The Regents of the University of California

COMMITTEE ON FINANCE
May 17, 2000

The Committee on Finance met on the above date at Covel Commons, Los Angeles campus.

Members present: Regents Atkinson, Bagley, Connerly, Davies, Hopkinson, Montoya, Pannor, Parsky, and Preuss; Advisory member Miura

In attendance: Regents Bustamante, Khachigian, Kozberg, Lansing, Moores, Sayles, Taylor, and Vining, Regents-designate Fong and Kohn, Faculty Representatives Coleman and Cowan, Secretary Trivette, General Counsel Holst, Provost King, Senior Vice President Kennedy, Vice Presidents Broome, Darling, Gomes, and Gurtner, Chancellors Berdahl, Bishop, Carnesale, Cicerone, Dynes, Greenwood, Orbach, Tomlinson-Keasey, Vanderhoef, and Yang, and Recording Secretary Nietfeld

The meeting convened at 11:16 a.m. with Committee Vice Chair Preuss presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETINGS**

Upon motion duly made and seconded, the minutes of the meetings of January 19-20, 2000 were approved.

2. **PARTNERSHIP FOR PERFORMANCE: ASSESSING THE EFFECTIVENESS OF THE UNIVERSITY=S ADMINISTRATIVE OPERATIONS**

Senior Vice President Kennedy recalled that in the early 1990s a group of University administrators produced a report entitled ASustaining Excellence in the 21st Century.@ This report drew attention to the need for a University of California framework to assess the performance of administrative operations. Because there were no models to emulate in higher education, the University formed a relationship with IBM. This relationship was designed to adapt leading private-sector models to the University and to introduce a performance-measurement approach throughout the University. It was recognized that a performance architecture would need to address two important components: diagnostics that would lead to improved operations and control mechanisms to help manage risk and exposure.

The Partnership for Performance is a partnership between the University of California campuses, the Office of the President, and the three national laboratories managed by the University of California. Its objective is to foster collaboration on organizational performance measurement within business administration and operations, as follows:

$ Develop departmental goals and objectives for improving the performance of departments and units throughout the University.

$ Improve decision-making at both the department and institutional level through the systematic collection and analysis of performance data.

$ Measure performance from multiple perspectives to ensure a balanced view of progress in achieving goals.

$ Incorporate two critical elements of performance measurement and management:tracking performance over time against goals and comparing UC campus performance to other UC institutions, higher education cohort groups, and organizations outside higher education.

$ Entrust ownership of the measurement activity to business unit managers and recognize the need for flexibility in addressing different campus priorities.

$ Improve communication and collaboration among departments with similar missions within and among UC institutions.

$ Focus on the critical indicators of performance for each business area, with an emphasis on controlling the time and costs associated with collecting the supporting data.

$ Contribute to a culture of accountability throughout the University.

$ Encourage UC administrative leadership to create a climate that encourages results supported by performance measurement data.

Senior managers from UC business administration departments are collaborating on the development of systemwide goals and performance measures for their business areas. They define metrics, set targets, gather data, and analyze results. Results are compared from campus to campus, and when available, performance data from other institutions are included to broaden the field of analysis. The ultimate objective is to identify opportunities to improve administrative organizations= delivery of critical services to the campuses.

Ms. Kristine Hafner, Director of Business Initiatives for the Office of the President, described the Abalanced scorecard,@ a model that is widely used in the private and public sectors for tracking the performance of organizational units. The balanced scorecard links performance measures to goals and assesses performance from the perspectives of customer satisfaction, financial indicators, business process metrics, and workplace climate gauges. There is significant momentum at the campuses to incorporate organizational performance measurement into campus administrative operations. Increasingly, the performance measures developed by Universitywide Partnership for Performance teams are used as input to campus business area measurement efforts. The balanced scorecard is being adopted at several campuses to communicate direction and to identify and track opportunities for business improvement. Ms. Hafner briefly described some of the objectives that had been reached in the area of purchasing, including the ability to leverage the University=s purchasing power across the system, to contain costs, and to increase the quality of goods and services. With respect to the area of human resources, the administration has learned that employee turnover is accelerating on many campuses. These data help the University to focus on its recruitment and retention efforts. Finally, Ms. Hafner reported that the environmental health and safety directors, working within the context of the Partnership for Performance, had been successful in reducing the cost of the disposal of hazardous waste by 63 percent, or $3 million in savings.

Executive Vice Chancellor Vani of Business and Administrative Services discussed how the Santa Cruz campus is incorporating performance measurement into the divisional resource planning and operational improvement process. Critical success factors and performance measures are identified for all key products and services delivered by BAS departments. The division initiated a customer satisfaction survey that will be administered regularly for all BAS departments, and the results of the survey have been posted on the division=s web page. Attention has been paid by the division to streamlining business practices. Mr. Vani reported that the Santa Cruz campus is an active participant on all of the systemwide teams, and results from these performance teams are widely disseminated on the campus. The balanced scoreboard facilitates communication between the division and the faculty with respect to budgeting and other business issues. Mr. Vani reported that Vice Chancellor Relyea of the San Diego campus would report at the July meeting on the Anew business architecture,@ which examines how the business sector of the University will support the missions of teaching and research over the coming decade using the following four objectives: to create and sustain a positive environment, to use resources strategically, to follow best practices, and to contain costs. From these objectives, six principles were developed:

$ to challenge current procedures and processes

$ to deploy e-commerce and enabling technology

$ to invest in the development of staff and managers

$ to establish a UC business portal as a focal point for ease of use

$ to enhance financial management and reporting

$ to incorporate performance metrics and controls.

President Atkinson noted that the new business architecture was an impressive development that had been created by a members of the University administration working with representatives from private-sector companies such as Cisco Systems, IBM, and Gateway

Computers. He stressed the importance of the University of California playing a leadership role in the use of computers and the world wide web.

3. **REVIEW OF THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN**

Senior Vice President Kennedy recalled that the University of California Retirement Plan (UCRP or Plan) is a defined benefit plan established and maintained under Internal Revenue Code '401(a). University of California employees need five years of service credit to qualify for Plan benefits that are determined by defined formulas that vary according to the type of benefit eventually paid rather than by the contributions made to the Plan. For eligible UC faculty and staff, the Plan provides several types of benefits: lifetime retirement income, disability protection, and a variety of death and survivor benefits. In addition, upon retirement, eligible members may elect a lump sum payment equal to the value of their accrued retirement benefit in lieu of lifetime retirement income. UCRP has not required contributions from either the employer or the employee since 1990.

Each year, the consulting actuary performs a Plan valuation that determines the normal cost, accrued liability, asset valuation, and related present values for UCRP and presents a report to the Board. A major goal has been to keep UCRP as a non-contributory plan. The Plan is a valuable component of the total compensation and benefits package provided to UC faculty and staff. However, the University must now evaluate whether there are changes that could be made to compare better with those entities with whom UC competes for the best talent.

Associate Vice President Boyette continued the presentation, noting that the recruitment and retention of qualified faculty and staff have become a primary focus for the University, which faces the tightest labor market in thirty years. It is crucial to use every possible advantage to attract and retain talented faculty and staff. The administration is re-evaluating the benefits that the University offers in light of the expected 43 percent increase in the student population over the next ten years and the corresponding need to recruit additional new faculty and staff to support the projected growth.

In a defined benefit plan like UCRP, retirement benefits are determined based on a formula that increases the benefit with age and length of service. If a member terminates employment before eligibility for retirement at age fifty, there is no benefit available for the employee to take with him or her to another employer. While the member may draw a pension when he or she reaches age fifty, there is at least a perceived loss because the vast majority of other employers have portable benefits.

Most of the University=s comparator universities and most private employers offer defined contribution plans, either instead of a defined benefit pension plan or as a choice for the individual in lieu of a pension. In a defined contribution plan, the benefits payable are based solely on employee and employer contributions plus earnings. Contributions from a defined contribution plan are portable, which means that employees can take all contributions and earnings with them if they move to another employer.

Ms. Boyette explained that, while the retirement plan has served UC well in a time when individuals had long careers with a single employer, the current design alone will not meet the portability demands of today's workforce and may have an effect on the University's ability to recruit qualified faculty and staff. Human Resources and Benefits in the Office of the President is exploring various alternatives that would address retirement benefit portability while maintaining and perhaps improving the current benefit formula for existing faculty and staff whom UC cannot afford to lose in this time of projected growth. One alternative may be to add an account balance feature to the retirement plan. This feature would provide some of the same advantages of a defined contribution plan while making benefits more portable, especially for new faculty and staff, by offering a lump sum payment at the time of termination prior to reaching age fifty. Under this type of benefit, there is an account comprised of contributions from the existing Defined Benefit Plan Trust Fund, plus interest. It is possible that such a feature could be added as an alternative to the current defined benefit formula. Human Resources is evaluating whether the University should provide vesting or entitlement to benefits sooner than five years in order to be more competitive. Many employers offer immediate vesting.

In addition to looking at recruitment issues, the administration is evaluating changes that may be necessary to retain the current workforce. Effective January 1, 2000, the California Public Employees' Retirement System (PERS) implemented a number of benefit enhancements for some of its members. These enhancements included changes in the age factors used in the retirement income formula. The effect of the changes was to increase benefits for PERS members fifty and older. Traditionally, UCRP benefits have paralleled benefits provided to PERS members. Until the recent PERS benefit enhancements, only a few differences existed between the two retirement plans. In addition, UCRP has reciprocity with PERS, which enables UC employees to transfer their retirement benefits to PERS if they take jobs in PERS-covered agencies. The PERS benefit enhancements have prompted interest by UCRP Members for similar enhancements to the retirement plan age factors. Because these age factors increase with age, increasing them would provide an incentive for members to remain longer.

Ms. Boyette reported that UC employees are now postponing their retirements in anticipation of possible enhancements to the UCRP age factors. This is creating human resource issues related to workforce planning and renewal for the campuses and laboratories. If there are no legal restrictions, the administration will likely ask The Regents to consider making any proposed changes to the retirement plan effective January 1, 2000 to parallel the timing of the PERS changes and to avoid potential claims by employees who may have terminated during this period of evaluation. While the administration will not recommend making the same changes as PERS, it is likely that some changes will be proposed.

Ms. Boyette reported that, in addition to looking at more portable benefits and possible changes to the age factors to remain competitive with the PERS system, the administration is assessing the need to address the difference in benefits currently provided to individuals who are married versus benefits provided to those who are not married. All potential changes are being evaluated based on their effect on the University's overall goals regarding recruitment, retention, and renewal of qualified faculty and staff, as well as their cost to the Plan. Discussions are under way with the relevant Academic Council committees, other interested constituent groups, the UCRS advisory board, and legal counsel. Further information on the results of the ongoing evaluation of UCRP and recommendations for action will be presented at future meetings.

Ms. Catherine Cole of Towers Perrin, the Consulting Actuary to the University of California Retirement Plan, presented some highlights of the upcoming actuarial valuation. The valuing of the Plan=s liabilities and the review of the assets takes place annually. An experience study which compares the University=s actual experience against assumptions is performed every three to five years. The annual actuarial valuation is based upon membership data and the plan provisions as of the valuation date. These data are used to project future liabilities and to ensure that adequate assets will be available to fund the Plan. The key assumptions used in formulating the actuarial valuation include the fact that current hires are expected to be in the Plan over fifty years, either earning or receiving benefits. The economic assumptions include the interest rate, the Consumer Price Index, and future salary increases. The demographic assumptions are those that affect post-employment mortality. The University=s retirement membership is attaining greater longevity. The valuation must also assume retirement rates for current employees in order to determine the funds needed.
The valuation of the Plan=s assets smoothes market volatility over a five-year period.

Ms. Cole presented a chart which provided the history of the Plan=s funded status from July 1, 1990 through July 1, 1999. In 1990, the Plan was funded at 139 percent; in the interim it dropped to as low as 107 percent in 1995. Due to outstanding performance over the past several years, the funded status of the Plan had increased to 145 percent by July 1, 1999.

Turning to membership data, Ms. Cole reported that the percentage increase in active and retired members remained constant in the mid-1990s but grew to 5.1 percent and 4.6 percent respectively in 1999. There is an expectation of continued increases in membership over the next ten years.

Contribution strategy studies are under way which forecast liabilities based upon such factors as membership growth, changes in plan provisions, and assumption changes. By comparing assets and liabilities over a long term, a range of results will provide the University with the ability to estimate contributions and the future funded status.

In response to a question from Regent Montoya regarding employee mobility, Ms. Boyette explained that this issue does not affect faculty members in the same way as it does other staff. Faculty who come to the University of California, however, are able to bring their previous retirement funds with them, and thus there has arisen the need to evaluate requests for more flexibility.

Senior Vice President Kennedy added that it is difficult for the University to recruit in the information technology arena because of the tremendous competition from Silicon Valley and internet companies. Many young people in this field would be interested in working for the University for the intellectual challenge, but they do not wish to pursue a life-long career. These potential workers would be more likely to come to the University if they knew that they could leave with a defined contribution program.

Regent Montoya stated that she had received several inquiries regarding any future early retirement incentive programs. Ms. Boyette reported that the changes which were implemented by PERS were intended to encourage people in the 50 to 57 age group to retire. This is the reason why it is unlikely that the administration will propose that similar changes be made with respect to UCRP. A balance must be found between remaining competitive in the marketplace while retaining valued employees.

Regent Hopkinson expressed concern about any action that might affect the zero contribution to the Plan. It was her understanding that PERS has a home mortgage program for all State employees that offers no down payment. She asked that the University pursue this option if her understanding of the program is accurate.

In response to a comment from Regent Moores, Associate Vice President Boyette pointed out that, because the University cannot compete with Silicon Valley in terms of salaries or stock options, it must pursue the option of a more mobile retirement plan.

Regent Moores asked what effect the adoption of a defined contribution plan might have on the Plan=s surplus. Ms. Cole responded that the intent would be that it have a minimal effect.

Regent Vining expressed concern that if short-term employees were able to leave University employment with a cash account, at some point long-term employees may need to resume making contributions to the Plan. Regent Taylor pointed out that this policy has not had a negative effect on PERS.

4. **REPORT OF NEW LITIGATION**

General Counsel Holst presented the **Report of New Litigation**. By this reference, the report is made a part of the official record of the meeting.

(For speakers= comments, see the minutes of the May 17, 2000 Committee of the Whole.)

The meeting adjourned at 12:15 p.m.

Attest:

Secretary