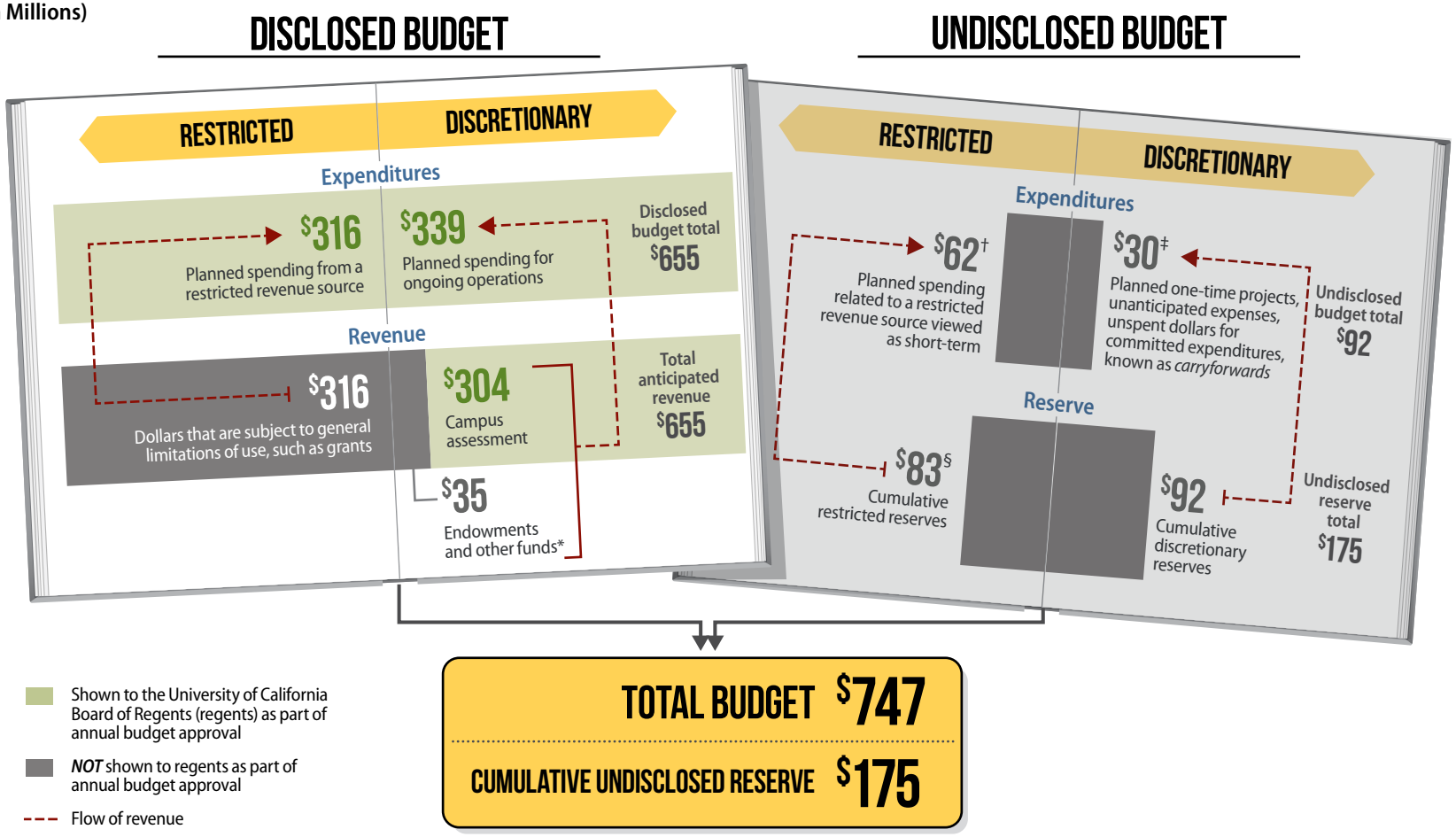
Figure 6 on the following page. From fiscal years 2012–13 through 2015–16, the disclosed budget that the Office of the President presented to the regents ranged from $557 million to $655 million. However, as Figure 7 on page 23 shows, the Office of the President's total budget—when accounting for both the disclosed and undisclosed budget—ranged from $638 million to $747 million during those same years. The combined disclosed and undisclosed budgets for the Office of the President grew faster than inflation, in part because of programs it funded using its undisclosed budget, such as a $1.3 million subsidy program to reduce employee contributions to the university's health insurance program and $2.2 million for its cybersecurity program. The consistent growth in the Office of the President's spending makes the lack of transparency of its budget to its stakeholders particularly troubling.

The Office of the President's undisclosed budget represents, in part, its planned spending from the undisclosed budget surpluses that it has accumulated annually over time. Over the past four years, the Office of the President has spent an average of $97 million less per year than it planned to spend. As a result of these budget surpluses, the Office of the President's undisclosed restricted and discretionary reserves have both grown. The Office of the President has amassed more than $175 million in undisclosed budget surpluses since fiscal year 2012–13, an increase of $74 million. Figure 6 shows that as of fiscal year 2015–16, it had $83 million in its restricted reserve and $92 million in its discretionary reserve. According to its undisclosed budget, the Office of the President planned to spend about $92 million in fiscal year 2015–16—$62 million in restricted funds and $30 million in discretionary funds. These amounts are in addition to its other planned spending of $655 million, which it disclosed to the regents for that same fiscal year.

The Office of the President's failure to disclose a significant portion of its budget is of concern because the regents make important decisions based upon the information the Office of the President presents to them. The impact of the undisclosed budget is not only that the Office of the President costs more than it has publicly reported but also that it is able to spend more than the regents approve each year. In fact, for fiscal year 2015–16, the Office of the President had up to $830 million of funds available to spend but only presented a budget totaling $655 million to the regents. As Figure 8 on page 24 shows, a comparison of the Office of the President's disclosed budget to its actual expenditures demonstrates that the Office of the President overspent its approved budgets for each of the fiscal years we reviewed. Nevertheless, the accumulation of undisclosed reserves allows the Office of the President to overspend on its disclosed budget and continue to maintain sizeable reserves.

The impact of the undisclosed budget is not only that the Office of the President costs more than it has publicly reported but also that it is able to spend more than the regents approve each year.

Figure 6
The Office of the President Has Not Disclosed a Significant Portion of Its Budget to the Board of Regents, the Legislature, and the Public
Fiscal Year 2015–16
(in Millions)



Sources: California State Auditor's analysis of the Office of the President's budget processes, fund balances, and data obtained from the Office of the President's budget development system.

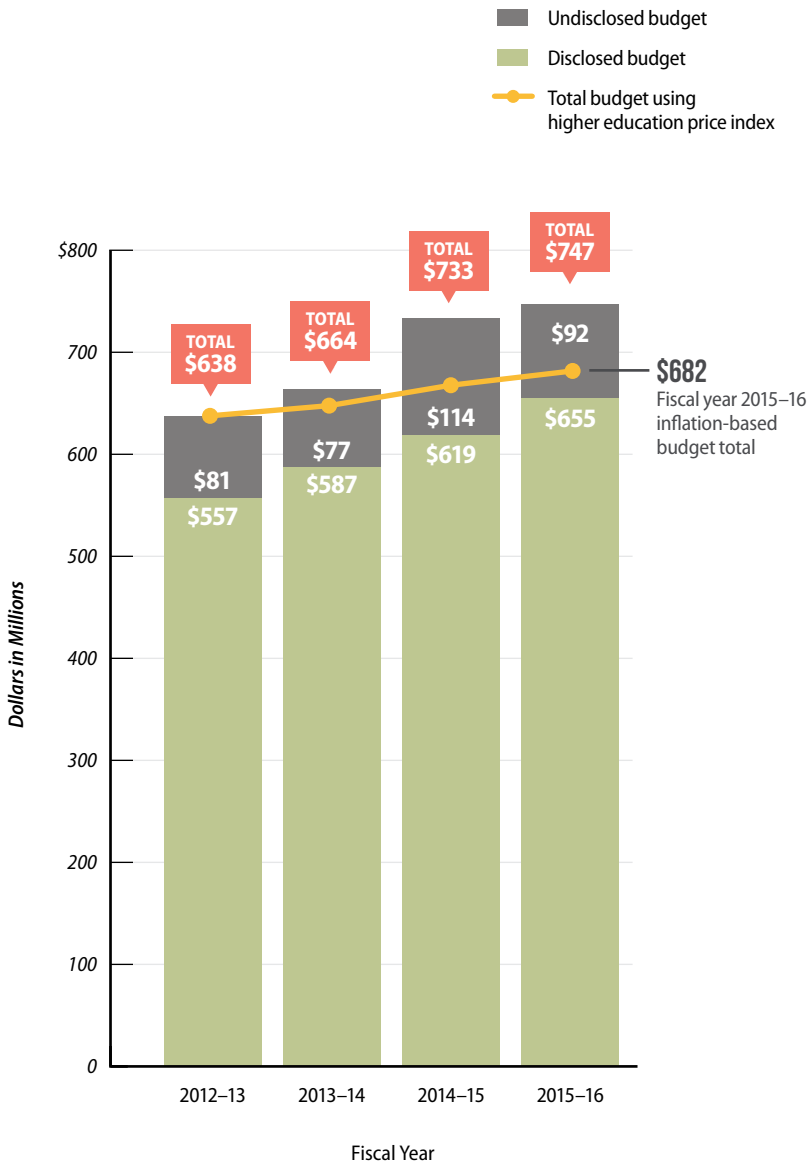
* Endowments and other funds include the Searles Fund, President's Endowment Fund, Common Fund, investment pool funds, and others.

† In addition to being funded by the restricted reserve, the restricted undisclosed budget is also funded by restricted revenues that the Office of the President considers to be temporary.

‡ Some of these expenditures may have been presented to the regents outside of the context of annual budget approval. For example, the Office of the President reported on the progress of a discretionary project funded via the undisclosed budget, such as its cybersecurity program. However, the Office of the President did not present the total dollar amount or the sources used to pay for this initiative to the regents as part of its annual budget approval.

§ According to the Office of the President's budget director, the restricted reserves include $13 million in extramural funds, such as contracts and grants, which were not included in the university's financial statements because the university may not fully realize those funds.

Figure 7
From Fiscal Years 2012–13 Through 2015–16, the Office of the President's Total Budget Outpaced Inflation by $65 Million



Sources: California State Auditor's analysis of the Office of the President's budgets presented to the Board of Regents, budget data obtained from the Office of the President's budget development system, and the higher education price index.

Note: The Office of the President could not provide comparable data for its fiscal year 2011–12 budget because it was not yet using the Budget Development System and did not retain the data that was used to prepare that year's budget.

Although the Office of the President's spending of its undisclosed reserve on its undisclosed budget does not directly violate the regents' budget policy, its actions do not align with the intent of a regents' policy as explained by the individual regents who

voted to recommend its approval. Specifically, the regents' policy states that the Office of the President shall not spend funds until the regents approve the budget each year. However, the minutes from November 2006, when the regents' committee on finance recommended approval of this policy, and which the entire Board of Regents later approved, states that the Office of the President shall have no authority to expend funds related to its operations for that fiscal year unless and until the regents approve the budget each year. Moreover, in approving the recommendation of this policy, the individual committee members remarked that it was a positive step to increase transparency, test the Office of the President's efficiency, measure its productivity, and make sure the university's "bloated bureaucracy" was trimmed. The Office of the President's decision not to disclose its entire budget each year does not allow the regents to fulfill those objectives.

Figure 8
The Office of the President's Actual Spending Exceeded the Budget Approved by the Board of Regents
(in Millions)

Sources: California State Auditor's analysis of the Office of the President's budget presented to the regents and obtained from the Office of the President's budget development system.

* The Office of the President does not separately identify expenditures from the disclosed and undisclosed budgets. Thus, the actual expenditures include spending from both budgets.

When we discussed this policy and the corresponding minutes with the Office of the President, it stated as justification for not disclosing to the regents the planned spending from the undisclosed budget that this budget represents carryforward expenditures for activities and programs and that the regents had previously approved these amounts. However, based on documents the Office of the President's budget office provided, carryforward expenditures only represented 6 percent to 22 percent of the total undisclosed discretionary budget amount from fiscal years 2012–13 through 2015–16. The remaining undisclosed reserve funds were spent on one-time projects and unanticipated expenses. Thus, most of the spending in this budget was for purposes that the regents had not explicitly approved. Further, the Office of the President's chief financial officer stated that he believed a presentation of these funds would not be material to the regents because they represent only a small fraction of the overall budget. Finally, the Office of the President could provide no formal authority for spending outside of the budget the regents had approved.

Most of the spending from the undisclosed budget was for purposes the regents had not explicitly approved.

The Office of the President spent its undisclosed reserves for a variety of purposes. According to the director of the Office of the President's budget (budget director), the Office of the President can use the discretionary reserve to fund any program or project at the Office of the President or at the campuses. In contrast, the Office of the President's use of the restricted reserve is generally subject to limitations because the reserve may contain, for example, state funds that the Legislature appropriated for a specific purpose. However, the Office of the President has flexibility in spending parts of its restricted reserve because some of these restrictions are self-imposed. For instance, although the Office of the President considers its systemwide administration cost recovery fund to be restricted because it is composed of fees charged to endowments in order to recover the reasonable and actual costs related to administration of those endowments, the Office of the President spends a significant portion of this fund on marketing. We attempted to analyze the purposes for which the Office of the President spent its undisclosed reserve, but the Office of the President does not differentiate between its expenditures that are paid for with its disclosed budget and those paid for with its undisclosed budget; instead, it only tracks total expenditures. We were able to identify the planned spending and found that the Office of the President planned to spend undisclosed funds for varied purposes as shown in Table 4 on the following page.

The Office of the President disagrees with the terminology we are using to describe the undisclosed budget. In particular, the Office of the President asserts that it has publicly disclosed this budget and the projects it funds from this budget. However, we disagree with this assertion. As a public entity and an institution

of higher education, the Office of the President has a responsibility to spend its funds in a transparent and prudent manner. Nonetheless, since at least fiscal year 2012–13, the Office of the President has not fully or consistently shared in a systematic manner its undisclosed budget with the regents, the Legislature, or the public.

Table 4
The Office of the President's Planned Spending From the Undisclosed Budget Includes a Number of Different Types of Expenditures
Fiscal Years 2012–13 Through 2015–16

	FISCAL YEAR			
EXAMPLES OF PLANNED SPENDING	2012–13	2013–14	2014–15	2015–16
Advertising, communications, and brand management	$3,700,000	$815,000	$77,000	$76,000
Historically Black Colleges and Universities Initiative*	785,000	—	2,191,000	2,271,000
Multi-campus research program institutes	—	—	2,610,000	—
Nonresident recruiting	686,000	490,000	490,000	97,000
President's Postdoctoral Fellowships Program	—	—	2,685,000	3,809,000
President's residence	252,000	252,000	179,000	179,000
Printer Initiative and Print Management Program	533,000	84,000	70,000	—
Sexual Violence Sexual Assault Task Force	—	—	5,887,000	3,110,000
Staffing costs†	95,000	303,000	1,115,000	687,000
Transcript Evaluation Services	291,000	1,389,000	1,048,000	—
University of California Merced faculty start-up support	—	—	5,000,000	5,000,000
University of California Riverside medical school start-up support	2,000,000	2,000,000	2,000,000	2,000,000

Sources: California State Auditor's analysis of the Office of the President's budget approval documents and data obtained from the Office of the President's budget development system.

* The Historically Black Colleges and Universities (HBCU) Initiative provides funding to support HBCU students to participate in summer research activities located at a University of California campus, as well as funding for doctoral students at the university who have graduated from HBCUs.

† Staffing costs include costs for firms to search for executive-level candidates, performance bonuses, $49,000 for staff appreciation including a breakfast, employee salary increases, contract positions, and $2,000 spent on a retirement party.

The Office of the President also asserted that the term *undisclosed* implied intent to conceal this budget which, from its perspective, was not the case. The Office of the President further stated that staff discuss the undisclosed budget at length internally within the Office of the President and document those discussions, which would be available to the public via a public records act request. However, when we asked the Office of the President to furnish documents that demonstrated that it—at any point—had explicitly shared its undisclosed budget via public statements or public records act requests, it could not convincingly do so. Specifically, the documents the Office of the President identified included only two statements that it made over the past five years that vaguely refer to the Office of the President's undisclosed budget, as shown in the text box. These two statements would not give a stakeholder the ability to determine that the Office of the President has an additional budget in which it records tens of millions

of dollars in planned spending each year. Furthermore, these documents were included in the materials presented to the regents' committee on finance, rather than as part of the presentation to the entire Board of Regents.

The Office of the President also claimed that it presents the projects and programs via its undisclosed budget to the regents and online; however, based on our review, these documents are not complete. In fact, although the materials the Office of the President provided demonstrate it publicly described many projects since fiscal year 2012–13, none of these adequately clarified that the projects were funded using the undisclosed budget. The Office of the President asserts that it did not intend to conceal its undisclosed budget; nevertheless, over the four-year period we reviewed, it consistently made the decision not to include this spending in the budgets it presented to the regents or in the descriptions of the projects it funded with its undisclosed budget. Merely discussing the undisclosed budget within the Office of the President falls short of providing the type of transparency we believe is necessary for stakeholders to make sound decisions.

Statements About the Undisclosed Budget

- "The Office of the President continues to draw down its own carryforwards and reserves in a responsible manner and to fund, on behalf of the campuses, systemwide or campus-based programs and other systemwide obligations. The total expended over the last two fiscal years for these purposes approaches $125 million, an amount that otherwise would have been largely shouldered by the campuses."
- "Comprehensiveness. The Office of the President budget has reconciled funding into one consolidated budget… [which includes] ongoing funding previously budgeted as temporary."

Sources: The Board of Regents' committee on finance action items related to the Office of the President's fiscal year 2012–13 and fiscal year 2013–14 budgets.

In addition to not informing the regents about the existence of the undisclosed budget and reserves, the Office of the President's budget does not provide the regents with the information that would allow them to fully understand the magnitude of its spending. As Figure 6 on page 22 shows, the Office of the President's fiscal year 2015–16 budget presentation to the regents did not include other key components of its annual spending plans, including the following:

- $316 million in projected revenues from restricted sources.
- $35 million in projected revenues from endowments and other funds.
- Its intention to use this $35 million to fund part of the disclosed discretionary budget.

Further, the budget inappropriately included $184 million in pass-through funds that the Office of the President sent to campuses, even though the use of these funds is restricted and they are not spent by the Office of the President. Examples of pass-through funds include patent royalties paid to inventors and state contract funds for research programs. These pass-through funds convolute the Office of the President's total budget, making it difficult to understand its true operating costs. A more transparent budget presentation would separate pass-through funds from the Office of the President's actual operating expenditures.

The Office of the President's budget presentation also makes it difficult for the regents to discern the amount of the budget increases that they approve each year. For example, the Office of the President's total budget for fiscal year 2015–16 was $55 million more than it actually spent in fiscal year 2014–15. However, because the Office of the President did not provide the regents with its actual fiscal year 2014–15 expenditures and instead only provided what it planned to spend in that previous fiscal year—which turned out to be overestimated—the regents believed they were approving a $28 million dollar increase.[1] Further, if the Office of the President had provided the prior fiscal year expenditures, the regents would have known that the Office of the President spent more in the prior year than the regents had approved. Consequently, we question whether the regents would have approved the Office of President's fiscal year 2015–16 budget—or the Office of the President's requested $10 million increase to the campus assessment, as we discuss in the next section—if they had known its actual expenditures in fiscal year 2014–15.

After we asked about its budgeting practices, the Office of the President systemwide controller told us that it began creating the temporary budget [undisclosed budget] as a result of the state budget process and that it had maintained the process because it had always budgeted in that manner. When we asked about the Office of the President's failure to base its budgets on the current year's estimated actual expenditures, its management asserted that they would consider using actual expenditures as the basis for future budget planning. However, its management expressed concern that basing budgets on actual expenditures would create incentives for the Office of the President's divisions to spend their full budgeted amounts each year so as not to lose their budget allocations for the following year.

We do not consider the Office of the President's concern to be valid because it annually sweeps unused discretionary budget allocations into a discretionary reserve, a practice that already could encourage its divisions to spend their entire budget allocations. The Office of the President has dealt with this potential problem by allowing its divisions to keep 5 percent of their unused discretionary budget allocations and by implementing a carryforward process that allows divisions to request that a portion of their unused allocations be carried forward into the next year. The Office of the President should base future budget planning on its actual expenditures to improve the accuracy of its estimated budgets, cut unnecessary spending, and reduce the financial burden the campus assessment places on the campuses.

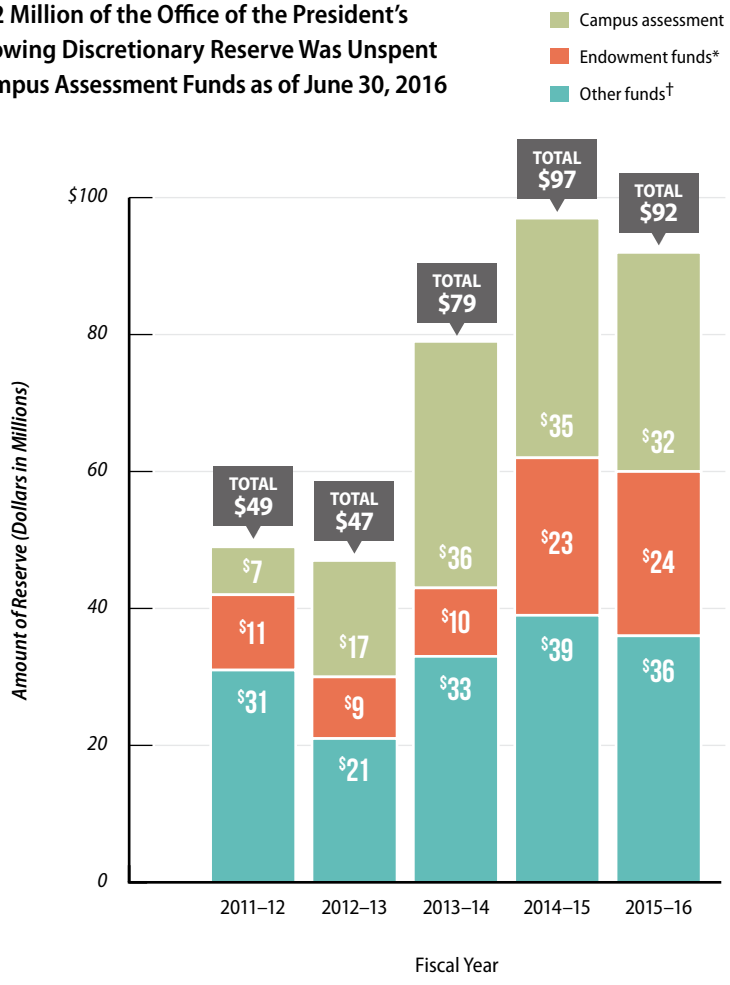
The Office of the President should base future budget planning on its actual expenditures to improve the accuracy of its estimated budgets, cut unnecessary spending, and reduce the financial burden the campus assessment places on the campuses.

[1] The Office of the President restated its 2014–15 budget, increasing it from $619 million, as shown in Figure 8 on page 24, to $627 million.

The Office of the President Has Overcharged Campuses and Made Certain Spending Decisions That May Not Reflect the Campuses' Best Interests

The Office of the President accumulated its significant reserves in large part because it calculates the campus assessment amount based on its budgets rather than on its actual spending. As stated in the Introduction, the largest portion of the Office of the President's discretionary revenue—$288 million in fiscal year 2015–16—comes from the annual assessment that the Office of the President levies on campuses. As part of approving the Office of the President's overall budget, the regents also approve the amount that the Office of the President proposes to assess the campuses. As Figure 9 shows, the Office of the President's discretionary reserve for fiscal year 2015–16 includes $32 million in unspent campus assessment funds.

Figure 9
$32 Million of the Office of the President's Growing Discretionary Reserve Was Unspent Campus Assessment Funds as of June 30, 2016



Sources: California State Auditor's analysis of discretionary fund balances for fiscal years 2011–12 through 2015–16 provided by the Office of the President.

* Endowment funds consist of the Searles Fund and the President's Endowment Fund.

† Other funds include the Common Fund, University General Fund, investment pool earnings, and miscellaneous others.

In the July 2011 meetings in which the regents approved the creation of the campus assessment, the Office of the President committed to keeping the campus assessment as low as possible. Nonetheless, for two of the subsequent four years, it asked the regents to approve increases to the campus assessment even though it had not spent all of the funds that the regents approved in the previous years, as Table 5 shows. It did not return any of these unused funds to campuses in the form of a refund.

Table 5
The Office of the President's Reserve Balances Indicate That It Did Not Keep the Campus Assessment as Low as Possible
(in Millions)

	FISCAL YEAR				
	2011–12	2012–13	2013–14	2014–15	2015–16
Campus assessment revenue	$266	$262	$279	$278	$288
Campus assessment expenditure	259	252	261	279	290
Budget surplus or (deficit)	7	10	18	(1)	(2)
Cumulative surplus	7	17	35	34	32

Sources: California State Auditor's analysis of the Office of the President's campus assessment revenue and fund balances for fiscal years 2011–12 through 2015–16 provided by the Office of the President.

Although in 2011 the Office of the President created a campus budget committee (committee) to review and advise on its budget, it has not convened the committee since May 2013. It created the committee, which consisted of campus provosts and vice chancellors of planning and budget, because it had begun assessing the campuses to fund its discretionary budget and it wanted a way to include campus involvement in its budgeting process. However, the committee advised the Office of the President on its budget for only two years. According to the Office of the President's chief financial officer, the committee no longer meets because it achieved its purpose of aligning the annual budget with campus priorities. He also explained that the Office of the President continues to brief the campuses on the development of the annual budget through informal monthly meetings with the campus vice chancellors of planning and budget. However, our review of several briefing documents shows that the vice chancellors of planning and budget learn about budget changes only after the president has already approved them. Thus, these vice chancellors have little opportunity to provide suggestions that affect the budget's development.

Some of the campus administrators with whom we spoke stated that the Office of the President should receive more suggestions from campuses regarding its budget decisions through a formal

advisory body. For example, Riverside's vice chancellor stated that the Office of the President should develop its budget in a more collaborative manner that includes the creation of a process to prioritize initiatives and programs in a way that is transparent and that allows the campuses to participate in the decision making. Without adequate opportunity for campuses to provide feedback on the Office of the President's budget, the Office of the President has less assurance that its budget continues to align with the university's priorities and serves the needs of campuses.

The Office of the President Could Use Between $38 and $175 Million of Its Undisclosed Reserves for Other University Priorities

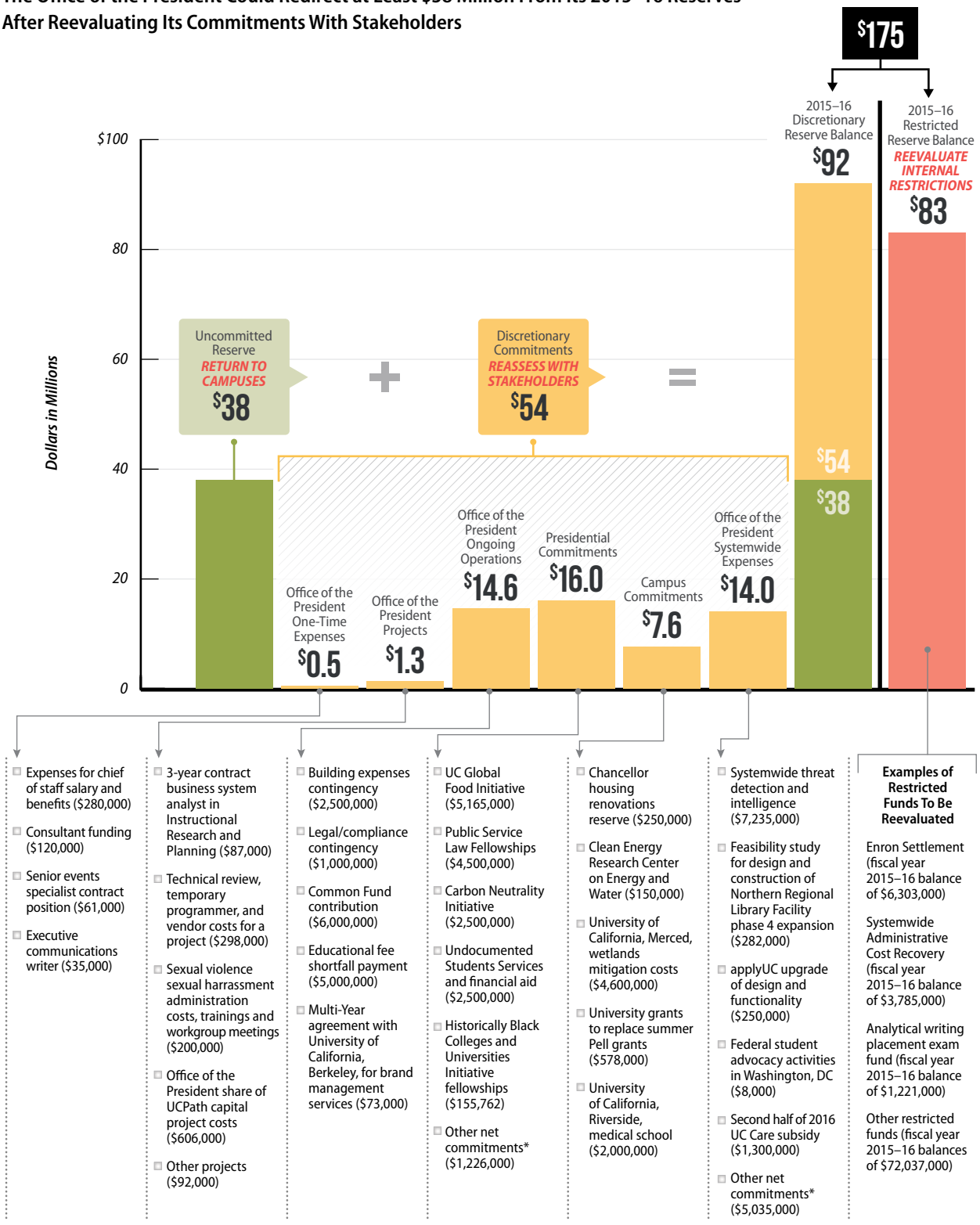
As previously discussed, the Office of the President had about $83 million in its undisclosed restricted reserve and about $92 million in its undisclosed discretionary reserve at the end of fiscal year 2015–16. Given the university's recently approved tuition increase and the campuses' ongoing struggles to ensure that they have sufficient funding to maintain academic quality, we believe the Office of the President should refund available funds in these reserves by returning them to the campuses for the benefit of students. Specifically, the Office of the President needs to reevaluate the planned uses of its $175 million in the undisclosed reserves.

Given the university's recently approved tuition increase and the campuses' ongoing struggles to ensure that they have sufficient funding to maintain academic quality, we believe the Office of the President should refund available funds in these reserves by returning them to the campuses for the benefit of students.

Our analysis suggests that the Office of the President could refund at least $38 million in uncommitted funds from its discretionary reserve as Figure 10 on the following page shows. According to its budget director, the Office of the President can use the $92 million in its discretionary reserve to fund any Office of the President or campus activity. The Office of the President identified $54 million in planned commitments from this $92 million reserve. Thus, we believe the remaining $38 million could be sent back to the campuses to be used for the university's priority of access and affordability for California undergraduate students. The Office of the President might also be able to return portions of the $54 million in discretionary reserve commitments to campuses. For example, the one-time expense of $280,000 in salary and benefit costs for the chief of staff's office. Finally, the Office of the President should also reevaluate the $83 million in its restricted reserve because some internal restrictions, if lifted, could allow the Office of the President to reallocate these dollars to the campuses.

The listing of planned commitments to be paid from the undisclosed discretionary reserve includes programs and projects that the Office of the President intends to provide. Although we recognize that the Office of the President needs some flexibility to fund these sorts of programs or projects if they arise during the year, the regents already approve an annual allocation

Figure 10
The Office of the President Could Redirect at Least $38 Million From Its 2015–16 Reserves After Reevaluating Its Commitments With Stakeholders



Source: California State Auditor's analysis of fiscal year 2016–17 fund commitments and fiscal year 2015–16 fund balances provided by the Office of the President.

* Other net commitments include projects such as the UC Mexico Initiative two-year work plans, DREAM Loan, and funding for the Presidential Postdoctoral Fellowship Program.

of $10 million in discretionary funds for presidential initiatives. In each of the past four fiscal years, the president did not spend all of this allocation. The fact that the president receives—and does not always fully spend—an allocation specifically for discretionary use demonstrates that the Office of the President might have opportunities to use some of the undisclosed discretionary reserve in a different way after an evaluation of what funding best serves the needs of the campuses and students. At the very least, the Office of the President should reevaluate the annual commitments it funds using the undisclosed discretionary reserve by implementing a more open and transparent budgeting process.

Furthermore, the Office of the President has opportunities to review—and potentially use—some of the $83 million in funds that were in its undisclosed restricted reserve at the end of fiscal year 2015–16. Although the Office of the President stated that most of the funds in the restricted reserve include grants, special state appropriations, and other funds with general spending restrictions, it cannot fully support this assertion. Specifically, when we asked for a list of all the restrictions tied to the funds, we found that the Office of the President did not maintain one. Moreover, the director of corporate accounting confirmed that the Office of the President can designate funds as restricted. An example is the systemwide administration cost recovery fund, of which the Office of the President spends a significant portion on marketing. Further, in the past, the Office of the President has reclassified some restricted funds as discretionary. For example, until fiscal year 2011–12, the Searles Fund, which provides about $7 million in revenue each year according to data provided by the Office of the President, was restricted for the use and benefit of the university. Beginning in fiscal year 2011–12, the Office of the President reclassified the Searles Fund as an unrestricted fund to minimize the campus assessment, citing the endowment's terms that allow the university to use the fund for purposes that cannot be covered by other funding sources.

The Office of the President's Budget Practices Are Ineffective and Preclude Accountability

The Office of the President's budget practices lack the processes and safeguards necessary to ensure that it consistently justifies and approves its expenditures. In particular, the Office of the President has not established safeguards over its expenditures related to its undisclosed budget, thus putting millions of dollars at risk of misuse. Although the regents' committee on finance adopted a recommendation that directed the Office of the President to create appropriate budget guidelines, processes, and standards in November 2006, the Office of the President has yet to do so. Because of its lack of budget standards, Office of the President management could not adequately explain many of the changes it has made in recent years to its practices for preparing its budget, even when those changes reduced feedback from the campuses.

The Office of the President has not established safeguards over its expenditures related to its undisclosed budget, thus putting millions of dollars at risk of misuse.

The Office of the President's Weak Internal Oversight of Its Undisclosed Budget Expenditures Creates the Risk of Wasteful Spending

The difficulty we had reconciling and validating the Office of the President's undisclosed budget expenditures led us to conclude that its budget practices may put tens of millions of dollars at risk for wasteful spending. As discussed previously, the Office of the President does not disclose these expenditures to the regents, the Legislature, or the public. As a result, we expected it would have adopted strong processes for justifying, approving, and tracking the expenditures to guard against misuse and to protect the Office of the President from outside criticism if the expenditures were questioned. However, the Office of the President generally did not have clear guidelines or expectations for approving undisclosed expenditures during the four years we reviewed. Moreover, the Office of the President's budget director and the deputy chief of staff to the president (deputy chief of staff) had a difficult time identifying approval documents for undisclosed expenditures it made from fiscal years 2012–13 through 2015–16. As we discuss in Chapter 3, the Office of the President took seven weeks to locate and provide requested approval documentation related to the undisclosed budget. Moreover, after the Office of the President provided this documentation, we found some of the approval documents were incomplete because they did not include the expenditures' justifications or identify the individuals who approved them.

Further, our analysis of undisclosed budget expenditures at five divisions of the Office of the President found that the expenditures were approved in a number of both formal and informal ways, but that these approvals were rarely fully documented. When we reviewed the approval documents for these expenditures from fiscal year 2012–13, we found that the Office of the President could not demonstrate adequate approval for 98 percent, or $37 million, of the expenditures that we analyzed. Although the Office of the President began using an improved approval process involving decision memos in November 2014 for some of its undisclosed budget expenditures, its use of this process was inconsistent. Specifically, these decision memos included descriptions of the expenditures, their justifications, and signatures from the management who approved them, including the president. However, according to the deputy chief of staff, the president verbally approves some expenditures during meetings, and the approval process remained flexible even after November 2014. Consequently, the Office of the President was unable to demonstrate adequate approval for 82 percent, or $34 million, of the five divisions' fiscal year 2015–16 expenditures that we reviewed subsequent to the improved approval process.

The Office of the President could not demonstrate adequate approval for 82 percent, or $34 million, of the undisclosed budget expenditures we analyzed from fiscal year 2015–16.

We also have concerns regarding the reliability of the Office of the President's budget data and its inability to determine the actual expenditures related to its undisclosed budget. Two of the five divisions with which we spoke identified more than $3 million in data entry errors in the Office of the President's budget data. Division staff attributed these errors to a lack of safeguards that would ensure that the historical budget data could not be changed after the end of the budget year. Further, Office of the President management confirmed that it could not easily determine the amount of the undisclosed budget that it actually spent for the years we reviewed because it does not separately identify actual expenditures from the undisclosed budget. In fact, we found it difficult to determine which decision memos related to the undisclosed budget because the Office of the President does not distinguish between these memos and ones related to its disclosed budget. The executive director for operations asserted that the Office of the President recently added tracking codes to undisclosed budget allocations so it will be able to determine the total amount of its undisclosed expenditures in the future.

The lack of safeguards and consistency creates the risk that Office of the President staff could inappropriately spend funds from the undisclosed budget because the divisions' budget allocations could exceed their needs or they could be spent on inadequately defined projects. The Office of the President has the critical responsibility of implementing strong budget processes so that its management has enough information to detect and prevent wasteful spending. Its lack of formalized budget processes, inability to find approval documents, inaccurate budget data, and failure to track undisclosed actual expenditures put tens of millions of dollars at risk for wasteful spending. According to the deputy chief of staff, changes in fiscal climate and administrations have meant that the Office of the President's budget preparation process has been unique each year; consequently, connecting approval documents and data is not always straightforward. Nevertheless, strong policies and procedures would have helped ensure the consistent approval and tracking of these expenditures across administrations. Further, it would have increased the Office of the President's ability to monitor budgets and detect any potential for wasteful spending.

Its lack of formalized budget processes, inability to find approval documents, inaccurate budget data, and failure to track undisclosed expenditures puts the Office of the President at risk for wasteful spending.

The Office of the President Lacks Adequate Policies and Procedures for Preparing Its Disclosed Budgets

The Office of the President has not followed a regents' committee on finance recommendation from 2006 directing it to create appropriate guidelines, procedures, and standards for preparing its budget. In addition to the problems with the undisclosed budget that we previously discussed, our review found that the Office of

Lacking clearly outlined budget procedures, the Office of the President has less assurance that it adequately addresses issues stakeholders raise during the budget development process.

the President's processes for preparing, reviewing, and approving its disclosed budget changed each year from fiscal years 2011–12 through 2015–16. Further, the Office of the President was not able to fully explain changes to its process for developing its disclosed budget or the standards it used to arrive at its spending decisions. Without clearly outlined procedures, the Office of the President has less assurance that it adequately addresses issues stakeholders raise during the budget development process.

Although the budget development process for any large organization is the result of a myriad of suggestions, negotiations, and compromises, these dynamics necessitate an orderly and formalized process to facilitate difficult budgeting decisions. Nevertheless, the Office of the President, which had a total budget of $747 million in fiscal year 2015–16, does not have a set of policies or procedures that describe its budgeting process. Instead, the Office of the President could only provide annual budget letters that it sent to its divisions that described at a high-level specific budgeting priorities—like reducing meeting costs—and changes to the budget review process. However, these letters did not sufficiently explain how the divisions were to implement these guidelines within the framework of an existing budgeting process.

For example, the annual budget letters describe a number of different committees, hearings, and other internal review processes that the Office of the President used at different times to make budgeting decisions. One of these committees was the President's Operations Group (operations group), which consisted of its senior leadership, who reviewed division budget requests and advised the president on what changes to approve for the proposed disclosed budget. However, the Office of the President did not establish standards to guide the operations group's budget review and did not document the results of the meetings. According to the Office of the President's budget director, the group instead set priorities that evolved over time and changed from year to year. The deputy chief of staff stated that the operations group ceased its involvement with the budget review in late 2013 because the responsibilities for this group were shifted elsewhere. Since that time, only the president has reviewed division budget change requests.

Turnover in the Office of the President's budget director position further emphasizes the need for consistent, documented processes for budget development. One rationale for creating such procedures is the need to maintain institutional knowledge in case of frequent staff turnover. The Office of the President's budget director changed three times from fiscal years 2011–12 through 2015–16, compounding its difficulties in explaining its evolving budget process. For example, the current budget director

has only been in her position for two years and could not answer many of the questions we had about the Office of the President's budget process.

The Office of the President Could Improve Its Budget Processes and Presentation by Aligning Them With Best Practices From Government Finance and Higher Education

The Office of the President has developed and presented its budgets in ways that preclude full transparency and accountability of its spending. Table 6 identifies the degree to which the Office of the President's processes do not align with a selection of recommended budget practices from the Government Finance Officers Association (GFOA) and the National Association of College and University Business Officers (NACUBO). Implementing these best practices would improve the Office of the President's budget development process and presentation to the regents.

Table 6
The Office of the President Does Not Follow Recommended Budget Practices

RECOMMENDED BUDGET PRACTICE	THE OFFICE OF THE PRESIDENT'S BUDGET PRACTICES	SCORECARD
Develop budget procedures to facilitate budget review, discussion, modification, and adoption.	No documented budget procedures, policies, or standards exist other than an annual letter sent to divisions containing general budget guidelines.	♦
Identify opportunities for stakeholder input.	Although the Office of the President holds monthly meetings with campus representatives and receives feedback related to its budget at some of those meetings, it no longer convenes an advisory budget committee consisting of campus representatives.	♦
Prepare and present a recommended budget that includes all programs, funds, and expenditures.	The budget omits expenditures from the temporary budget and fee-for-service expenditures that should be displayed and includes other expenditures—such as pass-through funds spent by campuses—that should not be displayed.	✕
Develop and evaluate financial options, which includes long-term forecasting of budgeted revenues and expenditures.	Annual budgets are prepared without long-term forecasts of revenues or expenditures.	✕
Reflect fiscal year-end actual expenditures in budget and monitor performance by comparing budget to actual expenditures.	Future budgets are based on current year budget, and the budget office does not regularly monitor actual expenditures.	✕
Develop a formal fund balance policy that sets appropriate fund balance level and uses.	No fund balance policy exists, and an excessive undisclosed unrestricted reserve exists that can be used to fund any program or project.	✕
Present a budget that includes sufficient information for external stakeholders and the governing body about the entity's operations, resources, fund balances, budgetary results, and key issues and choices.	Budget presentation does not include sufficient information about operations, resources, reserve balances, or key issues and choices. Budgetary results are not presented.	✕

Sources: California State Auditor's analysis of the Government Finance Officer Association's *Recommended Budget Practices*, the National Association of College and University Business Officers' presentation on *Budgeting and Capital Planning Best Practices*, the Office of the President's budget documents, and data obtained from the Office of the President's budget development system.

♦ = Partially implemented budget best practice.

✕ = Did not implement budget best practice.

For example, although the Office of the President sets aside a portion of its discretionary reserve to guard against unanticipated expenditures, it has not established a reserve policy that defines how much that reserve should be and how it can be spent. Instead, the Office of the President's documents show that it considers all of its discretionary reserve available for spending on discretionary programs. Further, establishing a prudent reserve policy would likely have prevented the Office of the President from accumulating the excessive reserve balances that we discuss earlier in this chapter.

The Office of the President's budget presentation lacks sufficient detail about its funding sources, which would provide the regents greater insight about possible means for keeping the campus assessment as low as possible.

The Office of the President's budget presentation also lacks sufficient detail about its funding sources, which is information that would provide the regents greater insight about possible means for keeping the campus assessment as low as possible. The GFOA recommends identifying funding requirements and sources of funds as well as providing any supplemental information necessary to understand the budget's funding plan. Although the Office of the President's budget provides the campus assessment amount, it does not include sufficient information about other available funding sources it will use to supplement the assessment, such as its endowment income, restricted revenue sources, and undisclosed discretionary reserve. The Office of the President's choice to omit information about its other available funding sources is of concern because we determined it could have used these sources to minimize the campus assessment or used these funds for other university priorities by returning excess reserves to the campuses in the form of a refund.

In the past, the Office of the President had addressed several of the missing elements we describe in Table 6 when presenting its budgets. We found that its budget for fiscal year 2010–11 separated pass-through expenditures from its operating budget, included some of the now-undisclosed budget, and highlighted expenditures it funded on a fee-for-service basis. The chief financial officer stated that the Office of the President created the detailed fiscal year 2010–11 budget to provide the regents additional information about its operations in preparation for the university's transition to the Funding Streams Initiative. He further stated that the Office of the President stopped providing this level of detail at the request of the regents. If the Office of the President had continued to use this budget framework, its publicly available documents would have addressed many of our concerns and questions.

Although the Office of the President's executive management agreed that it could improve its internal budget management by including its undisclosed budget, providing budgeted and actual expenditure results, and removing its pass-through expenditures, the systemwide controller disagreed that the Office of the President

should follow GFOA standards. The systemwide controller stated that GFOA budget practices do not necessarily apply to the Office of the President because it reports as a business-type activity whose operations are financed in part by fees charged for its services, making it different from other entities primarily funded through public funds. However, we believe that because the university receives $3 billion from taxpayers via the State's General Fund, it should follow GFOA best practices. Moreover, when we contacted the GFOA, a senior manager agreed that these best budget practices are applicable to public sector higher education institutions. In fact, the university's Division of Agriculture and Natural Resources (ANR), which is headquartered at the Office of the President, follows several of these best practices for budgeting including budgeted to actual expenditure comparisons and the use of long-term budget forecasts, which indicates that implementing at least some of these best practices is feasible.

Additionally, Office of the President management disagreed with the need to provide additional budget detail and information to the regents. The chief financial officer and chief operating officer stated that the regents do not expect or want this level of detail to understand the Office of the President's budget. However, when we spoke with the regents, they stated that although they believed the Office of the President had provided adequate detail regarding the budget, additional information—such as the amounts of the reserve balances—would be helpful. Moreover, the regents were open to recommendations for making the Office of the President's budget more transparent.

Contrary to the opinion of the Office of the President, implementing the best practices we suggest would not result in a voluminous amount of granular budget detail. In fact, we developed a proposal for a one-page budget display that the Office of the President could use for its presentation to the regents, which we display in Figure 11 on the following page. We believe this budget display would allow the regents to better understand and provide oversight of the Office of the President's proposed budgets and requests for revenue increases, which was part of the regents' committee on finance's rationale for recommending approval of the November 2006 policy requiring the Office of the President to present its budget for approval each year. Furthermore, we believe the regents, the Legislature, and the public would benefit from the transparency this display provides.

We developed a one-page budget display that the Office of the President could use for its presentation to the regents that would allow a better understanding of proposed budgets and requests for revenue increases.

Figure 11
By Implementing Best Practices, the Office of the President Could Ensure Its Budget Presentation Would Better Inform the Board of Regents and Other Stakeholders

The Office of the President's July 2015 Budget Summary

Fiscal Year 2015–16 PROPOSED BUDGET SUMMARY (in Millions)	TOTAL BUDGET TOTAL RESTATED Fiscal Year 2014–15	TOTAL Fiscal Year 2015–16
Office of the President		
Central and Administrative Services	$300	$315
Systemwide Academic & Public Service Programs	327	340
GRAND TOTAL	**$627**	**$655**
	% increase:	4%

BEST PRACTICES IMPLEMENTED

1. Include all budgetary allocations from the disclosed and undisclosed budgets and adjustments to budget.
2. Separately display other expenditures, such as the restricted pass-through funds that the Office of the President receives from external entities and sends directly to the campuses, and administrative services provided by the Office of the President to the campuses on a fee-for-service basis that are in addition to the services it provides through its operating budget.
3. Provide budget to actual results.
4. Base proposed budget on projected actual expenditures with other adjustments as needed for program changes.
5. Provide reserve balances.

The Office of the President's July 2015 Budget Summary *With Implemented Best Practices*

Fiscal Year 2015–16 PROPOSED BUDGET SUMMARY (in Millions)	TOTAL OPERATING EXPENDITURES 1 Fiscal Year 2014–15 Restated Budget	Projected Actual	Difference	2014–15 Projected Actual	Fiscal Year 2015–16 Proposed Change	Proposed Budget
Office of the President			3	4		
Central and Administrative Services	$310	$280	$30	$280	$15	$295
Systemwide Academic and Public Service Programs	248	212	36	212	38	250
OPERATING TOTAL	**$558**	**$492**	**$66**	**$492**	**$53**	**$545**
		% Spent:	*88%*		*% increase:*	*11%*
Other Expenditures						
2 Restricted Pass-Throughs	$214	$200	$14	$200	$16	$216
Administrative Services Fee-For-Service	95	118	(23)	118	37	155
OTHER EXPENDITURES TOTAL	**$309**	**$318**	**($9)**	**$318**	**$53**	**$371**
GRAND TOTAL EXPENDITURES	**$867**	**$810**	**$57**	**$810**	**$106**	**$916**

Discretionary Reserve Balance as of June 30, 2015 5	**$97**
Restricted Reserve Balance as of June 30, 2015	**$65**

Sources: California State Auditor's Analysis of the Office of the President's budget presented to the Board of Regents (regents) on July 22, 2015; data obtained from the Office of the President's budget development system; statements by the Office of the President's budget director; and recommended budgeting practices published by the Government Finance Officer Association and the National Association of College and University Business Officers.

Note: This figure is a hypothetical presentation for illustrative purposes, and is the minimum amount of information that should be presented. When implementing best practices, the Office of the President should work with the regents to determine the appropriate format and level of detail needed for the regents' oversight. The Office of the President should also explain to the regents why its restated budget amount differs from its originally approved budget amount, and update the regents on its final actual expenditures by September of each year. Finally the Office of the President's budget presentation should also include its total revenue sources.

A Financial Audit of the Office of the President Likely Would Have Identified Some of the Errors and Weak Processes We Identified

Over the last several years, the university's budget and finances have been subject to scrutiny from students, the Legislature, and the Governor. In light of this level of interest, we question why the Office of the President has not considered avenues for greater transparency through the annual financial audit it receives. Specifically, although the university receives an annual financial audit from an independent external auditor, this audit is conducted at a systemwide level, which obscures the Office of the President's financial activities and does not specifically evaluate the Office of the President's processes. Thus, the financial audit has not identified major issues that we found, including the Office of the President placing $96 million from the State intended for the university's retirement fund in its short-term investment pool instead and then failing to transfer almost $77,000 in interest to the university's retirement fund where it belonged.

The university's annual financial audit involves independent external auditors examining the campuses, the Office of the President, the medical centers, and other university programs as a single entity. Thus, the auditors only review the accuracy of the financial statements for the university system and do not specifically issue an opinion on the individual financial activities for each campus, the Office of the President, the medical centers, and the other university programs.[2] Combining all of the university's components into one audit essentially obscures the finances for specific components, such as the Office of the President. For example, the university's most recent annual financial report indicated that the university as a whole maintained a deficit unrestricted fund balance of $11 billion, a significant portion of which is attributable to pensions and retiree health benefit obligations. However, as we demonstrated earlier in this chapter, the Office of the President itself maintains a significant surplus reserve balance: $92 million of discretionary reserves at the end of fiscal year 2015–16.

Combining all of the university's components into one financial audit essentially obscures the finances for specific components, such as the Office of the President.

In fact, when we first analyzed the undisclosed discretionary reserve, the ending balance for fiscal year 2015–16 was initially $188 million because it inappropriately included $96 million that the Office of the President received from the State for the university's retirement plan. When we inquired about this $96 million, the systemwide controller asserted that the Office of the President placed this money in its short-term investment pool for one day

[2] The university's medical centers also issue their own audited financial statements that are separate from the university's systemwide financial statements.

In fiscal year 2015–16, the Office of the President inappropriately placed $96 million in its short-term investment pool that it received from the State for the university's retirement plan, earning $77,000 in interest that it failed to transfer to the retirement fund.

before transferring it out to the retirement fund. However, when we followed up with the director of corporate accounting to get evidence of this statement, it became apparent that this money actually remained in the short-term investment pool for 25 days before it was transferred out. During those 25 days, the $96 million earned almost $77,000 in interest that the Office of the President failed to transfer to the retirement fund. The Office of the President did not transfer this money until March 17, 2017, after we notified it of this issue.

This is of further concern because the Office of the President's standard practice is to deposit state appropriations, including the $96 million in funds for the retirement plan, and any other incoming receipts addressed to the university from external parties into its short-term investment pool. Without strong controls in place, the Office of the President risks inappropriately spending the interest generated from funds designated for a specific purpose on purposes for which these funds were not originally designated.

Moreover, we determined that the Office of the President does not centrally manage all of its expenditures and could not tell us the actual amount of restricted revenue it received. Specifically, the Office of the President's budget director stated that the budget office periodically assesses variances between its budget and actual expenditures at the midpoint and the end of the fiscal year. The Office of the President also requires divisions to more closely monitor their budgets throughout the year. The budget office views the more than 300 restricted funds as the responsibility of the divisions that receive them. Nevertheless, since this information is not managed centrally, it is not readily available, and therefore, the Office of the President was unable to provide us with information regarding the actual restricted revenue it received.

Finally, the Office of the President's Corporate Financial Reporting system (reporting system) does not distinguish between its own operating costs and systemwide costs, making it difficult to determine how much the Office of the President actually costs to run. Specifically, when we attempted to gain assurance about the accuracy and completeness of the actual expenditure data the Office of the President provided, we compared it to the university's reporting system, which is used to prepare the audited financial statements. However, the expenditures associated with the Office of the President's portion of the reporting system also included systemwide expenditures such as costs for pensions and other post-employment benefits for the entire system. Without a more distinct separation between the Office of the President's operating costs and systemwide costs, it is difficult to compare the Office of the President's expenditures to costs in its reporting system.

When we spoke with the university's independent auditors, they stated that separately auditing each of the university's units would be very expensive. The auditors also stated it would be difficult because some financial activities—like investments and retirement costs—would need additional analysis to allocate them to the campuses, medical centers, labs, and the Office of the President. Regardless, the current level of financial statement reporting does not allow the regents, the Legislature, or the public to accurately differentiate the Office of the President's financial activities from the rest of the university's components. In addition to improving transparency, a financial audit of the Office of the President would recommend detailed improvements to processes that led to the mistakes and weaknesses we found and allow the Office of the President to better justify its spending decisions.

Recommendations

The Office of the President

To determine the amount of money that it can reallocate to campuses and to ensure that it publicly presents comprehensive and accurate budget information, the Office of the President should do the following:

By April 2018:

- Document and review the restrictions on its funds and fund commitments to determine whether it can reallocate any of these funds to its discretionary budget for eventual reallocation to campuses.
- Develop a reserve policy that governs how large its reserves should be and the purposes for which they can be used.
- Implement our recommended budget presentation shown in Figure 11 on page 40. Specifically, the Office of the President's budget presentation to the regents should include a comparison of its proposed budget to its actual expenditures for the previous year. It should also include all its expenditures and identify changes to the discretionary and restricted reserves. The Office of the President should combine both the disclosed and undisclosed budgets into one budget presentation.
- Increase opportunities for campus stakeholder involvement in the budget development process by reconvening the campus budget committee and establishing an agreed-upon charter that describes the committee's scope, role, and protocol for reviewing and providing comments on the Office of the President's annual budget.

By April 2019:

- Publish the results of its review of fund restrictions and fund commitments and identify any funds it anticipates reallocating to campuses.
- Implement the best practices for budgeting identified by the GFOA and NACUBO, including developing budget policies and procedures and formally documenting, approving, and justifying all one-time and unexpected expenditure requests.
- Continue to present a comprehensive budget based on the presentation in Figure 11 to the regents, the Legislature, and the public.

By April 2020:

- Reallocate to the campuses funds that it identified during its review of fund restrictions and fund commitments.
- Evaluate its budget process to ensure that it is efficient and has adequate safeguards that ensure that staff approve and justify all budget expenditures. If the Office of the President determines that its safeguards are sufficient, it should begin developing a multiyear budget plan.
- Report to the regents on the amount of funds it reallocated to campuses as a result of implementing our recommendations.

The Regents

- To ensure the ongoing accountability of the Office of the President, the regents should require it to implement our recommendations and report periodically on its progress.
- To ensure that the Office of the President's spending aligns with the needs of campuses and students, the regents should hold a public meeting to discuss the results of the Office of the President's review of its fund restrictions and funding commitments, as well as its proposal to reallocate funds to campuses.
- To ensure that the Office of the President's financial safeguards are adequate, the regents should require the Office of the President to engage in a financial audit of only the Office of the President's operations.

Chapter 2

THE OFFICE OF THE PRESIDENT HAS NOT SUFFICIENTLY JUSTIFIED THE SIZE AND COST OF ITS STAFF

Chapter Summary

The University of California (university) Office of the President has increased its budget by 17 percent over the past four years. One of the central causes of the escalation is the number and cost of the staff that the Office of the President employs. Because one of the primary roles of the Office of the President is to support campuses, we expected that it would have aligned its staffing levels with the needs of its campuses; however, it has not done so. The Office of the President has yet to develop and implement a workforce plan, and its position control process, which requires management review for staffing increases, has not kept staff levels from rising. The Office of the President acknowledged the need to review staffing in the past: in January 2014, it issued a presidential directive calling for its divisions to create staffing plans and participate in a budget review that was supposed to identify redundancies and determine the appropriate size, shape, and role of the Office of the President. However, it did not document the results of the review. Further, our analysis shows that the review did not decrease staffing levels or costs.

The rapid growth of the Office of the President's staffing costs is in part attributable to its decision to pay its staff generous salaries and provide them with expensive employee benefits. Despite its status as the administrative headquarters of a large public university system, the Office of the President pays its executives and administrative staff significantly more than state agencies pay their employees. Our review of 10 executive and 10 administrative positions at the Office of the President shows that although these employees have similar duties to those of state government employees—such as human resource management and accounting—the Office of the President pays them significantly higher salaries. In fact, our review of these 20 positions indicates that the Office of the President could save at least $3.2 million annually by more closely aligning its executive and administrative staffs' salaries to those state agencies offer. Additionally, the Office of the President offers its staff benefits that state agencies rarely provide, such as paying for business meetings and entertainment at a cost of at least $2 million over the five-year period we reviewed. If the Office of the President chose to eliminate or reduce these generous employee benefits, it could direct the resulting savings to campuses.

Both the Office of the President and the Campuses Have Increased Their Staffing Levels

Although the Office of the President has consistently stated publicly that it is doing all it can to keep its costs low, its staffing levels have grown by 11 percent since fiscal year 2010–11. As Table 7 shows, this rate of growth outpaced the rate of staffing growth for the university by 1 percent. Only the medical centers' 15 percent rate of growth and the student staffs' 19 percent rate of growth over the past five years exceeded that of the Office of the President. The medical centers, for the most part, receive their funding from patient fees.

Table 7
Since Fiscal Year 2010–11, Staff Levels Have Increased at the Office of the President, the Campuses, and in Health Related Areas

	FISCAL YEAR						FIVE-YEAR GROWTH
	2010–11	2011–12	2012–13	2013–14	2014–15	2015–16	
Office of the President Total full-time equivalent staff	1,496	1,539	1,577	1,643	1,673	1,667	171
Percentage change		3%	2%	4%	2%	0%	11%
Total university staff (excluding Office of the President staff)	132,779	134,393	136,089	137,564	143,089	146,177	13,398
Percentage change		1%	1%	1%	4%	2%	10%
Academic total full-time equivalent staff (campus and health locations)	40,669	40,727	41,070	41,372	42,189	42,998	2,329
Percentage change		0%	1%	1%	2%	2%	6%
Campus total full-time equivalent staff (nonacademic, nonstudent)	37,412	37,567	37,683	38,928	44,542	40,095	2,683
Percentage change		0%	0%	3%	14%	(10%)	7%
Health total full-time equivalent staff (nonacademic, nonstudent)	48,242	49,562	50,460	50,145	48,839	55,412	7,170
Percentage change		3%	2%	(1%)	(3%)	13%	15%
Student staff total full-time equivalent staff (campus and health locations)	6,455	6,536	6,877	7,119	7,520	7,671	1,216
Percentage change		1%	5%	4%	6%	2%	19%

Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System and data from the University of California's infocenter website. The Office of the President total excludes the United States Department of Energy Laboratories and Agriculture and Natural Resources staff. The university total excludes the United States Department of Energy Laboratories staff because the infocenter website does not include them.

Because the Office of the President manages a number of systemwide initiatives, it employs staff both at the campuses and at its central headquarters in Oakland. However, its staffing growth occurred largely at its headquarters. From fiscal years 2010–11 through 2015–16, the Office of the President increased the number of staff at its Oakland location by 153 employees, while it employed only 18 additional staff at the campuses. Employees at the Office of the President's headquarters generally perform administrative functions, such as human resource administration, accounting, and information technology (IT) support.

The Office of the President has four general staffing groups, as the text box indicates. As shown in Figure 12 on the following page, the Office of the President's total salary costs have also increased over the past six years, especially for managers and senior professionals. Although the Office of the President has maintained relatively steady staffing and salary levels for its senior management group, it has increased both staffing and salary levels for its managers and senior professionals and for its professional and support staff. In fact, it increased its managers and senior professionals' staffing levels by 32 percent from fiscal years 2010–11 through 2015–16, from 519 employees to 685 employees. Further, the total salaries it paid its managers and senior professionals increased by $38 million, or 59 percent, and their average salaries increased by 21 percent, or nearly $25,600, over this same period.

The University of California's Employee Classification Groups

Senior management: Provide universitywide policy and program direction.

Managers and senior professionals: Provide leadership and professional expertise to major university units or fields of work.

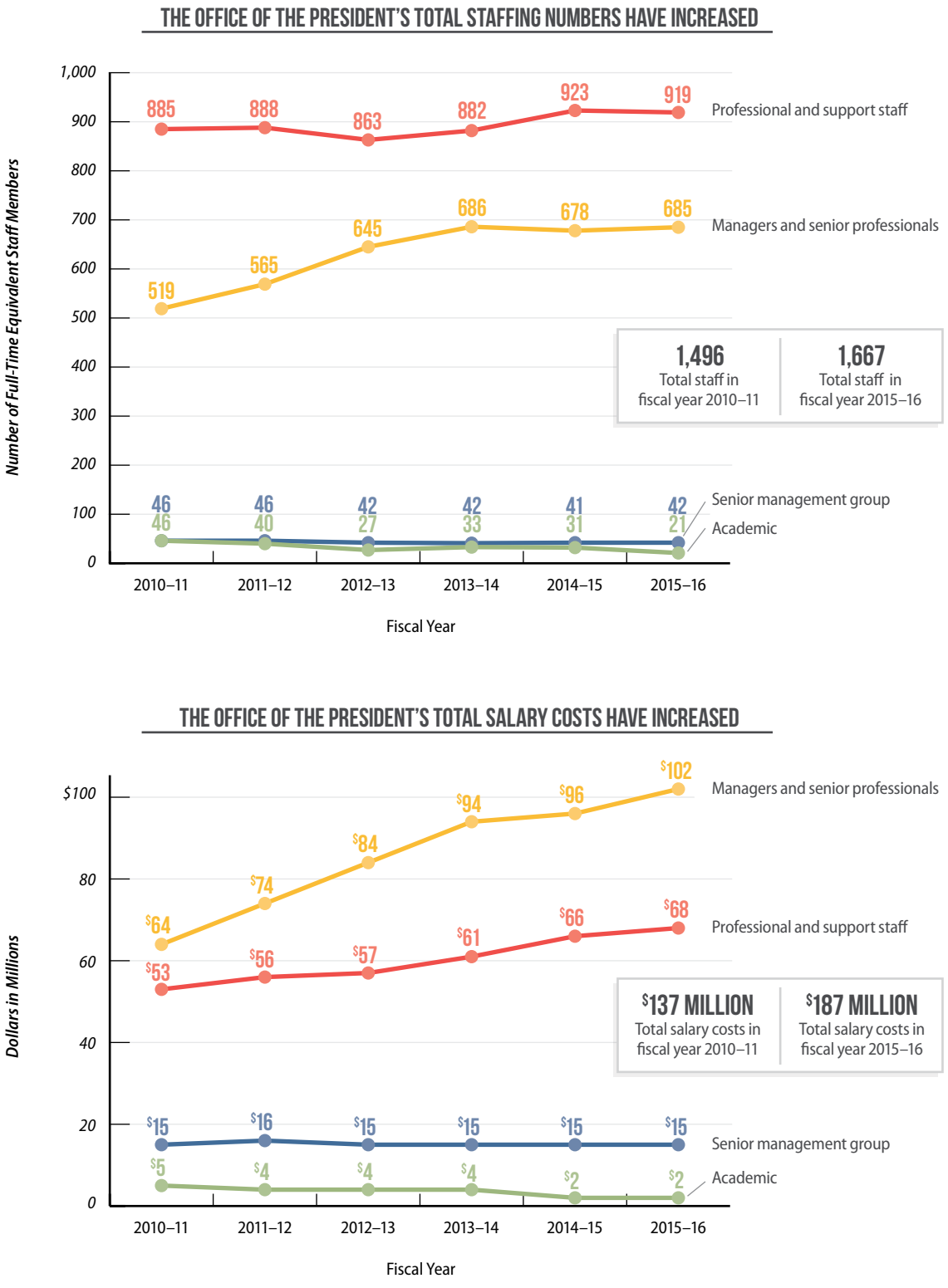
Professional and support staff: Provide administrative, technical, operational, or clerical support for the university.

Academic staff: Conduct teaching, research, and public service. This category includes nonfaculty staff such as researchers and administrators.

Sources: University of California's Career Tracks and Academic Personnel Manual.

Some of the increased costs for manager and senior professionals might be caused by the Office of the President's inefficient use of these positions. For example, although the Office of the President's guidance states that supervisory and management positions are supposed to supervise at least two full-time positions, our analysis of the Office of the President's organizational charts found that many supervisors and managers do not meet this guideline. For instance, one associate director in the public affairs division with an annual salary rate of nearly $160,700 does not directly manage any employees. Likewise, a manager in the academic affairs division with an annual salary rate of $120,200 manages only one employee. In fact, we identified 10 managers who appeared to oversee only one employee and six managers who did not oversee anyone. When we shared this analysis with the Office of the President, it stated that the guidance was not a strict rule. However, we question whether the number of managers and their corresponding pay is justified given the Office of the President's perspective that its managers do not necessarily need to oversee at least two staff. An analysis of management and staffing ratios can be incorporated into a workforce plan, which we discuss later.

Figure 12
Most of the Office of the President's Staffing and Salary Growth Has Related to Management and Senior Professionals



Source: California State Auditor's analysis of personnel data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System.

The Office of the President Pays Its Executives and Administrative Staff Significantly More Than Their Public Sector Counterparts Receive

The Office of the President could save millions of dollars in salary costs by paying its executive management and administrative staff salaries that more closely align with those that state agencies and the California State University (CSU) offer. The Office of the President's higher salaries are largely the result of its decision to use mostly private sector and higher education data when determining appropriate salaries for its positions. Further, the Office of the President has established wider salary ranges than those for comparable state employees, and this may not allow it to effectively control costs or provide incentives for employee development because employees do not necessarily have to take on additional responsibilities to earn more money.

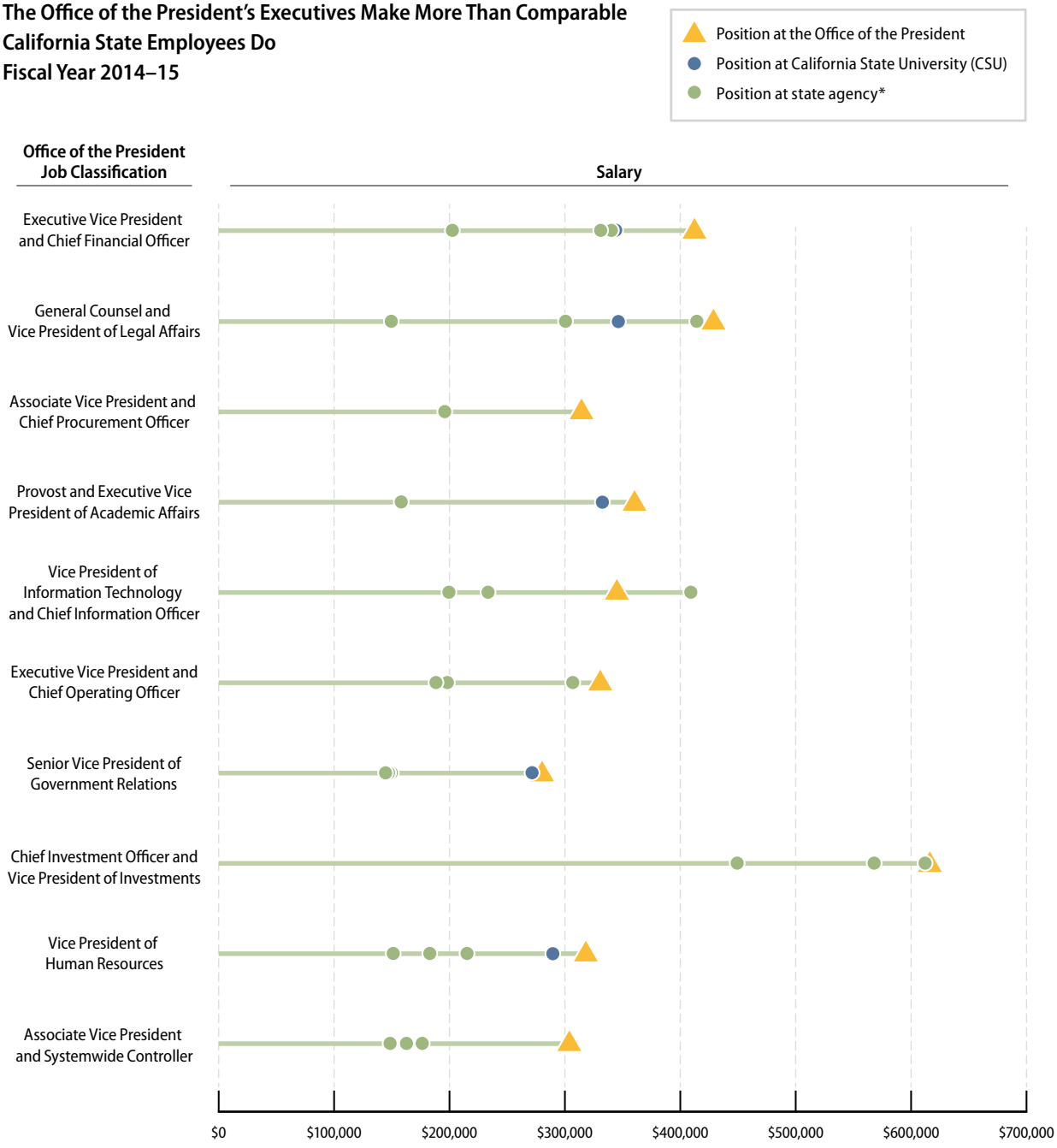
The Office of the President Could Save at Least $700,000 Annually by Aligning Its Executive Salaries to Those of Comparable Public Sector Executives

In the Budget Act of 2016, the Legislature required the University of California Board of Regents (regents) to consider compensation for comparable state positions when evaluating the salaries of certain Office of the President executives. The Office of the President's compensation program and strategy unit (compensation unit) stated that it was not able to find comparable state positions for many of its executives who worked for laboratory management or in its medical centers, although the unit did find matches for 35 percent of the executives within its senior management group. For example, the compensation unit determined that its chief financial officer position was comparable to several other positions, including the state finance director and the chief financial officer of the CSU system. According to the executive director of the compensation unit (compensation director), a salary above 90 percent of the range developed from this exercise would have been subject to a salary freeze. However, the compensation director was not aware of any instances in which the Office of the President actually froze salaries as a result of the review. In fact, the compensation director stated that salaries below 25 percent of the determined range for a position were eligible for an increase.

The Office of the President was not able to find comparable state positions for many of its executives; it found matches for 35 percent of its executives.

Nonetheless, our analysis indicated that the Office of the President's executives generally earn significantly higher salaries than state employees in similar positions. As shown in Figure 13 on the following page, we compared the salaries of a selection of the Office of the President's executive staff with the salaries of the three highest-paid state employees and one CSU employee in similar positions when possible for fiscal year 2014–15. (Appendix A presents the detailed data supporting Figure 13.) The 10 Office of the President executives we analyzed had combined salaries of $3.7 million—over $700,000 more than the combined salaries of their highest-paid state employee counterparts after adjusting for their

Figure 13
The Office of the President's Executives Make More Than Comparable California State Employees Do
Fiscal Year 2014–15



Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System and State Controller's Office information for CSU and state government employees.

Note: We compared the Office of the President's executives against the three highest-paid comparable executives in state government when possible. The Office of the President has 42 executive staff compared with only seven at the CSU Chancellor's Office; therefore, we were unable to find comparable executives at CSU for each position at the Office of the President.

* We increased the state executive and CSU employee salaries based on a cost-of-living adjustment calculated by comparing the cities where their agencies' main offices are located to the city of Oakland, where the Office of the President is headquartered. We calculated the adjustments using cost-of-living index information from the Council for Community and Economic Research for quarter two of 2016. We used the following adjustment rates: Sacramento: 26.2 percent; San Francisco: -15.7 percent; and Long Beach: 5.1 percent. We did not make adjustments for agencies headquartered in the East Bay Area.

respective cost of living.[3] Furthermore, in many instances, the state employee executives had roughly the same levels of responsibility as the Office of the President executives. For example, the director for the California Department of Human Resources (CalHR) earns about $100,000 less than the vice president of human resources at the Office of the President. Both positions are responsible for labor relations, collective bargaining, employee salaries and benefits, job classifications, recruitment, and retention; however, CalHR is responsible for over 225,000 employees compared to 190,000 at the university.

In many instances, the state employee executives had roughly the same levels of responsibility as the Office of the President executives.

The Office of the President also paid its executives higher salaries than CSU paid its executives during fiscal year 2014–15. Although CSU's executives oversee 13 more campuses and 200,000 more students than the Office of the President oversees, the CSU Chancellor's Office—the administrative body equivalent to the Office of the President—has only seven executive-level staff while the Office of the President has 42. A partial explanation for this difference is that the State manages certain aspects of CSU, such as its payroll system and retirement programs. Additionally, the university's tripartite mission of teaching, research, and public service means the Office of the President oversees medical centers, graduate education, and programs that exceed the scope of CSU's mission. Nonetheless, CSU's executives have more responsibility than their Office of the President's counterparts in some instances. For example, CSU's chief financial officer—whose annual salary was $70,000 less than the university's chief financial officer's salary in fiscal year 2014–15—is in charge of the business and finance division, whose mission includes management of IT services. Although the Office of the President's chief financial officer has some IT duties, such as serving as an executive sponsor on the UCPath project—the university's replacement payroll and human resources system—the Office of the President also has an executive serving as vice president of information technology who performs these duties and who received a salary rate of $345,100 in fiscal year 2014–15.

The Office of the President Could Save More Than $2.5 Million Annually by Reevaluating Its Administrative Staff Salaries

The Office of the President has asserted that the higher education environment necessitates higher pay for its staff. Although that assertion may have merit for certain executive employees, it has much less merit for administrative staff who perform similar duties no matter where they work. Table 8 on the following page shows that the Office of the

[3] We increased the state executive and CSU employee salaries based on a cost-of-living adjustment calculated by comparing the cities where their agencies' main offices are located to the city of Oakland, where the Office of the President is headquartered. We calculated the adjustments using cost-of-living index information from the Council for Community and Economic Research for quarter two of 2016. We used the following adjustment rates: Sacramento: 26.2 percent; San Francisco: -15.7 percent; and Long Beach: 5.1 percent. We did not make adjustments for agencies headquartered in the East Bay Area.

Table 8

The Office of the President's Administrative Staff Annual Salaries Generally Exceeded the Annual Salary Ranges of Comparable State Employees
Fiscal Year 2015–16

OFFICE OF THE PRESIDENT*				STATE EMPLOYEE			COMPARABLE CALIFORNIA STATE UNIVERSITY (CSU) JOB CLASSIFICATIONS		
JOB CLASSIFICATION	NUMBER OF EMPLOYEES IN CLASSIFICATION	AVERAGE ANNUAL SALARY	MAXIMUM ANNUAL SALARY RANGE	JOB CLASSIFICATION	MAXIMUM ANNUAL SALARY RANGE†	MONETARY EFFECT‡	JOB CLASSIFICATION	MAXIMUM ANNUAL SALARY RANGE§	MONETARY EFFECT‡
Accounting Manager 2	3	$142,600	$169,600	Accounting Administrator II	$90,400	$156,500	No Comparable Classification‖		
Applications Programmer 3	55	95,400	120,600	Staff Programmer Analyst (Specialist)	86,900	494,600	Analyst / Programmer Range 2	$112,800	$13,000
Business Systems Analyst 3	32	84,100	120,600	Staff Information Systems Analyst (Specialist)	86,900	96,000	Analyst / Programmer Range 2	112,800	0
Executive Assistant 3	24	68,900	98,100	Executive Assistant	53,700	367,200	Presidential Aide	93,800	0
Financial Analyst 3	13	86,700	120,600	Staff Finance Budget Analyst	86,500	45,000	Senior Budget Analyst	93,000	13,600
Information Systems Analyst 4#	25	122,900	169,600	Senior Information Systems Analyst (Specialist) Senior Programmer Analyst (Specialist)	95,500	684,900	Operating Systems Analyst Range 3 Analyst/ Programmer Range 3	126,500	78,000
Information Systems Manager 3	2	185,800	258,000	Information Systems Manager	110,700	150,100	No Comparable Classification‖		
Strategic Sourcing Professional 4	17	110,000	169,600	Purchasing Manager	116,300	83,600	Buyer III	76,100	575,800
Systems Administrator 4#	19	119,700	169,600	Senior Information Systems Analyst (Supervisor)	100,300	368,200	Operating Systems Analyst Range 3 Network Analyst Range 3 Analyst/ Programmer Range 3	126,500	8,600
Writer Editor 3	5	93,200	107,900	Associate Editor of Publications	71,900	110,200	No Comparable Classification		
					Total	**$2,556,300**		**Total**	**$689,000**

Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse, the State of California's civil service pay scale, the CSU Salary Schedule, and job descriptions from all three entities.

Note: Dollar amounts have been rounded to the nearest hundred.

* We excluded systemwide employees who are located at campuses because campuses may have different salary ranges.

† We added a 4 percent cost-of-living adjustment when comparing state employees to Office of the President employees. The cost-of-living adjustment uses a statewide number we developed by calculating the cost of living for counties in which state employees worked. We compared this weighted average against Alameda County's cost of living because that is where the Office of the President is located. Cost-of-living data are from the Council for Community and Economic Research.

‡ These amounts are the cumulative totals for the portion of each employee's annual salary rate that exceeded the state and CSU maximum salary range. We included this amount for each Office of the President employee in the respective job classification without adjusting for how long the employee worked in the position. Therefore, the actual monetary effect for these job classifications may be less if an employee did not work for a full year. However, if the Office of the President performed a similar analysis for all administrative positions, it may identify greater savings.

§ We did not adjust CSU's salary ranges with a cost-of-living index adjustment because CSU has structured the ranges so that it can adjust salary costs to accommodate any geographic region in the State.

‖ CSU's Management Personnel Program uses generic classifications for management employees; therefore, we were unable to make valid comparisons between these employees.

Because of differences in the job descriptions and overlapping job duties, we found multiple comparable state and CSU classifications at the equivalent skill level that shared a common salary.

President's annual salary rates for the administrative staff we reviewed amounted to $2.5 million more than the maximum annual salary ranges for comparable state employees, even after including a cost-of-living adjustment.[4] We analyzed the job duties, responsibilities, and qualifications of the Office of the President administrative classifications to identify similar state positions. We found that the *average* Office of the President salary was higher than the *maximum* amount the State pays an employee to perform the same administrative duties for eight of the 10 positions we reviewed.

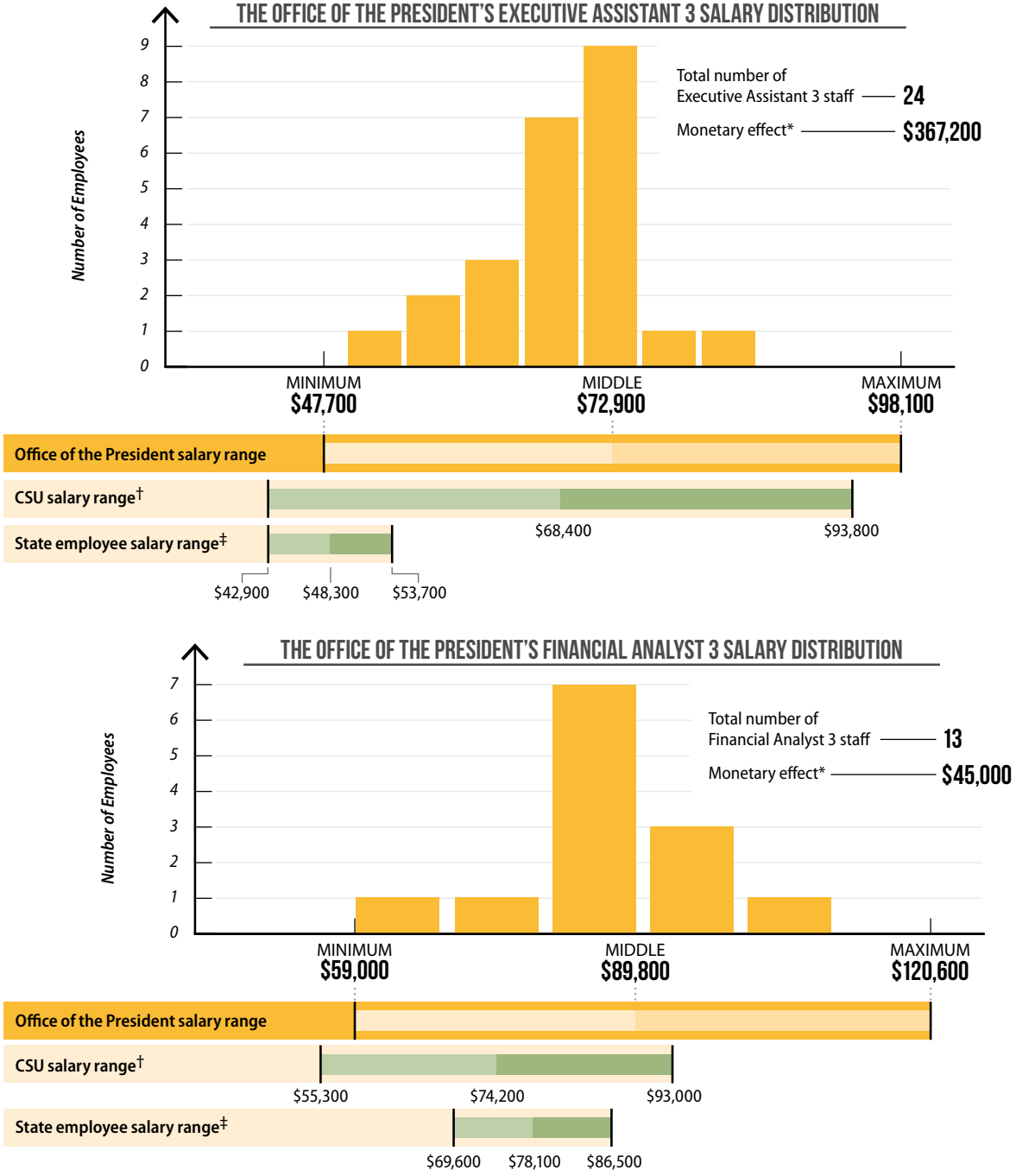
For eight of the 10 administrative positions we reviewed, the average Office of the President salary was higher than the maximum amount the State pays an employee to perform the same duties.

When we performed a similar analysis comparing the Office of the President's administrative positions to similar positions at CSU, we found that although CSU's maximum salary ranges for all but one comparable position were higher than the average salaries of the Office of the President's classifications, the Office of the President established higher maximum salary ranges for all seven of the comparable classifications we reviewed. As the examples in Figure 14 on the following page show, CSU has wide salary ranges, similar to those of the Office of the President. As a result, the Office of the President would save $689,000 annually if it aligned its salaries for the classifications in our analysis with CSU's ranges. However, according to CSU's compensation guide, CSU's salary ranges are wide in part to allow the system to adjust salaries based on the employees' geographic regions in California. This is contrary to the Office of the President's salary ranges, which are already adjusted for geographic region. Moreover, as Figure 14 demonstrates, the true cost of employees depends on where they are placed in the salary range, creating the potential—because our estimated savings are based on CSU's salary range maximums—that a wider gap exists between Office of the President and CSU salaries.

To set the salaries of its employees, the Office of the President uses market surveys that largely rely on national private sector and higher education data; thus, the vast majority of the entities against which it compares itself are private companies that typically pay their staff higher salaries than public entities do. Specifically, the market survey the Office of the President most commonly uses contained only 28 government or higher education participants out of a total of 694 entities for the positions we analyzed.

[4] We added a 4 percent cost-of-living adjustment when comparing the salaries of administrative state employees to Office of the President administrative employees. The cost-of-living adjustment uses a statewide number we developed by calculating the cost-of-living for the counties in which all state employees worked. We compared this weighted average to Alameda County's cost-of-living because the Office of the President is located in Alameda County. We used cost-of-living data from the Council for Community and Economic Research.

Figure 14
The Office of the President's Employee Salaries Generally Fall in the Middle of Its Salary Ranges
Fiscal Year 2015–16



Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse and job specifications for comparable positions at the Office of the President, California Department of Human Resources, and CSU.

Note: Dollar amounts have been rounded to the nearest hundred.

* These amounts are the cumulative totals for the portion of each employee's annual salary rate that exceeded the state maximum salary range. We included this amount for each Office of the President employee in the job classification without adjusting for how long the employee worked in the position. Therefore, the actual monetary effect may be less if an employee did not work for a full year.

† We did not adjust CSU's salary ranges with a cost-of-living index adjustment because CSU has structured the ranges so that it can adjust salary costs to accommodate any geographic region in the State.

‡ We added a 4 percent cost-of-living adjustment when comparing state employees to Office of the President employees. The cost-of-living adjustment uses a statewide number we developed by calculating the cost of living for counties in which all state employees worked. We compared this weighted average against Alameda County's cost of living because that is where the Office of the President is located. Cost-of-living data are from the Council for Community and Economic Research.

Other surveys that the Office of the President uses also rely heavily upon private sector data, particularly from the technology, aerospace, laboratory, consumer product, life science, and higher education industries. Because state employee salary information is publicly available, we believe the Office of the President could have more strongly focused on state salaries when determining salaries for its administrative positions.

When we suggested that the Office of the President give greater weight to state salaries when setting its salaries, it claimed that lowering salaries would make it less competitive in the Bay Area job market and therefore affect its ability to attract talent. It especially emphasized this point for the technology positions we selected. Nonetheless, we disagree with the implication that pay alone attracts talent. The Office of the President offers stability and generous benefits, including a retirement plan, that are not always provided in the private sector. Moreover, the Office of the President can attract individuals for whom working for the public sector to advance the university's prestigious reputation has an intangible benefit. These factors help to offset the pay differential between the Office of the President and the private sector.

We disagree with the implication of the Office of the President's assertion that pay alone attracts talent considering it offers stability and generous benefits that are not always provided in the private sector.

The Office of the President's Salary Ranges Are Too Wide to Control Payroll Costs, Ensure Pay Equity, and Create Incentives for Employee Development

The Office of the President's salary ranges are too wide to effectively control payroll costs or ensure internal equity within job classifications. The maximum of every salary range the Office of the President uses for its nonrepresented employees who are not executives is at least double the minimum salary for the same range. For example, the Office of the President's highest salary range that was effective from July 2014 through June 2016 spans from $124,600 to $344,600—a difference of $220,000. The Office of the President's policy states that its divisions generally cannot hire new employees above the 75th percentile without the approval of the chief of human resources. For the salary range discussed above, that policy would allow a division to hire a new employee without additional approval for a starting salary between $124,600 and $289,600. However, according to the executive director of human resources, in practice the Office of the President tends to hire new employees at salaries near the midpoint of their respective ranges.

Further, the use of such wide salary ranges can create situations in which two employees perform similar duties and have similar responsibilities but earn vastly different amounts. In fact, we noted 51 instances of employees in the Office of the President who had pay rates that were more than 50 percent higher than those of peers in the same classifications. In these instances, the salary differences could not be attributed to the employees' responsibilities or skill

levels because—according to the university's policy manual—the purpose of the classification process is to ensure that the university correctly identifies positions' required skill levels and assigned responsibilities. If an employee operates at a higher skill level or performs more difficult work than others in his or her classification, that employee should be in a higher classification. Although some of the salary differences we observed might be attributed to the length of time an employee had been in his or her position, we do not believe that would explain a 50 percent difference in pay rates between Office of the President employees in the same classification.

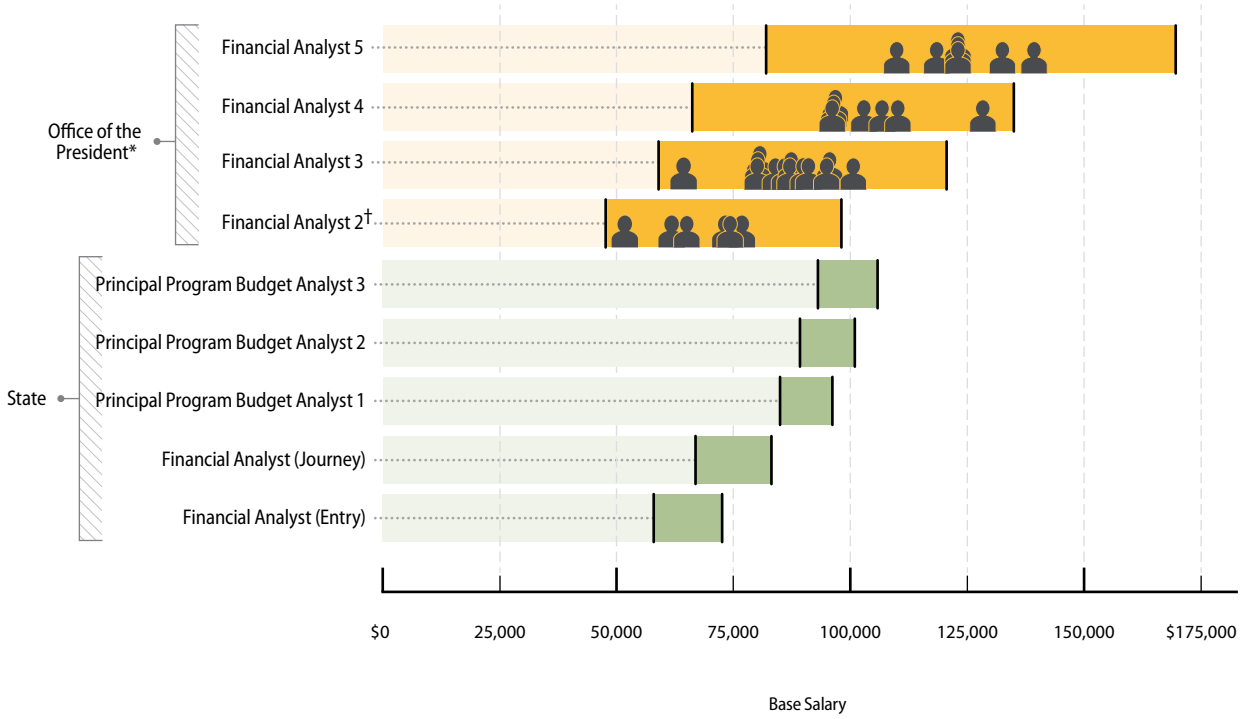
The Office of the President's use of wide salary ranges presents challenges in maintaining equity between different levels within the same job classification series.

The Office of the President's use of wide salary ranges also presents challenges in maintaining equity between different levels within the same job classification series. In describing its job classification system, the university indicates that higher levels within a job classification series are supposed to denote greater expertise and responsibility. Consequently, higher levels within a series carry higher salary ranges than lower levels. For example, financial analyst 3 is an "experienced" position, whereas financial analyst 2 is an "intermediate" position; thus, a financial analyst 3 should generally have a higher salary than a financial analyst 2. However, because of the Office of the President's wide salary ranges for each job classification, significant overlap exists between different job levels. For example, the salary ranges for a financial analyst 2 and a financial analyst 3 overlap by $39,100, as Figure 15 shows.

Although some overlap in salaries for different job levels may be inevitable, the equivalent state financial analyst classification series only has a $5,700 overlap in its annual salary ranges. As a result of the Office of the President's wide salary ranges, a financial analyst 4 with a salary rate of $128,500 in fiscal year 2015–16, was the third highest-paid person among the Office of the President's employees in the financial analyst series. In fact, this individual's salary rate was higher than the salary rates for five staff at the financial analyst 5 level, which ranged from $110,300 to $123,100 during this same year. Thus, these five employees received less pay than an employee whose job level required less skill and fewer responsibilities.

According to the director of compensation programs and strategies, the university structured its salary ranges to accommodate salaries for junior-level employees and employees with deep expertise. She also indicated that the Office of the President aligns its salary ranges with the marketplace so it can compete for employees. However, we disagree that the wide salary ranges are necessary because the Office of the President's classification system already ensures salary accommodation for junior-level staff at lower tiers within a series and more experienced staff at higher tiers. In fact, the large salary ranges paired with the classification system create an environment in which staff do not need to perform additional responsibilities to earn higher salaries.

Figure 15
The Office of the President's Salary Ranges Contain Significant Overlap and Are Wider Than the Ranges for Similar Classifications for State Employees
Fiscal Year 2015–16



Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse as well as Office of the President's job specifications, California Department of Human Resources job specifications for comparable job series, and the State of California's CMI service pay scale.

= Actual placement of the Office of the President's employees at their fiscal year 2015–16 salary rates.

* We excluded systemwide employees who are located at campuses because campuses may have different salary ranges.

† The Office of the President did not employ any staff in the entry-level financial analyst 1 position as of fiscal year 2015–16.

The Office of the President Offers a Generous Retirement Benefit That the State Does Not Offer

In addition to paying salaries that significantly exceed those of employees in comparable high-level executive branch positions, the Office of the President spent $2.5 million from fiscal years 2011–12 through 2015–16 to provide a generous retirement benefit to certain executive employees. Specifically, the Office of the President contributes an amount equal to between 3 percent and 5 percent of these executives' monthly base salaries to their retirement savings plans. For example, the former chief compliance and audit officer earned a base salary of $417,200 in fiscal year 2014–15 and would have received $20,900 that year to her elected retirement savings plan. This retirement benefit is in addition to the university's regular pension plan, to which the Office of President contributes 14 percent and employees contribute 8 percent of their gross pay.

Although the State also offers a regular retirement plan to which both it and its employees contribute, the State does not make contributions towards employees' retirement savings plans as an additional benefit.

Furthermore, the Office of the President made a questionable decision about its retirement plan that has drastically increased the amounts it must contribute for all its employees. Beginning in 1990, the Office of the President suspended both its and its employees' contributions into the university retirement plan because of an actuarial study that concluded that the retirement plan was adequately funded for many years into the future. Although the State also suspended executive branch contributions to the state retirement system, it did so only for one year. The Office of the President, however, did not resume the university's contributions until 2010, a 20-year lapse in funding.

Employer-Paid Retirement Savings Contributions for the Office of the President's Employees

FISCAL YEAR	PERCENTAGE OF SALARY	EMPLOYER CONTRIBUTION (IN MILLIONS)
2011–12	7	$8.9
2012–13	10	13.7
2013–14	12	18.1
2014–15	14	22.2
2015–16	14	23.4
	Total	**$86.3**

Sources: California State Auditor's analysis of the University of California's 2016–17 *Budget for Current Operations* and employer contribution amounts the Office of the President provided.

The Office of the President acknowledged that this decision created a serious problem in which the university's retirement plan was underfunded by $12.1 billion as of July 2015. In fact, a July 2010 task force report on the university's retirement benefits program estimated that its retirement plan would have been more than 120 percent funded in 2009 had the university and its employees continued making normal contributions. As shown in the text box, the Office of the President's contributions to its employees' retirement plans have risen dramatically in recent years. It contributed $8.9 million in fiscal year 2011–12, and that amount nearly tripled to $23.4 million in fiscal year 2015–16.

The Office of the President Offers Its Staff Generous Benefits That State Employees Do Not Generally Receive

The Office of the President offers its employees a number of generous benefits, some of which we summarize in Table 9.[5] For example, it spent at least $35.8 million from fiscal years 2012–13 through 2015–16 on travel, meetings, and other related expenses. To understand the policies related to these expenses and determine their prudency, we examined certain categories in detail. Specifically, while the state policy permits the reimbursement of meals for employees on travel and prohibits reimbursement for business meetings with agency employees, the university's policy allows for reimbursements up to $174 per person per day in reimbursements for business meetings and entertainment. As a result, the Office of the President has reimbursed its staff more than $2 million for such expenses since fiscal year 2011–12. Although the Office of the

[5] Please see the note to Table 9 with the ‡ symbol on page 60 for an explanation of why the information in this table is incomplete.

President's executive director of operations asserted that events generally only occur during part of the day, we identified an instance in which the Office of the President paid for all three meals for attendees when it hosted a conference. For a three-day compliance symposium it hosted in 2015, the Office of the President spent $153 in meals per person in one day for about 280 attendees. The total cost of catering for this symposium was $74,000, most of which the Office of the President paid for out of the campus assessment fund. Additionally, the Office of the President spent $2,370 on alcohol that it charged to the Searles Fund, an endowment from a private donor. The Office of the President reclassified the Searles Fund as a discretionary funding source in 2011–12, as discussed in Chapter 1. The Office of the President also spent at least $940,000 in campus assessment funds for food and beverage expenses over the five-year period we reviewed.

Table 9
The Office of the President's Employee Benefits Are More Generous Than the State of California's Policies and Practices

STAFFING BENEFIT	OFFICE OF THE PRESIDENT'S POLICY OR PRACTICE	OFFICE OF THE PRESIDENT'S COST FROM 2011–12 THROUGH 2015–16*	STATE OF CALIFORNIA'S POLICY OR PRACTICE	CALIFORNIA STATE UNIVERSITY'S (CSU) POLICY OR PRACTICE
Car allowance	The president and 23 other staff from the senior management group (SMG) received monthly car allowances up to $743.	$603,900	The Governor and other high-ranking executives receive state cars to use for official state business. The State does not offer employees car allowances.	12 executives from the CSU received a monthly car allowance of $1,000.
Cell phones	The University of California (university) provides cell phones to certain staff. The phones must be primarily for business use.	2,040,300†	Effective February 2017, state agencies must ensure that the use of mobile computing devices will cost-effectively meet a significant business need and increase the efficiency of the agency.	The CSU allows cell phones for certain Chancellor's Office employees who have telecommuting agreements.
Meals	The allowable per-person limit for meals and incidentals for overnight travel is $74 per day.	1,490,300‡	The allowable per-person limit for meals and incidentals for overnight travel is $46 per day.	The allowable per-person limit for meals and incidentals for overnight travel is $62 per day.
Lodging	The cost for lodging must be reasonable and supported by a receipt. The policy recommends that if lodging expenses exceed 200 percent of the federal per diem, the traveler should submit additional documentation supporting the higher lodging rate.	6,724,900‡	The in-state and out-of-state rates for reimbursement range from $90 to $250 per night depending on a traveler's destination. Out-of-country travel reimbursements must not exceed the federal per diem.	For in-state and out-of-state travel, the maximum reimbursement may not exceed $275 per night. Out-of-country travel reimbursements must not exceed the federal per diem.
Business meetings and entertainment	The university may pay or reimburse expenses for meals and light refreshments provided in connection with business meetings and entertainment. The maximum per-person expenditures for meals and light refreshments furnished by the university may not exceed $27 for breakfast, $47 for lunch, $81 for dinner, and $19 for light refreshments, equaling a maximum daily total of $174.	2,151,000‡	The State does not reimburse business meals when agencies call meetings with their own and/or other agency employees to conduct state business. In a limited number of instances, agencies may reimburse employees for meal expenses in connection to official state business with individuals from outside state government.	The CSU reimburses hospitality expenses to the extent that they are necessary, appropriate, reasonable in amount, and serve a purpose consistent with the mission and fiduciary responsibilities of the CSU.

continued on next page . . .

STAFFING BENEFIT	OFFICE OF THE PRESIDENT'S POLICY OR PRACTICE	OFFICE OF THE PRESIDENT'S COST FROM 2011–12 THROUGH 2015–16*	STATE OF CALIFORNIA'S POLICY OR PRACTICE	CALIFORNIA STATE UNIVERSITY'S (CSU) POLICY OR PRACTICE
Relocation allowance	The university provides certain SMG staff with a relocation allowance as part of their employment offers. The only limit on the amount is that it cannot exceed 25 percent of the employees' starting base salaries.	$1,095,300	State employees are eligible for lodging and meal reimbursement for up to 60 days while relocating to a permanent residency at the new location.	The CSU reimburses actual, necessary, and reasonable moving expenses when employees are required to change the place of their residence or when they accept long-term temporary assignments.
Moving reimbursement	The university reimburses certain SMG staff for the costs associated with moving as part of their employment offers.	697,800	The State will reimburse certain employees for the costs associated with moving as part of their employment.	The CSU reimburses actual, necessary, and reasonable moving expenses when employees are appointed.
Employer contributions toward a retirement savings plan for SMGs	In addition to the university's regular pension plan, it makes contributions to retirement savings plans for SMG employees with full-time, nontenured academic appointments at the rate of 3 percent to 5 percent of their monthly base salaries.	2,541,100	Although state employees do participate in a regular pension plan, the State does not offer additional employer contributions toward a retirement savings plan.	Although CSU employees do participate in the State's regular pension plan, the CSU does not offer additional employer contributions toward a retirement savings plan.
Performance bonus	The STAR Program provides employees, excluding SMG staff, with cash awards that may generally not exceed 10 percent of their base salaries or $5,000, whichever is lower. Employees are eligible for this award if they receive a ranking of "meets expectations" or better on their most recent performance evaluation.	1,884,400§	Employees with the State are eligible for cash awards for exceptional performance. Cash awards can range from $50 to $500. Some state agencies have discretion to start their own bonus programs outside of these cash awards.	Some employees are eligible for performance bonuses that amount to up to 15 percent of their salaries when they meet predetermined measurable objectives.
Stipends	Employees may receive an administrative stipend when they temporarily perform responsibilities of higher-level positions. The stipend amount cannot exceed 25 percent of the employee's base salary. Generally, out-of-classification assignments may not exceed 12 months.	2,389,500§	The State will compensate certain employees who temporarily perform duties of higher classifications for more than 15 days with the rates of pay that the employees would receive if the assignments were permanent. Generally, out-of-classification assignments may not exceed four months.	Certain employees temporarily assigned to perform duties of higher classifications receive compensation appropriate to the higher classifications for the duration of the assignments. There is not a limit on the amount of time employees can be in an out-of-classification assignment.
Monetary effect		**$21,618,500**		

Sources: California State Auditor's analysis of data obtained from the Office of the President, Corporate Data Warehouse and Decision Support System, the Office of the President's policies, state policies, and CSU policies.

Note: Total costs rounded to the nearest hundred.

* Except for performance bonuses and stipends, these amounts include payments to Office of the President staff from the Agriculture and Natural Resources division.

† Data only available from July 1, 2012. Amounts for fiscal year 2015–16 include cell phones, wifi-enabled iPads, and hot spots.

‡ We requested the Office of the President to provide expenditures for lodging, meals, business meetings, entertainment, and similar expenses for the five-year period from fiscal years 2011–12 through 2015–16. However, during our quality control review, we determined that the Office of the President did not provide all the expenditures we requested as it excluded foreign travel, catering, and other related expenses. Using the Office of the President's budget data, we determined the Office of the President spent at least $35.8 million over the four-year period from fiscal years 2012–13 through 2015–16 as opposed to the $10.4 million it provided for the five-year period from fiscal years 2011–12 through 2015–16. Thus, the analysis in this table only represents a portion of the Office of the President's actual spending for these purposes.

§ Excludes Office of the President staff from the treasurer, chief investment officer, and health divisions because they receive special bonuses based on specific investment and health performance goals.

Moreover, the Office of the President has not established a maximum rate for reimbursing employees for domestic lodging requests, although we recommended in December 2012 that it do so. Specifically, in our *Investigations of Improper Activities by State Agencies and Employees*, Report I2012-1, we found that a high-level official at the Office of the President wasted more than $6,000 on inappropriate travel expenses. To prevent similar improper expenses in the future, we recommended that the Office of the President revise its policies to include established rates for domestic lodging expenses. In response, the Office of the President provided a policy that *recommended* travelers submit additional documentation when seeking payment for lodging expenses exceeding 200 percent of the federal lodging rate. However, currently, the Office of the President's only requirement for lodging reimbursement is that the cost be reasonable and supported by a receipt. When we informed the Office of the President that its policy did not address our concern, it stated that it would not take any additional action on our recommendation.

From fiscal years 2011–12 through 2015–16, the Office of the President spent at least $8.2 million reimbursing its staff for lodging and meals while on certain types of travel, and our review of three travel expense claims found an instance in which reimbursements exceeded allowable amounts for federal and state employees. Specifically, one employee spent more than $350 per night on a hotel room, even though this cost exceeded the federal and state allowable limits by $140 per night. Similarly, the Office of the President's maximum allowance for meals is $74 per day when its employees travel domestically, while the State's reimbursement rate is capped at $46 per day. In our review of the three travel reimbursement claims, we identified six instances in which employees claimed over the State's maximum meal rate of $46 per day. We also identified other instances in which the Office of the President reimbursed questionable travel expenses, including a ticket for a theater performance and limousine services.

The Office of the President reimbursed questionable travel expenses, including a ticket for a theater performance and limousine services.

Although some of the more than $21.6 million the Office of the President spent on the employee benefits we evaluated was necessary and justified, the Office of the President could better control its costs by evaluating its policies. When we shared Table 9 with the Office of the President, it did not agree with our analysis. For example, the executive director of operations stated that the Office of the President has a rigorous process for approving lodging requests that requires employees to book standard rooms as opposed to clubrooms or suites. However, its process is significantly less rigorous than the processes the State and the federal government use, both of which include caps on the amounts employees may spend on lodging without obtaining additional approval. We question how the Office of the President can ensure that lodging expenses are justified without

establishing a similar threshold. Of further concern is that the Office of the President lacks controls to monitor all of its costs associated with certain benefits. For example, although the Office of the President spent at least $2 million on cell phones and other electronic devices for its employees, it has no formal process for tracking the number of devices it issues.

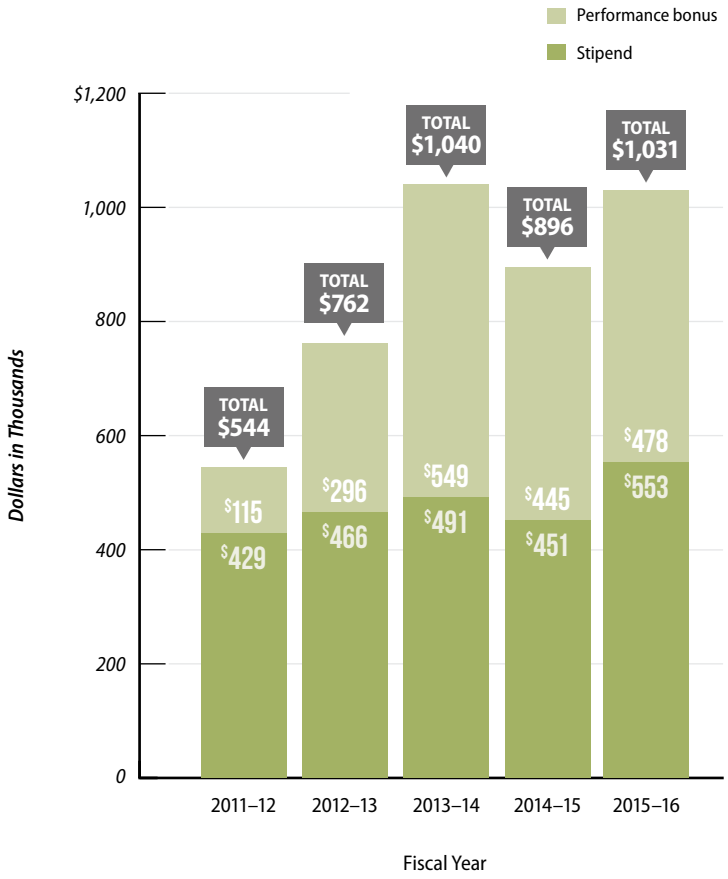
The Office of the President has also spent nearly $4.3 million on staff performance bonuses and stipends since fiscal year 2011–12. It offers certain employees performance bonuses, and it provides stipends to employees who are temporarily assigned higher-level responsibilities that are not part of their normal duties. Figure 16 shows that during the economic crisis the Office of the President awarded fewer bonuses and reduced its spending on stipends; however, as the economy improved, it increased its total spending on stipends and bonuses.

We examined the Office of the President's performance bonus program, which it calls the Staff Appreciation and Recognition (STAR) awards, on which it has spent almost $1.9 million since fiscal year 2011–12. Even though the Office of the President confirmed that it provided its employees with salary increases for three of the last five years, the employees were also eligible for cash awards if they received a rating of "meets expectations" or better on their most recent performance evaluations and their supervisors asserted that they demonstrated "sustained, superior performance." According to personnel data, STAR awards ranged from $30 to $5,300; the chief operating officer must approve awards that exceed $2,500 and the president must approve those that exceed $5,000. Although some state departments have discretion to implement their own bonus programs, CalHR's guidelines specify that performance bonuses for state employees range from $25 to $500 and require employees to exhibit exceptional performance that results in increasing the efficiency of state government.

We identified several instances in which employees received both stipends and bonuses in addition to their regular pay. This appears excessive since the Office of the President already asserts that it pays market-based salaries.

We identified several instances in which employees received both stipends and bonuses in addition to their regular pay. For example, since fiscal year 2011–12, the current director of the operating budget (university budget director) has collected nearly $47,200 in bonuses and stipends. In fiscal year 2012–13 alone, he received more than $18,300 in stipends and a $5,000 bonus in addition to his $122,100 salary. Similarly, the current executive director of student services, whose base salary ranged from $147,400 to $185,300 between fiscal years 2011–12 and 2015–16, received nearly $37,900 in stipends and bonuses. She received bonuses each year for the last four years, ranging from $2,000 to $5,000. Since the Office of the President asserts that it already pays market-based salaries, these stipends and bonuses appear to be excessive.

Figure 16
The Amount the Office of the President Has Spent on Stipends and Performance Bonuses Has Increased Since Fiscal Year 2011–12



Source: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System.

Note: The Office of the President's management and senior professional staff, professional and support staff, and academic staff are eligible to receive bonuses and stipends. Senior management group employees can receive stipends but are not eligible for bonuses. We excluded Office of the President staff from the treasurer, chief investment officer, and health divisions because they are eligible for separate bonuses based on specific investment or health performance goals.

The Office of the President Has Not Completed a Thorough Workforce Plan That Could Enable It to Justify the Size and Cost of Its Staff

The Office of the President has not yet completed a workforce plan that could justify the size of its staff and identify any redundancies between the work it performs and the work the campuses perform. CalHR recommends that agencies adopt a comprehensive workforce plan that addresses their long-term staffing needs over three to five years. It also provides a workforce planning model to help state agencies determine their staffing needs based on current and future business needs. We view this as a best practice

and compared CalHR's guidance in this area with the Office of the President's practices. The Office of the President's current workforce plan template only projects staffing costs for one year and does not include strategies for meeting long-term workforce goals. Instead, the template simply calculates each division's projection of its staff costs for the year without consideration of the Office of the President's mission or goals.

Until it implements a true workforce plan, the Office of the President is at risk both for maintaining redundant positions and for not having the appropriate number and type of staff to meet its needs.

As shown in Table 10, the CalHR model involves five separate phases. Although the Office of the President has partially completed some of these phases, it has not started others. We believe that until it implements a true workforce plan similar to the model CalHR recommends, the Office of the President is at risk both for maintaining redundant positions and for not having the appropriate number and type of staff to meet its needs.

The Office of the President has only partially completed the first step of CalHR's model, which involves setting the strategic direction for an entity's workforce plan. CalHR states that an agency should develop a strategic plan that outlines its critical functions and factors that may impact its workforce. Although the Office of the President has yet to develop a plan for itself as a whole organization, three of its 11 divisions participating in the Office of the President's strategic planning have completed strategic plans. For example, the chief financial officer's division has adopted a strategic plan that defines the objectives for this division and provides a timeline for completing these objectives. Although the divisions' individual plans are likely helpful, they cannot take the place of an overarching strategic plan that would guide the organization as a whole.

In addition, the Office of the President has only partially completed the second phase of the workforce plan model, which involves developing a current workforce profile and analyzing current and future staffing needs. In January 2014, as part of a measure intended to cap the Office of the President's budget, the president issued a directive calling for its divisions to develop such staffing analyses. The directive also stated that the Office of the President would review its budget to determine its appropriate size, shape, and role, and it would identify internal redundancies within the Office of the President and overlap with campuses. However, the deputy chief of staff stated that the president did not intend this directive to result in a report and that no documentation exists demonstrating what services or programs the Office of the President found to be redundant. Rather, the president's intent was that divisions develop more thoughtful ways to prepare their budgets. Nevertheless, changes to the budget process do not appear to us to have met the president's directive.

Table 10
The Office of the President's Steps to Evaluate Its Organization Fall Short of the Best Practices Advocated by the California Department of Human Resources' Workforce Planning Model

CALIFORNIA DEPARTMENT OF HUMAN RESOURCES' WORKFORCE PLANNING MODEL	PHASE 1 SET THE STRATEGIC DIRECTION FOR THE WORKFORCE PLAN	PHASE 2 GATHER AND ANALYZE DEPARTMENTAL DATA FOR THE WORKFORCE PLAN	PHASE 3 DEVELOP THE WORKFORCE STRATEGIES AND PLAN	PHASE 4 IMPLEMENT STRATEGIES	PHASE 5 EVALUATE THE WORKFORCE PLAN
Purpose	The organization determines its strategic goals so that the workforce plan can align staffing and business needs to meet these goals.	The organization analyzes its current workforce and its skills. It should determine gaps between its current workforce and its current and future needs to fulfill its goals. It should also project changes to its workforce.	Based on the strategic plan and the workforce analysis, the organization develops a comprehensive plan to meet its workforce needs over the next three to five years.	The organization communicates its plan to its employees and carries out the strategies developed in the workforce plan.	The organization reviews its workforce plan after it is implemented to ensure that the organization is meeting its goals.
Deliverable	A document that outlines the strategic goals of the organization. This should identify factors such as technological or economic changes that could impact the organization's workforce.	A comprehensive analysis of the organization's staffing and competency gaps. This includes a list of positions that pose a risk because of retirement, vacancies, critical importance, or other factors that could impact the organization.	A workforce plan that includes strategies for reaching the workforce the organization needs over the next three to five years. It should include general steps, an estimated budget, and milestones for fulfilling these strategies.	Completion of the workforce plan by the organization under the direction of a steering committee.	An evaluation of the results of the workforce plan and revisions, if necessary.
	STATUS				
	PARTIALLY COMPLETED	PARTIALLY COMPLETED	NOT COMPLETED	NOT COMPLETED	NOT COMPLETED
Office of the President Actions	The Office of the President does not have a strategic plan that documents its critical functions and the internal and external factors that impact its workforce. Three out of 11 divisions participating in the Office of the President's strategic planning have strategic plans and the other divisions are in the process of developing strategic plans to be completed by December 2017.	None of the workforce-related documents the Office of the President provided contained an analysis of staffing and competency gaps, although it has some staffing data that could inform this analysis.	The Office of the President does not have a workforce plan that meets this model.	This phase cannot be completed because the Office of the President does not have a workforce plan as described in phase 3.	This phase cannot be completed because the Office of the President does not have a workforce plan as described in phase 3.

Sources: California State Auditor's analysis of California Department of Human Resources' workforce planning model, which we consider a best practice, and the documentation provided by the Office of the President related to workforce planning activities.

Despite a presidential directive to assess the Office of the President's size, shape, and role, it cannot demonstrate that it identified and eliminated internal redundancies and overlap with campuses, as the president intended.

Because of the lack of documentation related to that review, the Office of the President cannot demonstrate whether it is the appropriate size, shape, or fulfills an appropriate role. Moreover, the Office of the President could not show us that it had identified and eliminated internal redundancies and overlap with the campuses, as the president intended. The deputy chief of staff stated that any cost savings realized as part of the review process were reflected in the fiscal year 2015–16 budget. However, the fiscal year 2015–16 budget the Office of the President presented to the regents included $36 million more in spending than the fiscal year 2014–15 budget. Furthermore, despite the directive, the Office of the President's staff in Oakland and at the campuses grew from 1,577 staff in 2012–13—the fiscal year before the budget review announcement—to 1,667 staff in 2015–16.

Additionally, the Office of the President implemented an internal realignment of its chief operating officer's division and its chief financial officer's division in 2014 that could have streamlined operations in the two divisions but that did not include proposals to change staffing levels or eliminate redundancies. Consequently, the Office of the President missed an opportunity to identify and address potential staffing excesses. According to an Office of the President's presentation to its staff in 2014 describing the realignment, its goal was to improve the organization's effectiveness and efficiency. However, it does not state that reducing staff was a goal. After analyzing the Office of the President's staffing levels in Oakland, we found that staff increased by 3 percent, or 38 staff, from fiscal years 2013–14 through 2015–16.

The Office of the President also has not completed the third phase of the best practices workforce planning model, which is to develop workforce strategies and plans, but it has adopted a process designed to control staff increases that could be part of the fourth phase, which is to implement strategies. Specifically, in September 2013, the Office of the President implemented a position control process to regulate staff levels and costs. This process—which is facilitated over email—requires management approval of all proposals to temporarily or permanently fill positions in addition to an assessment of whether each position overlaps or is redundant to another position within the Office of the President. This process could have ensured that the Office of the President only filled positions that fit within its strategic goals had it previously identified such goals. Instead, it did not prevent the Office of the President's staffing levels from increasing. In fact, the Office of the President was unable to demonstrate management approval for 19 of the 35 new or refilled positions we reviewed, and it was only able to provide four of the redundancy analyses required for these positions because of its email retention policy. Therefore, we cannot determine how effectively this process was implemented.

Ultimately, we believe that the Office of the President needs to engage in a workforce planning process that follows CalHR's model to ensure that it can justify its staffing levels and costs. Further, the Office of the President should obtain feedback from the campuses—which are key stakeholders—as part of this process. In addition, the Office of the President should perform and document an assessment of whether its positions overlap or are redundant to other positions within it. Finally, the Office of the President should make its workforce plan publicly available to show that it is using its resources effectively.

Recommendations

The Office of the President

To ensure that its staffing costs align with the needs of campuses and other stakeholders, the Office of the President should do the following:

By April 2018

- Develop a method for weighing comparable public and private sector pay data when establishing salaries for all positions.
- Determine how to restructure salary ranges to make certain the ranges encourage employee development and ensure pay equity.
- Evaluate and identify needed changes in employee benefit policies to ensure that they include reasonable safeguards to control costs.
- Complete phase one of CalHR's best-practice workforce planning model by developing a strategic direction for its workforce plan.

By April 2019

- Set targets for any needed reductions to salary amounts using the results from its public and private sector comparison and adjust its salaries accordingly.
- Narrow its salary ranges.
- Set targets for appropriate employee benefits and implement new processes that ensure that employees adhere to the revised policies regarding employee benefits.

- Create a plan for reallocating funds that it saves to campuses as it reduces its staffing costs.

- Implement phase two of CalHR's best-practice workforce planning model by determining its current and future staffing and competency gaps. As part of this phase, the Office of the President should consider the input of stakeholders, including campuses and students, regarding which elements of its organization are of critical importance and which elements it could eliminate or downsize.

By April 2020

- Adjust its salary levels and ranges to meet its established targets.

- Adjust its employee benefits to meet its established targets.

- Reallocate funds to campuses when adjustments to its salaries and benefits result in savings.

- Implement phase three of CalHR's best-practice workforce planning model by presenting the final workforce plan to its staff and beginning its implementation by carrying out workforce planning strategies covering a three-to five-year period. The Office of the President should make its final workforce plan publicly available.

- Implement phases four and five of CalHR's best practice workforce planning model by implementing its workforce plan strategies and annually evaluating the completed workforce plan strategies against defined performance indicators and revising the plan where necessary.

- Report to the regents on the amount of funds it reallocates to campuses as a result of implementing our recommendations.

The Regents

To ensure that the Office of the President's staffing levels are justified and that costs are reasonable and align with the needs of campuses and other stakeholders, the regents should require the Office of the President to implement our recommendations and report periodically on its progress.

Chapter 3

SIGNIFICANT CHANGE IS NECESSARY TO ENSURE THAT THE OFFICE OF THE PRESIDENT'S ACTIONS ALIGN WITH THE MISSION OF THE UNIVERSITY OF CALIFORNIA

Chapter Summary

Significant change is necessary to ensure the future accountability, transparency, and efficiency of the University of California (university) Office of the President. In particular, we found that the Office of the President budgeted about $210 million in discretionary money for systemwide initiatives in fiscal year 2015–16, using funds that the campuses could have otherwise spent on other priorities. Although many of these initiatives provide academic or public benefits, we question the Office of the President's decision to prioritize them over other activities such as campus spending on students especially given it has not sufficiently evaluated these initiatives' purpose and intent. Further, even though it has publicly stated that it has consolidated its own and the campuses' operations, both the Office of the President and campus administrative costs have increased, and the Office of the President's budget and staff exceed those of the central administration at comparable institutions. Moreover, we found that the Office of the President has not established a consistent definition for or method of tracking its administrative spending. Because a clear definition is lacking, we do not believe the Office of the President has fully justified its administrative costs.

In addition, the Office of the President's actions have limited its transparency and made it difficult for stakeholders—including the University of California Board of Regents (regents)—to hold it accountable. For example, it has at times made inaccurate and misleading claims to the regents, the Legislature, and the public about its budget. Further, it interfered with surveys we sent to campuses, which we intended to use to evaluate the services it performs. Auditing standards require that we disclose this interference and prohibit us from drawing conclusions based on this portion of our work. As a consequence of these concerns and the other problems we have highlighted throughout this report, we believe the Legislature needs to take a more significant role in ensuring that the Office of the President implements necessary reforms.

The Office of the President's Poor Tracking and Monitoring of Its Systemwide Initiatives Convolutes Its Administrative Cost Totals

The Office of the President has not prioritized its spending decisions to ensure that the university system is able to dedicate the maximum amount of funding possible to supporting its priority of access and

affordability for California residents. The Office of the President defines *systemwide initiatives* as initiatives that it administers or funds for the benefit of the entire university. Systemwide initiatives include critical academic and research programs, such as the University of California Observatories and the California Institutes for Science and Innovation, and non-campus based academic research programs, such as the University of California Washington Center. Some systemwide initiatives were established by the Legislature; examples include the California Breast Cancer Research Program and University of California, Berkeley, Institute of Transportation Studies. However, we found that the Office of the President does not adequately track all of its systemwide initiatives' costs or systematically assess their continued benefit to the university system.

According to the Office of the President, systemwide initiatives account for half of its annual disclosed budget. However, when we requested a list of systemwide initiatives and their associated costs, the Office of the President could not provide a complete listing of the systemwide initiatives it administers. Based on the documents we obtained, we identified at least 79 systemwide initiatives, with a total cost that we estimated at $434 million in fiscal year 2015–16, as Table 11 shows.[6] For some of the initiatives—highlighted in grey in Table 11—the Office of the President has provided funding to campuses and programs, and it assumed they spent the full amount rather than monitoring the use of these funds. Thus, it does not have actual expenditure data for these systemwide initiatives, nor does it know with certainty if these initiatives are delivering their intended benefits.

The Office of the President's definition of activities that constitute systemwide initiatives is broad and inconsistent.

The Office of the President's definition of activities that constitute systemwide initiatives is broad and inconsistent. Consequently, some of the items the Office of the President identifies as systemwide initiatives in its budget data—but has not presented as such to the regents—are of questionable benefit to the entire university system. For example, we believe initiatives such as the president's residence and the deficit related to the Office of the President's general counsel's office should not be classified as systemwide initiatives in the Office of the President's budget data. Moreover, we identified several examples of expenditures that the Office of the President reclassified as systemwide initiatives after initially classifying them as regular administrative expenses. For example, the Office of the President classified UCPath—the university's replacement payroll and human resources system—as part of its central administrative budget in fiscal years 2013–14 and

[6] Our estimated cost of systemwide initiatives is higher than what the Office of the President includes in the budget it presents to the regents because we include the disclosed and undisclosed budget totals for systemwide initiatives. For example, we include an additional $90 million for Agriculture and Natural Resources that is not presented to the regents.

2015–16 but changed it to a systemwide initiative in fiscal year 2016–17. In another example, in fiscal year 2014–15, the Office of the President reclassified $4 million in lab management expenditures from a regular administrative expense to a systemwide initiative. According to Office of the President staff, it made these changes to highlight the systemwide nature and benefits of both programs. It also stated that it will move UCPath back to the central administration for the fiscal year 2017–18 budget. However, with a very broad and inconsistent definition of what activities constitute a systemwide initiative, the decisions to reclassify these expenditures appear arbitrary.

Table 11
The Office of the President Does Not Consistently Track Spending on Systemwide Initiatives
Fiscal Year 2015–16

COUNT	SYSTEMWIDE INITIATIVE	ESTIMATED EXPENDITURES	ESTIMATED AMOUNT (UNDER)/OVER BUDGET
Category: Academic Support		**$48,588,000**	**$(5,170,000)**
1	California Digital Library	$21,909,000	$(944,000)
2	Casa de California	266,000	(382,000)
3	Graduate Fellows	41,000	–
4	Mathematics Diagnostic Testing Project	59,000	–
5	Academic Senate	2,022,000	(55,000)
6	University of California Press	22,960,000	(2,621,000)
7	Historically Black Colleges and Universities Initiative	1,207,000	(1,156,000)
8	President's Postdoctoral Fellowship Program	75,000	3,000
9	Librarian's Association of the University of California	49,000	(15,000)
Category: Agriculture and Natural Resources		**$188,568,000**	**$2,006,000**
10	Division of Agriculture and Natural Resources	$188,568,000	$2,006,000
Category: Instruction		**$52,737,000**	**$(1,861,000)**
11	University of California Education Abroad Program	$34,983,000	–
12	Governor's Teacher Scholars Program	320,000	–
13	Innovative Learning Technology Initiative	10,045,000	$45,000
14	Principal Leadership Institutes	300,000	–
15	University of California Online	519,000	519,000
16	University of California Sacramento Center	674,000	–
17	University of California Washington Center	4,700,000	(2,425,000)
18	President's Postdoctoral Fellowship Program	1,196,000	–
Category: National Laboratories		**$3,714,000**	**$(826,000)**
19	Office of the National Laboratories	$3,714,000	$(826,000)
Category: Presidential Initiatives*		**$8,244,000**	**$(6,580,000)**
20	Presidential Initiatives	$8,244,000	$(6,580,000)

continued on next page . . .

COUNT	SYSTEMWIDE INITIATIVE	ESTIMATED EXPENDITURES	ESTIMATED AMOUNT (UNDER)/OVER BUDGET
Category: Public Service		**$27,452,000**	**$(5,039,000)**
21	Armenian University Project	$(2,000)	$(2,000)
22	California Subject Matter Project	7,191,000	(1,943,000)
23	Community College Assist Program	1,371,000	215,000
24	Career Technical Education Initiative	–	–
25	Diversity Pipeline	547,000	97,000
26	Gaining Early Awareness and Readiness for Undergraduate Programs	4,721,000	(279,000)
27	Graduate and Professional Outreach	4,000	(42,000)
28	High School Articulation	883,000	(218,000)
29	Mathematics Diagnostic Testing Project	224,000	(755,000)
30	Student Academic Preparation and Educational Partnerships	8,756,000	(1,524,000)
31	Student Preparation	$280,000	$(530,000)
32	Science and Math Teacher Initiative	191,000	(12,000)
33	Teaching, Learning, and Leadership	49,000	(1,000)
34	Transfer Articulation	248,000	(73,000)
35	University of California Leads	97,000	45,000
36	University of California Curriculum Integration	543,000	(17,000)
37	University of California–Mexico Initiative	2,349,000	–
Category: Research		**$88,399,000**	**$(25,829,000)**
38	Breast Cancer Research	$1,783,000	$(8,616,000)
39	California Cancer Research	2,271,000	(129,000)
40	California Institute for Science and Innovation	16,660,000	–
41	California Program on Access to Care	935,000	–
42	California State Summer School for Mathematics and Science	241,000	–
43	California Advancement Research Association Board	5,000	–
44	Center for Health Quality and Innovation	1,142,000	(3,411,000)
45	David Hayes-Bautista Project	557,000	–
46	Discovery Grants	–	–
47	Drew Matching Funds	475,000	–
48	Health Affairs	2,163,000	140,000
49	California Human Immunodeficiency Virus/Acquired Immune Deficiency Syndrome Research	1,201,000	(7,566,000)
50	University of California, Berkeley, Institute of Transportation Studies	980,000	–
51	Los Alamos National Security/Lawrence Livermore National Security	(57,000)	(9,845,000)
52	Natural Reserve System	2,892,000	255,000
53	New Graduate Studies Initiative	25,000	(975,000)
54	Research Program Communication Support	–	–
55	Research Program Evaluation	–	–
56	Research Grants Program Office	16,000	16,000
57	Song Brown Act	100,000	–
58	Special Research Program	24,598,000	24,636,000
59	Tobacco-Related Disease Research Program	1,590,000	(8,538,000)
60	University of California Institute for Mexico and the United States	930,000	–

COUNT	SYSTEMWIDE INITIATIVE	ESTIMATED EXPENDITURES	ESTIMATED AMOUNT (UNDER)/OVER BUDGET
61	University of California Observatories	$20,511,000	$91,000
62	University of California Research Initiatives	9,907,000	(342,000)
63	Historically Black Colleges and Universities Initiative	1,806,000	(103,000)
64	Youth Leadership	50,000	–
65	Social Security/Double Taxation	187,000	–
66	President's Postdoctoral Fellowship Program	511,000	–
67	Non-Multicampus Research Unit	(3,080,000)	(11,442,000)
Category: Other Systemwide Initiatives in Budget Data but Not Classified as Systemwide Programs in Presentation to Regents		**$16,325,000**	**$(3,563,000)**
68	Advocacy Communication	$184,000	–
69	Chancellor's House Maintenance	1,030,000	–
70	Collaborative Exchange	144,000	–
71	Fresno Center Debt Service	647,000	$(43,000)
72	Sustainability	291,000	20,000
73	UCPath†	12,194,000	(3,401,000)
74	President's Residence	253,000	–
75	Chancellor's Administrative Funds	435,000	–
76	Chancellor Inaugurations	–	(197,000)
77	Office of the General Counsel Deficit	854,000	–
78	Presidents Emeriti Expenses	163,000	58,000
79	Special Supplemental Retirement Contribution	130,000	–
		$434,027,000	**$(46,862,000)**

Sources: California State Auditor's analysis of data from the Office of the President's budget development system and other information regarding systemwide initiatives and programs.

Note 1: The Office of the President's budget development system does not consistently track budgets, reimbursements, or expenditures for systemwide initiatives. For example, many systemwide initiatives have a budget but no actual expenditures. As a result, the amounts we present in this table represent estimates of the amount the Office of the President budgeted and spent on systemwide initiatives.

Note 2: Cells without amounts either contain an amount less than $1,000 or received an adjustment.

[ ] The Office of the President's data did not show complete actual expenditures for some of its accounts because it assumes all budgeted amounts were spent. Thus, we use the amount budgeted to estimate the actual expenditure. Systemwide initiatives can have multiple accounts.

[ ] Agriculture and Natural Resources is highlighted in green because these amounts are its total expenditures, which Agriculture and Natural Resources provided us. The Office of the President's budget data did not include the Agriculture and Natural Resources' total expenditures.

* Although the Office of the President's budget system contains one category labeled *presidential initiatives*, we show 24 different presidential initiatives as of fiscal year 2015–16 in Figure 17 on page 76. The Office of the President labels some presidential initiatives, such as UCPath, separately in its budget system.

† UCPath is the university's replacement payroll and human resources system.

Moreover, the manner in which the Office of the President presents the costs of these initiatives to the regents and the Legislature is misleading and obscures the amount the Office of the President spends to actually administer the university. For example, in its 2016–17 *Budget for Current Operations*—which is one way it communicates its budget to the public—the Office of the President stated that half of its budget supports systemwide initiatives and that the other half supports central and administrative services. The costs related to the central and administrative services represented about 1 percent of the university's overall budget.

However, our analysis demonstrates that the Office of the President's claim that it spent only about $314 million in fiscal year 2015–16 to administer the university is inaccurate because its administrative budget did not always account for administrative activities connected to systemwide initiatives. For example, the Office of the President's budget data shows that in fiscal year 2015–16, $500,000 was budgeted for administration of the Breast Cancer Research Program, but this was captured in the systemwide initiatives budget.

Furthermore, the Office of the President does not regularly evaluate those programs that it classifies as systemwide initiatives to assess their continued benefit to the university. We acknowledge that many of these initiatives undoubtedly have value. However, absent any analysis of the benefits the systemwide initiatives may provide, we question the Office of the President's decision to prioritize these initiatives over other priorities, such as campus spending on students. This is particularly important given that the State's recent budget crises and the university's decision to raise tuition have increased the financial burden on students and their families. The Office of the President budgeted about $210 million in discretionary revenue in fiscal year 2015–16 alone to pay for 55 of the 79 systemwide initiatives we identified. About 90 percent of the Office of the President's discretionary revenue in fiscal year 2015–16 came from the annual assessment it levied on the campuses. In other words, the campuses indirectly paid for many of these initiatives.

We acknowledge that many of these initiatives undoubtedly have value, but question the Office of the President's decision to prioritize these initiatives over other priorities, such as campus spending on students.

Given the number of systemwide initiatives that we identified, we believe that opportunities exist for the Office of the President to evaluate their continued prioritization and to allow campuses to retain more of their own funds. For example, because the Office of the President funds many of the systemwide initiatives—such as advocacy communication and special supplemental retirement contributions—using discretionary revenue, it ostensibly has significant discretion to decide whether to continue funding them at their current levels. Further, in our March 2016 audit report, *The University of California: Its Admission and Financial Decisions Have Disadvantaged California Resident Students*, Report 2015-107, we listed 18 programs that we recommended the Office of the President evaluate in light of its own and the State's current priorities. Eight of the 18 programs, with a combined cost of $49 million in fiscal year 2014–15, pertain directly to the Office of the President's spending on systemwide initiatives and may present an opportunity for reductions in funding, possibly through the identification of alternative sources to pay for them. Specifically, to provide the university more flexibility in allocating its funds, in fiscal year 2012–13 the Governor eliminated earmarks for specific programs, such as the California Human Immunodeficiency Virus/Acquired Immune Deficiency Syndrome Research program. Yet as we noted in our previous report, the university has continued to fund these programs despite internal evaluations indicating that they could be funded using other sources.

Spending on Presidential Initiatives Shifts Funding Away From Campus Priorities

The Office of the President also budgets $10 million per year of discretionary funds on what it calls *presidential initiatives*, which represent a subset of systemwide initiatives. The cost of presidential initiatives—which are discretionary programs launched by the university president—increased from about $4 million in fiscal year 2012–13 to about $23 million in fiscal year 2015–16. As Figure 17 on the following page shows the Office of the President's presidential initiatives increased by 10 programs from fiscal years 2012–13 through 2015–16. For example, the Global Food Initiative—at an estimated cost of $1.5 million—is a program that the president, together with campus chancellors, implemented in 2014 to enhance collaboration and research related to food security and health among the university campuses, the Lawrence Berkeley National Laboratory, and Agriculture and Natural Resources.

The cost of presidential initiatives—which are discretionary programs launched by the president—increased from about $4 million in fiscal year 2012–13 to about $23 million in fiscal year 2015–16.

Similar to our concern with systemwide initiatives, we question the prioritization of some of these expenditures over other university priorities, such as direct campus spending on students especially given it has not sufficiently evaluated these initiatives' purpose and intent. As an example of a questionable spending decision on a presidential initiative, since fiscal year 2012–13, the Office of the President has spent $1.4 million on Casa de California—a facility in Mexico City that is part of its University of California's Mexico Initiative. In 2015 the Office of the President asserted that Casa de California's Casona—a building located on the property—had been underused since the Office of the President purchased it in 2003. In fact, the Office of the President's chief risk officer advised that the university not use the building for any events or program activities until it completed deferred maintenance and upgrade work to address serious safety issues. Through its decision memo process, which we describe in Chapter 1, the president elected to keep the property and approved using $323,400 in unspent campus assessment dollars, previously allocated to the Casa de California, for essential repairs and upgrades, like replacing the roof. Considering that the Office of the President acknowledged the building had been underused since 2003, the decision to continue to invest campus funds on Casa de California is questionable.

Further, the Office of the President can require that campuses directly invest funds in presidential initiatives. For example, both the Office of the President and the campuses are bearing the project development costs associated with UCPath, which as of April 2017 was estimated to cost $504 million. This investment in UCPath further decreased the amounts the campuses had available to spend on their own priorities, such as instruction or student housing. According to executive management at the Riverside and Santa Cruz campuses, the Office of the President's increases in spending have shifted money away from campus priorities like instruction, academic support, and

student housing. In general, because smaller campuses have greater difficulty increasing discretionary revenue, the Office of the President's spending decisions have a greater impact on their budgets.

Figure 17
The Number of Presidential Initiatives Has Increased Since Fiscal Year 2012–13

		FISCAL YEAR			
	INITIATIVE TITLE	2012–13	2013–14	2014–15	2015–16
1	Historically Black Colleges and Universities				
2	Accountability Report				
3	Blue and Gold Opportunity Plan				
4	UCPath*				
5	Science and Mathematics Teacher Initiative				
6	Sustainability				
7	Working Smarter				
8	Innovative Learning Technology Initiative				
9	University of California Online				
10	Enterprise Risk Management				
11	Commission on the Future				
12	Campus Climate				
13	Project You Can				
14	Data Improvement Project				
15	Civil Disobedience Initiative				
16	Innovation and Entrepreneurship Initiative				
17	Global Food Initiative				
18	President's Postdoctoral Fellowship Program				
19	Undocumented Students Initiative				
20	Transfer Students Action Team				
21	University of California–Mexico Initiative				
22	Carbon Neutrality Initiative				
23	Research Catalyst Awards				
24	University of California–Oakland Partnership				
25	We Vote				
26	Lesbian-Gay-Bisexual-Transgender Initiative				
27	Staff Appreciation				
28	Sexual Violence Initiatives				
29	Western Hemisphere Initiative				
30	Blum Federation Grant				
31	Various Initiative-Related Charges				
32	Staff Education Scholarships				
	Total presidential initiatives	**14**	**18**	**25**	**24**

Sources: California State Auditor's analysis of initiatives reported on the Office of the President's website and information provided by the Office of the President.

* UCPath is the university's replacement payroll and human resources system.

= Presidential initiative.

= No longer identified as a presidential initiative online but ongoing as of February 2017.

The Riverside campus' vice chancellor for planning and budget stated that even if these systemwide initiatives are valuable, there are always more requests for funding than there are resources available, consequently, she believes that the Office of the President needs to consider its activities in collaboration with the campuses and in terms of trade-offs. Similarly, executive management at Santa Cruz stated that Office of the President's initiatives crowd out campus discretionary spending and that the campus could otherwise use the funds for instruction, research, academic support, or deferred maintenance. In fact, a former university president stated in a 2008 letter to the regents that spending on discretionary programs diverts funds away from campuses. To ensure that campus spending remains a priority, we believe the Office of the President should work with campuses and students to evaluate the purpose, intent, and prioritization of these initiatives.

To ensure that campus spending remains a priority, the Office of the President should work with campuses and students to evaluate the purpose, intent, and prioritization of these initiatives.

The University's Administrative Spending Has Increased and the Office of the President's Budget and Staff Exceeds Those of Similar Institutions

Although we have concerns about the accuracy of the Office of the President's tracking of the university's administrative costs, its data indicate that its administrative spending has increased by 28 percent, or $80 million, since fiscal year 2012–13. Further, its budget and staffing levels are larger than the central administrations of comparable institutions, in part, because the Office of the President manages certain systemwide activities other institutions do not, such as the university's retirement program. In addition to our concerns with the lack of a standard definition of administrative costs and a consistent method of categorizing its costs, we question whether the Office of the President can adequately justify the university's administrative expenses.

The Office of the President Cannot Accurately Determine Its or the Campuses' Administrative Costs

The Office of the President does not have a standard definition for or method of tracking its administrative costs. Instead, it separates its expenditures into central administration services and systemwide initiatives. However, because the Office of the President does not consistently use these two categories, neither accurately depicts its administrative costs. As we discuss in the Introduction, the Office of the President and the campuses track costs using the higher education expenditures categories developed by the National Association of College and University Business Officers (NACUBO). In fact, the Office of the President at times presents its expenditures in these NACUBO categories,

including in the Governor's Budget. For that reason, we used these categories in our attempt to determine how much the Office of the President and the university as a whole spend on administration.

Nonetheless, the NACUBO uniform accounting structure does not clearly delineate the university's administrative costs. As Table 12 demonstrates, the institutional support, academic support, and operations categories are all largely—rather than wholly—administrative in nature. For example, institutional support includes costs associated with activities such as on-campus law enforcement that could be viewed as a direct student service. Similarly, academic support includes costs associated with campus libraries—another activity that could be considered a direct student service. Further, every category we termed *largely nonadministrative* includes some elements of administrative overhead. For example, the student services category includes costs associated with the administration of financial aid and the management of student admissions and records—activities that could both be considered administrative. As a result of these overlaps, accurately determining the university's administrative costs is difficult, if not impossible.

Table 12
The University of California's Functional Categories Do Not Clearly Delineate Administrative Activities

UNIVERSITY OF CALIFORNIA FUNCTION CATEGORY	DESCRIPTION
Largely Administrative	
Institutional support	Central, executive-level activities concerned with management and long-range planning for the entire university, containing many of the university's administrative costs. These activities include the Office of the President, campus chancellors, procurement, accounting, and human resources.
Academic support	Support services for the university's missions of instruction, research, and public service, including academic administration and computing support.
Operation and maintenance of plant	Maintenance of the institution's physical plant, including utilities, facilities services, and related administration.
Largely Nonadministrative	
Instruction	Activities that are part of the university's instruction program, including academic and vocational instruction, research, summer sessions, and university extensions.
Research	Activities specifically organized to produce individual or project research, as well as research from institutes and research centers.
Public service	Noninstructional services beneficial to individuals and groups external to the university, such as community service programs.
Student services	Noninstructional activities related to students, including admissions, registrars' offices, athletics, student health services, and counseling.
Student financial aid	Scholarships and fellowships in the form of grants to students.
Auxiliary enterprises	Entities that furnish goods or services, such as parking and food services to students, faculty, and staff.
Teaching hospitals	Patient care operations of hospitals, including nursing and other professional services, general services, administrative services, fiscal services, and charges for physical plant operations.

Source: California State Auditor's analysis of the University of California's *Uniform Accounting Structure Manual* and the National Association of Colleges and University Business Officers' functional categories.

Further, the Office of the President's lax oversight leads us to question the accuracy of the university's NACUBO data. The university's decentralized financial reporting system relies on each campus to implement its own set of practices to record and report expenditures by category. The Office of the President's systemwide controller explained that the unique organizational arrangement at each campus and the broad NACUBO functional definitions mean that each campus must exercise judgment and subjectivity when assigning expenditures by category, leading to inconsistent practices among the campuses.

These inconsistencies are compounded because the Office of the President does not monitor expenditures by functional category but rather relies on the campuses to report this information correctly. Further, the university does not require its independent auditor to audit the categories for accuracy. Given the opportunities for inconsistency and the absence of oversight by the Office of the President, analyses of campuses' administrative expenditures are not likely to be accurate or reliable. For example, the director of general accounting for the San Diego campus explained that the campus overstated its institutional support expenditures by $19 million and $23 million in fiscal years 2014–15 and 2015–16, respectively, because it unintentionally misclassified some costs. The university's inaccurate reporting is of further concern because the university reports its expenditures by function as part of the annual Governor's Budget.

The Administrative Costs of the Office of the President and the Campuses Have Increased in Recent Years

Even though we have concerns with the accuracy of the NACUBO categories, we used them to evaluate whether the administrative costs of the Office of the President and the campuses were reasonable because these categories represent the best data available. Our analysis found that over four years, the Office of the President spent an average of 69 percent of its total expenditures on administrative costs, while campuses consistently spent 14 percent of their expenditures on administrative functions. In its 2015–16 *Budget for Current Operations*, the Office of the President stated that in response to budget cuts, university administrative units had implemented new processes, improved their use of technology, and consolidated their operations to increase productivity in order to meet increasing workload demands under constrained budget circumstances. Nonetheless, since fiscal year 2012–13, both campus and Office of the President administrative costs have increased by almost 26 and 28 percent, respectively.

Both campus and Office of the President administrative costs have increased by almost 26 and 28 percent, respectively.

The expenditure data also show that although campus administrative costs have increased at the same rate as their nonadministrative costs, the Office of the President's administrative costs have escalated while its nonadministrative costs dropped. Specifically, at the campuses, both administrative and nonadministrative categories have grown by about 27 percent. In total, campus administrative costs increased by $800 million and nonadministrative costs increased by more than $5 billion from fiscal years 2012–13 through 2015–16. In contrast, the Office of the President's administrative costs increased over this same time period by 28 percent, or $80 million, while its nonadministrative costs *decreased* by 15 percent, or $24 million. Causes for the increases to the Office of the President's administrative costs include UCPath and a procurement initiative—an effort to centralize contracting efforts for the university. Figure 18 shows changes to administrative and nonadministrative costs at the campuses and the Office of the President since fiscal year 2012–13.

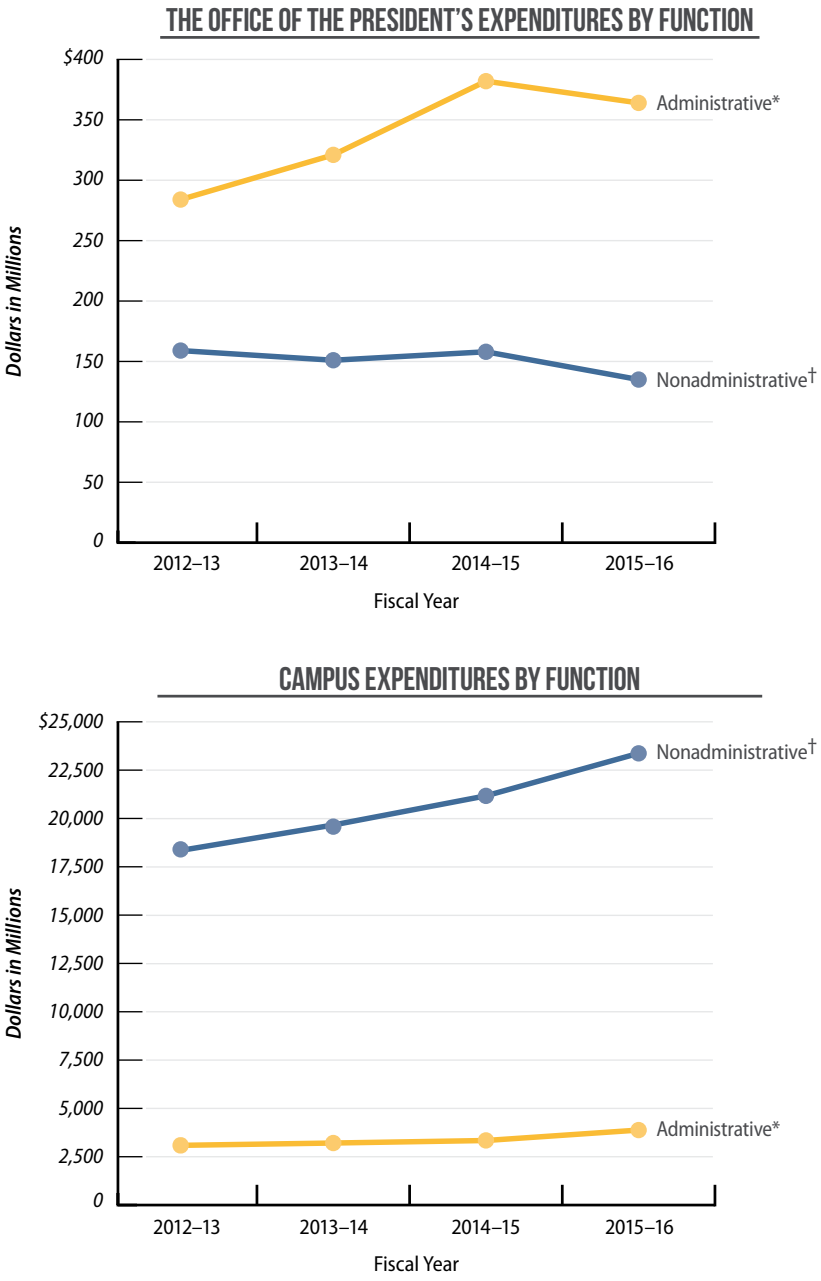
The Office of the President's Budget and Staffing Levels Exceed Those of the Central Administrations at Comparable Institutions

Additionally, we found that the Office of the President's annual budget and staffing levels are higher than the central administrations at comparable public universities. Specifically, we identified the University of Texas (Texas), the State University System of Florida (Florida), and the California State University (CSU) as comparable because of their size and because they have central administrative offices that provide services for multiple campuses. Our review of budget and staffing data for these institutions indicates that for fiscal year 2015–16, the Office of the President's $655 million disclosed budget and 1,667 staff exceeded the cost and size of the central administrations for these institutions. Table 13 on page 82 shows the Office of the President's budget and staffing levels compared to the central administrations of the comparable institutions.

The Office of the President stated that it may spend more on administration than other institutions, in part, because it provides services to its campuses and employees that other universities do not provide, such as retirement management. Moreover, the Office of the President stated its role in creating and administering systemwide initiatives also contributes to increased costs as compared to other systems. Nonetheless, we believe there are opportunities for the Office of the President to reduce its costs through an evaluation of its budget and staffing practices.

There are opportunities for the Office of the President to reduce its costs through an evaluation of its budget and staffing practices.

Figure 18
Total Administrative Costs Have Grown at Both the Office of the President and at University Campuses



Sources: California State Auditor's analysis of data obtained from the Office of the President's budget development system, the Office of the President's campus financial schedules, and functional categories established by the National Association of College and University Business Officers.

Note: These expenditures do not include the Office of the President's systemwide initiatives, the United States Department of Education Laboratories, depreciation and amortization, impairment of capital assets, and other expenses reported in the University of California's (university) annual financial report.

* Administrative expenditures include those classified by the university as institutional support, academic support (excluding libraries), and operation and maintenance of plant.

† Nonadministrative expenditures include those classified by the university as instruction, research, public service, libraries, student services, student financial aid, auxiliary enterprises, and teaching hospitals.

Table 13
The Office of the President's Budget and Staffing Levels Are Larger Than Those of the Administrative Offices of Comparable Institutions

INSTITUTIONS' CENTRAL ADMINISTRATION	BUDGET (IN MILLIONS)	NUMBER OF STAFF	CAMPUSES IN SYSTEM	FALL 2015 ENROLLMENT*
University of California Office of the President	$655†	1,667	10	257,438
California State University Chancellor's Office	98	498	23	451,209
State University System of Florida Board of Governors	8	63	12	345,672
University of Texas System Office	202	763	8	221,337

Sources: California State Auditor's analysis of personnel data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System, and budget data for the Office of the President as well as publicly available information for the central administrations of the California State University for fiscal year 2015–16, State University System of Florida for fiscal year 2015–16, and a 2016 presentation from the University of Texas Board of Regents meeting.

* *Enrollment* refers to student headcount.

† This amount does not include the Office of the President's undisclosed budget.

The Office of the President Has at Times Made Inaccurate and Misleading Claims About Its Budget to the Regents, the Legislature, and the Public

Transparency is critical to ensuring that public entities spend public funds and make decisions in a prudent manner; however, we found in our review of documents related to the Office of the President's budget that it had not always provided accurate or complete information to its stakeholders. As Table 14 shows, when we asked the Office of the President to substantiate a number of its public claims and statements related to its budget, it was unable to do so in many instances. Additionally, our review determined that a significant number of these claims were incorrect. For example, in fiscal year 2012–13, the Office of the President's budget presentation to the regents claimed that its budget was comprehensive and that its budget totals included ongoing funding permanently budgeted as *temporary*. However, we determined that the Office of the President did not include $81 million in expenditures from its undisclosed budget—which it internally refers to as its *temporary budget*—in this budget presentation. Furthermore, during the regents' meeting in which the Office of the President presented the fiscal year 2012–13 budget, the current chief financial officer claimed the Office of the President no longer received state funds. However, the current chief financial officer's claim was also incorrect because campuses used money from the State General Fund to pay for up to one-third—about $79 million—of the campus assessment that year, which the Office of the President used to fund its operations.

Table 14
The Office of the President Was Unable to Fully Substantiate Its Statements Regarding Its Budget

PUBLIC DOCUMENT	OFFICE OF THE PRESIDENT STATEMENT	OUR ASSESSMENT
Fiscal year 2012–13 Office of the President budget	"The Office of the President has developed a rigorous and transparent budget that fully reflects the complexities of the central administration's structure and funding mechanisms."	This budget did not present all the Office of the President's revenue sources, show spending from its undisclosed budget, or describe the purposes of its divisions.
	"Comprehensiveness. The Office of the President's budget has reconciled funding into one consolidated budget… [which includes] ongoing funding previously budgeted as temporary*."	The Office of the President did not present to the Board of Regents (regents) $81 million dollars in expenditures from its undisclosed budget.
	"Rigor. New reporting and budget development systems at the Office of the President provide comprehensive oversight over department budgets."	We determined that during this fiscal year, the Office of the President could only demonstrate approval for 2 percent of the $38 million in undisclosed budget expenditures that we tested.
Regents' minutes from the fiscal year 2012–13 Office of the President budget presentation	The current chief financial officer stated "the Office of the President is no longer funded by State money."	Although the Office of the President no longer directly received state funding, the campuses used up to $79 million in fiscal year 2012–13 from their State General Fund appropriations to pay for the Office of the President's campus assessment. Those funds constituted almost one-third of the total campus assessment amount that year.
Regents' minutes from the fiscal year 2013–14 Office of the President's budget presentation	"The Office of the President plans to engage in multiyear budgeting so that campuses can be advised of the possible impact on their budgets."	The Office of the President has yet to develop multiyear budgets.
Fiscal year 2014–15 Office of the President's budget	The president requested that her staff reduce travel costs by 10 percent.	The Office of the President's budget data show that its disclosed budget included an estimated 21 percent increase for meetings, travel, and other related costs.
	"A new process for approving the use of consultants is expected to lower the amount of funding spent overall for this purpose."	The Office of the President's budget data show that its disclosed budget included an estimated 2.5 percent increase for consultant costs.
Regents' minutes from the fiscal year 2014–15 Office of the President's budget presentation	"The Office of the President considered which functions should be centralized and which should remain at the campuses."	The Office of the President is unable to demonstrate that any services were centralized as a result of this process.
	In response to Governor Brown's request for a document analyzing all elements of the Office of the President, both historically and at present, the chief financial officer stated that many documents are available.	The Office of the President never provided the office of the Governor with such a document but stated that it had many communications with the office of the Governor.
	In response to a question from Governor Brown, the current chief financial officer stated that "a great deal of the Office of the President's budget flows through to the campuses… actual administrative functions account for about $90 million of the budget."	After subtracting all of the funds that flowed through to campuses, the Office of the President's central and administrative budget was $280 million.
	A regent-designate asked about funding for UCPath and why it was not listed on the budget shown to the regents. The chief financial officer responded by saying that all of UCPath's costs to date were being capitalized and that once UCPath was operational, its costs would appear on the Office of the President's budget in the next fiscal year.†	Budget data for fiscal years 2013–14 and 2014–15 show that the Office of the President spent $14.9 million and $13.7 million, respectively, for UCPath's operational costs.

continued on next page . . .

PUBLIC DOCUMENT	OFFICE OF THE PRESIDENT STATEMENT	OUR ASSESSMENT
Fiscal year 2015–16 Office of the President's budget	The Office of the President characterized a portion of a $13.4 million budget increase as a cost-of-living adjustment for its employees and stated that it was only the fourth increase in the last eight years.	The budget increase for staff salaries was actually a 3 percent across-the-board increase. The Office of the President's leadership determined the amount rather than using a cost-of-living metric. The Office of the President also gave 3 percent salary increases that were not tied to a cost-of-living adjustment in fiscal years 2011–12, 2013–14, and 2014–15.
Regents' minutes from the fiscal year 2015–16 Office of the President budget presentation	"Monies received from campus assessments would not affect enrollment."	Since campuses can choose to pay the campus assessment using appropriations from the State General Fund, tuition, and fees, it is possible that the amount of the campus assessment does affect enrollment.

Sources: California State Auditor's analysis of the Office of the President's public statements in its budget presentations and during related regents meetings as compared to data obtained from its budget development system, budget documentation, and interviews with Office of the President staff and campus administrators.

* The Office of the President internally refers to the undisclosed budget as its *temporary budget*.

† UCPath is the university's replacement payroll and human resources system.

Additionally, we determined that the Office of the President did not share information with the regents regarding $83 million in significant budget changes from fiscal years 2013–14 through 2015–16. When we asked the Office of the President how it determined which budget changes to share with the regents, the chief operating officer stated that the Office of the President shares what it considers to be strategic budget changes and that it does not have a dollar threshold for when it must share information with the regents. Because we did not have a quantitative threshold from the Office of the President, we developed our own criteria for significant budget changes, which the text box outlines. We found that during the four years for which the Office of the President could provide data, it did not share more than $83 million in significant budget changes—both increases and decreases—with the regents. For example, according to the Office of the President's budget data, it did not highlight a $2.5 million increase in the UCPath budget for fiscal year 2014–15. In fact, during the regents' meeting discussing the fiscal year 2014–15 budget, the chief financial officer incorrectly claimed that there were no UCPath costs included in that fiscal year.

Finally, although the Office of the President publishes the *Budget for Current Operations* each year, it does not ensure that this document contains sufficient and updated information about its operations. As we previously mentioned, the *Budget for Current Operations* is a means that the Office of the President uses to communicate the university's budget to the public. Nevertheless, since at least fiscal year 2011–12, it has dedicated less than two pages of the budget presentation document—a presentation that is upwards of 230 pages in length—to describing its own budget and operations. Moreover, it uses nearly identical language each year to describe

its operations. For example, since fiscal year 2011–12, the Office of the President has not updated the analyses supporting its statement that its budget compares favorably to those of other public university systems. When we asked the director of the operating budget for the underlying information for this assertion, he could not fully support the statement; instead, he could only provide us an analysis that was more limited in scope than the statement in the *Budget for Current Operations* implies.

Our Criteria for Significant Budget Changes

We defined *significant budget changes* as changes that met all of the following criteria:

- Involved an amount greater than $500,000.
- Involved a change of at least 10 percent from the prior year.
- Involved expenditures that were more than 50 percent funded by discretionary dollars.

Source: California State Auditor's definition of a significant budget change.

The Office of the President Inappropriately Interfered With Our Audit and Limited Our Ability to Provide Complete Information to the Legislature and the Public

In accordance with Government Code Section 8546.1, we conduct our audits under generally accepted government auditing standards published by the United States Government Accountability Office. Therefore, it is important that the entities we audit cooperate with us in a manner that ensures that we can meet these auditing standards, which are meant, in turn, to ensure that the quality of the evidence we collect is sufficient and appropriate so that we can reach accurate conclusions. However, the Office of the President's actions throughout this audit infringed upon our ability to meet these standards and, as a result of those actions, we are prohibited from drawing conclusions from some of the work we were asked to complete.

Auditing Standards Prohibit Us From Drawing Conclusions Based on Our Campuswide Surveys Because of Interference From the Office of the President

In October 2016, we sent two surveys to each campus to assess their use of Office of the President's services and programs as well as their perceptions of the Office of the President's process for establishing the amount of the campus assessment they pay. We based the first survey on a list of programs and services that the Office of the President provided. These programs and services covered many areas of university administration, including academic affairs, government relations, systemwide financial services, and more. The survey asked campus executives to document whether they used these services or programs and to rate the quality of the services and programs they used. The second survey asked open-ended questions about the campus assessment, such as whether the amounts the campuses paid fairly reflected the value of the services the Office of the President provided. It also included a section in which we asked campus executives to rate their satisfaction with the campus assessment amount and the process for setting and paying the assessment.

Although we explicitly asked each campus not to share its survey results with anyone outside of the campus, we learned in February 2017 that the Office of the President had requested campuses to send their survey responses to it and that the deputy chief of staff of the Office of the President (deputy chief of staff) organized a conference call with all campuses to discuss the survey and screened the surveys before the campuses submitted them to us. According to auditing standards, evaluating how surveys are administered assists auditors in evaluating their reliability. To that end, we contacted the Office of the President to determine whether it took any part in the survey's administration. In response to our query, the deputy chief of staff informed us that he had communicated with campuses related to both surveys so that he could determine whether their answers met the following criteria:

- Fell within the audit scope.
- Were factually accurate.
- Reflected a chancellor's perspective as the head of the campus.

When we compared the prescreened versions of the surveys to the versions the campuses subsequently submitted to us, we found that the responses were changed to make the Office of the President appear more efficient and effective.

Upon our further request, the deputy chief of staff provided the survey responses that the campuses had sent to the Office of the President. When we compared the prescreened versions of the surveys to the versions the campuses subsequently submitted to us, we discovered trends that concerned us. Specifically, we found that the survey responses were changed in ways that made the Office of the President appear more efficient and effective. The most extensive changes were in the open-ended comments that campuses provided in response to our broad questions. Table 15 summarizes several examples of those changes. Further, after the Office of the President's review, campuses also changed 13 ratings that we know of; 12 of these made the Office of the President look better. For example, in the prescreened version of its survey, San Diego stated that it was dissatisfied with the transparency regarding what the campus assessment pays for within the Office of the President. However, the survey we received stated that the campus was satisfied with the level of transparency. In addition, San Diego's comments documenting concerns with the Office of the President's budget process were deleted.

We also question the link between the criteria the Office of the President stated it used for its review and the information that was subsequently removed from the surveys. For example, one of our audit objectives was to identify duplicative administrative functions between the Office of the President and the campuses. The vice provost of academic personnel (vice provost) at the Irvine campus identified the Information Learning and Technology Initiative—a program that helps campuses provide online courses—as duplicating efforts on individual campuses. This comment was removed from the survey, although it clearly

fell within the audit's scope and cannot be factually inaccurate because it reflects the perspective of the vice provost. Further, we find it peculiar that the deputy chief of staff would understand the perspectives of the 10 campus chancellors better than their own executive management.

Table 15
Campus Surveys Responses Were Changed After the Office of the President's Review

CAMPUS	EXAMPLE OF CHANGES
Irvine	The Office of the President organizes regular peer group discussions that focus on review of systemwide policy and practice. These are extremely useful in that discussion of current practices as they evolve to adjust to changing conditions can be shared in a way that result in best practices and helps to maintain consistency across campuses. There are systemwide programs that also have major benefits for both the system as a whole as well as the individual campuses. This includes the presidential postdoctoral fellow program that supports hiring of a more diverse faculty. ~~The Information Learning and Technology Initiative is an example of a systemwide program that has a number of challenges and this is an example of an initiative that does duplicate efforts on the individual campuses in a way that many feel is not value added. The Office of the President used to provide faculty diversity reports and analyses by campus, which provided useful comparisons with our University peers. The website was taken offline and has been under development for some time.~~
Riverside	The Information Learning Technology Initiative has been very helpful for our campus in development of online courses. The accounting of students cross enrolled has not been as smooth as I would like. ~~I also think that it would be helpful for the Office of the President to require some training/mentoring, either centrally or on the campus, for faculty who are teaching an online course for the first time. I worry that not all faculty offering these courses are familiar with best practices in online instruction.~~
San Diego	Ideally we would want to keep the assessment amount flat with a small, predictable inflation factor. This would help campuses and the Office of the President to plan over a multi-year period. Early in the February to March timeframe would be best time to communicate as campuses are kicking off budget planning processes for upcoming year. ~~We would also like a better understanding of the base budget we are funding, so the assessment could be delivered together with a breakdown of the Office of the President budget it's intended to fund, with an opportunity for question and answers prior to the Office of the President budget being finalized. This could be done via an early vice chancellor of planning and budget meetings, sometime in January timeframe at latest.~~
	~~We would like to have organized and timely materials to inform a discussion of the Office of the President budget in total, including a breakdown of what portion is funded by assessment versus other means. We would like to see a justification and brief description of what services the different Office of the President departments provide to campuses and how they are staffed and funded (drivers to justify staffing and funding level).~~ We would ideally like the communication of the annual assessment to happen in February to March timeframe to better align with local budget planning for the upcoming year.
Santa Cruz	~~While the Office of the President does indeed exist through a "tax" on the ten campuses, it does serve several essential functions. Having central offices with general counsel, with auditors, with budget people, with quality control on graduate programs, and with centralized admissions offices serves to benefit all campuses. In particular, the centralized Office of General Counsel has surely saved the system a great deal of money. In many cases, the smaller (and much more diverse) campuses may benefit the most because they cannot always provide those services themselves at reasonable cost. An example of that is finance and construction, where the new Systemwide housing initiative will initially benefit Santa Cruz and Riverside the most. Some Office of the President initiatives, such as UCPath were at first very poorly and inefficiently run, but they seem to have figured it out and are on the way to bringing a huge and (often) failure prone project to a successful conclusion. The key issue is that the Office of the President provides the leadership, vision, and public relations acumen to keep the University on the best course.~~
	The services and leadership provided by the Office of the President are crucial for the success of the system. Especially for a smaller campus like ours, it would be both expensive and inefficient to provide those services ourselves. In addition, there is a true public policy benefit to the role that the Office of the President plays in providing uniform standards (both academic and business) as well as coordination to the system.

Source: California State Auditor's analysis of documents campuses sent to the deputy chief of staff to the president (deputy chief of staff) compared to the campuses' final survey submissions to the California State Auditor.

~~Text~~ = Text with strike out was included in surveys sent to the deputy chief of staff but not in the surveys submitted to the California State Auditor.

Text = Underlined text is language that was added after the review by the deputy chief of staff.

The deputy chief of staff asserted to us that because the Office of the President and the campuses are parts of a single entity, he and the campuses communicated in a manner that was consistent with the way in which the divisions within a given campus may have communicated to complete the surveys. However, our review clearly indicates that, because of the text and rating changes, the Office of the President's actions exceeded that of communication; further, as a result of its actions, the survey results no longer reflect campuses' opinions on the services that the Office of the President provides. Because of the Office of the President's involvement, we believe that the survey results carry an unacceptably high risk of leading us and users of the survey results to reach incorrect or improper conclusions regarding the efficacy of the Office of the President's operations. Auditing standards prohibit us from using such evidence as support for findings and conclusions. Nevertheless, we have included the survey responses exactly as campuses submitted them to us on our website, and in Appendix B beginning on page 97 offers summaries of the responses. Ultimately, we are disappointed that the Office of the President's interference led to this outcome, especially because the campuses put significant effort into responding to these surveys.

Because of the Office of the President's interference, the survey results carry an unacceptably high risk of leading us or others to reach incorrect or improper conclusions regarding the efficacy of the Office of the President's operations.

The Office of the President Delayed Our Access to Expenditure Approval Documents Related to Its Undisclosed Budget, and It Failed to Provide Us All of the Information We Requested

The Office of the President also failed to give us access to the expenditure approval documents related to its undisclosed budget for seven weeks despite our legal right to access the information upon request and our need for direct access to these documents to meet auditing standards. Specifically, in November 2016, we requested access to the Office of the President's decision memos—the documents it used to approve certain undisclosed budget expenditures, as we discuss in Chapter 1. Initially the deputy chief of staff named himself as the point of contact for retrieving the decision memos, but he did not tell us where they were stored until early in December. Later in December, he sent us copies of the documents he believed were responsive to our request, although upon our review we discovered that he had not provided many of the documents we requested. He also redacted the copies so we could not see notes related to the president's approval of the requests, even though we later discovered that these notes sometimes demonstrated that the president questioned expenses and lowered approved budget amounts in an effort to be fiscally prudent.

Finally at the end of December 2016—after extensive communication with our legal counsel—the Office of the President provided full access to the documents. However, the deputy chief of staff and the

Office of the President's legal counsel continued to contest some of the documents that we had determined we needed, claiming that they were outside the scope of the audit. Auditing standards require auditors to determine and continually assess the scope of an audit in terms of the sufficiency and appropriateness of the evidence that is available to address audit objectives. To ensure that audits remain independent, auditing standards do not allow those being audited to dictate what information is relevant to the auditors' work, a point we frequently reiterated to Office of the President's management. Further, auditing standards require that we report the limitations we face, including excessive delays in providing access to records, such as those we encountered in this audit. This delay is one such example.

In addition, the Office of the President did not provide us all of the information we requested related to its travel and entertainment expenses. Specifically, in January 2017, we requested information concerning all of the expenditures the Office of the President had made for the five-year period from fiscal years 2011–12 through 2015–16 for business meetings and entertainment, lodging, meals, and other expenses employees incurred while on business travel. During our quality control process in March 2017, we recognized a discrepancy between the Office of the President's actual expenditures—which capture meetings, travel, and related expenses at a high level—and the data previously provided by the Office of the President. Although this high-level expenditure information indicated that the Office of the President had spent at least $35.8 million for the four-year period from fiscal years 2012–13 through 2015–16 on meetings, travel, and related expenses, the Office of the President only provided us with data relating to $10.4 million in expenditures it made for such activities supposedly over a five-year period, a discrepancy of $25.4 million. When we followed up with the Office of the President for an explanation of this discrepancy, the director of its business resource center confirmed that the data provided to us in January 2017 was incomplete and did not include expenses related to foreign travel, catering, vehicle rentals, airfare, hospitality travel outside of California, non-food and beverage entertainment costs, and other costs that reasonably fell within our original request. As a result, the Office of the President limited the analysis we were able to perform, and thus Table 9 in Chapter 2 represents only a portion of the Office of the President's actual spending in this area as indicated by the symbol ‡ on page 59.

The Office of the President did not provide us information regarding at least $25.4 million in travel and entertainment expenses that we requested.

Legislative Oversight Is Necessary to Ensure That the Office of the President Implements Crucial Reforms

Throughout this report, we have identified numerous concerns regarding the Office of President's accountability, transparency, and decision making. These concerns specifically relate to the Office of

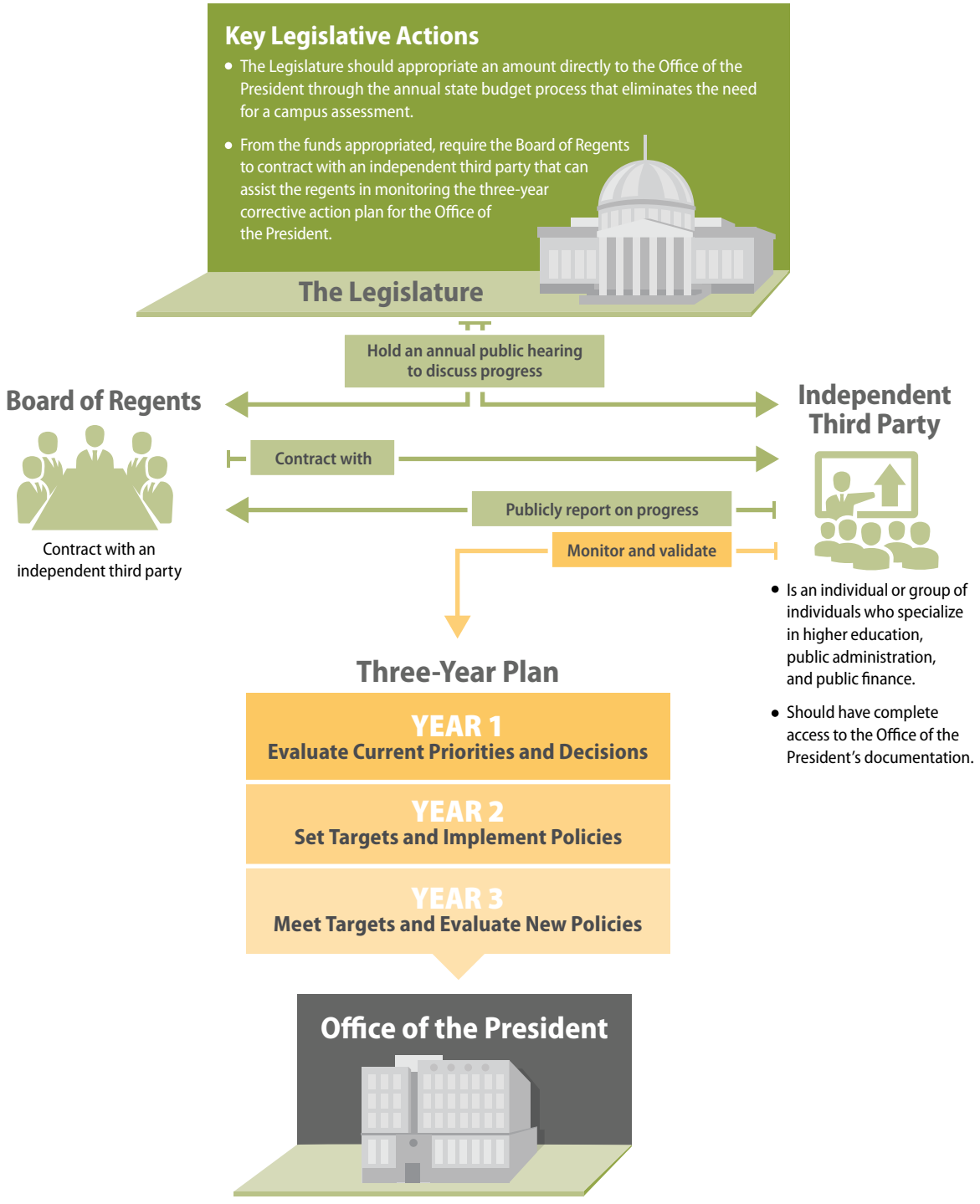
Significant change is necessary to strengthen the public's trust in the University of California. To achieve this change, the Legislature should increase its oversight of the Office of the President.

the President's weak budget processes, failure to disclose certain budgets and reserves, generous staff compensation, lax oversight, lack of a workforce plan, use of campus funds for initiatives that may not benefit students, and questionable actions that limited our ability to address certain audit objectives. Taken as a whole, these problems indicate that significant change is necessary to strengthen the public's trust in the University of California. To achieve this change, we believe the Legislature should increase its oversight of the Office of the President.

The Legislature has several options for overseeing the Office of the President's operations. Because of the university's constitutional autonomy, the Legislature is limited in the means by which it can effect these changes; however, it can require some changes as a condition of the university's annual state appropriation. We believe the first step is for the Legislature to directly fund the portion of the Office of the President's discretionary budget that the campuses currently fund through the annual assessments they pay. The Legislature would not need to increase the total amount of state funding the university receives; rather, it could more specifically allocate the funding it currently provides. Under this change, campuses would receive less state funding, but they would not be required to pay the Office of the President each year. A direct appropriation would create an avenue for legislative oversight over the Office of the President's use of its discretionary funds. Further, it could create cost pressures that would require the Office of the President to assess its costs and justify the number of its staff and the necessity of its programs. Directly allocating money to the central administration of a university system is not a new idea; the Florida legislature makes direct appropriations to the central administration for its higher education system.

Additionally, we believe that the Legislature should, from the funds appropriated, require the regents to contract with an independent third party that can assist the regents in monitoring the implementation of the three-year plan we outline in each chapter of this report. This plan contains specific steps intended to increase transparency and accountability. If implemented thoughtfully and thoroughly, it would aid in correcting the problems we identify in this report and strengthen the accountability and transparency of the Office of the President. Also, the Legislature should hold annual hearings that include a status report by the independent third party regarding the Office of the President's progress, challenges, and barriers to success in implementing the three-year corrective action plan. Figure 19 presents a high-level summary of our recommendations.

Figure 19
Actions by the Legislature Will Be More Effective at Establishing Long-Term Accountability and Transparency at the Office of the President



Source: Based on the California State Auditor's recommendations to the Legislature, the Board of Regents, and the Office of the President.

Recommendations

The Legislature

To ensure that the Office of the President's actions align with the university's primary mission, the Legislature should do the following:

- Appropriate an amount directly to the Office of the President through the annual state budget process that eliminates the need for a campus assessment. Based on the Office of the President's actions as it implements its three-year plan, evaluate the amount of the direct appropriation annually. Once the Office of the President has completed the three-year plan, evaluate the necessity of a continued direct appropriation after assessing the strength of the Office of the President's new budget, accounting, and staffing policies, as well as its demonstrated commitment to ongoing transparency.
- From the funds appropriated, require the regents to contract with an independent third party that can assist the regents in monitoring the three-year corrective action plan for the Office of the President. The Legislature should hold annual hearings that include a status report by the independent third party regarding the Office of the President's progress, challenges, and barriers to success in implementing the three-year corrective action plan.

The Regents

To ensure that the Office of the President is engaging in a thorough review of its systemwide and administrative costs and implementing our recommendations, the regents should do the following:

- Develop a contract for an independent third party that can assist the regents in monitoring implementation of the three-year corrective action plan for the Office of the President. The independent third party should have expertise in higher education, public administration, and public finance. Moreover, the independent third party should have complete access to the Office of the President's documentation and its staff so that it has sufficient and appropriate information to verify the Office of the President's actions. The independent third party should report to the regents on the Office of the President's progress, challenges, and barriers to success at least quarterly.
- Hold a public meeting that includes university stakeholders, including campuses and students, to discuss the purpose, intent, and prioritization of each systemwide and presidential initiative in light of campus funding levels for students. Require the Office of the President to publish the results of this meeting, including

any systemwide or presidential initiatives that are eliminated or scaled down and the amount of money that will be reallocated to campuses for students.

- To ensure the ongoing accountability of the Office of the President, the regents should require it to implement our recommendations and report periodically on its progress in doing so.

The Office of the President

To ensure that its spending aligns with the needs of its stakeholders, including campuses and students, the Office of the President should do the following:

By April 2018:

- Develop and use a clear definition of systemwide initiatives and administration to ensure consistency in future budgets.
- Develop a comprehensive list of systemwide initiatives and presidential initiatives, including their purpose and actual cost that will be used in the regents' meeting previously recommended.

By April 2019:

- Establish spending targets for systemwide initiatives and administrative costs.
- Publish the results of the review of systemwide and presidential initiatives, including any funds the Office of the President anticipates reallocating to the campuses.
- Restructure budget and accounting systems to ensure that the costs of the Office of the President can be clearly tracked and reported annually. Specifically, the budget and accounting systems should be able to distinguish between systemwide initiatives, presidential initiatives, and administrative costs.

By April 2020:

- Publicly publish its progress in meeting systemwide initiative and administrative cost targets.
- Reallocate funds from the review of systemwide and presidential initiatives, as well as any administrative cost savings, to campuses.
- Report to the regents on the amount of funds reallocated to campuses.

We conducted this audit under the authority vested in the California State Auditor by 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives specified in the scope section of the report. We believe that the evidence obtained provide a reasonable basis for our findings and conclusions based on our objectives, except for the work related to our two campuswide surveys. Specifically, because the Office of the President interfered with the survey process, we believe that the survey responses carry an unacceptably high risk of leading us and users of the survey results to reach incorrect or improper conclusions about the efficacy of the Office of the President's operations.

Respectfully submitted,

Elaine M. Howle

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State Auditor

Date: April 25, 2017

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For questions regarding the contents of this report, please contact Margarita Fernández, Chief of Public Affairs, at 916.445.0255.

APPENDIX A

DATA FROM OUR ANALYSIS OF THE OFFICE OF THE PRESIDENT'S EXECUTIVE STAFF SALARIES

Figure 13 on page 50 in Chapter 2 displays the results of our comparison of the salaries of the Office of the President's executives to those of three similar state executives and similar California State University executives. The data supporting Figure 13 are summarized in Table A.

Table A
Selected Office of the President, California State University, and State Executive Salaries for Fiscal Year 2014–15

UNIVERSITY OF CALIFORNIA OFFICE OF THE PRESIDENT		STATE AND CALIFORNIA STATE UNIVERSITY (CSU) EXECUTIVES			DIFFERENCE BETWEEN THE OFFICE OF THE PRESIDENT AND STATE AND CSU SALARIES
JOB CLASSIFICATION	BASE SALARY	JOB CLASSIFICATION	AGENCY	SALARY PLUS COST-OF-LIVING INDEX ADJUSTMENT[1]	
Executive Vice President and Chief Financial Officer	$412,000	Executive Vice Chancellor and Chief Financial Officer	California State University	$341,500	$70,500
		Chief Financial Officer	Public Employees Retirement System	340,900	71,100
		Chief Financial Officer	State Compensation Insurance Fund	331,000	81,000
		Chief Financial Officer	California Health Benefit Exchange	202,500	209,500
General Counsel and Vice President of Legal Affairs	428,500	General Counsel	Public Employees Retirement System	414,300	14,200
		Executive Vice Chancellor and General Counsel	California State University	342,300	86,200
		General Counsel	Teachers' Retirement System	300,500	128,000
		General Counsel and Division Director	Judicial Council	148,900	279,600
Associate Vice President and Chief Procurement Officer	314,200	Deputy Director of the Procurement Division	Department of General Services	195,900	118,300
		No other comparable state employees found			
Provost and Executive Vice President of Academic Affairs	360,500	Executive Vice Chancellor and Chief Academic Officer	California State University	335,600	24,900
		Vice Chancellor of Academic Affairs	Board of Governors of Community Colleges	158,200	202,300
Vice President of Information Technology and Chief Information Officer	345,100	Chief Information Officer	State Compensation Insurance Fund	409,100	(64,000)
		Director and State Chief Information Officer	California Department of Technology	230,200	114,900
		Information Technology Director	California Institute for Regenerative Medicine	200,600	144,500

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UNIVERSITY OF CALIFORNIA OFFICE OF THE PRESIDENT		STATE AND CALIFORNIA STATE UNIVERSITY (CSU) EXECUTIVES			DIFFERENCE BETWEEN THE OFFICE OF THE PRESIDENT AND STATE AND CSU SALARIES
JOB CLASSIFICATION	BASE SALARY	JOB CLASSIFICATION	AGENCY	SALARY PLUS COST-OF-LIVING INDEX ADJUSTMENT[1]	
Executive Vice President and Chief Operating Officer	$330,000	Chief Operating Officer	State Compensation Insurance Fund	$306,800	$23,200
		Chief Administrative Officer	Judicial Council	198,500	131,500
		Chief Deputy Director of Operations	California Department of Technology	189,800	140,200
Senior Vice President of Government Relations	280,000	Vice Chancellor, University Relations and Advancement	California State University	264,200	15,800
		Vice Chancellor of Governmental Relations	Board of Governors of Community Colleges	149,600	130,400
		Deputy Secretary for Border and Intergovernmental Relations	California Environmental Protection Agency	146,800	133,200
		Deputy Director of Legislative and Governmental Affairs	California Department of Public Health	145,900	134,100
Chief Investment Officer and Vice President of Investments	615,000	Chief Investment Officer	Public Employees Retirement System	614,500	500
		Chief Investment Officer	Teachers' Retirement System	568,000	47,000
		Chief Operating Investment Officer	Public Employees Retirement System	449,300	165,700
Vice President of Human Resources	318,300	Vice Chancellor, Human Resources	California State University	287,700	30,600
		Director	Department of Human Resources	215,200	103,100
		Human Resources Officer	California Institute for Regenerative Medicine	182,900	135,400
		Deputy Secretary of Human Resources	California Government Operations Agency	151,400	166,900
Associate Vice President and Systemwide Controller	303,900	State Controller	State Controller's Office	176,400	127,500
		Deputy State Controller	State Controller's Office	162,700	141,200
		Chief of Accounting and Reporting	State Controller's Office	148,500	155,400

Sources: California State Auditor's analysis of data obtained from the Office of the President's Corporate Data Warehouse and Decision Support System, and State Controller's Office information for the CSU and state government employees.

* We increased the state executive and CSU employee salaries based on a cost-of-living adjustment calculated by comparing the city where each agency's main office is located to the city of Oakland, where the Office of the President is headquartered. The adjustments were calculated using cost-of-living index information from the Council for Community and Economic Research for quarter two of 2016. We used the following adjustment rates: Sacramento 26.2%, San Francisco -15.7%, and Long Beach 5.1%. We did not make adjustments for agencies headquartered in the East Bay Area.

APPENDIX B

OUR CAMPUSWIDE SURVEY RESULTS, WHICH AUDITING STANDARDS PROHIBIT US FROM USING TO DRAW CONCLUSIONS

As we discuss in Chapter 3, the Office of the President screened our two campuswide surveys, and we therefore have serious concerns regarding the accuracy of the survey responses we summarize in this Appendix. We sent the two surveys to each campus to obtain feedback about the services the Office of the President provides and the costs campuses pay for those services. We explicitly directed campuses not to share their responses beyond their respective campus. Although all of the campuses responded to both of our surveys, correspondence between the Office of the President and some campuses shows that the Office of the President reviewed their survey responses and campuses subsequently changed or deleted answers that were critical of the Office of the President. In effect, the Office of the President participated in our survey without asking us if its participation was appropriate—to which we would have responded it was not—and without telling us about its involvement until after we requested documentation regarding the administration of the survey to satisfy auditing standards. As a result, the survey responses we received may not accurately or completely represent the campuses' perspectives.

Because of the Office of the President's involvement, we believe that the survey results carry an unacceptably high risk of leading us and readers of this report to reach incorrect or improper conclusions about the efficacy of the Office of the President's operations. Auditing standards prohibit us from using such evidence as support for findings and conclusions. Nevertheless, we are including a summary of the survey results exactly as campuses submitted them to us. Survey responses are also available on our website.

Summary of Our Campuswide Survey Regarding the Use and Quality of the Office of the President's Services and Programs

The Office of the President provided us with a list of services and programs it offers campuses. Using this list as a basis, our survey asked the campuses to report whether they used the Office of the President's services and programs. If a campus did use a service or program, we asked it to rate the service or program's quality. Additionally, we asked campuses to indicate whether services were redundant, partially redundant, or not redundant. Their responses are shown in Tables B.1 through B.4 on the following pages.

Table B.1
Number of the Office of the President's Services That University of California Campuses Reported Using

	NUMBER OF INDIVIDUAL SERVICES	NUMBER OF SERVICES MULTIPLIED BY 10 CAMPUSES	NUMBER OF SERVICES CAMPUSES REPORTED THEY USED	NUMBER OF SERVICES CAMPUSES REPORTED THEY DID NOT USE	PERCENTAGE OF SERVICES USED*
Totals	**110**	**1,100**	**937†**	**163**	**85%**

QUALITY RATINGS FOR OFFICE OF THE PRESIDENT SERVICES

RATING	NUMBER†	PERCENT†
Exceptional	373	39%
Good	517	55
Fair	57	6
Poor	1	0

Source: California State Auditor's analysis of the results of the campus services survey.

Note: Data are not reliable because of the Office of the President's interference.

* At least one campus used each service.

† The total number of quality ratings is not equal to the number of services that campuses reported they used because some survey respondents provided a quality rating for some services they marked as *not used*.

Table B.2
Number of The Office of the President's Programs That University of California Campuses Reported Using

	NUMBER OF INDIVIDUAL PROGRAMS	NUMBER OF PROGRAMS MULTIPLIED BY 10 CAMPUSES	NUMBER OF PROGRAMS CAMPUSES REPORTED THEY USED	NUMBER OF PROGRAMS CAMPUSES REPORTED THEY DID NOT USE*	PERCENTAGE OF PROGRAMS USED
Totals	**31**	**310**	**187†**	**123**	**60%**

QUALITY RATINGS FOR OFFICE OF THE PRESIDENT PROGRAMS

RATING	NUMBER†	PERCENT†
Exceptional	105	56%
Good	68	36
Fair	14	7
Poor	1	1

Source: California State Auditor's analysis of the results of the campus services survey.

Note: Data are not reliable because of the Office of the President's interference.

* Some campuses reported not using systemwide programs because those programs are not connected to campus activities. For example, programs associated with the Office of National Laboratories are not associated with campuses.

† The total number of quality ratings is not equal to the number of programs that campuses reported they used because a survey respondent provided a quality rating for a program marked as *not used*.

Table B.3
University of California Campuses' Redundancy Ratings for the Office of the President's Divisions Offering Services or Programs

NUMBER OF DIVISIONS OFFERING SERVICES	NUMBER OF DIVISIONS OFFERING SERVICES MULTIPLIED BY 10 CAMPUSES	NUMBER OF DIVISIONS OFFERING PROGRAMS	NUMBER OF DIVISIONS OFFERING PROGRAMS MULTIPLIED BY 10 CAMPUSES
11	110	5	50

RATING	SERVICES	PROGRAMS
Redundant	1	0
Partially redundant	19	3
Not redundant	90	47
Totals	**110**	**50**

Source: California State Auditor's analysis of the results of the campus services survey.
Note: Data are not reliable because of the Office of the President's interference.

Summary of Campuswide Survey Regarding the Campus Assessment Process

Our second survey asked the chief financial officer—or equivalent executive manager—at each campus to provide feedback regarding the Office of the President's process for determining the campus assessment amount. The ratings these individuals provided are presented below.

Table B.4
University of California Campuses' Quality Ratings for the Campus Assessment Process

RATE YOUR CAMPUS'S CURRENT SATISFACTION WITH THE OFFICE OF THE PRESIDENT'S...	VERY DISSATISFIED	DISSATISFIED	OKAY	SATISFIED	VERY SATISFIED
Collaboration with your campus related to the total campus assessment amount			4	6	
Collaboration with your campus related to the formula for the campus assessment distribution among all University of California campuses	1		1	3	5
Process for announcing when your campus must pay the assessment		1	2	5	2
Transparency regarding what the campus assessment pays for within the Office of the President			4	4	2
Guidance on what funds are appropriate for paying the campus assessment			2	5	3
Coordination with your budget unit regarding the impact of the campus assessment increases or decreases		1	3	5	1

Source: California State Auditor's analysis of the results of the campus assessment survey.
Note: Data are not reliable because of the Office of the President's interference.

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THE REGENTS OF THE UNIVERSITY OF CALIFORNIA

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April 5, 2017

Ms. Elaine Howle *
California State Auditor
621 Capitol Mall, Suite 1200
Sacramento, CA 95814

State Auditor Howle:

Thank you for the opportunity to respond directly to the draft audit report on UC's Office of the President administrative expenditures. On April 3, the Compliance and Audit Committee met to discuss all aspects of the report, paying particular attention to its recommendations to the Regents and the Legislature. This response reflects the discussion of the committee members in attendance and is submitted in addition to UCOP's response. Of note, we formally request you remove recommendations from the report that we feel encroach upon the constitutional autonomy of the University and are inconsistent with many of the constructive recommendations related to improved processes, accountability, and transparency. (1)

There is nothing that the Board of Regents takes more seriously than its fiduciary duty. Board members have committed ourselves to serving as strong stewards of the University and its tripartite mission of teaching, research, and public service. In doing so, we seek to be fiscally prudent, to deploy University funds in a manner most consistent with that mission, and above all else, maintain the public trust in this exceptional institution. We have done so consistently throughout UC's history and wish to reaffirm that to you now.

As you will note, UCOP agrees with the vast majority of the draft report's recommendations regarding budget and administrative processes. We, too, believe these recommendations are largely helpful and constructive. As in any large and complex organization, there is always room for improvement at the University and as UC's fiduciaries we are fully committed to working with UCOP to pursue greater efficiency and transparency. We look forward to discussing with the full Board of Regents how to best partner with UCOP to successfully implement the recommendations. We feel it important to note, however, that over the past several years, UCOP has made significant improvements to its budget and administrative process, and has demonstrated important leadership in advancing significant priorities for both the Regents and the State. We have great confidence in UCOP leadership and hope that overriding fact does not get lost in our discussion of this report.

While we agree with most of your recommendations, we have serious concerns with the recommendations you intend to make to the Legislature. As written, we believe these recommendations threaten the University's standing as a constitutionally autonomous entity, and the Board of Regents itself. (1)

One of your recommendations calls on the Legislature to directly appropriate funding for UCOP's budget, while limiting its ability to seek additional financial support from campuses. This is deeply troubling for many reasons, key among them the undermining of the constitutional autonomy of the University. (1)

Since its inception, UC's constitutional autonomy has ensured that the University's mission, vision and values emanated from its students, faculty and staff, free from political or sectarian influence, in the words of

* California State Auditor's comments appear on page 103.

Article IX, Section IX of our State Constitution. Along with the Master Plan for Higher Education, constitutional autonomy has allowed UC to grow into a world renowned system of 10 flagship quality research institutions. The scale and scope of this achievement distinguishes UC from other public university systems across the country.

(1) A second problematic recommendation asks that the Legislature order the Regents to hire a third-party entity to manage a corrective action plan for UCOP. In addition to this fundamental issue of constitutionality, we embrace the notion of subsidiarity. This concept appropriately places the greatest authority in the most local decision-maker, which in this case, is the Board of Regents. Moreover, given the Board's fiduciary responsibilities, the Regents are best positioned to provide policy direction, guidance, and oversight of the University. As with all the recommendations in the report, the Board of Regents will carefully consider the best ways to ensure the recommended process and policy improvements.

(2) We also want to address a third recommendation that calls for an open hearing on systemwide and presidential initiatives. The report implies that the initiatives are inconsistent with the University's missions and fail to incorporate adequate stakeholder input. We strongly disagree. These initiatives represent forward-thinking efforts that we and many in the UC community are most proud of. They also reflect all parts of UC's mission – educating the full range of California's population, conducting ground-breaking research and applying that research to real-world problems, and providing service to address some of the most critical issues facing the state.

(2) In addition, these initiatives represent shared priorities with State leadership. They were, and continue to be developed with significant input from the Regents, campus leadership, student representatives and other key UC constituents. They have been discussed and promoted in a wide range of public settings – from Regents meetings, to state and federal legislative hearings, to public events throughout California. We recognize that there is room to provide even more robust reporting, and we intend to work with UCOP on future presentations. However, as currently presented, this report recommendation suggests defunding and devaluing these priorities, which we cannot support.

(1) We would like to meet with you next week as part of our continued engagement with you and to underscore our commitment to comply with recommendations that will improve UCOP's budgetary and administrative processes. As we mentioned in the outset of this letter, we also formally request that the recommendations made to the Legislature be excluded from the final report. This step would preserve the established role of the Regents in the oversight of the University and ensure its constitutional autonomy. Our office will be in touch with you to schedule a meeting where we can discuss these matters in greater detail. Thank you for your attention to these important matters.

Respectfully,

Monica C. Lozano
Chair, UC Board of Regents

Charlene Zettel
Chair, Compliance and Audit Committee

Comments

CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM THE UNIVERSITY OF CALIFORNIA BOARD OF REGENTS

Although we met with the regents and considered their perspective, we have chosen not to remove our legislative recommendations from the final report. We believe these recommendations are important for the Legislature to consider in light of the nature and number of concerns we identified in the course of this audit. We did, however, slightly modify the wording. ①

Based on our meeting with the regents we have made minor modifications to the report to clarify that we believe the Office of the President needs to evaluate the intent, purpose, and prioritization of systemwide and presidential initiatives in relation to the university's other activities such as campus spending on students. At no point do we suggest defunding or devaluing these priorities and, on page 4, we acknowledge that many of these programs undoubtedly provide a benefit to the public and to students. However, we question whether all of these initiatives are developed with "significant input" from the university's stakeholders, such as chancellor's administrative funds and president emeriti expenses, among other initiatives, listed in Table 11 on page 73. Our recommendations are meant to institutionalize stakeholder input in key spending decisions, not to create an expectation that programs will be eliminated or downsized. ②

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UNIVERSITY OF CALIFORNIA

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April 5, 2017

Ms. Elaine M. Howle*
California State Auditor
621 Capitol Mall, Suite 1200
Sacramento, California 95814

State Auditor Howle:

I write to respond to your draft audit report for the University of California Office of the President's (UCOP) administrative expenditures. The recommendations to UCOP are helpful. We welcome this constructive input, which align with our proactive efforts to continually improve UCOP's operations, and UCOP intends to implement the recommendations. Before turning to discussing the recommendations, I would like to clarify some other important points.

First, beginning with its subtitle, the report fundamentally and unfairly mischaracterizes UCOP's budget processes and practices in a way that does not accurately capture our current operations nor our efforts and plans for continued improvement. The report falsely claims that UCOP failed to disclose "tens of millions in surplus funds" and that UCOP's "budget practices are misleading." In fact, **UCOP's budget and financial approaches reflect strategic, deliberate, and transparent spending and investment in UC and State priorities**. ①

During my time as President, I have instituted measures to ensure UC's resources are carefully managed and deployed for mission-critical investments, while being transparent and accountable to The Regents and our many important stakeholders. I require and expect this office to continually improve its performance, processes, and services, while simultaneously evaluating ways to cut costs. Both efforts are integral to the operation of a world-class university system and its fundamental missions of teaching, research and public service. At the same time, I realize no organization is perfect. This audit is a chance to welcome feedback and build upon our already significant progress.

Second, the report asserts that UCOP "amassed more than $175 million in reserve funds" and raises associated concerns about the management and transparency of those funds. I disagree with all of these assertions. ②

* California State Auditor's comments begin on page 121.

State Auditor Howle
April 5, 2017
Page 2

③ To start, **the $175 million figure mischaracterizes the true amount of UCOP's available and uncommitted reserve, which is $38 million, a modest amount for an organization our size**. Moreover, the $175 million ④ amount cited should actually be $170 million, as $5 million is not UCOP-related fund balance data.

Of that $170 million, $83 million are restricted funds and $87 million are ④⑤ unrestricted funds. The $83 million in restricted funds supports a range of programs and initiatives, many of which are related to the systemwide and Presidential Initiatives. Among those receiving the largest portions of these funds are:

- grant programs to support groundbreaking research ($18 million for Lab Research Grant Programs);
- the medical centers and medical schools core to our patient care and health research missions ($10 million for UC Health);
- the academic program designed to immerse undergraduate students in Washington DC-based public service programs ($8 million to the UC Washington Center);
- and an innovative program to shift UC's energy usage to more sustainable sources ($7 million to the Wholesale Power Program).
- In some cases, these funds are transferred directly to campuses in the form of research grant funding or other program services by agreement (i.e., Wholesale Power, UC Health).

Of the $87 million with more spending flexibility, as of July 1, 2016, $49 million ④⑥ was already committed to academic programs, systemwide initiatives, and multi-year campus commitments that the Chancellors and I have agreed are high priorities.

The largest items in the $49 million include:

- a sustained effort to develop, demonstrate, and export solutions — throughout California, the United States and the world — for food security, health, and sustainability ($5.2 million for the Global Food Initiative);
- support for current law students and recent law-school grads to pursue public service internships and careers ($4.5 million for the Public Service Law Fellowships);

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- investments in UC's efforts to become carbon neutral and develop groundbreaking climate solutions ($2.5 million for the Carbon Neutrality Initiative);
- support for the growth of UC's newest campus in Merced ($4.6 million for UC Merced Wetlands);
- investment in a new medical school to increase the number of physicians and address underserved patient communities in California ($2 million for UC Riverside Medical School);
- efforts to significantly bolster UC's readiness for increasingly sophisticated threats to its student, research, patient, and alumni data ($7.2 million for cybersecurity).

That leaves $38 million, which accounts for roughly 10 percent of UCOP's operating and administrative budget. Ten percent is a prudent and reasonable reserve amount for the University to be fully prepared for unexpected expenses, such as cybersecurity threat response, and emerging issues, such as support for undocumented students. That said, I believe it makes sense to develop a UCOP-specific reserve policy to more clearly articulate to our stakeholders our approach toward fiscal forethought and prudence. We will do so. (3) (7)

Third, the report questions whether the systemwide and Presidential Initiatives are of value and in alignment with UC's mission. **Systemwide and Presidential Initiatives are critical programs that reflect core values of The Regents and address some of the most pressing issues facing the State.** The recommendations suggest reducing or eliminating these programs, which would impede the ability of some of our most vulnerable students to succeed, undermine research into critical issues, and lessen UC's public service impact – thereby undermining all three of UC's core missions. (8) (9)

UC's initiatives advance several of the State's highest priorities, including providing resources and support for undocumented students, developing groundbreaking climate solutions and mitigating the University's carbon footprint, advancing health-related research and programs, and strengthening the State's relationship with Mexico. (10)

The initiatives also address some of The Regents' most pressing priorities, including enhancing diversity of students, faculty, and staff, improving the transfer process for community college students, ensuring increasingly comprehensive outreach to high schools and community colleges throughout the State, and serving the Central Valley through support of UC Merced's ambitious campus expansion. The elimination of these programs would be contrary to UC's (8) (9)

longstanding roles as an engine of social mobility for students from a wide-range of backgrounds and circumstances and as a driver of innovative and research-based solutions to some of the State and nation's most challenging issues.

(11) All of these initiatives have received substantial public attention and promotion. UCOP frequently confers with The Regents about the initiatives, updates them on these initiatives, and provides the public relevant information through public events, press releases, press interviews, websites, and social media channels. In addition, many initiatives – such as those pertaining to cyber security and preventing and responding to sexual violence and sexual harassment – are ongoing efforts and are included as part of the formal budget presentation to The Regents. We do agree, though, that there is always room to improve our communication and presentation of the initiatives, and we look forward to adopting many of the report's recommendations in this area.

(8) **Systemwide and Presidential Initiatives not only reflect UC's mission, but also substantially benefit the campuses and their students, faculty, and staff.** A portion of funds for these initiatives and the majority of UCOP's budget comes from an assessment of the campuses. This structure is a result of the Funding Streams Initiative launched in fiscal year 2011-12, which shifted revenues directly to the campuses. It was designed to simplify University financial activity, improve transparency, and incentivize campuses to maximize
(12) revenue. The primary goal of Funding Streams was to establish an appropriate level of core funding for UCOP's central administration and governance activities while minimizing campus assessment funds; doing so maximizes funding for the University's fundamental teaching, research, and public service missions. UCOP has worked to limit the growth and volatility of the assessment, allowing for more predictable campus level budgeting and better long-term financial planning.

From fiscal year 2011-12 to fiscal year 2015-16 the assessment increased from $278 million to $304 million, a compound annual growth of only 2.3 percent. Over this same period, our systemwide revenue increased from $24 billion to $31 billion, a compound annual growth of 6.8 percent, and the number of students has grown from 237,057 in 2011-12 to 253,489 in 2015-16, an increase of nearly 7 percent.
(13) **Since I joined UC in 2013, the assessment share of total systemwide revenue has dropped from 1.08 percent to 0.98 percent.** Nowhere in the draft report is there mention of this critical context.

Fourth, the report suggests that UCOP has not adequately shared information about its budget and financial activities. **Through a variety of methods, UCOP**
(14) **has made wide-ranging and extensive information about its budget and financials publicly available.**

State Auditor Howle
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Since 2007, when UC adopted an entirely new funding methodology for the campuses and for UCOP, the UCOP budget has been presented annually to The Regents for approval. Historically, the UCOP budget is presented to The Regents at their May or July meetings. In addition to the Regents' Meeting itself, the Chair and Vice Chair of the Finance Committee receive a more detailed briefing about the UCOP budget, including information at the divisional and department level. ⑮

UC provides even greater financial detail publicly in its annual Campus Financial Schedules, which show revenue by fund source, expenditures by functional area, and expenditures by department. UCOP is included in this detailed presentation format. As your team was made aware, schedules dating back to 2004-05 are available at http://ucop.edu/financial-accounting/financial-reports/campus-financial-schedules/index.html. Finally, annual financial statements for the University of California, including UCOP, are prepared and audited on a consolidated basis by an outside auditor. The audited financial statements are included in the University's Annual Financial Reports and are available at http://reportingtransparency.universityofcalifornia.edu/. ⑯ ⑰

Fifth, the draft report understates the extensive controls that have been instituted since I joined the Office of the President in 2013. Over the past several years, we have made many improvements to our budget and administrative processes – and will continue to further such progress. **Expenditures from the unrestricted or discretionary carry-forward funds must be approved through UCOP's formal decision-making process. The documents associated with that process outline the purpose, objective, and options for the expenditure and the vast majority must be reviewed and approved by me, personally.** In addition to expenditures from those funds, I have instituted a process that requires my explicit approval for use of outside consultants and contractors. While I am proud of the increasingly rigorous controls we have put into place at UCOP over the past few years, I agree that we can further enhance these processes and remain committed to doing so. ⑱ ⑱

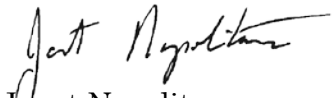
Finally, I have concerns that this draft report also understates how UCOP differs from every other university system office in the nation. **UCOP manages programs that serve the entire system, allowing campuses to capture the savings and efficiencies of centralized operations, while coordinating activities that allow them to operate as one university – all this, with its core operations and staff comprising just 1 percent of UC's overall budget.** By way of example, across 15 activity areas, ranging from the administration of systemwide retirement plans, to the centralized management of systemwide debt, to the administration of a systemwide financial aid, none of the ⑲ ⑳

other 10 largest system offices (as measured by total systemwide expenditures) provide more than four functions. UCOP, by contrast, provides all 15 critical systemwide services. These efforts have generated significant savings. For instance, through UC Health's Leveraging Scale for Value Program, the system has saved approximately $520 million over the past two years.

As I have stated throughout this response, I believe a majority of your recommendations are reasonable and align with UCOP's existing practices, current plans, as well as its proactive efforts to continually improve. For many, we agree with the recommendation as written, such as exploring the development of a reserve policy with The Regents, working with them to incorporate your suggested additions to our annual budget presentation, and evaluating our employee reimbursement policies and appropriately revising them. For others, we agree with the spirit and intent of the recommendation, and will take a slightly varied approach to address the underlying concerns. Examples include limiting assessment growth in the place of reallocating savings to campuses or analyzing the impact of narrowing our salary ranges before committing to doing so.

As you can see, we have taken your recommendations seriously and are committed to their implementation. Our willingness to incorporate into our policies your
(21) evaluation and recommendations is reflected in our detailed response. UCOP will seize this opportunity to further enhance its value to students, campuses, Regents, the Legislature, and the citizens of California.

Yours very truly,



Janet Napolitano
President

Enclosures:
Attachment 1: CSA Recommendations to UCOP – Response
Attachment 2: CSA Report Assertions – Detailed Response

Attachment 1
Recommendations from State Audit of UCOP Administrative Expenditures

Staffing Recommendations

Salary Levels and Ranges

By April 2018:

1. **Develop a method for weighing public and private sector pay data when establishing salaries for all positions.**
2. **Determine how to restructure salary ranges to make certain the ranges encourage employee development and ensure pay equity.**

By April 2019:

5. **Set targets for any needed reductions to salary amounts using the results from its public and private sector comparison and adjust its salaries accordingly.**
6. **Narrow its salary ranges.**
8. **Create a plan for reallocating funds to campuses that it saves as it reduces its staffing costs.**

By April 2020:

10. **Adjust its salary levels and ranges to meet its established targets.**
12. **Reallocate funds to campuses when adjustments to its salaries and benefits result in savings.**
15. **Report to the regents on the amount of funds it reallocates to campuses as a result of implementing our recommendations.**

Response:

UCOP agrees with these recommendations.

UC has already undertaken efforts consistent with this recommendation. UC updated the Market Reference Zones for executives in March 2016, incorporating compensation data from State, county, CSU, and other public higher education institutions where appropriate based on the criteria established by the 2016 Budget Act, e.g., for positions with comparable scope of responsibilities, complexity, breadth of job functions, experience requirements, and other relevant factors. Going forward, UCOP will leverage third-party published surveys, which include appropriate and relevant public and private sector pay comparisons, to define salary ranges and utilize midpoints in these ranges as proxy for the median pay in the market. Appropriate salary amounts for individuals will be based on pay comparisons, market information, individual experience levels, availability of talent, and other relevant factors. (22)

UCOP will review salary market data to ensure ranges support both employee development and pay equity. This is consistent with existing practice, with such reviews occurring annually. UCOP will ensure guidelines for equity and promotion reviews are clear and applied consistently across UCOP.

(23) Since implementing Career Tracks in 2013, UC has once narrowed salary ranges and once held ranges to prior-year levels based on market assessments and our internal analyses. UCOP's systemwide human resources will perform an annual review of salary ranges based on the cost of labor in the market. As part of this process, UCOP will consider the potential for narrowing its salary ranges. This is consistent with existing practice, with such reviews occurring annually. More generally, UCOP will follow cross-industry human resources best practices in maintaining appropriate salary ranges and salary range structures for non-represented positions, which make up the bulk of UCOP positions. Ranges for union-represented positions will be determined through negotiations with applicable unions.

UCOP will make changes to salary levels and ranges in accordance with our market analyses and the strategic plan. These salary adjustments will be implemented as attrition occurs in the organization.

(24) UCOP will utilize savings either by reducing the total amount of the assessment or by directing them to initiatives and programs that benefit the campuses and the system. UCOP's primary goal is to effectively limit assessment growth, aiming to incorporate areas of savings where available.

UCOP will periodically report on the financial impact of implementing the audit recommendations at a frequency determined by the Regents.

Employee Reimbursement Policies

By April 2018:

3. **Evaluate and identify needed changes in employee benefit policies to ensure they include reasonable safeguards to control costs.**

By April 2019:

7. **Set targets for appropriate employee benefits and implement new processes that ensure employees adhere to the revised policies regarding employee benefits.**
8. **Create a plan for reallocating funds to campuses that it saves as it reduces its staffing costs.**

By April 2020:

11. **Adjust its employee benefits to meet its established targets.**
12. **Reallocate funds to campuses when adjustments to its salaries and benefits result in savings.**

15. **Report to the regents on the amount of funds it reallocates to campuses as a result of implementing our recommendations.**

Response:

UCOP agrees with these recommendations.

UCOP will compare current employee benefit and reimbursement policies to comparable organizations. It will consider policy changes and incorporate any necessary safeguards to control costs. UCOP will adjust employee benefits and reimbursement amounts in accordance with updated policies and will implement processes to ensure employee compliance. UCOP has already taken efforts to review benefit policies. For example, Family Member Eligibility Verification is a project which, in calendar year 2012, validated every single individual claimed as a dependent and covered by UC's health benefits. By ensuring only eligible dependents are covered, the University realized a $35 million annual reduction in employer contribution costs beginning in the plan (calendar) year 2013. As part of the project, a more stringent set of verification measures was put in place and a systemwide Family Member Eligibility Verification process will be conducted every four years. The next full-scale verification of family member eligibility began in 2016.

UCOP will utilize savings either by reducing the total amount of the assessment or by directing them to initiatives and programs that benefit the campuses and the system. UCOP's primary goal is to effectively limit assessment growth, aiming to incorporate areas of savings where available. (24)

UCOP will periodically report on the financial impact of implementing the audit recommendations at a frequency determined by the Regents.

Workforce Planning

By April 2018:

4. **Complete phase one of CalHR's best practice workforce planning model by developing a strategic direction for its workforce plan.**

By April 2019:

9. **Implement phase two of CalHR's best practice workforce planning model by determining its current and future staffing and competency gaps. As part of this phase, the Office of the President should consider the input of stakeholders including campuses and students, regarding which elements of its organization are of critical importance and which elements it could potentially eliminate or downsize.**

By April 2020:

13. **Implement phase three of CalHR's best practice workforce planning model by presenting the final workforce plan to its staff and beginning its implementation by carrying out workforce planning strategies covering a three-to five-year period. The Office of the President should make its final workforce plan publically available.**
14. **Implement phase four and five of CalHR's best practice workforce planning model by implementing its workforce plan strategies and annually evaluating the completed workforce plan strategies against defined performance indicators and revising the plan where necessary.**

Response:

UCOP agrees with these recommendations and will implement human resources workforce planning best practices, including but not limited to CalHR, as part of the development of an integrated strategic plan for UCOP that leverages the strategic planning of all divisions. UCOP has already completed strategic plans for the Chief Financial Officer division and the Chief Operating Officer Division, and is well underway on the strategic plans for the Academic Affairs Division and the Agriculture and Natural Resources division. UCOP has a schedule in place for completing the strategic plans for all other divisions.

UCOP will expand upon and further define a long-range workforce planning framework within our strategic planning process – one that is suitable for our organization and based on human resource management best practices. UCOP will ensure alignment with strategic plans, and review and analyze data to determine the overall impact. In preparation of this upcoming year's UCOP budget, all annual divisional budget submissions were required to include preliminary workforce plans.

(25) UCOP will continue its practice of regularly reviewing its programs and services. UCOP reviews the scope of its services and programs offered to ensure that the system creates and leverages efficiencies of scale; provides incentives for campus collaboration; and provides critical programs and services to its stakeholders. UCOP presents the programs and services it supports to the Regents in the annual UCOP budget presentation. It also works regularly with senior leadership from all the campuses through a variety of regular consultative meetings, including monthly meetings with the Council of Chancellors, the Executive Vice Chancellors (Provosts), the Vice Chancellors of Planning and Budget, and Vice Chancellors of Administration. The President also meets regularly with student government leadership across the campuses.

In each instance of strategic planning by UCOP's divisions, formal and informal steps are taken to solicit campus feedback on the development of those plans.

UCOP will ensure alignment with strategic plans, and review and analyze data to determine overall impact. Divisional strategic plans, which will include workforce planning elements, will be made publicly available.

As part of the implementation process of an appropriate workforce planning framework, UCOP will define metrics and produce management reports.

Budget and Expenditures Recommendations

Fund Restrictions and Commitments

By April 2018:

16. Document and review the restrictions on its funds and fund commitments to determine whether it can reallocate any of these funds to its discretionary budget for reallocation to campuses.

By April 2019:

20. Publish the results of its review of fund restrictions and fund commitments and any funds it anticipates reallocating to campuses.

By April 2020:

23. Reallocate to the campuses funds that it identified during its review of fund restrictions and fund commitments.

Response:

UCOP agrees with these recommendations.

By July 2018, UCOP will review restricted funds. (26)

By July 2019, UCOP will publish the results of its review of fund restrictions. (26)

UCOP will utilize savings either by reducing the total amount of the assessment or by directing them to initiatives and programs that benefit the campuses and the system. UCOP's primary goal is to effectively limit assessment growth, aiming to incorporate areas of savings where available. (24)

Reserve Policy

By April 2018:

17. Develop a reserve policy that governs how large its reserve should be and the purposes for which it can be used.

Response:

UCOP agrees with this recommendation.

UCOP will develop an operating reserve policy that governs how large its reserve should be and the purposes for which it can be used.

Budget Presentation

By April 2018:

18. Implement our recommended budget presentation shown in figure 11. Specifically, the Office of the President's budget presentation to the regents should include a comparison of its proposed budget to its actual expenditures for the previous year. It should also include all its expenditures and identify changes to the discretionary and restricted reserves. The Office of the President should combine both the disclosed and undisclosed budget into one budget presentation.

By April 2019:

22. Continue to present a comprehensive budget based on the presentation in Figure 11 to the regents, the Legislature, and the public.

Response:

UCOP agrees with this recommendation.

(27) While UCOP agrees with the substance of this recommendation, UCOP disagrees with the characterization that there is a "disclosed" and "undisclosed" budget. Nevertheless, by July (26) 2018, in consultation with the Regents, UCOP agrees to implement a revised budget presentation format, evaluating best practices and incorporating what would be most useful to the Regents in their budget review.

(26) By July 2019, UCOP will present a comprehensive budget to the Regents and make it available to the Legislature and the public, in formats developed in consultation with the Regents.

Budget Process

By April 2018:

19. Increase campus stakeholder input in the budget development process by reconvening the campus budget committee and establishing an agreed upon charter that describes the committee's scope, role, and protocol for reviewing and providing comments on the Office of the President's annual budget.

By April 2019:

21. Implement the best practices for budgeting identified by GFOA and NACUBO, including developing budget policies and procedures and formally documenting, approving, and justifying all one-time and unexpended expenditure requests.

By April 2020:

24. **Evaluate its budget process to ensure it is efficient and has adequate safeguards that ensure staff approve and justify all budget expenditures. If the Office of the President determines that its safeguards are sufficient, it should begin developing a multi-year budget plan.**
25. **Report to the regents on the amount of funds it reallocates to campuses as a result of implementing our recommendations.**

Response:

UCOP agrees with these recommendations, which are consistent with plans already in place to improve UCOP budget processes.

UCOP will continue its efforts to engage campuses in its budget process. UCOP currently engages campus leaders monthly on various topics and the UCOP budget is consistently discussed. (28)

By July 2019, UCOP will ensure budgeting best practices, including but not limited to GFOA and NACUBO, are being utilized. UCOP will ensure that budget policies and procedures that formally document, approve, and justify all one-time and unexpended expenditure requests are being utilized. (26)

By July 2020, UCOP will evaluate its budget process to ensure it is efficient and has adequate safeguards to ensure all budget expenditures are approved and justified. UCOP will begin developing a multi-year budget plan by this date. (26)

UCOP will periodically report on the financial impact of implementing the audit recommendations at a frequency determined by the Regents.

Systemwide and Presidential Initiatives Recommendations

By April 2018:

26. **Develop and use a clear definition of systemwide initiatives and administration that will be used to ensure consistency in future budgets.**
27. **Develop a comprehensive list of systemwide initiatives and presidential initiatives including their purpose and actual cost that will be used in the regents hearing recommended below.**

By April 2019:

30. **Restructure budget and accounting systems to ensure the costs of the Office of the President can be clearly tracked and reported annually. Specifically, the budget**

and accounting systems should be able to distinguish between systemwide initiatives, presidential initiatives, and administrative costs.

Response:

UCOP agrees with these recommendations.

(26) By July 2018, UCOP will develop a clear definition of systemwide initiatives within the budget, consistent with our plans to enhance budget reporting. UCOP will also provide a comprehensive list of systemwide initiatives and presidential initiatives, including their purposes and costs. UCOP has already implemented a process to track actual expenditures against budget for systemwide initiatives. (29)

To provide the more extensive reports recommended, UCOP's current budget and accounting software may not be adequate. To the extent possible within the current systems, separate accounts for collecting costs for systemwide initiatives will be established. If UCOP systems are replaced in the future, a more robust approach for gathering costs for systemwide initiatives will be built into the software's functionality.

By April 2018:

28. **Establish spending targets for systemwide initiatives and administrative costs.**
29. **Publish the results of the review of systemwide and presidential initiatives including any funds the Office of the President anticipates reallocating to the campuses.**

By April 2020:

31. **Publish its progress in meeting systemwide initiative and administrative cost targets publically.**
32. **Reallocate funds from the review of systemwide and presidential initiatives as well as any administrative cost savings to campuses.**
33. **Report to the regents on the amount of funds reallocated to campuses.**

Response:

UCOP agrees with these recommendations.

(26) (30) By July 2019, UCOP will set annual budget targets, mindful of the fact that unexpected events will require spending flexibility. UCOP will also publish the results of its review of systemwide and presidential initiatives.

(26) By July 2020, as part of its annual budget presentation, UCOP will report progress related to systemwide initiative and administrative costs.

(24) UCOP will utilize any savings either by reducing the total amount of the assessment or by directing them to initiatives and programs that benefit the campuses and the system.

UCOP's primary goal is to effectively limit assessment growth, aiming to incorporate areas of savings where available.

UCOP will periodically report on the financial impact of its review of systemwide and presidential initiatives at a frequency determined by the Regents.

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Comments

CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM THE UNIVERSITY OF CALIFORNIA OFFICE OF THE PRESIDENT

To provide clarity and perspective, we are commenting on the response to our audit report from the Office of the President. The numbers below correspond to the numbers we have placed in the margin of the Office of the President's response.

The report's title aptly summarizes our conclusions. We conducted this audit according to generally accepted government auditing standards and the California State Auditor's thorough quality control process. In following auditing standards, we are required to obtain sufficient and appropriate audit evidence to support our conclusions. Thus, we stand by our conclusions that the Office of the President consistently omitted tens of millions of dollars from the public presentation of its budget and that over the course of our audit period its budget did not accurately convey the cost of its operations. Furthermore, although the Office of the President's budget and financial decisions may have been strategic and deliberate, those decisions were by no means transparent. Lacking the transparency that would allow stakeholders to meaningfully participate in the Office of the President's decision making processes, the claim that the Office of the President's spending reflects university and state priorities is questionable. (1)

We have not made assertions; we have developed conclusions based on evidence. In Chapter 1 we outline the many conclusions we reached based on the evidence we obtained that relate to the management and transparency of the Office of the President's undisclosed reserves. Specifically, on page 34 we state that the Office of the President's weak internal oversight of its undisclosed budget expenditures creates the risk of wasteful spending. We also show in Figure 6 on page 22 that the Office of the President does not publicly disclose its reserves or the purposes for which it intends to spend these reserves. (2)

The Office of the President's statement attempts to convey the notion that $38 million is the maximum amount it has available to spend on other priorities when, in actuality, it is the minimum. As we depict in Figure 10 on page 32, $38 million represents the amount that the Office of the President had not yet committed from its fiscal year 2015–16 discretionary reserve. Although the Office of the President asserted that the remaining $54 million in discretionary funds had already been *committed*, to the extent that these commitments have not yet been fully *expended*, they can be spent for other priorities. Furthermore, because the Office of the (3)

President has significant flexibility in how it spends its discretionary reserve, it can choose to make different decisions with these reserves in the future. For example, we deemed some of $54 million in committed discretionary reserves as questionable, such as $280,000 for chief of staff expenses and $120,000 for consultants. Spending decisions such as these, if eliminated in the future, present opportunities to return funds to the campuses.

④ We stand by our conclusion that the Office of the President's total reserve balance was $175 million at the end of fiscal year 2015–16. This amount comprises $83 million in restricted and $92 million in discretionary reserves. As we state on page 41, the Office of the President's financial data originally indicated that the discretionary reserve was $188 million. Subsequently, the Office of the President's budget director asserted that we should exclude $101 million from our calculation because "the majority use of these funds is non-operational." We followed up with the Office of the President to confirm this assertion and found that the Office of the President had made a $96 million accounting error that inflated its reserve balance to $188 million. Although we subtracted the $96 million from the total reserve balance after the Office of the President furnished additional documentation, we did not exclude the $5 million in question because the Office of the President did not provide evidence to support its assertion that we should exclude it. Auditing standards require that we obtain sufficient and appropriate evidence when making conclusions. Therefore, we considered the $5 million to be part of the Office of the President's fiscal year 2015–16 discretionary reserve commitments—totaling $54 million—which is depicted in Figure 10 on page 32.

⑤ As we state on page 33, there are opportunities for the Office of the President to review—and potentially use—some of the $83 million in restricted reserves for other priorities by lifting its own self-imposed restrictions. As an example, in the past the Office of the President lifted the restrictions on its Searles Fund to minimize the campus assessment. Normally, the term *restricted* refers to legal or contractual restrictions on how a fund can be used; however, the Office of the President imposes its own restrictions on some funds. Funds with internal restrictions can potentially be, and have been, reallocated for other university priorities.

⑥ We question whether the Office of the President can provide evidence to fully support this assertion. Although it seems reasonable that the Office of the President would have consulted with the chancellors for some of its high-profile initiatives, we question whether it has consulted campus chancellors regarding all of its expenses from its reserves, such as the $16.4 million the Office of the President committed for its own one-time expenses, projects, and ongoing operations as shown in Figure 10 on page 32.

Furthermore, we discuss on pages 30, 31, and 77 that executives from the campuses we spoke with stated that the Office of the President's budget and spending decisions could be more transparent and collaborative.

Absent an analysis that considers the volatility of the Office of the President's revenue sources and an evaluation of its historical and current spending decisions, we question how the Office of the President determined 10 percent is a prudent and reasonable reserve amount. (7)

The Office of the President has consistently made fiscal choices without providing the regents, the Legislature, or the public the information necessary to understand their full fiscal impact and without weighing the tradeoffs that would result from these choices. We demonstrate this in Chapter 1 related to failing to disclose its reserves, and in Chapter 3 related to failing to fully disclose and track all of its systemwide initiatives. We further state on page 74 that the Office of the President does not regularly evaluate these initiatives to assess their continued benefit to the university. Thus, it is perplexing how the Office of the President can state that these programs reflect the core values of the regents or the university's mission. Absent a fully transparent process, the Office of the President's spending decisions are not adequately justified. Because the university receives billions in public funds, it is crucial that spending decisions receive public scrutiny and feedback. (8)

At no point do we recommend reducing or eliminating these programs. In fact, on page 4 we state that many of these programs undoubtedly provide a benefit to the public and to students. However, we note on that same page that the choice to pay for these programs may come at the expense of the university's priority of access and affordability for California undergraduate students. We also recommend on page 92 that the regents hold a public meeting that includes university stakeholders to discuss the prioritization of initiatives and that the Office of the President should report on the results, including any initiatives that are eliminated or scaled down. This recommendation is intended to institutionalize stakeholder input in key spending decisions, not to create an expectation that programs will be eliminated or downsized. (9)

Some of the Office of the President's initiatives outlined in Table 11 beginning on page 71 and Figure 17 on page 76 represent initiatives that the Office of the President continues to fund even though they may no longer represent state priorities. For example, as we discuss on page 74, the Governor eliminated earmarks for specific programs to give the university more flexibility in allocating its funds; eight of these programs, with a combined cost of $49 million in fiscal year 2014–15, pertain directly to the Office of the President's (10)

spending on systemwide initiatives. Yet the university continues to fund these programs despite internal evaluations indicating that they could be funded using other sources.

(11) We question whether "all of these initiatives have received substantial public attention and promotion." The Office of the President is selectively omitting certain initiatives that it classifies as systemwide, such as chancellor's administrative funds and president emeriti expenses, among others, listed in Table 11 on page 73. Although the Office of the President continually mentions its notable initiatives throughout its response, we identified at least 79 initiatives that also include lesser known programs and programs that are smaller in scope.

(12) Although the Funding Streams Initiative increased the transparency of the university's financial activity, it has convoluted the Office of the President's revenue streams. Specifically, the Office of the President now receives its revenue from a variety of sources including the State's General Fund and tuition and fees through its annual campus assessment as shown in Figure 4 on page 13. Moreover, the $32 million in campus assessment reserves the Office of the President has accumulated, shown in Figure 9 on page 29, demonstrate that the Office of the President has not done all it can to minimize the campus assessment. In fact, as discussed on page 30, the Office of the President asked for increases to the campus assessment for two of the four years in our audit period even though it had not spent all of the funds the regents approved in previous years. The campuses we spoke to also had concerns regarding the growth of the assessment and their ability to plan for it. For example, an assistant vice chancellor at the San Diego campus stated that she wanted to know about the assessment earlier in the year and that she believed the assessment should be flat with a small, predictable inflation factor.

(13) The Office of the President seems to suggest that there should be a positive correlation between overall university revenue growth and the growth of its own operations and revenue, when it has provided no evidence to support why this would be necessary. For example, a significant amount of the university's revenue and expenditures are related to its medical centers, as we show in Figures 1 and 2 on pages 7 and 9. Although the Office of the President provides some services for the medical centers, this fact does not necessitate commensurate growth of central administration. Furthermore, as university entities grow, the Office of the President should be recognizing economies of scale for many of the services it provides. Thus, this context is neither critical nor relevant.

As we describe in detail throughout Chapter 1 and Chapter 3, the information that is publicly available regarding the Office of the President's budget is insufficient, is not wide-ranging, or extensive. An individual would not be able to fully understand the Office of the President's budget without the information we obtained throughout the course of this audit. (14)

For clarity, 2007 was the first year that a regents' policy required the Office of the President to present a budget for approval. As we discuss in Chapter 1, the budgets that the Office of the President disclosed to the regents lacked tens of millions of dollars in planned spending, anticipated revenue, estimated actual expenditures, and were convoluted with pass-through funds that obscured the Office of the President's operational costs. In addition, as we state on page 35, in 2006 the regents' committee on finance also directed the Office of the President to create appropriate guidelines, procedures, and standards for preparing its budget, yet the Office of the President still has not done so. Moreover, we confirmed with the systemwide audit coordinator that no other budget materials were provided to the regents, other than action items, for fiscal years 2011–12 through 2015–16. These action items are publicly available online and served as the core of our analysis in Chapter 1. Thus, we do not know what additional information the Office of the President is referring to. (15)

Without a detailed understanding of the Office of the President's organization, the public would be unable to determine which portions of the campus financial schedules that apply to the Office of the President and thus could not easily determine the Office of the President's costs. Part of the issue is that the Office of the President's expenses are generally combined with systemwide expenses in the financial schedule, which showed $3.4 billion in expenditures for fiscal year 2015–16. The only section of the financial schedules that specifically refer to the Office of the President's administration shows a total of $241 million in institutional support expenditures—significantly less than the $655 million shown in the budget as depicted in Figure 7 on page 23 and presented to the regents that year. (16)

As we describe on page 41, because of its systemwide focus the university's financial audit does not adequately display the Office of the President's financial activity. The information necessary to view and assess the Office of the President's financial activity simply does not exist in the audited financial statements. In fact, the terms "Office of the President" and "UCOP" appear only three times in the entire 109 page 2015–16 annual audited financial statement and, in each of the three instances, no reference is made to specific financial activity. (17)

It is extremely concerning that the Office of the President would describe the current budget processes as having "extensive" or "rigorous" controls. As we note on page 33, the Office of the President (18)

has not established safeguards over its expenditures related to its undisclosed budget, thus putting million of dollars at risk of misuse. Although the Office of the President is correct that the undisclosed budget approval process has improved since its implementation in November 2014, we state on page 34 that the Office of the President was unable to demonstrate adequate approval for 82 percent, or $34 million, of the five divisions' fiscal year 2015–16 expenditures that we reviewed subsequent to the improved approval process. Moreover on that same page, the deputy chief of staff stated that the president verbally approves some [undisclosed] expenditures during meetings, and the approval process remained flexible even after November 2014. This statement, as well as our analysis, do not support that "extensive" or "rigorous" controls exist.

(19) We disagree that the size of the university's overall budget is critical context for justifying the Office of the President's budget or staff. One percent of the $30 billion the university received in fiscal year 2015–16 equates to $300 million—a sizeable amount that should not be dismissed because of its relative size to the university as a whole. Moreover, the $90 million tuition increase that the regents recently approved—representing only about 0.3 percent of the university's total budget—was not characterized as an immaterial amount, especially given the financial impact it will have on students and families.

(20) We are disappointed that the Office of the President failed to share the analysis it alludes to regarding the number of systemwide services provided by other large system offices even though we requested documentation supporting the statement that the central operations budget compares favorably to other public university systems. We asked the systemwide budget director to provide such an analysis in early January and he stated that he could not locate one. In fact, even though the *Budget for Current Operations* contained this statement each year since at least fiscal year 2010–11, the Office of the President deleted it from the fiscal year 2017–18 *Budget for Current Operations*, which the Office of the President published later in January 2017, after our request for this analysis.

(21) We are hopeful that the Office of the President will engage in a genuine effort to change despite the fact that it fails to acknowledge many of our concerns and downplays the severity of the issues we identified. We are further concerned by the Office of the President's past history in regard to implementing legislative actions as well as our prior recommendations. Specifically, it has not fully implemented many of the recommendations from our report that was issued over a year ago. It is for these reasons, and others that we outline in Chapter 3, that we believe oversight from the Legislature is necessary to ensure the Office of the President adequately implements reforms.

The efforts that the Office of the President has already undertaken are not a substitution for our recommendation. As we discuss on page 49, in the Budget Act of 2016 the Legislature required the regents to consider compensation for comparable state positions when evaluating the salaries of certain Office of the President executives. The Legislature noted that many state employees hold positions with comparable scope of responsibilities, complexity, breadth of job functions and experience requirements. However, as the table below demonstrates, some of the comparisons the Office of the President used in its own analysis do not meet the scope of responsibility and complexity that the Legislature likely intended. Moreover on that same page, the Office of the President compensation director stated he was not aware of any instances in which salaries were frozen as a result of the analysis that the Office of the President conducted. (22)

Table R.1
The Office of the President Compared Itself to Local Government Staff That Receive High Salaries and Are Not Comparable in Terms of Overall Staffing Size and Budget

OFFICE OF THE PRESIDENT POSITION	NUMBER OF GOVERNMENT POSITIONS USED FOR THE COMPARISON	EXAMPLES OF POSITIONS THE OFFICE OF THE PRESIDENT COMPARED ITSELF AGAINST	BASE SALARY OF THE OFFICIAL	NUMBER OF STAFF	SIZE OF THE AGENCY'S BUDGET
Chief Operating Officer $330,000 base salary 190,000 university employees $32.5 billion in university expenditures	1 State employee 13 local government employees	San Luis Obispo County Administrative Officer	$200,200	2,800	$573 million
		Santa Cruz County Administrative Officer	$250,900	2,400	$582 million
		Chief Administrative Officer, Agency Unknown*	$135,282*	Unknown†	Unknown†
Vice President of Human Resources $318,300 base salary 190,000 university employees $32.5 billion in university expenditures	1 State employee 1 California State University employee 3 local government employees	Orange County Human Resources Director	$181,300	18,000	$5.8 billion
		San Bernardino County Director of Human Resources	$186,900	21,800	$5.2 billion
		Director of the California Department of Human Resources	$171,200	225,000 total state employees	$89 million

Sources: Positions and salaries from the Office of the President's budget act analysis as well as publicly available documentation regarding the size and budgets of the agencies the Office of the President compared itself against. Note the comparisons come from a draft version of the budget act analysis because the compensation director confirmed that a final version does not exist. We confirmed that, for the positions used in this table, the final number of positions aligns with the Office of the President's presentation to the regents.

* According to the Office of the President's information, there was no one in this position at the time of the evaluation so the Office of the President used the median salary range for that position.

† The Office of the President did not identify which agency this position was associated with.

(23) Although the Office of the President has narrowed its salary ranges since 2013, we do not believe those adjustments were adequate and thus we stand by our recommendation. Specifically on page 55 we conclude that the Office of the President's salary ranges are too wide to effectively control payroll costs or ensure internal equity within job classifications. The Office of the President uses best practices from the Society for Human Resources Management (SHRM) when making decisions regarding the design and modifications of its salary ranges. According to these best practices, traditional salary ranges commonly span between 15 to 20 percent on either side of the identified midpoint. Yet, even after the adjustment in 2013, the Office of the President's salary ranges exceed the traditional salary ranges identified by SHRM. Specifically, the lowest salary ranges have a width of 34 percent on either side of the identified midpoint and the highest ranges have a width of 47 percent on either side of the identified midpoint. In contrast, the two state classifications shown in Figure 14 on page 57 have a width of 11 percent on either side of the identified midpoint.

(24) We recognize that a variety of options exist for using the savings that the Office of the President may realize by implementing our recommendations. However, the Office of the President should not make these decisions in a vacuum. As we state beginning on page 30, the campus administrators with whom we spoke stated that the Office of the President should receive more suggestions from campuses regarding its budget decisions through a formal advisory body. However, based on the Office of the President's response to this recommendation, we are concerned that it intends to continue its practice of not sufficiently involving its stakeholders when making critical decisions related to the university's funds. Moreover, by stating it will redirect savings back to initiatives and programs, the Office of the President risks undermining the goal of our recommendations—to ensure that systemwide initiatives benefit the entire university and are thoroughly vetted by the university's stakeholders.

(25) We are curious what reviews that the Office of the President intends to continue practicing when, as we state on page 66, the Office of the President was unable to provide any documentation of these reviews and could not demonstrate that the reviews resulted in the identification and elimination of internal redundancies and overlap with the campuses. Furthermore, as we state on page 73, the manner in which the Office of the President presents the costs of these initiatives to the regents and the Legislature is misleading. In fact, as we state on page 70, it could not even provide us with a complete list of its systemwide and presidential initiatives. Moreover, as we discuss in Chapter 1, the Office of the President presents its budget at such a high-level that a stakeholder cannot, from those budget presentations, understand the services the Office of the President provides for campuses or the systemwide initiatives it administers.

Finally, as we state on pages 30 and 31, the campus executives with whom we spoke believe the Office of the President should receive more suggestions from campuses regarding its budget decisions and develop its budget in a more collaborative manner.

The Office of the President changed the due date from April to July for these recommendations. An April implementation date allows the Office of the President one year from the report's release to implement the recommendations and aligns more closely with the state's budget process, which is especially important if the Legislature chooses to appropriate funds directly to the Office of the President. Moreover, the Office of the President's suggestion that these recommendations be completed by July is too late in the year considering that the fiscal year begins on July 1st. (26)

We acknowledge the Office of the President's disagreement with the terminology we use to describe the undisclosed budget on pages 25 and 26 of Chapter 1. Nonetheless, as we state on page 26, since at least fiscal year 2012–13, the Office of the President has not provided evidence that it fully or consistently shared in a systematic manner its undisclosed budget with the regents, the Legislature, or the public. Therefore we stand by the terminology used in our report. (27)

As we state on page 30, although in 2011 the Office of the President created a campus budget committee (committee) to review and advise on the budget, it has not convened the committee since May 2013. Therefore, the Office of the President currently lacks a formal venue for obtaining campus input on its budget decisions. Our review of briefing documents shows that campuses learn about changes to the Office of the President's budget only after the President has already approved them. Moreover, as noted on pages 30 and 31, campuses believe the Office of the President's budget process can be more collaborative. For these reasons, the Office of the President needs to enhance its efforts to engage campuses as opposed to continuing efforts that have proven to be ineffective. (28)

The Office of the President states that it has already implemented a process to track actual expenditures against budget for systemwide initiatives because, as we describe on page 70 and depict by using grey shading in Table 11 beginning on page 71, the Office of the President does not have actual expenditure data for some systemwide initiatives and instead assumes that the entire budget is spent. (29)

We caution the Office of the President and its stakeholders to ensure that spending flexibility is contained through a prudent reserve policy. As we state on page 38, establishing a prudent reserve policy would likely have prevented the Office of the President from accumulating the excessive reserve balances we identified and discuss in this report. (30)

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Attachment 2*
Identified Issues in Draft Audit Report Content

Results in Brief

1. **Page 2: The Office of the President did not disclose to the University of California Board of Regents that it had amassed more than $175M in reserve funds as of fiscal year 2015-16.**

   While UC agrees that all funds should be disclosed in a transparent way, the implication behind the draft audit report's statement, especially the use of the word "amassed," is that the University has done something wrong in using temporary savings for high-priority programs. In some instances, the University maintains a prudent reserve associated with specific programs, which will have the effect of creating an ongoing unexpended balance each year. By way of example, the University's program in Washington, D.C. maintains a prudent reserve on a regular basis to fund unforeseen expenses associated with managing a building and the academic program. In another instance, funds received from a law suit settlement with Enron related to prior energy contracts are held in reserve and used as a revolving fund to support sophisticated studies and complex data retrieval performed in furtherance of the University's climate goals – and these funds are restricted to energy use. In other instances, vacancies and other unexpected events occur in any given budget and create one-time savings. These are not permanent savings and therefore cannot be used to support permanent expenditures; however, they do provide an opportunity each year to redirect some portion of the budget to one-time needs that otherwise would not be funded.

   The $175M in reserve funds (later outlined in Figure 10, pg. 19) should be reflected as $170M (the draft report included $5M that was not UCOP-related fund balance data). The $170M is comprised of $83M in restricted funds (see chart below) and $87M in unrestricted funds.

   FY 15-16 Restricted Fund Year End Balance Summary

Restricted Funds	$M
Lab Research Grant Programs (multi year)	$ 18
Contracts and Grants	13
UC Health (source: UC Medical Centers)	10
UCDC Reserves / PP&E (incl. residence halls)	8
Wholesale Power Program (campus agreement)	7
Building Reserves	7
UC Press	7
Enron Settlement	6
Other Administrative Funds	4
Endowment Cost Recovery	4
Other Program or Academic Funds	3
California Digital Library	2
Specific Academic Program Donations / Income	2
Office of National Laboratories	2
Endowments	1
ANR Federal Funds, State Appropriations	(1)
Internal Loans (UCOP funded)	(9)
Total Restricted Funds	**$ 83**

This document identifies the most apparent and notable issues contained within the draft report, but does not comprehensively address every inaccuracy and mischaracterization. The page numbers and table numbers are references to the draft audit report and may change in the final version of the report.

* California State Auditor's comments begin on page 165.

Restricted funds are provided for specific purposes and generally cannot be used for other purposes. Moreover, maintaining ongoing reserves for restricted funds is prudent management of funds where they are intended to support one designated purpose.

Of the unrestricted fund balance of $87M, $49M was committed as of July 1, 2016 to academic programs, systemwide initiatives, and multi-year campus commitments that the president and chancellors have agreed are high priorities. The largest items in the $49M include: $5.2M for the Global Food Initiative, $4.5M for the Public Service Law Fellowships, $2.5M for Carbon Neutrality, $4.6M for UC Merced Wetlands, $2M for UC Riverside's medical school, and $7.2M for cybersecurity. The Regents are kept apprised of these issues and expenditures throughout the year in their regular, public meetings. The remaining unallocated $38M in the unrestricted fund balance serves as a reserve for unexpected events. Temporary savings that allow for contingencies and some flexibility for unexpected events in large university settings are normal practice and can be referenced via NACUBO using terminology such as "flexible budget." The varying amounts each year underscore the reality that these savings are unpredictable, often one-time in nature and therefore cannot and should not be included in the permanent budget plan. UCOP agrees with CSA that spending from the carry-forward or flexible budget can be more transparent and that appropriate reserve levels should be based on best practices and an agreed-upon methodology to be reviewed and approved by the Regents.

2. **Page 3: The "undisclosed budget" ranged from $77 million up to $114 million in the four years we reviewed.**

The draft report includes new, non-standard budgeting terminology by using "undisclosed budget" to reference UCOP's carry-forward budget. UCOP uses this funding to support programs and initiatives that benefit the University systemwide, as well as individual campuses, faculty, staff and students. The funds were from unexpended budget savings that Regents had approved in prior budgets. Despite these shifts in timing, these initiatives are approved by the president and reviewed by the Regents. Furthermore, applications of temporary savings that allow for contingencies and some flexibility for unexpected events in large university settings are standard practice and can be referenced via NACUBO using terminology such as "flexible budget." The varying amounts each year underscore the reality that these savings are unpredictable and often one-time in nature; they therefore cannot and should not be included in the permanent budget plan.

3. **Page 3**: **Further, even though the Office of the President stated that expenditures from its undisclosed budget went through a rigorous approval process, it could not demonstrate adequate approval for 82 percent, or $34M, of the expenditures we reviewed from its undisclosed budget in fiscal year 2015-16.**
&
Page 34: Consequently, the Office of the President was unable to demonstrate adequate approval for 82 percent, or $34 million, of the five divisions' fiscal year 2015-16 undisclosed budget expenditures that we selected for review.

   CSA did not provide documentation associated with the $34 million identified, so UCOP cannot directly address these claims. Furthermore, it does not identify the methodology of testing the approval, the five divisions in question, or the manner in which the divisions were identified. That said, UCOP provided CSA unfettered access to archives that contain hundreds of decision documents and, when asked, undertook extra efforts to identify others. Because the report does not reveal the expenditures they reviewed, it is impossible for UCOP to respond to this statement.

   Generally, expenditures that are funded from the unrestricted or discretionary carry-forward budget must be approved through UCOP's formal decision-making process. The documents associated with that process outline the purpose, objective and options for the expenditure and must be reviewed and approved by the president**.** The unrestricted budget for carry-forward funds was $30M for FY 15-16, including $14.8M for the Presidential Initiatives fund.

   Since the start of President Napolitano's tenure, the level of rigor applied to financial decisions made in the Office of the President has increased dramatically. In its report, CSA acknowledges this process improvement.

4. **Page 4: Over the past five years, the Office of the President has underspent the revenue it received from campus assessment by $30M, and as a result, a significant portion of the Office of the President's discretionary reserve consists of funds the campuses could have retained and spent for other purposes.**

   UCOP's governance and charter preserves the authority of the President to, on behalf of the system, make investments that might not otherwise be made at the campus level. Key examples and priorities include UC Riverside's School of Medicine, UC Merced's development, and support services and financial aid for undocumented students. These investments are aligned with the University's mission and more suitably and effectively managed through UC's headquarters, in complete accord with campus priorities, as agreed upon by the president and chancellors.

5. **Page 5: Further, the Office of the President spent at least $21 million between fiscal years 2011-12 and 2015-16 on generous employee benefits...**

   The details of the benefits in the $21 million are provided in Table 9 of the report. Included in draft report's listing are reimbursements for meals, lodging, business meetings and

entertainment and cell phones. The University does not consider these employee benefits. All of these are specific business expenses (totaling than $12 million) incurred by employees or on behalf of employees in the normal course of performing their job duties for the University.

6. **Page 6: When we attempted to quantify the costs of its systemwide initiatives, we found that the Office of the President was unable to provide a complete listing of the systemwide initiatives it administers or their cost.**
&
Page 72: However, when we requested a list of systemwide initiatives and their associated costs, we found that the Office of the President was unable to provide a complete listing of the systemwide initiatives it administers.

   UCOP provided CSA with a list of systemwide initiatives as requested. UCOP groups these initiatives separately and accounts for them systematically in its budget system.

7. **Page 7: The Office of the President's administrative spending has increased by 28 percent, or $80M, while campus administrative costs have increased by 26 percent over the same time period (from fiscal year 2012-13 through 2015-16).**

   In the aforementioned UCOP numbers, CSA has elected to include costs associated with the UCPath initiative, a new central payroll system that replaces individual campus programs. It is important to note that this vital program increases expenditures centrally, at the immense long-term benefit of eventually replacing current campus-level expenditures. During this period, UCPath costs totaled $15M. Had CSA excluded UCPath from the figures above, UCOP's increase would have been 23%, lower than the 26% increase of campuses. In addition, UCOP's figure includes increasing costs for major initiatives undertaken on behalf of the campuses, such as cybersecurity and large-scale strategic sourcing designed to generate significant systemwide savings.

8. **Page 7: Furthermore, the Office of the President's budget and staffing levels exceed those of the central administration at comparable university systems, such as the University of Texas. The Office of the President explained that this may be because it provides services to its campuses and employees that other universities do not such as the management costs associated with the university's retirement program.**

   There are considerable differences in the structure, scope of services, and level of State-provided direct support between UC and the University of Texas at Austin. That institution serves as both a flagship campus for the system and a major provider of programs and services for its smaller campuses. As a result, the central administration of that system relies heavily on that campus to support several systemwide activities. This is a fundamentally different model than UC and thus makes for an unfair and misrepresentative comparison.

Chapter 1

9. Figure 3: The University of California Has Multiple Levels of Administration

The diagram in Figure 3 shows that the University is governed by the Regents and advised by the Academic Senate on matters of academic policy, admissions and curricula. The diagram that characterizes UCOP's role is misleading, as it excludes integral functions of UC's headquarters: Office of General Counsel, UC Health, systemwide human resources, information technology services and other support for campuses. In addition, UCOP's Operations budget rolls into the Central and Administrative Services budget; it is not a separate item.

10. Page 16 and Figure 4: The university's campus in Berkeley chose to pay its entire $28 million fiscal year 15-16 assessment with its share of [state general fund appropriations] … In total, the Office of the President collected $288 million in assessments from the campuses, of which 37 percent -- $106 million – was paid using the State's general fund appropriation.

The Berkeley campus has confirmed that it did not exclusively use State General Funds to pay the assessment. The fund from which the assessment was paid includes both unrestricted state and non-state funds, including Nonresident Supplemental Tuition, Tuition, and other unrestricted sources. As a result, the figures of $28 million, $106 million, and 37 percent that appear on page 16 are inaccurate, as is the depiction of the Berkeley assessment in Figure 4.

11. Page 17: Between academic years 2006-07 and 2011-12, the university nearly doubled resident tuition from $6,141 to $12,192 per year.

To make this one point, CSA has included selective data that falls outside of the identified and established period of this audit, which is generally 2010-11 to 2015-16. CSA used the latter timeframe for almost all of the other comparisons, data and findings. Furthermore, during the near entirety of the selected audit period, UC maintained tuition at constant levels.

12. Page 17: The portion of its budget that the Office of the President discloses to the regents for approval increased by more than $100M from fiscal years 2011-12 to 2015-16.

The increase of $100 million between 2011-12 and 2015-16 reflects several changes to the programs and initiatives provided by UCOP. The increase is due in large part – 70 percent – to increases in restricted funds that flow through UCOP, mainly the management of the patent portfolio for most of the campuses and the funds for the Education Abroad Program, which is managed at the Santa Barbara campus. The draft audit report fails to clarify this and implies that administrative operations grew dramatically; in reality, the vast majority of

this increase was from programs that directly benefit campuses and students. The increase in the unrestricted portion of the budget was due to key systemwide initiatives that include UCPath, investments to address cybersecurity risk, and strategic sourcing, all of which – again – directly benefit the campuses.

13. **Page 19: The budget for the University of California (university) Office of the President has grown without adequate justification.**
&
Page 47: The Office of the President acknowledged the need to review staffing in the past: in January 2014, it issued a presidential directive calling for its divisions to create staffing plans in addition to a budget review that was supposed to identify redundancies and determine the appropriate size, shape, and role of the Office of the President. However, it did not document the results of the review. Further, our analysis shows that the review did not decrease staffing levels or costs.

Growth at UCOP has not been in administrative functions as implied by the draft audit report; rather, by design, it has been entirely in strategic areas that benefit the campuses and allow for long-term savings:

- Information Technology: Much of the growth here has been movement from external contractors to internal resources, such as Apply UC. Between 2011-12 and 2015-16, growth in this area was 11.1 full-time equivalent staff (FTE).
- Office of the General Counsel: To reduce overall spending and increase efficiency, UCOP has expanded in-house legal services. Between 2011-12 and 2015-16, there was growth of 14.3 FTE.
- UCPath: This new initiative replaces eleven separate antiquated systems with one vendor-based product to standardize and streamline human resource and payroll functions across all campuses and to centralize certain services for the system. Between 2011-12 and 2015-16, there was growth of 160 FTE.
- Chief Investment Officer (CIO): The CIO's office identified opportunities to save money long-term by bringing certain investment management functions in-house instead of using outside consultants and managers. Between 2011-12 and 15-16, there was growth of 6.7 FTE.
- Risk Services: UCOP created Fiat Lux, a captive insurance company, to allow the University to self-insure and buy re-insurance directly in the market, eliminating the need to purchase coverage through insurance carriers at higher rates. Between 2011-12 and 2015-16, there was growth of 11.9 FTE.
- Procurement Services: The P200 initiative has saved over $200M thus far. It has expanded its scope and set its next savings goal at $500M (SC500). Between 2011-12 and 2015-16, there was growth of 16.6 FTE.

- ILTI (Innovative Learning Technology Initiative): This program aims to create high-quality online education experiences across all campuses. Between 2011-12 and 2015-16, there was growth of 15.8 FTE.

The remainder of the Office of the President administrative functions have decreased by 40 FTE since President Napolitano assumed leadership in 2013.

14. **Page 19: As a result of these convoluted and misleading budgets, the Office of the President has received little meaningful oversight of its finances.**

    This language suggests intent by UCOP to mislead through its reporting of budgets and expenditures. While UCOP acknowledges the importance of continuous improvement, there is no evidence that funds were used for any purpose inconsistent with the missions of the University.

15. **Page 20: Our analysis suggests the Office of the President could currently use from $38 to $175 million from its reserves for other university priorities depending on the results of a review of its funds and commitments.**

    The total fund balance as of June 30, 2016 was $170 million. As stated above, portions of the restricted balance are funds provided for a specific purpose and cannot be redirected to other uses. Moreover, another portion of these fund balances will be transferred to campuses in the form of research grant funding or other program services by agreement (i.e. Wholesale Power, UC Health). For more information, see chart in response to issue #1 above. In addition, all of the programs included in the $49 million represent direct alignment with UC's mission; reflect significant stakeholder input from campuses, students, and Regents; and demonstrate shared priorities with the State.

16. **Page 20: The Office of the President maintains two budgets.**

    Carry-forward funds are not a separate budget. They generally result from savings from temporary vacancies caused by staff turnover or retirement, as well as other reasons during any given year.

    The Office of the President conducts periodic reviews of departments to identify budget trends and to determine if departments annually carry forward an appropriate level of funding. In certain instances, UCOP trims department budgets. However, in most cases, the large variances reflect one-time vacancies or the multi-year nature of projects and are therefore temporary in nature.

17. **Page 21: The combined disclosed and undisclosed budgets for the Office of the President grew faster than inflation; in part because of programs it funded using its undisclosed budget, such as a $1.3 million subsidy program to reduce employee contributions to the university's health insurance program and its $2.2 million**

cybersecurity initiative. The consistent growth in the Office of the President's spending makes the lack of transparency of its budget to its stakeholders particularly troubling.

UCOP lists major areas of growth each year in the Regents item of the UCOP budget submitted for approval. UCOP is fully transparent about such increases. In addition, growth of the University of California systemwide has outpaced that of the Office of the President.

Inflation is only one of the increasing cost pressures on UCOP; rising student enrollment and expanding research and health budgets also impact existing resources. That said, UCOP has grown significantly slower than the University as a whole.

18. **Page 21: Over the past four years for which it has data, the Office of the President has spent an average of $97 million less per year than it planned to spend.**

    UCOP has maintained conservative spending practices through the years. The general management philosophy is to not exceed annual budget targets. The average annual savings amount has varied from year to year and is made up of roughly 60% restricted funds, which are often supporting multi-year awards that are spent in future years. Much of the year-to-year savings can be attributed to temporary vacancies and turnover of staffing at the Office of the President. Consistent with its management practices, UCOP seeks to underspend, as opposed to overspend, in any given year.

19. **Page 22: In fact, as of 2015-16, the Office of the President had $830 million of funds available to spend, but only presented a budget totaling $655 million to the regents.**

    This statement is misleading and inaccurate. The variance between $830M and $655M is the draft report's calculated $175M reserve. The report states that the entire balance is available, neglecting the fact that $83M is restricted (see Figure 6 in the draft report), and $49M was committed in prior years.

20. **Page 23: The remaining undisclosed reserve funds were spent on one-time projects and unanticipated expenses. Thus, most of the spending in this budget was for purposes not approved by the Regents.**

    Funds within the carry-forward budget are spent in accordance with the overall mission and key priorities of the University. Many of the expenditures are for programs that are already established in the permanent budget or are added to the permanent budget in subsequent years, such as the cybersecurity program, the Presidential Postdoctoral Fellows Program or the Sexual Violence/Sexual Harassment office. Moreover, the Regents approve the UCOP budget at the division level, not by program. Some carry-forward funds are spent within the same division they were originally approved, and are thus consistent with the funding levels the Regents originally reviewed and approved. Moreover, these programs are frequently discussed with the Regents in their public meetings.

21. Page 24, Table 4 The Office of the President's Planned Spending From the Undisclosed Budget Includes a Number of Different Types of Expenditures

Many of the items in the table (Historically Black Colleges and Universities, Multi-campus Research Programs and Initiatives, President's Postdoctoral Fellowship Program, Sexual Violence, Sexual Assault) are also in the permanent budget. The carry-forward funding in the table represents supplemental funding to advance or commence the program. This table also wrongly categorizes the President's Residence funding; this is not a carry-forward budget item.

22. Page 25: Furthermore, these documents were included in the materials presented to the regents' committee on finance, rather than as part of the presentation to the entire board.

All presentations and documents presented during the Finance Committee meeting are available to the full Board of Regents. During the audit period, the entire board was present for all of the presentations and details.

23. Page 27: A more transparent budget presentation would separate pass-through funds from the Office of the President's actual operating expenditures.

The most recent budget item presented to the Regents clearly distinguished systemwide programs. In previous presentations, systemwide programs were separately identified in an accompanying table.

24. Page 27: Further, if the Office of the President had provided the prior fiscal year 2014-15 expenditures, the regents would have known that the Office of the President spent more in the prior year than what was approved. We question whether the regents would have approved the Office of the President's fiscal year 2015-16 budget – or the Office of the President's requested $10 million increase to the campus assessment…

UCOP rejects the assumption that if the Regents had known about the most recent year's expenditure of carry-forward funds, they would not have approved the budgeted level of funding. Carry-forward funds are temporary, one-time funds and should not be used to support permanently budgeted programs. The budget the Regents approve each year is the permanent budget, which is prudently managed through permanent fund sources. The two are not related and, as such, budget approvals would not have been different.

25. Page 27: After we asked about its budgeting practices, the Office of the President systemwide controller asserted that it began creating undisclosed budgets as a result of the state budget process and that it had maintained the process because it had always budgeted in that manner.

The systemwide controller did not make this statement, and she was not given any documentation to validate this assertion as part of the audit process. This is in violation of CSA's standard auditing practices, which require documented support for all content included in the audit report.

26. Page 27: When we asked about the Office of the President's failure to base its budgets on the current year's estimated actual expenditures, its management asserted that they would consider using actual expenditures as the basis for future budget planning. However, its management expressed concern that basing budgets on actual expenditures would create incentives for the Office of the President's divisions to spend their full budgeted amounts each year so as not to lose their budget allocations for the following year.
&
Page 28: The Office of the President should base future budget planning on its actual expenditures to improve the accuracy of its estimated budgets, cut unnecessary spending, and reduce the financial burden the campus assessment places on the campuses.

Most similarly complex entities funded by California's state budget use incremental budgeting – the University of California is no exception. Neither the Governor's Budget nor the final budget adopted each year "is based on the current year's actual expenditures," per CSA's recommendation. UC acknowledges that it is important to review budgets periodically to determine if actual expenditures over several years are in line with permanent budgets. In instances where actual expenditures and planned budgets have been found to be out of alignment over several years, budgets have been reduced. However, it would be imprudent to manage budgets year-by-year on temporary changes that occur in any given year.

27. Page 28: We do not consider the Office of the President's concerns to be valid because it annually sweeps unused discretionary budget allocations into a discretionary reserve, a practice that already encourages its divisions to spend their entire budget allocations.

UCOP considers this an inaccurate statement and the draft report does not provide any evidence to support it. As CSA itself has noted, the vast majority of divisions do not spend their entire budget allocations.

28. Table 5. The Office of the President's reserve balances indicate that it did not keep the campus assessment as low as possible.

This table represents the growth of a reserve balance for a new revenue stream. This balance grew to approximately $30 million. This reserve was then deployed to limit volatility in the campus assessment for the past two years. Based on consultation with the campuses, UCOP chose an approach that led to modest reserves that in turn ensured a predictable assessment.

29. Page 30: Without adequate opportunity for campuses to provide input on the Office of the President's budget, the Office of the President has less assurance that its budget continues to align with the university's priorities and serve the needs of campuses.

The Office of the President develops its priorities with extensive campus consultation. On a monthly basis, the President formally meets with the campus chancellors; the Provost formally meets with campus Provosts; and the Chief Financial Officer formally meets with the Chief Financial Officers of the campuses, among a range of similarly consultative efforts. Ultimately, the Board of Regents and the president establish the priorities of the University, after extensive and purposeful consultation.

30. Page 31. Although we recognize that the Office of the President needs some flexibility to fund these sorts of programs or projects if they arise during the year, the regents already approve an annual allocation of $10 million for the president to use as she sees fit for the mission of the university. In each of the past four fiscal years, the president did not spend all of this allocation.

The unspent expenditure of this allocation represents financial prudence by the University and the current and immediate past presidents. At the time of his departure, President Yudof had not expended the entirety of these budgeted funds. Upon assuming leadership, President Napolitano reviewed University operations and priorities before deciding on the most prudent investments. Since her arrival, the actual expenditures of these funds have effectively come into alignment with the budgeted amount. Again, UCOP's approach is to underspend rather than overspend.

31. Page 32: Moreover, the director of corporate accounting confirmed that the Office of the President can designate funds as restricted, such as the systemwide administration cost recovery fund which it largely spends on marketing.

This is not an accurate statement, and the Director of Corporate Accounting did not make it. No documentation to validate this assertion was provided as part of the audit process. This is in violation of CSA's standard auditing practices, which require documented support for all content included in the audit report.

32. Page 34: Moreover, after the Office of the President provided this documentation, we found some of the approval documents were incomplete because they did not include the expenditures' justifications or identify the individuals who approved them.

CSA did not provide documentation associated with this claim, so UCOP cannot directly address it. Furthermore, it does not elaborate on "some" of the approval documents. Since the start of President Napolitano's tenure, the level of rigor applied to financial decisions made in the Office of the President has increased dramatically. In its report, CSA acknowledges this process improvement.

33. Page 35: In fact, we found it difficult to determine which decision memos related to the undisclosed budget because the Office of the President does not distinguish between these memos and ones related to its disclosed budget.

This statement validates UCOP's stance that it does not, in fact, maintain two budgets.

34. Page 36: Instead, the Office of the President could only provide annual budget letters that it sent to its divisions that described at a high level specific budget priorities – like reducing meeting costs – and changes to the budget review process.
&
Page 37: However, these letters did not sufficiently explain how the divisions were to implement these guidelines within the framework of an existing budget process.

As with the development of the budget at the State level, other universities, and countless other complex, multifaceted organizations, UCOP's budget letters describe the priorities and goals the president has established for development of the following year's budget. It is within a UCOP division's purview to determine how to implement these goals.

35. Table 6. Future budgets are based on current year budget and actual expenditures are not regularly monitored by the budget office.

UCOP periodically reviews actual expenditures to determine if departments are over-budgeted. It does so using several years' worth of actual expenditures.

36. Page 39: The Office of the President's choice to omit information about its other available funding sources is concerning because we determined it could have used these sources to minimize the campus assessment or minimize these funds for other university priorities by returning excess reserves to the campuses in the form of a refund.

The Office of the President publicly reports its funding sources by group in the annual presentation to the Regents. Available sources of funding for the ongoing budget were

evaluated as part of the preparation of the annual budget, and then included in the high-level funding sources by restriction, as applicable. Providing additional detail around the sources and uses of funds within the UCOP budget is what UCOP has been doing internally for several years, and will provide at the level of detail appropriate and necessary for review by the Regents.

37. **Page 39: The systemwide controller stated that GFOA budget practices do not necessarily apply to the Office of the President because it reports business-type activity whose operations are financed in part by fees charged for its services, making it different from other entities primarily funded through public funds. However, we believe that because the university receives $3 billion in state general funds from taxpayers it should follow GFOA best practices. Moreover, when we contacted the GFOA, a senior manager agreed that these best budget practices are applicable to public sector higher education institutions.**

    This paraphrased misinterpretation of a quote from the Systemwide Controller confuses her comments on Governmental Accounting Standards Board (GASB) requirements with GFOA requirements. The confirmed documented response to CSA from the Systemwide Controller contains the following statement, which is not incorporated in the draft report: "GFOA budget practices are an appropriate overall framework for assessing OP's budgeting process."

38. **Page 41: Specifically, although the university receives an annual financial audit by an independent external auditor, this audit is conducted at a systemwide level, which obscures the Office of the President's financial activities and does not specifically valuate the Office of the President processes.**

    UCOP rejects the assertion that this process obscures financial activities – deliberately or otherwise. There is no intent to "obscure" information, and the draft report includes no corroboration for that characterization. The purpose of the annual financial audit is to carefully assess the entire University, which it does comprehensively according to accepted audit standards.

39. **Page 42: For example, the university's most recent annual financial report indicated that the university as a whole maintained a deficit unrestricted fund balance of $11 billion, a significant portion of which is attributable to pensions and retiree health benefit obligations. However, as we demonstrated earlier in this chapter, the Office of the President itself maintains a significant surplus reserve balance – $92 million of discretionary reserves at the end of the fiscal year 2015-16.**

    The $92 million of discretionary reserves referenced above should be corrected to reflect $87M after the $5M adjustment ($175M vs. $170M, see issue #1 above). Furthermore, as clarified earlier, the $87M has commitments of $49M against it yielding an unallocated carry-forward balance of $38M. With regard to the pension and retiree health benefits, any comparison of either the purported $11 billion deficit or UC's reserve to UCOP's carry-

forward balance is comparing apples to oranges. The $11 billion deficit is related to the requirement by GASB rules that the current value of retirement health benefits be reflected on balance sheets. The $11 billion is associated with the entire University system and includes the Office of the President's proportionate share of these costs. The $87M million in carry-forward funds is an entirely separate matter. Lastly, with regard to the pension issue, UC has taken steps in recent years to restructure and address financial issues associated with pension and retirement benefits in order to correct the $11 billion issue.

40. **Page 43: …the Office of the President was unable to provide us with information regarding the actual restricted revenue it received.**

    This statement neglects to mention the lack of time provided by CSA for UCOP to meet this request. CSA made the request to UCOP on March 22, one week before the release of their draft report. The Budget and Finance office responded that it would require an extensive manual effort to compile this data for the entire audit period, which could not be completed in such a short time. The CSA statement implies that UC is "unable" to provide it at all, which is not a correct representation of UC's response.

Chapter 2

41. **Page 48: Although the Office of the President has consistently stated publically (sic) that it is doing all it can to keep its operating costs low, its staffing levels have grown by 11 percent since fiscal year 2010-11. As Table 7 shows, this rate of growth outpaced the rate of staffing growth for the university by 1 percent.**

    As draft report itself points out, many of the projects and programs managed by UCOP are systemwide. The increase in UCOP staff has been necessitated by additional systemwide projects that reduce redundancy on the campus level. In addition, the 11% growth for the 6-year period equates to annualized growth of less than 2% per year.

42. **Page 48/49: From fiscal years 2010-11 through 2016-17, the Office of The President increased the number of staff at its Oakland location by 153 employees, while it employed only 17 additional staff at the campuses. Employees at the Office of the President's headquarters generally perform administrative functions, such as human resource administration, accounting, and information technology (IT) support.**

    The draft report is dramatically understating the scope and scale of functions provided by UCOP. The office manages programs that serve the entire system, allowing campuses to capture the savings and efficiencies of centralized operations, while coordinating activities that allow them to operate as one university – all this, with its core operations and staff comprising just 1 percent of UC's overall budget.

Among UCOP's most critical functions:

- Serving students: Maintain UC's admissions process and centralized application portal; administer over $5 billion financial aid annually; provide academic support for underrepresented K-12 students; partner with community colleges and education groups for enrollment outreach
- Serving the public: Oversee five medical centers that provide critical care, serving 1 million patients each year; administer $220 million in grants that support campus research and innovation; overseeing State-funded research programs combatting cancer, HIV/AIDS and tobacco
- Serving UC's mission: Provide funding for and, in many cases, manage a wide array of programs, including: improving K-12 education through programs focused on low-income, underserved or underrepresented student groups as well as teacher training and support; an extensive network of researchers and educators reaching out to every CA county to solve local economic, agricultural and natural resource problems; leading efforts in areas of societal and global impact such as climate change and sustainability, food security, and innovation and entrepreneurship
- Serving UC: Manage fiscal operations of UC's $30B budget and UC's $100B investment portfolio; negotiate systemwide collective bargaining agreements; oversee legal and ethical compliance; promote UC's interests in Sacramento and Washington, D.C.; administer plans for 200,000 current and retired faculty and staff

UCOP's identified growth of 153 employees supports additional systemwide initiatives. The limited campus growth proves the fact that UCOP's systemwide initiatives indeed benefit the campuses by diminishing redundancies.

43. Page 49: Although the Office of the President has maintained relatively steady staffing and salary levels for its senior management group, it has increased both staffing and salary levels for its managers and senior professionals and for its professional and support staff. In fact, it increased its managers and senior professionals' staffing levels by 32 percent from fiscal years 2010-11 through 2015-16, from 519 employees to 685 employees. Further, the total salaries it paid its managers and senior professionals increased by $38 million, a 59 percent increase, and their average salaries increased by 22 percent, or nearly $27,000, over this same time period.

UC has transitioned to a new system called Career Tracks, which has enabled UCOP to standardize job classifications, and review and update job descriptions to better reflect employees' day-to-day responsibilities. In addition, UCOP Human Resources conducted reviews to ensure the management structure was consistent with the Career Tracks system, i.e., that managers must supervise two or more full-time career staff. This

analysis, the transition to Career Tracks, as well as the restructuring of UCOP that began in 2008-09, reduced the number of UCOP employees designated as managers. Furthermore, UCOP staff are now in job classifications that more closely reflect their actual duties. Thus, when Career Tracks was implemented in 2014, of the 91 employees classified as managers under the old system, 41 were moved to non-manager classifications.

A broader review of data between 2007-08 and 2015-16 (which includes pre-recession years) actually shows a 29% drop in UCOP managers working in largely administrative functions.

44. Page 50: For instance, an associate director in the public affairs division with an annual salary of $160,632 does not directly manage any employees. Likewise, a manager in the academic affairs division with an annual salary of $120,200 manages only one employee. In fact, we identified 10 managers who appeared to oversee only one employee and 6 managers who did not oversee anyone at all. When we shared this analysis with the Office of the President it stated that the guidance was not a strict rule. However, we question whether the number of managers and their corresponding pay is justified given the Office of the President's perspective that its managers do not necessarily need to oversee at least two staff.

Since many UCOP managers oversee systemwide projects and programs, a manager of a systemwide program leverages existing staff in the same programmatic function at the campuses rather than adding staff under the manager at UCOP. Because UCOP managers are accountable for systemwide programs, their job duties, their title, classification and pay reflect the scope of their responsibilities accordingly.

45. Page 50: The Office of the President could save millions of dollars in salary costs by paying its executive management and administrative staff salaries that more closely align with those offered by state agencies and the California State University (CSU). The Office of the President's higher salaries are largely the result of its decision to use mostly private sector data when determining appropriate salaries for its positions.

The University's salary ranges and pay practices are aligned with the marketplace in which it competes for talent. Its medical enterprise is aligned with other public and not-for-profit teaching hospitals' pay practices; its academic positions are aligned with public and private higher education institutions; and its administrative and operational positions are aligned with public and private employers in the geographies that it targets for recruitment. In the last category, higher education pay data accounts for at least 50% of the data UCOP uses to create the pay structures for executives. In

addition, where there were reasonable matches at CSU, the State, counties and municipalities, UCOP included that data in the creation of the market reference zones (MRZs). For example, the Chief Investment Officer position is matched to CalPERS and CalSTRS, in addition to a host of other public higher education institutions.

46. Page 50: Further, the Office of the President has established wider salary ranges than comparable state employees that may not allow it to effectively control costs or provide incentives for employee development because employees do not necessarily have to take on additional responsibilities to earn more money.

The State is heavily unionized and its ranges reflect that reality and are influenced by the bargaining process. For UC, MRZs reflect actual pay ranging from the 25th to the 90th percentile of our market comparators. Our salary ranges are similarly situated with the median market pay reflected by our salary range midpoints. Those ranges are indicative of pay for seasoned professionals at the higher end and those with little or no job-related experience at the lower end. This encourages employee development, allowing them to migrate through a given salary band by increasing their skills and abilities. This is a much more fiscally prudent way of managing staff and compensation, as it helps control grade inflation and better manage salary compression.

47. Page 51: The Office of the President could save at least $700,000 annually by aligning its executive salaries to those of comparable public sector executives

While salary levels paid in the public sector should be an important component in the University's market comparisons, they should not be the only component. The University largely recruits from a very different market than state government. Moreover, the State has historically recognized the importance of the University's need to be competitive with both public and private institutions. Its State-approved faculty salary comparison institutions are half public and half private for this reason, acknowledging that the University must compete with both kinds of institutions for its faculty. The same is true for staff. As a result of the last audit, the Legislature inserted language into the 2015-16 budget requesting the University include more public-employee comparisons in its market zones analysis, and UC has complied where applicable.

48. Page 51/52: The 10 Office of the President executives we analyzed had combined salaries of $3.7 million-over $700,000 more than their combined highest paid state employee counterparts. Furthermore, in many instances, the state employee executives had roughly the same levels of responsibility compared to Office of the President executives. For example, the director for the California Department of Human Resources (CalHR) earns about $100,000

less than the vice president of human resources at the Office of the President. Both positions are responsible for labor relations, collective bargaining, employee salaries and benefits, job classifications, recruitment, and retention; however, CalHR is responsible for over 225,000 employees compared to 190,000 at the university.

In this example, CSA is overlooking the additional scope of UCOP's Vice President of Human Resources role, including the complexity of the strategic programs focusing on talent and retention, and the oversight and creation of compensation and benefits programs, including pension and retiree benefits. It should be noted that retirement programs for CalHR are administered by CalPERS, and having the vast majority of State staff unionized further simplifies the CalHR position. In addition, the complexity of the research and health services organizations, which does not exist at CalHR, expands the scope of the UC job.

49. **Page 52: Nonetheless, CSU executives have more responsibility than their Office of the President counterparts in some instances. For example, the CSU's chief financial officer-whose annual salary was $70,000 less than the university's chief financial officer in fiscal year 2014-15-is in charge of the business and finance division, the mission of which includes management of information technology services.**

The draft audit report highlights information technology services that are not in the portfolio of the UC CFO, while it ignores all the other critical aspects of the UC CFO portfolio that are not in the CSU CFO's scope of job responsibilities. These include the roles the UC CFO plays with respect to asset management, financial investments, and capital finance, among others.

The UC CIO also has significantly greater levels of complexity than CSU or the State, since the role includes supporting UC's expansive research and health enterprise, including the strategic initiative supporting the use of big data in the enhancement of clinical delivery.

50. **Page 53: The Office of the President has asserted that the higher education environment necessitates higher pay for its staff. Although that assertion may have merit for certain executive employees, it has much less merit for administrative staff who perform similar duties no matter where they work. Nonetheless, Table 8 shows that the Office of the President paid the administrative staff we reviewed over $2.5 million more in annual salaries than the maximum salaries for comparable state employees, even after including a cost of living adjustment. We analyzed the job duties, responsibilities, and qualifications of the Office of the President**

administrative classifications to identify similar state positions. We found that the *average* Office of the President salary was higher than the *maximum* amount the State could pay an employee to perform the same administrative duties for eight of the 10 positions we reviewed.

UC does not believe that CSA chose truly comparable jobs in its analysis. First, job comparisons to CSU and the State may not be appropriate given potentially vast differences in the scope of responsibilities. For instance, when UCOP reviewed the job description that CSA selected from the State for an Executive Assistant 3 (EA3), it found that the State job was much lower level with fewer responsibilities. In addition, the CSU range was much closer to the range for the UC EA3 position and their duties are more aligned.

Additionally, the draft audit report indicates that CSA, "…added a 4 percent cost-of-living adjustment for comparing the salaries of State employees to OP employees." Best practices for compensation would not apply cost-of-living differentials, but rather cost-of-labor differentials. UC uses data from the Economic Research Institute, which includes thousands of employers, and indicates that the cost of labor in Sacramento is approximately 6% greater than the national average while Oakland is 17% greater than the national labor average.

The draft audit report compares represented IT positions at the State to a non-represented position at UC. Market demand for qualified IT employees is extremely high in the Bay Area. UC must pay the Bay Area's competitive wages in order to attract and retain qualified employees and prevent costly turnover.

51. Table 8. Office of the President Administrative Staff Salaries Generally Exceeded Salaries of Comparable State Employees.

While salary levels in the public sector should be an important component in the University's market comparisons, they should not be the only one. The University largely recruits from a different market than state government. Moreover, the State has historically recognized the importance of the University's need to be competitive with both public and private institutions.

52. Page 55: When we suggested that the Office of the President give greater weight to public sector pay when setting its salaries, it claimed lowering salaries would make it less competitive in the Bay Area job market and therefore affect its ability to attract talent. It especially emphasized this point for the technology positions we selected. Nonetheless, we disagree with the implication that pay alone attracts talent. The Office of the President offers stability and generous benefits including a retirement plan that are not always provided in the private sector. Moreover, the Office of the President

can attract individuals for whom working for the public sector to advance the university's prestigious reputation has an intangible benefit. These factors help to offset the pay differential between the Office of the President and the private sector.

UCOP never asserted that pay alone is the single factor attracting talent and agrees that many other factors may attract employees to UC, one of which is UC's prestigious reputation. However, without competitive pay, prospective employees may not even consider UC as a viable employer.

The University's retirement plan is a consideration for employees who plan to spend a large portion of their career at UC. However, for prospective employees who for various reasons anticipate a shorter tenure with the University, cash compensation is more critical than long-term benefits that will not impact them.

53. **Page 55: The Office of the President's salary ranges are too wide to effectively control payroll costs or ensure internal equity within job classifications. The maximum of every salary range the Office of the President uses for its non-represented employees is at least double the minimum salary for the same range. For example, the Office of the President's highest salary range that was effective from July 2014 through June 2016 spans from $124,600 to $344,600-a difference of $220,000.**

The spread of the State's salary range for the IT position, a minimum (~$65,000) and maximum (~$86,000), is approximately 35%. This narrow band would not allow much latitude to attract new hires with differing skills or abilities, nor would it allow for encouraging employee development without costly promotions to the next level. This type of structure causes grade inflation and lessens the institution's ability to provide meaningful opportunity for employee growth and development.

UCOP regularly assesses internal equity within job classifications, and when promotions are requested, human resources conducts additional reviews to assess skills and abilities against pay.

54. **Page 56: Further, the use of such wide salary ranges can create situations in which two employees perform similar duties and have similar responsibilities but earn vastly different amounts. In fact, we noted 51 instances of employees in the Office of the President who had pay rates that were more than 50 percent higher than those of peers in the same classifications. In these instances, the salary differences could not be attributed to the employees' responsibilities or skill levels because-according to the university's policy manual-the purpose of the classification process is to ensure that the university correctly identifies**

positions' required skill levels and assigned responsibilities. If an employee operates at a higher skill level or performs more difficult work than others in his or her classification, that employee should have been placed in a higher classification.
&
Page 58: However, we disagree that the wide salary ranges are necessary because the Office of the President's classification system already ensures salary accommodation for junior-level staff at lower tiers within a series and more experienced staff at higher tiers. In fact, the large salary ranges paired with the classification system creates an environment in which staff do not need to perform additional responsibilities to earn higher salaries.

UCOP is uncertain how CSA was able to reach the conclusion that "the salary differences could not be attributed to the employees' responsibilities or skill levels" without the underlying data required.

In addition, the notion that "if an employee operates at a higher skill level or performs more difficult work than others in his or her classification, that employee should have been placed in a higher classification" is not true since the overall responsibilities, as well as the higher level of skill and ability requirements, dictate the classification for a job. The draft audit report seems to suggest that UCOP should be promoting more people, rather than managing their career development within a classification system more defined than the State's, which could actually lead to higher salaries and less savings.

55. **Page 60: Specifically, while State policy only permits the reimbursement of meals for employees on travel and prohibits reimbursement for business meetings with agency employees, the university's policy allows for up to $174 per person per day in reimbursements for business meetings, entertainment, and other occasions. As a result, the Office of the President has reimbursed its staff more than $2 million for meals since fiscal year 2011-12.**

It is very rare that a UC employee would have a daily expense total of $174. This is covered in policy BUS-79 and there are caps for each type of meal (http://policy.ucop.edu/doc/3420364/BFB-BUS-79). In most instances there would be one or two meals catered (for example a light breakfast and a lunch for a conference or all day meeting). Another example would be a lunch meeting with a donor, which has a cap of $47 per person including tax, tip, etc. The policy requires that the event or meeting support University business.

In addition, while the accumulated amount referenced is technically correct, the amount of $2 million is for 5 years, which amounts to $400K per year.

56. Page 60: …we identified an instance in which the Office of the president paid for all three meals for attendees when it hosted a conference. For example, for a one-day compliance symposium it hosted in 2015, the Office of President spent $153 in meals per person for about 280 university attendees. The total cost of catering for the symposium was $74,000, most of which the Office of the President paid for out of campus assessment fund.

While it is accurate that the Office of the President spent $74,000 on meals for about 280 attendees at a sponsored compliance symposium, it is factually incorrect to describe the event as a one-day compliance symposium. This was a three-day compliance symposium to provide professional development training for the University's compliance and audit personnel as well as many other employees. The training was provided in multiple simultaneous instruction tracks with all participants attending common general session lunches. Many of the University attendees received continuing education hours required for their respective professional associations or certifications (legal, CPA, internal audit, compliance and healthcare) in a cost-effective manner.

57. Page 60: The Office of the President reclassified the Searles Fund as a discretionary funding source in 2011-12 as discussed in Chapter 1

UCOP undertakes periodic reviews of fund restrictions, and the release of the Searles Fund was one result of that action. UCOP believes this a prudent financial action that is consistent with appropriate budgeting practices.

58. Page 61: Specifically, an employee spent more than $350 per night on a hotel room, even though this cost exceeded the federal and state allowable limits by $140 per night.

Since CSA did not provide any data or context for this expenditure, UCOP is unable to verify it, or provide evidence showing the reservation was necessary due to geographic or other factors.

59. Page 62: For example, although the Office of the President spent at least $2 million on cell phones and other electronic devices for its employees, it has no formal process for tracking the number of devices it issues.

UCOP does not agree with this statement. It provided CSA extensive detail regarding the electronic devices issued to employees. During the audited period prior to President Napolitano's arrival, fewer controls were in place for electronic device issuance. She has since undertaken proactive efforts to enhance practices and controls in this area.

60. Page 63: We identified several instances in which employees received both stipends and bonuses in addition to their regular pay. For example, since

fiscal year 2011-12, the current director of the operating budget (university budget director) has collected more than $47,000 in bonuses and stipends. In fiscal year 2012-13 alone, this individual received more than $18,000 in stipends and a $5,000 bonus in addition to his $122,000 salary.

Beginning in 2015, UCOP instituted new procedures to review and approve stipends to ensure that the amount of the requested stipend align with increased responsibilities.

The $18,321 in stipend pay that the individual in question received in 2012-13 was entirely due to his appointment as interim Director of Student Financial Support from July 2012 to June 2013 following the retirement of an individual from that position in June 2012. During that time, he was performing two jobs – his official position (deputy director) and that of the director – at great savings to the department.

Similarly, in 2011-12, he received stipends totaling $11,307 because his manager had taken on the role of Interim Executive Director of Admissions following a retirement in June 2011, also resulting in great savings to the department.

Those two temporary appointments accounted for $29,628 of the $47,000 figure cited. The remaining $17,500 was attributable to four bonuses that he received during the five-year period from 2011-12 to 2015-16, which represented about 2.6% of the total base salary that he received during that period.

61. **Page 66: However the fiscal year 2015-16 budget the Office of the President presented to the regents included $36 million more in spending than the fiscal year 2014-16 budget. Furthermore, despite the directive the Office of the President's staff in Oakland and at the campuses grew from 1,577 full-time staff in 2012-13 – the fiscal year before the budget review announcement to 1,667 full-time staff in 2015-16.**
&
Page 71: Further, even though it has publicly stated that it has consolidated its own and the campuses' operations, both the Office of the President and campus administrative costs have increased.

Since the Great Recession of 2008, the number of UCOP staff performing administrative functions has grown in primarily strategic areas. UCOP made deliberate investments to expand its legal, investment, and technology management services to attain large savings for the entire UC system. In addition, in the effort to be more cost-effective (especially long-term), UC brought many core services in house, rather than extending contracts with outside service providers.

Areas of strategic growth include:

- Information Technology: Much of the growth here has been movement from external contractors to internal resources such as Apply UC.
- Office of the General Counsel: UCOP has expanded in-house legal services that were formerly performed by outside counsel as part of the effort to reduce overall spending and increase efficiency.
- UCPath: This new initiative replaces eleven separate antiquated systems with one platform. It allows UC to standardize and streamline human resource and payroll functions across all campuses while centralize other services.
- Chief Investment Officer (CIO): The CIO's office identified and acted on money-saving opportunities by bringing certain investment management functions in-house rather than continuing to rely on outside consultants and managers.
- Business Resources Center: Created to standardize business practices, this office provides support for UCOP. Since President Napolitano assumed leadership, increased automation has led to improvements in efficiency and, therefore, lower staffing levels.
- Risk Services: UCOP created Fiat Lux, a captive insurance company, to allow the University to self-insure and buy re-insurance directly in the market, eliminating the need to purchase coverage through insurance carriers at higher rates.
- Procurement Services: The P200 initiative has saved over $200M and has expanded in scope, with the next savings target set at $500M (SC500).
- ILTI Online Education: This program creates high quality online education across all campuses, in line with the State goal to expand digital instruction.

Together, these areas of strategic growth have grown 113% (+317.9 FTE) while the remaining administrative areas of UCOP fell by 8% (-68.9 FTE) between 2007-08 and 2015-16.

Since President Napolitano began leading the University in mid-2013, staff working in other administrative functions at UCOP have been cut by 5% (-39.2 FTE between 2013-14 and 2015-16).

The areas of strategic growth have relied predominantly on increasing technical and professional staff at UCOP.

Chapter 3

62. Page 71: In particular, we found that the Office of the President budgeted $210 million in discretionary money on system wide initiatives in fiscal year 2015-16, using funds that the campuses could have otherwise spent to support the university's core missions. Although many of these initiatives provide academic or public benefits, we question the Office of the President's decision to prioritize them over campus spending on students.
&
Page 72: The Office of the President has not prioritized its spending decisions to ensure that the university system is able to dedicate the maximum amount of funding possible to support its goals of access and affordability for California residents.
&
Page 74: We acknowledge many of these initiatives have value. However we question the Office of the President's decision to prioritize them over campus spending on students

UC operates in a dynamic environment where funds are expended in response to internal and external needs and demands. This is true for UCOP, which not only provides critical management of functions on behalf of the campuses, but also increasingly coordinates and funds key systemwide activities. UC has three primary missions: teaching, research, and public service. Funds are allocated in a manner consistent with those missions.

These one-time expenditures go towards some of the most important and topical initiatives undertaken by the University. In recent years, UCOP has funded activities that include:

- Support for undocumented students, including expanded financial, legal and student services
- Systemwide initiatives that diversify UC's undergraduate, graduate and faculty populations and provide them continual support, i.e. partnerships with Historically Black Colleges and Universities
- Programs that enhance student opportunity and experience, including the President's Postdoctoral Fellowship Program as well as the Public Service Fellowships for law students and other students taking advantage of UC's Sacramento and Washington, DC centers
- Investments in UC's transfer infrastructure, further simplifying and streamlining the transfer process to UC for California Community College students
- The Carbon Neutrality Initiative and associated investments in climate science research systemwide
- Campus-driven programs such as start-up funds for UC Merced to recruit top-notch academic staff, support for UC Riverside's medical school expansion, and establishment of Blum centers for Developing Economies on several campuses

- The Global Food Initiative and funding vital resources that address food security issues on the campuses
- Innovation and entrepreneurship activities, including a centralized investment fund to catalyze innovation and award programs to stimulate research in strategic areas

Furthermore, CSA's perspective fails to acknowledge that UC is a system of individual campuses that benefit from accomplishing shared objectives.

63. Table 11. The Office of the President does not Consistently Track Spending on Systemwide Initiatives

UCOP rejects this assertion. This table includes a significant amount of restricted funding that is either multi-year, or carried over from year to year in order to satisfy multi-year commitments to campuses and third parties. This is true for Breast Cancer Research Program funds, HIV/AIDS research funds and the Los Alamos National Laboratory/Lawrence Livermore National Laboratory Research funds. The table also represents a mix of programs that are housed and overseen directly by UCOP (including the President's Postdoctoral Fellows or the Historically Black Colleges and Universities Initiative), and those that are housed outside of UCOP but are included in UCOP's budget, such as the Education Abroad Program.

64. Page 74: According to the *Budget for Current Operations*, the costs related to the central and administrative services represent about 2.3% of the university's overall budget.

This statement is not accurate. The summary of the UCOP budget within the report (page 150) states that "the total central budget represents 2.3% of the overall University of California budget." This refers to the entire UCOP budget, both the Central and Administrative Services portion and the Systemwide Academic and Public Service Programs. The entire budget represents 2.3% of the University's overall budget. The costs related to the central and administrative services at UCOP represent only about 1% of the University's overall budget.

65. Page 74: However, our analysis demonstrates that the Office of the President's claim that it spent only about $314 million in fiscal year 2015-16 to administer the university is inaccurate because its administrative budget did not always account for administrative activities connected to systemwide initiatives.

CSA has not provided any evidence to support this assertion.

66. Page 77: Considering that the Office of the President acknowledged the building had been underutilized since 2003, the decision to continue to invest campus funds on Casa de California is questionable.

UC takes enormous pride in its longstanding relationship and work with Mexico. Casa de California (Casa) serves as a tangible representation of that relationship. UCOP does not contest that Casa was underutilized in the past, but rejects the idea that the solution would be to disinvest. Instead, catalyzed by the President's UC Mexico Initiative, UC advanced its efforts to collaborate with Mexico and better utilize Casa de California. UCOP also recognizes the significant support it has received from key State legislators and the Latino Caucus in its engagement of Mexico at large and for Casa de California specifically.

67. **Page 81: Our analysis found that over four years, the Office of the President spent an average of 69 percent of its total expenditures on administrative costs while campuses consistently spent 14 percent of their expenditures on administrative functions.**
&
Page 81: The expenditure data also show that although campus administrative costs have increased at the same rate as their nonadministrative costs, the Office of the President's administrative costs have escalated, while nonadministrative expenditures have dropped.

This statement does not account for the different functions of the Office of the President and the campuses. By design, UCOP seeks to alleviate administrative burdens and responsibilities on the campuses. As such, a higher average rate of administrative costs and expenditures are expected at UCOP, with non-administrative priorities residing with the campuses.

68. **Page 82: Our review of budget and staffing data for these institutions indicates that for fiscal year 2015-16 the Office of the President's $655 million disclosed budget and 1,670 staff exceeded the cost of central administration for these institutions. The Office of the President stated that it may spend more on administration than other institutions in part because it provides services to its campuses and employees that other universities do not provide, such as retirement management.**

This statement does not provide a sufficiently robust picture of UCOP's programs and services. It is an indisputable fact that UCOP manages many more programs than other institutions: centralized admissions, procurement, medical center procurement, tuition and financial aid policy, faculty salary policies, as well as the largest retirement plan in the State other than CalPERS – and, of course, the systemwide initiatives identified in this report. The draft audit report implies that because other institutions' central offices do so with less funding, UC's should be able to as well – while failing to acknowledge the greatly expanded scope of services UCOP provides and the subsequent benefits to the campuses and to the entire system as a whole.

69. Table 14

Reference: Fiscal Year 2012-13 Office of the President Budget

Statement: The Office of the President has developed a rigorous and transparent budget that fully reflects the complexities of the central administration's structure and funding mechanisms.

CSA Assessment: This budget does not present all the Office of the President's revenue sources, show spending from its undisclosed budget, or describe the purpose of its units.

UCOP Response: UCOP presents the UCOP budgeted revenues to the Regents by fund source (restricted and unrestricted), including the amounts and calculation of the campus assessment. All total budgeted revenues are summarized at the level of detail appropriate for the Regent's review.

As part of the continuing improvement to the budget process, in subsequent budget years, the "Background" section of the UCOP Regent's budget presentation was expanded to include discussion and details key programs and their related funding/revenue (see FY15/16 items F5 and F6).

All UCOP actual expenditures are made from approved and budgeted funds. A small percentage of actual unrestricted expenditures (3% of total budget in FY12/13) were made through the carry-forward budget (referred to in the draft report as the "undisclosed budget"). The carry-forward budget's funding results from prior-year savings from Regents' approved budgets. Carry-forward budget funding is used for programs with systemwide benefits such as academic programs, student support and UCOP-sponsored technology improvements, which are reported to the Regents.

The purpose of the units or divisions at UCOP is to improve organizational management, accountability and efficiency across the UC system. The structure and purpose of UCOP was presented to the Regents when UCOP began bringing its budget for Regents approval, in May 2007. *Reference item F3 in the Committee on Finance meeting of May 17, 2007.*

Statement: Comprehensive: The Office of the President budget has reconciled funding into one consolidated budget… including ongoing funding previously in the undisclosed budget.

CSA Assessment: The Office of the President did not present $80 million dollars in expenditures from its undisclosed budget to the regents.

UCOP Response: The carry-forward budget total of $80M was comprised of $62M in restricted funds and $18M in unrestricted funds. The carry-forward budget's funding results from prior-year savings from Regents' approved budgets. Carry-forward budget funding is

used for programs with systemwide benefits, such as academic programs, student support and UCOP-sponsored technology improvements, which are discussed with the Regents.

Items that were deemed annual recurring expenses were reclassified as permanent and were consolidated into the permanent budget for consistency.

Statement: Rigor: New reporting and budget development systems at the Office of the President provide comprehensive oversight over department budgets.

CSA Assessment: We determined during this fiscal year the Office of the President could only demonstrate approval for 2 percent of the $37 million in undisclosed budget expenditures that we tested.

UCOP Response: The Budget Development System, in its first year of use, introduced significant improvements to controls, reporting, budget management and approval workflows. The implementation of the system and associated process changes have increased reporting and tracking mechanisms on a trajectory towards continual improvements in these areas. Without additional information that supports CSA's assessment, UC is unable to provide additional detail on our system's efficacy.

Reference: Regents Minutes from 2012-13 Office of the President Budget Presentation

Statement: The Chief Financial Officer stated that the Office of the President is no longer funded using state money.

CSA Assessment: Although the Office of the President no longer directly levies the State General Fund, the campuses used $79 million in fiscal year 2012-13 from their State General Fund appropriations to pay for the Office of the President's campus assessment. State General Funds constituted almost one-third of the total campus assessment amount.

UCOP Response: Prior to the institution of funding streams, UCOP was funded in part directly from State General Funds. The Office of the President does not direct the campuses on which sources of funding to use to pay the assessment. The Systemwide Budget Manual states: "Campuses are permitted to use any fund source or combination of fund sources not otherwise legally restricted to cover their share of the annual assessment." Furthermore, the report does not acknowledge the possibility that the Chief Financial Officer was conveying that UCOP was not receiving a direct State allocation. On numerous occasions, the CFO confirmed to CSA this was the intent of his statement; the report fails to acknowledge this.

Reference: Regents Minutes from 2013-14 Office of the President Budget Presentation

Statement: The Office of the President plans to engage in multi-year budgeting so that campuses can be advised of the possible impact on their budgets.

CSA Assessment: The Office of the President has yet to develop multi-year budgets.

UCOP Response: In past years, the Office of the President has, at times, asked divisions to prepare multi-year projections. However, because of the considerable fiscal uncertainty in recent years, developing multi-year budgets has been difficult. However, the development of this process remains a key priority.

Reference: Fiscal Year 2014-15 Office of the President Budget

Statement: The President directed her staff to reduce travel costs by 10 percent.

CSA Assessment: The Office of the President's budget data shows that its disclosed budget included an estimated 21 percent increase for meetings, travel, and other related costs.

UCOP Response: Overall, actual spending outside of UCPath project-related travel decreased over 9% between FY13-14 and FY15-16.

Statement: A new process for approving the use of consultants was expected to lower the amount of funding spent for this purpose.

CSA Assessment: The Office of the President's budget data shows that its disclosed budget included an estimated 2.5 percent increase for consultant costs.

UCOP Response: The new process for evaluating and approving any consultant spend over $20K was implemented starting 2014. There was not an expectation that the spending in this category would be reduced right away; rather, UCOP anticipated that these new procedures would reduce the spending over time, ensure it was directly in line with its critical initiatives, and validate the work done by consultants that could not otherwise be performed by existing UCOP staff. The increase noted in that year was mainly due to the consultants hired to work on the UCPath project, while other areas held flat or decreased in consultant spending.

Reference: Regents Minutes from 2014-15 Office of the President Budget Presentation

Statement: The Office of the President considered which functions should be centralized and which should remain at the campuses.

CSA Assessment: The Office of the President is unable to demonstrate that any services were centralized as result of this process.

UCOP Response: The aforementioned statement was part of a larger statement from the 2014-2015 Office of the President Budget Presentation. The full statement from the minutes is as follows: "Mr. Brostrom noted that the effort this year to maintain the UCOP unrestricted fund budget at a flat level was a springboard for a broader assessment of UCOP, for considering which functions should be centralized and which left on the campuses. Following the departure of former Chief Financial Officer Taylor, UCOP is considering realignment and possible consolidation of certain offices." In that full context, it is clear that UCOP has demonstrated both centralization of key services, and realignment and consolidation of certain offices. Since that time, UCOP has increased centralization of HR and Payroll functions through the roll-out of our UCPath system. Additionally, UC has seen increased centralization in our Procurement department as evidenced by the creation of strategic sourcing centers of excellence in Life Sciences, IT, Professional Services, and MRO commodities. UCOP has also followed through on realignment and centralization of certain offices. UCOP undertook an elaborate "assessment" of both the CFO/COO structure and systemwide vs. campus activities, which many campuses participated in. The result was that the CFO and COO divisions went through a significant reorganization that eliminated multiple SMG positions. Additionally, multiple groups were consolidated into one OP Operations Department; capital markets finance and capital programs were consolidated into capital asset strategies and finance; and banking and treasury were consolidated into the OCIO division. It is clear that the CFO's statement was factually correct.

Statement: In response to Governor Brown's request for a document analyzing all elements of the Office of the President, both historically and at present, the Chief Financial Officer stated that many documents were available.

CSA Assessment: The Office of the President never provided the office of the Governor with such a document, but stated that it had many communications with the Governor's Office.

UCOP Response: The Chief Financial Officer stated that many documents were available and this remains true to this day. Our website provides a multitude of reports including our budget plan, organizational structures for the divisions and departments at UCOP, and others. Any member of the Governor's Office, as well as the general public, can access these documents at any time. The CFO's comment was not a commitment to send documents, but rather a statement about the availability of such documents online. Furthermore, the Office of the President has had many communications with the Governor's Office, and the CFO meets frequently with Director of Finance Michael Cohen in addition to other individuals from the Department of Finance. Additionally, after the Regents meeting, UCOP entered into a months-long work effort with the President, Director of Finance, and many members of his team looking at the cost structure of the University (Committee of Two process). This involved several meetings, which lasted several hours each, as well as extensive review of documents, both for UCOP and for campuses.

Statement: In response to a question from Governor Brown, the Chief Financial Officer stated that a great deal of the Office of the President's budget flows through to the campuses, and that its actual administrative functions account for $90 million of the budget.

CSA Assessment: After subtracting all of the funds that flowed through to campuses, the Office of the President's central and administrative budget was $279 million.

UCOP Response: The UCOP budget can be divided into three large buckets: one representing traditionally administrative functions; one related to central services provided for all campuses such as benefits, retirement plan management, legal services, etc.; and one for systemwide academic and public service programs and initiatives. The CFO's statement was related to just that portion of the budget that is primarily administrative in nature.

Statement: A regent-designate asked about funding for UCPath and why it was not listed on the budget shown to the regents. The Chief Financial Officer responded by saying that all of UCPath's costs to date were being capitalized and that once UCPath was operational, its costs would appear on the Office of the President's budget in the next fiscal year.

CSA Assessment: Budget data for fiscal years 2013-14 and 2014-15 show that the Office of the President spent $14.9 million and $13.7 million respectively for UCPath's operational costs.

UCOP Response: The expenses associated with the UCPath project design and build-out have been and will be capitalized until the system is implemented and operational. Outside of those expenses, funds have been budgeted in the operating budget for the UCPath Center operations since fiscal year 2013-14.

Reference: Fiscal Year 2015-16 Office of the President Budget

Statement: The Office of the President characterized a $13.4 million budget increase as a cost of living adjustment for its employees and stated that it was only the fourth increase in the last eight years.

CSA Assessment: The budget increase for staff salaries was actually a three percent across-the-board increase. The Office of the President leadership determined the amount rather than using a cost of living metric. The Office of the President also gave 3 percent salary increases in fiscal years 2011-12, 2013-14, and 2014-15 that were not tied to a cost-of-living adjustment.

UCOP Response: This has been clarified in CSA discussions with the Chief Operating Officer and the Deputy Chief of Staff. Response from the COO: *"The description of that increase as a COLA is an error. Both by design and in its implementation, it was an across-the-board increase. You will note that a COLA is tied to a certain metric, but this was a level determined by leadership and as such was an across the board increase."*

Reference: Regents Minutes from 2015-16 Office of the President Budget Presentation

Statement: Monies received from campus assessments would not affect enrollment.

CSA Assessment: Since campuses can choose to pay the campus assessment using State General Funds, tuition and fees, it is possible that the amount of the campus assessment affects enrollment.

UCOP Response: The aforementioned statement was part of a larger statement from the 2015-16 Office of the President Budget Presentation. The full statement from the minutes is as follows: "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." The 2015-16 assessment increase was 3.5% for a total of $10M systemwide. When reviewed at the campus level, it is clear that such a miniscule change in the budget would not impact enrollment levels. The auditor's reference to Santa Cruz, whose assessment increased by just under $87K, demonstrates this fact as the $87K increase represents only 0.01% of their total 2015-16 operating budget. Between 2014-15 and 2015-16, UCSC revenues increased by $40 million and expenditures increased by just under $25 million, with the assessment representing only .3% of this increase; within this context, it is improbable that the campus assessment affected enrollment decisions. As stated in public documents frequently throughout the year, the University's goal is to enroll as many eligible California residents as the State is able to fund – and there is no connection between enrollment and the assessment.

70. Page 84: When we asked the Office of the President how it determined which changes to share with the regents, the chief operating officer stated that the Office of the President only shares what it considers to be strategic budget changes and that it does not have a dollar threshold for when it must share information with the regents.

This is not an accurate reflection of the discussion as it occurred, nor did the individual in question, the Chief Operating Officer, receive documentation to validate this assertion as part of the audit process. This is in violation of CSA's standard auditing practices, which require documented support for all content included in the audit report. What the report neglected to include was her statement that UCOP shares material changes as well as those

things that are matters of strategic importance. UCOP also has concerns about the use of the word "only," which is untrue, as UCOP shares additional information when helpful and productive.

71. Page 85: The Office of the President Inappropriately Interfered With Our Audit and Limited Our Ability to Provide Complete Information to the Legislature and Public

During the course of the audit, members of the CSA audit team submitted two surveys to each of the campuses. One survey was 52 pages and the other was 6 pages. These surveys were sent to various individuals at the campuses, without CSA soliciting any guidance about who on the campuses was knowledgeable about a particular issue or best-positioned to respond on behalf of the respective campus. The coordinating processes facilitated by UCOP that followed were designed to get the auditors accurate information and ensure that the information they received was from the individual best-positioned to respond to a particular issue on behalf of the given campus.

72. Page 89: The Office of the President Delayed Our Access to Expenditure Approval Documents Related to Its Undisclosed Budget and Failed to Provide Us All of the Information We Requested

Over the course of this audit, UCOP staff expended more than 3,600 hours meeting with CSA representatives or preparing responses to their requests and questions. This included at least 250 information requests made over a 7 month period, with many of these involving a significant number of sub-requests. One such request contained 225 sub-requests or requests for additional information. It should also be noted that most of these requests were addressed to a small number of staff members. The volume and process by which the requests were made severely impacted UCOP staff's ability to perform their University work and had an adverse impact on UCOP's operations.

With specific regard to the approval documents referenced, the draft report fails to identify that the delays associated with their request to have unfettered access to an archive of material outside the scope of CSA's audit included 1) all archived documentation from the past four UC presidents, 2) privileged legal advice memos and documentation, 3) confidential and sensitive personnel information, and 4) correspondence with a range of elected officials. Any delay associated with UCOP's response was related to efforts to coordinate with CSA's legal counsel to identify the material within this broader archive that was needed for the audit, while limiting unnecessary risks associated with providing unfettered access to a massive set of confidential, sensitive, and privileged materials, the vast majority of which were well outside of the scope of CSA's audit.

Additional Comments

CALIFORNIA STATE AUDITOR'S COMMENTS ON "ATTACHMENT 2" FROM THE UNIVERSITY OF CALIFORNIA OFFICE OF THE PRESIDENT

The Office of the President's 34-page Attachment 2 is demonstrative of the barriers we faced throughout the course of this audit. Ultimately, Attachment 2 contained no additional information that would cause us to change the conclusions reached in our report. Rather, the Office of the President goes to great lengths to describe its dissatisfaction with the context we included surrounding the conclusions and the underlying philosophy related to transparency and accountability upon which we based those conclusions. As a result, we are choosing not to comment on each of the 72 points that the Office of the President included in Attachment 2 because doing so would not ultimately change the overarching conclusion that we convey in this report: that the Office of the President needs to better serve its stakeholders by making decisions in a transparent and accountable manner.

Moreover, we are disappointed by the Office of the President's approach to responding to the draft report and believe its actions further demonstrate its unwillingness to cooperate with us throughout this audit. Specifically, we discussed our findings with the appropriate staff of the Office of the President throughout our fieldwork. Moreover, between January and March we met with Office of the President executive management four times to share our findings and conclusions and obtain their perspective. In addition, we provided the Office of the President this draft report during our customary five business day review period and encouraged its staff to contact us regarding any concerns it had about the report's contents. Despite our repeated attempts to contact the Office of the President during this five-day review period, it chose to provide its feedback regarding the report via Attachment 2, rather than speaking to us directly. Nonetheless, based on our review of Attachment 2, we made minor changes to the report that we believe were warranted.

Additionally, we would like to provide clarity on the following general areas of Attachment 2:

- The Office of the President continually asserts that its undisclosed budget is actually a carryforward budget generated from temporary savings; however, these statements are inaccurate and misleading. Specifically, as we state on page 25, the Office of the President's documentation demonstrated that carryforward expenditures only represented 6 to 22 percent of the total undisclosed discretionary budget from fiscal

years 2012–13 through 2015–16. The remaining funds in the undisclosed budget included restricted funds, one-time expenditures, and unanticipated costs funded by cumulative undisclosed reserves. Moreover, the undisclosed budget does not represent temporary savings as much as it represents chronically inflated budgets that shifted spending outside of the regents', the Legislature's, and the public's purview.

- The Office of the President asserts in several places in Attachment 2 that we violated our "standard auditing practices, which require documented support for all content included in the audit report." These assertions are untrue as we do have documented support for all of the content included in the report. Certain comments that Attachment 2 highlights were made at meetings at which nearly 30 attendees—most of whom were Office of the President staff—were present. Documenting statements made at large meetings is a standard practice and satisfies auditing standards.

- Item 71 of Attachment 2 implies that the Office of the President did nothing more than coordinate survey responses among the campuses, which is not the case. Contrary to the Office of the President's assertion that we failed to send our survey to those knowledgeable about specific subject areas, we determined that the campus audit coordinator was best positioned to facilitate the response to one survey and the campus chief financial officer, or an equivalent position, was best suited to respond to the other survey. After we sent the survey, the Office of the President's systemwide deputy audit officer contacted us and followed-up on some technical questions posed by multiple campuses. This level of coordination was appropriate and we took no issue with it.

  However, *four days before the survey was due*, the deputy chief of staff to the president organized a conference call with all of the campuses to discuss the survey. Subsequently, the emails he provided to us show campuses sent him completed surveys which he reviewed to determine, in part, whether the campus responses were within the scope of our audit. However, as we discuss on page 86, the surveys that campuses sent to the deputy chief of staff were much different than the final surveys submitted to us. As is clearly shown in Table 15 on page 87, significant changes and deletions were made to the original surveys sent to the deputy chief of staff for the Office of the President. The purpose of these surveys was to assess potential redundancies between the Office of the President and its campuses as well as to obtain the campuses' perspectives regarding their annual assessment. However, because of the Office of the President's involvement we could not complete a

critical objective or answer important questions the Legislature has about the cost and duplication of activities at the Office of the President.

- The second paragraph of item 72 discusses the Office of the President delaying us access to the expenditure records that we needed. We explain the circumstances surrounding our request in detail beginning on page 88 of the report. The Joint Legislative Audit Committee asked us to assess the methods that the Office of the President uses to determine its budget and staffing levels and to assess any other issues that are significant to the audit. The records that we requested were not only necessary to address these objectives, but also to ensure that we selected a sample from a complete set of records. Regardless, the State Auditor's enabling statute gives us access *upon request* to all the records of any publicly created entity for an audit. Nothing in the statute allows an entity being audited to prevent or delay access because the records are privileged or confidential or because the entity claims that the records are outside the scope of the audit. The refusal of the Office of the President's staff to provide access to these records for over a month prompted our legal staff to contact the Office of the President's legal staff. Over the course of seven days, our legal staff explained our access rights orally and in writing until the Office of the President's legal staff finally agreed to provide access as required by law. Moreover, the Office of the President's inability to distinguish between standard budget expenditure approval documents and confidential privileged information is its own shortcoming.