The Regents of the University of California

COMMITTEE ON FINANCE
March 17, 2004

The Committee on Finance met on the above date at UCSF–Laurel Heights, San Francisco.

Members present: Regents Connerly, Dynes, Hopkinson, Lozano, Montoya, Moores, Murray, Preuss, and Sayles; Advisory members Anderson, Novack, and Pitts

In attendance: Regents Blum, Bodine, Johnson, Kozberg, Marcus, O'Connell, and Seigler, Regent-designate Ornellas, Faculty Representative Blumenthal, Secretary Trivette, General Counsel Holst, Treasurer Russ, Provost King, Senior Vice Presidents Darling and Mullinix, Vice Presidents Doby, Drake, Gomes, and Hershman, Chancellors Bishop, Carnesale, Cicerone, Córdova, Greenwood, Tomlinson-Keasey, Vanderhoef, and Yang, Acting Chancellor Chandler, Executive Vice Chancellor Gray representing Chancellor Berdahl, and Recording Secretary Bryan

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

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

Upon motion duly made and seconded, the minutes of the meeting of January 14, 2004 were approved.

2. **UPDATE ON UNIVERSITY OF CALIFORNIA 2004-05 BUDGET**

Vice President Hershman recalled that in past years, at the November meeting The Regents had adopted a budget plan for the coming fiscal year that then formed the basis for budget negotiations with the Governor and the Legislature. In a departure from past practice, the 2004-05 budget plan for the University has not yet been approved because of the uncertainty that has existed related to the State's budget crisis. Instead, The Regents approved a set of principles to be used in negotiating the budget with the expectation that a budget plan would be approved once the Governor had submitted his own budget proposal. This action was further refined at the January meeting, when the Board supported budget priorities expressed in terms of both short- and long-term goals. Discussions are continuing with the Schwarzenegger administration related to the proposals presented in the Governor's Budget for 2004-05. The University is learning more about the administration's views and rationales for various proposals and hopes to have the benefit of further discussion before recommending specific action.

Vice President Hershman noted that the budget proposed by the Governor represents the fourth consecutive year in which the University has sustained major base budget reductions and endured underfunding for basic budget needs critical to maintaining quality. This increasing shortfall has severely challenged the ability of the University to maintain quality while preserving access for all eligible students wishing to attend. Salaries for faculty and staff have fallen seriously behind the market; it could take years to close the salary gaps that have been created. Core needs of the University are not being met, such as those for instructional equipment, instructional technology, libraries, and maintenance. Base budget cuts are far beyond the order of magnitude that could be resolved with mere belt tightening. The major support network for offering educational and research programs and performing necessary business functions has been seriously eroded. Students are paying more for less.

Discussions are under way with the Schwarzenegger Administration about a multi-year approach to funding the University in future years, focusing on levels of State funding, enrollment, and student fees. It is hoped that such a new agreement would put an end to further erosion of the University's resources and help the University address budgetary shortfalls in critical areas over the long term. It is anticipated that the new agreement will include funding principles intended to meet the basic budget needs of the University sufficient to fulfill the institution's missions under the Master Plan, as well as accountability principles intended to measure desirable outcomes of interest to the University and the State.

The budget proposed by the Governor includes significant student fee increases, along with suggestions for a long-term student fee policy for undergraduate and graduate academic students, proposes enrollment reductions, assigns further base budget reductions, and provides some increases to the budget due mostly to technical adjustments. Although the proposed budget reductions and student fee increases are of deep concern, the State's budget crisis requires that the University participate in the solution.

Student Fee Increases

The Governor has proposed a long-term student fee policy for the University of California and the California State University that calls for increases in student fees equivalent to the rise in California per capita personal income. In years in which the segments determine that fiscal circumstances require increases that exceed the rate of growth in per capita personal income, UC and CSU may determine that fee increases of up to 10 percent are necessary to provide sufficient funding for existing programs and to preserve quality.

The Governor proposes the following student fee increases for 2004-05:

- <u>Undergraduates</u>: a 10 percent increase in mandatory systemwide student fees, limiting the return to aid to 20 percent of new revenue. ($63.6 million State General Fund savings)

- Graduate Academics: a 40 percent increase in mandatory systemwide student fees, limiting the return to aid to 20 percent of new revenue. ($57.4 million State General Fund savings)

- Professional Schools: increases in the Fee for Selected Professional School Students sufficient to reduce the total State subsidy provided to these programs by 25 percent, allowing flexibility for the University to determine the actual fee increases for each school. The estimates of revenue generated assume no return to financial aid related to this increase. ($42.2 million State General Fund savings)

- Nonresidents: a 20 percent increase in nonresident tuition, with a return to aid of 20 percent of new revenue. ($32.6 million State General Fund Savings)

- Excess Units Fee: implementation of a new fee to be applied against credit units taken by resident undergraduate students that exceed a threshold of 10 percent above the minimum needed to graduate. Such credits would be charged at the full cost of instruction. ($9.3 million State General Fund savings)

These proposals, which are expected to generate $205 million in savings for the State, present several concerns for the University.

Long-Term Student Fee Policy. The University's principles adopted at the November 2003 meeting and further supported at the January 2004 meeting reaffirm the University's interest in developing a new long-term student fee policy. As stated in those principles, it would be the University's preference to have a fee policy accepted by both the University and the State government that would provide for annual increases in student fees consistent with an economic measure, such as per capita personal income; however, such a policy must be contingent upon the State's being able to provide adequate support for the University's basic needs. Consistent with the principles adopted by The Regents in January, the University would support a long-term student fee policy only if it included recognition of the need for adequate State support to maintain quality.

Undergraduate and Graduate Academic Student Fee Increases. Wide consultation within the University community makes it clear the 40 percent increase proposed for graduate academic students is of deep concern, given the need to continue to attract the very best graduate students from around the world. California has fallen seriously behind in meeting state workforce needs for managerial and professional workers in California's growing industries. If California universities continue to under-produce graduates to fill the growing number of professional and managerial jobs, there will be a substantial impact on California's economy and on job creation.

Leaders produced by UC graduate programs create jobs and opportunities for many other people, but compared to other states California falls in the lower third in terms of graduate students per resident aged 25-64 and per state resident with a bachelor's degree. The University has been striving in recent years to become more competitive in attracting top- quality graduate students to this state. The Regents established a Commission on the Growth and Support of Graduate Education to devise ways to improve support for graduate students. Unfortunately, the dramatic increase in fees proposed in the Governor's Budget would make it more difficult to develop the financial support packages necessary to attract these students; therefore, the University is considering alternatives to the graduate student fee increase proposed in the January budget. One alternative could be to increase undergraduate fees slightly more than proposed by the Governor in order to reduce the level of the graduate fee increase. Under such an alternative, undergraduate fees would be increased somewhere between 10 percent and 15 percent and graduate academic fees would increase by 20 percent to 25 percent. For example, if undergraduate fees were increased by 15 percent rather than the 10 percent proposed by the Governor, the increase for graduate academic fees could be lowered to 20 percent rather than the 40 percent proposed by the Governor. Undergraduate student fees would increase by $750, which is about $250 more than proposed by the administration, and graduate academic fees would increase by $1,050 rather than the proposed $2,088. This would enable the University to moderate the effect on graduate students.

If an alternative were adopted for 2004-05 that exceeds the 10 percent threshold the Governor wishes to establish in a new student fee policy, it would be the University's intention to increase undergraduate student fees less than 10 percent in each of the next two years, assuming that the State provides sufficient funds to support the University's basic budget needs and prevent further erosion of quality, so that the average over three years would be 10 percent per year, in keeping with the Governor's proposal. The benefit of further discussion in Sacramento and further analysis are needed before making a recommendation to the Board. In the meantime, students and their parents will be informed about the potential fee increases under consideration in the University.

Under the Governor's proposal, total undergraduate student fees, including mandatory systemwide fees and campus-based fees, would be about $1,400 below the average of the University's public comparison institutions. Fees for graduate students would be about $900 below the average. Excluding the University of Michigan, which charges extraordinarily high fees for graduate students, graduate academic fees would be about $500 higher than the other three public institutions.

Under the alternative 15 percent increase for undergraduates and 20 percent increase for graduate academic students, the total fees paid by undergraduate students would be more than $1,100 below the average of UC's public comparison institutions. Graduate academic student fees would be $1,900 below the average; however, if the University of Michigan were excluded from the average, the University's fees would be only about $500 less.

Concerns about total student costs have been raised at past meetings of the Board. In 2003-04, student fees represented 31 percent of the average total cost to undergraduate students, which is $17,814 in the current year and includes non-fee expenses such as room and board and mandatory books and supplies. In past years, the University's average cost of attendance has been above the average of its four public salary comparison institutions, largely due to the high cost of living in the areas in which UC campuses are located; however, when financial aid is taken into account, the University's average net cost of attendance for needy students falls to a level below the average of its comparison institutions.

Under the Governor's plan, it is estimated that the 2004-05 average total cost of attendance would be $19,123. Under the alternative to the Governor's plan currently under consideration, it is estimated that the 2004-05 average total cost of attendance would be $19,375. It is anticipated that, in terms of net cost, the University will continue to be below the average of its public comparison institutions under either the Governor's proposal or under the alternative fee proposal described above.

Fee for Selected Professional School Students. The Governor's Budget assumes the University will develop a plan for achieving the $42.2 million in revenue expected from professional school fee increases. In order to achieve this revenue target, fees at each of the schools would need to increase by about $5,000; however, the University has been asked to exempt nursing from these increases and to implement smaller-than-average increases for students in the schools of medicine. In addition, a few of the schools probably could not sustain increases of $5,000 and still attract sufficient numbers of highly qualified students. To make up the deficit, fees at some schools may need to be increased higher than the average.

The Governor's proposal does not assume any return-to-aid from the increase in professional school fees. The schools are concerned about their ability to maintain the quality of their programs and to be competitive with other professional schools. This is particularly important if students will be paying significantly more to attend these schools. To address the academic quality and financial aid issues associated with this proposal, one alternative could be to delegate authority to the President to raise the fee at any of the professional schools by an additional amount not to exceed 10 percent of total systemwide fees paid by professional school students if it is determined the school must do so to provide sufficient financial aid and to maintain the quality of the academic program. Any fee increases approved under such authority would be reported to the Board. Under such a scenario, UC fees would be comparable to those charged in these disciplines at other public comparison institutions.

While considering market conditions and the need to remain competitive in attracting students, the University is working on a plan for achieving the Governor's proposed revenue target. Proposals for fee increases for each professional degree program will be presented to the Board for approval, along with other fee actions needed for 2004-05, later in the spring.

As part of the effort to consider options for the future with respect to these professional programs, each campus will be asked to develop a long-term plan for professional fees over the next five years that includes consideration of the following factors: average fees at other public comparison institutions, market factors, the need to preserve and enhance the quality of the professional programs, the State's need for more graduates in a particular discipline, and financial aid requirements of professional school students.

Nonresident Tuition. The Governor has proposed a 20 percent increase in nonresident tuition. The University has already witnessed a 22 percent decline in the number of undergraduate nonresidents applying to the University in the last two years. It should be noted that these students pay significantly more than the cost of their education. In addition to nonresident tuition, students pay mandatory systemwide student fees and campus-based fees.

Excess Units Fee. The Governor has proposed establishment of a policy to charge the full cost of instruction for excess units that exceed a specified threshold. The President will develop a plan for phasing in the policy over a four-year period, beginning in 2004-05, as requested by the Governor. Action to approve this plan will be brought before the Board along with other fee actions later in the spring.

It is estimated that a total of 555 FTE students could be affected by implementation of such a policy. Therefore, the University estimates that $4.5 million is the most revenue that can be generated from this fee. Assuming a four-year phase-in of such a policy, only $1.1 million could be generated in the budget year, which is $8.2 million less than the amount proposed in the Governor's Budget. The University is requesting that the budget be adjusted to reflect this change.

Financial Aid. As the total cost of attending UC continues to increase, the resources available for needy students to help cover these costs are eroding. The Governor's proposal calls for significant reductions to the amount of new student fee revenue that can be used for financial aid and proposes changes to the Cal Grant Program that will also affect financial aid for needy students. Compounding this problem is the fact that for the first time in ten years, Pell Grant awards will not increase. This combination of factors raises several concerns related to financial aid for both undergraduates and graduate academic students.

In order to address the issue of affordability for the neediest undergraduates, and consistent with the priorities supported by The Regents in January, the University intends to continue to provide grant aid to mitigate the impact of fee increases for those students with the most need. Because of the shortfalls in funding for financial aid anticipated for 2004-05, grant aid previously provided to needy middle-income students, who generally come from families with incomes of $60,000 to $90,000, will no longer be available. Also, it is expected that the student contribution from loan and work in 2004-05 could rise from $8,600 to about $9,600 for all needy undergraduates, depending on the fee increase that is ultimately approved.

The dramatic fee and nonresident tuition increases proposed for graduate students create a large financial liability for the University, due in part to the contractual obligation to offset the full amount of the fee increase for teaching assistants (TAs). As a matter of policy, the University also offsets fee increases for research assistants (RAs). Thus, the fee increases for eligible TAs and RAs, who comprise over half of graduate academic students, must be funded from University sources or through federal and private research grants, reducing the funds available for research.

Graduate students without TA or RA fee offsets will experience an erosion in their support packages unless fellowship support increases are provided to cover the large fee increase. As noted earlier, this is contrary to The Regents' priority for improving support packages for graduate students and weakens the University's ability to compete for talented students.

Addressing these challenges will require the University to make several decisions affecting student support which could vary considerably depending on the fee increases that are ultimately agreed upon. For example, the University will have to determine the appropriate allocation of available student aid between undergraduate and graduate students. Although higher fees and a reduced return-to-aid will have a negative impact for both undergraduate and graduate students, the effect of the Governor's proposal is far greater for graduate students. In order to address the challenges described above, the University could redirect a portion of the return-to-aid generated from undergraduate fees to provide additional graduate student support.

If an agreement can be reached on an alternative to the fee proposals in the Governor's Budget, there would be several mitigating factors to help address the financial aid challenges: (1) the University would be able to reduce the portion of the undergraduate return-to-aid funds that would need to be redirected to graduate support; (2) the cost to the University of providing TA and RA fee remission would be reduced; (3) the effect of the fee increase on graduate students' net stipend would be smaller; and (4) undergraduates' expected contribution from loan and work, though higher than 2003-04 levels, would be lower than under the Governor's budget.

For the long term, the University is concerned about limiting to 20 percent the return-to-aid generated from fee increases. The University will develop a justification for an appropriate level of return-to-aid for future years.

Enrollment Reductions

The Governor proposed removing funding for 3,200 FTE students in 2004-05, which is equivalent to a 10 percent reduction from the number of new freshmen budgeted in 2003-04. It is his proposal that these students participate in a dual admissions program under which they would be admitted to a specific University campus but would be asked to undertake their lower division work at a California community college. Upon successful completion of that work, they would attend the University for their upper-division work and receive a University of California degree. While this is a departure from the State's past policies of fully funding all eligible students wishing to attend the University, this proposal provides all eligible students with an assured path to a University of California degree.

Turning away eligible students is deeply regrettable; however, the budget principles supported by the Board in January call for enrollment levels to match resources provided. Consistent with that principle, campuses have been provided with revised enrollment targets that reflect the Governor's proposal. It is hoped that this is a one-time necessity and that the State's long-standing commitment to the Master Plan will be reaffirmed the following year. This proposal will save the State $24.8 million; however, because of the lower cost of educating undergraduate lower division students, actual savings to the University will be less.

As the Board has been informed at the last several meetings, UC enrollment currently exceeds by 12,000 students the planned enrollment levels for 2003-04 as established in 1999 for the decade. The enrollment actions proposed in the Governor's Budget will help the University get back on track with its original enrollment plan. Campuses are being asked to develop plans for the remainder of the decade to return to the level previously indicated in the University's 1999 enrollment plan for 2010-11, which will total nearly 217,000 FTE systemwide.

Preliminary studies conducted for the California Postsecondary Education Commission's eligibility study indicate that more than the top 12.5 percent of California high school graduating seniors are achieving eligibility. The study, which is due to be released in May, is likely to generate a wide public policy debate about eligibility and resources. The Governor's Budget also proposes an augmentation of $1.6 million to support counselors and the tracking of these students to help ensure their ultimate enrollment in the University of California.

Next Steps

As soon as the University has explored all alternatives with the Governor's office, the information will be submitted to the Regents, who will be asked to approve a budget plan for 2004-05 and student fee levels. The Legislature will begin budget hearings in early March that will continue through mid-May. The University has been informed that release of the Governor's May revision will probably remain as scheduled for mid-month. The budget Conference Committee generally begins its deliberations in early June. Once the budget is completed, the President will present to the Board an action item to approve a final budget plan for 2004-05.

Outline of Other Proposals from the 2004-05 Governor's Budget

Base Budget Reductions

Student-Faculty Ratio. The proposal would result in the budgeted student-faculty ratio's being increased to 20.7:1. Consistent with the action taken in 2003-04 and with the principles approved by The Regents in January, the University will regard this as an unallocated reduction. The Regents have declared that the student-faculty ratio is directly tied to quality and any further deterioration of quality must be avoided. It is critical that in addressing this reduction, campuses ensure that students get the classes they need to graduate in a timely manner.

Academic and Institutional Support. The Governor's Budget includes a proposal for reducing academic and institutional support by 7.5 percent, or $45.4 million. These programs provide support services and the core infrastructure for the University's academic programs. Budget cuts in the early 1990s were severe in these areas and have never been recouped. Furthermore, regulatory requirements have intensified. To the extent possible, the University will achieve these savings through efficiencies and cost-saving measures, some of which may require negotiating changes to State reporting and regulatory requirements in order to reduce costs. The President will work with State government officials to determine all possible savings that can be achieved while maintaining basic operations without further erosion to needed academic infrastructure.

Research. The Governor's Budget proposes to cut research another 5 percent, or $11.6 million, on top of the 20 percent research programs have already been cut during the State's budget crisis. Rather than implementing another across-the-board reduction, the University will target this cut to specific research programs. Core research programs, such as agricultural research, Scripps Institution of Oceanography, and many others, cannot sustain further cuts and continue to maintain the quality of their programs. They received disproportionate cuts in the early 1990s and never recovered those funds. Furthermore, most of these core research programs will be contending already with large cuts next year because of the need to cover the significant fee increases proposed for graduate students. It would be the University's intention to allocate the $11.6 million in cuts proposed for 2004-05 to programs that received large increases in the 1990s as well as those that do not have large numbers of graduate students and therefore will not be coping with the added problem of providing graduate student support to cover the proposed fee increases for next year.

Institute for Labor and Employment. The Governor proposes to eliminate State funding totaling $4 million for this research institute. The University will work with both the Legislature and the Governor to arrive at a compromise that will allow the University to continue to provide needed research in the area of labor and employment.

Outreach. The Governor's Budget proposes to save $33.3 million in the budget year by eliminating all funding for outreach. Vice President Doby is working with the chancellors on a major systemwide effort to identify priorities within the outreach program. While it may not be possible to continue the scope and breadth of current programs, the University hopes to work out an agreement with the Governor and the Legislature for continued support for these programs.

Digital California Project (K-12 Internet). The Governor's Budget proposes eliminating all remaining funding for this program from the University's budget. Instead, he has included a total of $21 million in Proposition 98 funding in his budget specifically designated for schools to contract with providers for access to the high-speed Internet. The Digital California Project is hard at work to negotiate contracts with individual counties and school districts to continue providing established services.

Other Budget Adjustments and One-Time Actions

Restoration of $80.5 Million One-Time Reduction. The 2003-04 Budget Act included an additional one-time reduction of $80.5 million beyond the cuts included in the Governor's Budget. Language included in the Budget Act clearly designated this reduction as one-time. The University addressed this cut in part by borrowing $47.5 million; along with other reductions to the University's budget, the remainder was accommodated through fee increases and base budget reductions. Consistent with the legislative language included in the 2003-04 Budget Act, the Governor's Budget restores this funding to the University. A total of $47.5 million of these funds will be used to replace funds borrowed in the current year; the remaining $33 million will be used to help cover budget deficits for unfunded cost increases that far exceed this amount, such as faculty merit salary increases, price increases related to the non-salary portion of the budget, employee health benefits, and maintenance of new space – totaling about $100 million in real costs – all of which must be funded despite the lack of State support provided for them.

Merced. Consistent with the last several years, the Governor's Budget provides one-time funding to allow the Merced campus to continue its preparations to open the campus by 2005. These funds are needed for faculty start-up costs and to help establish the systems and core infrastructure needed to ready the campus for its opening in 18 months. The $2.7 million provided will increase to $10 million the amount of one-time funds provided for this purpose. However, this is significantly less than was requested for 2004-05. As a result, the campus has developed a new plan that will require a delay in hiring some faculty and in phasing in of some academic majors. Nevertheless, the campus is still on track to open with approximately 1,000 students in 2005-06.

Annuitant Health Care Benefits and Lease Revenue Bond Payments. The Governor's Budget provided the normal budget adjustments for these purposes, consistent with past years.

Continuing Budgetary Challenges

Competitive Salaries. The University estimates that UC faculty salaries will lag behind the average of comparison institutions by over 10 percent by next year. There is a similar problem with respect to staff salaries. This is a major issue, both now and for the long term. The University has been recruiting and will continue to recruit large numbers of faculty and staff throughout this decade to support enrollment growth. Compounding the problem is the fact that deep cuts are occurring in basic programs throughout the University. Competitiveness in terms of both salaries and working conditions is critical to the University's ability to recruit and retain faculty and staff. Yet, because of continued underfunding of basic needs, the University is increasingly unable to pay competitive salaries. This inability to compete could potentially have long-term negative consequences for the quality of the University's academic programs.

There is a particular problem with respect to faculty merits. The University's faculty merit system is essential to maintaining quality. Faculty undergo a thorough peer review every three years to determine merit and promotion status. In this way, the very best faculty are rewarded. A serious inequity would occur if faculty merit increases are not paid in any one year because the one-third of the faculty who are scheduled for their review in that year would be treated very differently from faculty whose reviews occur in another year. Consistent with the short-term priorities endorsed by The Regents in January, the University must fund faculty merits, even if it means cutting other program budgets further.

Recognizing that the University's longer-term priority is to return to paying competitive salaries, it is critical that the University develop a multi-year plan for bringing faculty salaries back into line with the average at comparison institutions. This is among the University's highest priorities for the long term. The issue of staff salaries must also be addressed, but this may be more difficult in the fiscally constrained environment expected for the next several years.

Employee Health Benefits. Health benefit costs are increasing at rates similar to last year's – around 15 percent. Because these costs are not being funded, the take-home pay of many UC employees is being reduced, although for the last couple of years, funding has been provided to reduce the impact of health benefit increases for low-income employees. The University intends to take a similar action for lower-paid employees again for 2004-05 and will do as much as possible to keep costs down for other UC employees.

Core Needs. Instructional equipment, instructional technology, libraries, and maintenance are core areas of the budget that directly support the academic program of the University and yet have suffered chronic shortages in funding. The Partnership Agreement with Governor Davis included a provision for closing the funding gap in these areas, but only two years of that agreement were funded, and since then, base budget cuts have eroded any previous gains made.

Other Unavoidable Costs. There are a number of other cost increases for which no funding is being provided, including energy costs, maintenance of new space, and other inflation costs associated with the non-salary portion of the budget. These are significant problems and will place further pressure on the campuses to redirect resources from existing programs to pay for these costs.

Noting that the issue of student fees is receiving particular attention, Vice President Hershman stressed that as a policy is developed, it will be important to consider all costs; financial aid, fees, and student funds. The Governor's budget proposal assumes an increase in revenue from mandatory systemwide fees, net of 20 percent for financial aid, of $121 million with respect to increasing undergraduate fees by 10 percent and graduate fees by 40 percent. If his suggestion is implemented, it will not generate the calculated $121 million savings but rather a figure closer to $113 million. Normally, the University would set aside one-third of the fees for financial aid, which in this case would reduce the savings to $95 million. Mr. Hershman emphasized that it is generally agreed that a 40 percent increase in graduate student fees would be unacceptable to the University.

Mr. Hershman discussed a series of possible options that had been mentioned for mandatory systemwide student fee increases and explained their revenue implications. He presented a chart to illustrate the results, using as examples cuts of 15 percent and 20 percent, 13 percent and 25 percent, and 10 percent and 15 percent for undergraduate and graduate academic student fees, respectively. He presented a chart also to illustrate the effects of the fee increase options on financial aid, noting that this year, University grant recipients must work or borrow $8,500 toward the total cost of their attendance. Under the Governor's 10 percent fee increase proposal, that figure would rise to $9,400. Shifting some financial aid from undergraduate to graduate students would increase the expectation further. An alternative that would bring down the fee for graduate students would help, because less financial aid would need shifting. Mr. Hershman explained, however, that all of the options involve tradeoffs. Low income undergraduates would do better if there were a higher fee increase for them and a lower fee increase for graduates, because so much financial aid would not be siphoned off. Middle to upper income students would be worse off; they do not get grant aid. They will pay a higher fee and will have to work and borrow more. He reiterated that the University has contractual obligations for covering fee increases for teaching and research assistants and fellowship recipients. Under the 10 percent/40 percent proposal, the University would require an additional $19 million to $32 million to cover 2004-05 fee increases beyond available financial aid. If the increase were 15 percent/20percent, that would be reduced to an additional $6 million to $12 million.

With respect to professional fees, Mr. Hershman noted that the Governor's proposal is to reduce the State subsidy by 25 percent. It assumes an increase in revenue from professional fees of $42 million, with no funds set aside for financial aid. Fees for law and business schools would increase by $2,600; medicine, dentistry, and veterinary medicine by $7,500; and pharmacy and optometry by $3,800. Increases of this magnitude could cripple the schools' ability to remain competitive. He suggested some options and discussed their implications. To achieve the $42 million savings, the University could increase its fees by $4,850 for every student, with no money for financial aid, and sacrifice quality. It could alter fees for law and business schools. It could increase the spread between what residents and nonresidents pay. None of these options would achieve the $42 million target, and each option has implications that would be explored with the chancellors as they prepare to develop their multi-year plans.

Mr. Hershman believed that there would be no way to maintain nonresident enrollment under the 20 percent increase in the Governor's budget, thus damaging quality. He believed also that savings from the Governor's implementation of a new fee to be applied for credit units taken by resident undergraduates above 10 percent of the minimum needed to graduate had been calculated incorrectly and over the planned four years would save only $5 million rather than $9 million.

Mr. Hershman then discussed potential unallocated reductions in the 2004-05 budget. He noted that the Regents will not accept any change in the student-faculty ratio, nor, based on history, will the University save as much as the Governor's budget indicates by reducing the entering freshman class by 3,200. Adding all potential unallocated reductions, including student fees and financial aid, excess unit fees, and professional school fees, it appears that the University could end up between $70 million and $170 million short. He noted further that the Governor's budget does not provide for cost increases. If the University were to fund normal faculty merits, give nothing more to staff but try to cover their health benefits, have to pay more for energy than was budgeted, forego maintaining new space and not cover price increases not in its control, it would be short another $100 million. This underscores the necessity of considering issues related to student fees while weighing the implications for other areas within the University.

Mr. Hershman returned to the subject of cutting 3,200 students from the freshman class, noting that under normal circumstances freshman enrollment would have grown by 5,000. He reported that the University is working to implement its dual admissions program, which cannot wait for legislative decisions in June or July. It is acknowledged generally that this effort will not lead to 3,200 students' deciding to attend community colleges and then transfer to UC. Although some may take this route if promised admittance to their campus of choice after two years, most students preparing for UC want to attend a four-year institution. Each campus has been directed to cut its enrollment by approximately 400 students. Eligible students who were not accepted at any of their preferred campuses but under normal circumstances would have been accommodated at some other UC campus will be offered the dual admissions program choice. He recalled that the University has enrolled 12,000 students beyond the number envisioned under the Master Plan, under which the University is pledged to accept students for which it receives State funding. A study by the California Postsecondary Education Commission concerning eligibility is determining whether the University is enrolling more than 12.5 percent of eligible high school students. The administration is working with the Governor and the Legislature to develop the details necessary to formulate budget plans as they relate to enrollment.

President Dynes invited Mr. Matthew Kaczmarek, president of the University of California Student Association, to address the Board. Mr. Kaczmarek reported that students strongly oppose further student fee increases on top of those implemented last year for undergraduate, graduate, and professional students. They also strongly oppose cuts to financial aid. He believed that of all the Governor's proposals, the most immediately damaging is the decision to deny eligible students attendance. Every week, UCSA representatives travel to Sacramento to appear in committee hearings, meet with legislators, and make the student voice heard. He hoped that the Regents would make a greater effort to advocate for the University, discussing the proposed budget cuts and how they affect students. He noted that application of the Governor's proposed fee increase would result in a 60 percent increase in student fees for undergraduates within 21 months and a 102 percent increase for graduate students. He observed that the University has offered the possibility of undergraduate fee revenue to subsidize the graduate fee increase, an approach that he believed would do little to strengthen any future argument with the Governor that a high return-to-aid principle is of value to the University. Students are strongly opposed to this proposal, as it would only shift the burden from graduate students to the most needy of undergraduates, who would be affected by the increased loan and work requirements. Students also advocate retaining outreach programs and the Institutes of Labor and Employment. He stated that the budget choices made by The Regents within the next few months would either preserve the best university in the world or push it over the edge.

Regent Connerly recalled that during the Wilson administration, the University was directed to change the way it was doing business by, among other things, reducing the length of time to graduation and by making its professional schools self supporting. Even in good times during the Davis administration, that direction remained unchanged. He believed that Governor Schwarzenegger also was establishing clear principles, among which was to send more students to community college. He believed that, rather than trying to make a case for more money, the Regents should focus on reshaping the University, based on what they believe is best, and move forward on that basis, recognizing that times have fundamentally changed and that the changes may be permanent. It was his opinion that education is not going to be a right in this new paradigm; that the taxpayers are not going to be willing to support law schools and business schools. He advocated trying to identify common threads established starting with Governor Wilson, discard some principles, choose some principles to embrace and move towards them while arguing for their support. He believed that it was unrealistic to cling to the notion that the University could continue to do business the same way as in the past.

Committee Chair Hopkinson expressed her sense that all Regents agreed with Regent Connerly's point and are attempting to be more strategic in considering how to address those issues within the near term.

Vice President Hershman acknowledged that it was critical to work out an agreement with the Governor and to engage Regents in those negotiations. He was hopeful that any agreement would provide flexibility sufficient to allow the Regents to make decisions concerning spending priorities.

President Dynes agreed that times are changing irreversibly. He believed that the Regents need to campaign to stem the bleeding in the short term and to think about where the University needs to be in ten years.

Faculty Representative Pitts agreed with Regent Connerly's characterization, except that he maintained that a major role exists for advocacy by Regents, faculty, and students so that Californians will come to understand the seriousness of the situation. They must become convinced that the University has been inordinately valuable and that broader support could safeguard it against further erosion. Regent Murray agreed. He agreed also with Mr. Kaczmerek's position concerning diverting financial aid money from undergraduate to graduate students. Concerning the possibility of establishing a long-term fee policy with the government, he noted that in the past the State had not upheld such agreements.

Regent Bodine was doubtful that people generally had looked upon a university education as a right. She characterized it as a covenant between the State and the student, based on the fulfillment of certain requirements. She believed that providing educational opportunity is a state's or society's basic responsibility rather than a luxury.

Regent Montoya commented that she expected the Committee eventually to address the question of whether the University was top-heavy with managers. Also, she noted that the California Digital Project to support K-12 internet use had successfully negotiated contracts with individual counties and school districts to continue providing established services, an entrepreneurial approach she applauded.

Vice President Hershman invited Provost King to address faculty recruitment and retention as related to the budget situation. Provost King reported that there had been a divergence in UC salaries of about 10.6 percent from those of its comparison eight institutions in recent years. UC's salary levels are between the comparison public four and private four, but within those, much of the University's competition for faculty is with the leading private institutions. The difference between the private four and UC is about 22 percent. Such things have happened before, but plans were developed that succeeded in bringing salaries back to a more competitive range. It is less clear how to accomplish this at present.

Provost King reported that by 2011 the University will need to be hiring 530 faculty per year. The need for housing assistance has grown from 36 percent of new faculty in 1999 to over 70 percent in 2003. He noted that faculty salary and benefits make up about half of the total general campus instruction and research budget. When the scope is widened to consider general campus and health science faculty, faculty salaries and benefits are about 40 percent of the total general funds budget and 10 percent of the total UC budget.

Provost King reported that the faculty salary scale is being departed from more frequently in order to meet market demands. In 2003, 50 percent of UC faculty were paid at something other than the rate that matches their particular steps. Disciplines with over 60 percent off-scale salaries include business, engineering, computer science, communications, public health, and social welfare. Faculty resignations have increased only slightly in the past four years, but the average faculty age has increased from 49 in 1990 to 51 in 2003, producing an increasing retirement rate.

Provost King introduced Executive Vice Chancellor Gray, who discussed the salary issue from the perspective of the Berkeley campus, noting that keeping faculty salaries competitive is a problem that must be solved quickly in order to prevent quality from being eroded. He observed that all members of a university community contribute to its impact but that the quality of the faculty is the most important determinant of a university's stature. The ability of the institution to stimulate economic growth through innovation in science and technology, to shape and lead the public debate on matters of public policy, and to offer a rich environment for students is directly dependent on their quality. He believed that the most important indicator of the health of an institution is the success it has in recruiting its first-choice faculty candidates. With a few exceptions, the University does not pay competitive salaries.

Mr. Gray discussed some of the ways to measure institutional quality. He noted that the Berkeley campus is represented prominently among private institutions, its most direct competitors, in national rankings and percentage of faculty membership in national organizations. Other measurements are the quality of the undergraduate experience and the opportunity to learn from outstanding faculty, and the linkage of research to local economic development in a region or state. When it comes to the economic growth of high technology and the distribution of venture capital investments, California dominates the picture. California also dominates the list of top graduate programs. Public investment in strong research universities correlates with economic development and benefits future job creation.

Mr. Gray addressed the issue of recruitment and retention of faculty, who make career choices for many reasons. Attraction to the Berkeley campus is based on the physical location and environment and the opportunity to work with top faculty and graduate students, but there is a corresponding disadvantage; faculty members must include in their calculations the expense of living in the Bay Area. The University attempts to mitigate this problem by offering a number of housing assistance programs. Nevertheless, if the University can match or almost match the salary of a competing offer from a top institution, it usually prevails in hiring or keeping a faculty member, but that is becoming more difficult as the salary gap between the University and its competing institutions increases. To close that gap in parity with the average of its comparison institutions, the annual faculty salary budget at Berkeley would have to increase by $20 million. Its relatively good record in recruitment and retention is coming at an unsustainable cost. During the past four years, there have been 160 attempts to recruit faculty away from the Berkeley campus–122 from private and 38 from public institutions. The private institutions succeeded in 31 cases, and 26 remain undecided. Few are lost to the public institutions. He reported that the top seven competitors concentrate their offers mainly on faculty in their 40s and early 50s. Each year, about one-third of the University's faculty receives a merit review. In 2002-03, permanent faculty merit funds that were given out in the normal process to 335 individuals averaged almost $8,000, for a total of $2.6 million. The awards given for 32 retention cases averaged an increased $26,000 per salary, costing $834,000 in permanent funds; thus, the Berkeley campus used about 25 percent of its total merit pool to retain 10 percent of its eligible faculty, and the figure is expected to increase for 2003-04.

Moving to the issue of hiring, Mr. Gray reported that the overall success rate during the past ten years had been about 75 percent of first-choice applicants, a rate that, as in the case of retention, has dropped little. This also has come at a severe cost to the Berkeley campus. When a faculty member is hired, he is assigned a step within the professional ranks that corresponds to seniority and academic merit. Then if a competitive salary environment has to be addressed with a higher salary than that step would normally give, the campus uses decoupling, which means paying a salary that is more than 5 percent higher than the step system would otherwise allow. Last year, the campus made almost two-thirds of new faculty appointments at the decoupled level. One-fifth of the existing faculty have decoupled salaries. The negative effects are salary impaction and equity problems.

Mr. Gray commented that the combination of increased start-up costs plus faculty salary demands is increasing the shortfall of available funds. The campus will be limited in its ability to reach its targeted faculty size, and the student-faculty ratio will be affected adversely as a result, damaging the quality of the undergraduate experience. The University's mixture of providing access for a diverse group of students and giving them an excellent education is being severely challenged.

Committee Chair Hopkinson expressed appreciation for Provost King's and Executive Vice Chancellor Gray's presentations and requested that copies be provided to all Regents.

Regent Montoya requested a comparison of administrative burden between UC and other universities, including the amount of money that is taken out of faculty research grants in order to pay for administrative support. She believed that administrative barriers were preventing faculty from applying for multidisciplinary research funding. Provost King responded that one measure of administrative burden is the indirect cost rate, which at UC is average. Executive Vice Chancellor Gray added that anyone expressing difficulty with grant costs may have been responding to the situation caused by the dramatic increase in student fees which falls upon contracts and grants and puts the campuses in an uncompetitive situation. He believed that the single greatest challenge in making a research university progress is to foster interdisciplinary activity, which he believed was a strong point of the Berkeley campus. He stated that on competitive campuses the administration returns some of the overhead to the faculty member in some form of individual support, which at Berkeley is not possible because the overhead is designated to pay for specific things. In response to a further question by Regent Montoya, Mr. Gray acknowledged that faculty often complain about the level of bureaucracy, but he pointed out that much of it is tied to the need for complex requirements governing regulatory compliance.

Regent Marcus asked whether, given the kinds of changes that are occurring in the University's budget allocations, other solutions to bridge the faculty income gap had been sought. Mr. Gray responded that reducing the age distribution by focusing new recruitments on the junior level and implementing various means on the campus to encourage faculty to retire have been quite successful. He noted that salary is a necessary condition when faculty consider accepting an appointment, but most important is the quality of the colleagues with whom they will be working. Private funding also is critically important, not on income but on peer recognition and because of its flexibility of use. Provost King added that while it is true that the distribution between hires at the assistant and senior professor levels is an important control valve with regard to the average salary, universities sometimes need to hire at the senior level in order to get the greatest expertise.

Faculty Representative Pitts commented that when salaries had dipped in the past, faculty did not leave in large numbers. In those instances there was an expectation that the situation was temporary. If potential recruits cannot see a promising future at the University, they will not be interested in accepting positions there. In response to Regent Montoya's earlier question, he noted that issues about multidisciplinary research are increasingly important. Many high-quality areas of research require multiple players across campuses and institutions. It is important to design the appropriate administration for that kind of endeavor. The Academic Senate has formed a small working group to study how to facilitate relationships among faculty. Also, he noted that all universities are experiencing increases in overhead because federal regulations are creating new burdens.

Regent Kozberg asked how common it was for entire departments to be raided by other institutions. Mr. Gray responded that, although that kind of raiding had not happened on the Berkeley campus, he predicted that it could escalate if faculty salaries continue to lag the market.

Regent Montoya asked whether there was the potential for faculty to abuse the counter-offer strategy. Mr. Gray responded that a faculty member who threatens to leave must present to his department chair a documented, written offer from a peer institution. The department chair would then present the case to the dean, who would review it along with the vice chancellor.

Committee Chair Hopkinson then introduced Vice President Gomes and Chancellor Córdova, who presented a general background of agriculture and natural resources at the University and discussed specific campus examples of their work.

Vice President Gomes reported that farm income in the state contributes $27 billion and 1.1 million jobs to the state's economy. Since its birth as a land-grant university, the

University has served as the research arm of that industry and has maintained a strong interaction among agriculture, natural resources, and California consumers. The continuum from laboratory to consumer has played a major role in shaping the reputation of the University. The basis of this continuum has been the University's long-standing interaction among scientists on the Berkeley, Davis, and Riverside campuses; its statewide programs; its research and extension centers across the state; and its ability successfully to address important issues.

Mr. Gomes noted that historically the State had funded the infrastructure of the Agricultural Experiment Station at $100 million annually and Cooperative Extension at $50 million. Over the last two years, the State has cut $19 million from the research budget and $12 million from Cooperative Extension. The Governor's Budget for 2004-05 contains an undesignated cut of 5 percent for the University's agricultural research program and no change in Cooperative Extension funding. He provided specific examples of how these cuts translate into people lost and programs put in jeopardy. On the Davis campus, the cuts have meant the loss of 50 faculty FTEs, which is more than 20 percent of the research force at that site. The loss of these 50 positions means that the University will not be able to cover specializations and will provide mentors for fewer students. It also means the loss of people who would have brought in $10 million a year from outside grants. In Cooperative Extension, positions have been lost on campuses, in research centers, and in county offices throughout the state. Milk and cheese are California's leading commodities, and California is the nation's leading producer of them. The University's nine advisors disseminating research information in this area have been reduced to six. California produces more than half of the nation's fresh fruit and vegetables. Eight advisors in this area have already been lost. UC research and extension have been key to the development of the California wine industry, but the University's ability to meet its viticulture and enology needs is in jeopardy. In addition to losses of people, programs have been closed or consolidated and research grants in some areas have been suspended. He commented that any additional cuts will prevent the University from fielding the professionals needed to keep several programs alive.

Mr. Gomes reported that a new pest appears in California every 60 days, along with new diseases such as sudden oak death and west Nile virus. When the glassy-winged sharpshooter threatened to spread Pierce's disease throughout the wine, raisin, and table grape industries, the University took a leadership role, working closely with the USDA, the National Academy of Sciences, and the grape industry to put together funding, to leverage resources, and to develop interdisciplinary teams to address stop-gap responses and long-term research solutions. The successes in this area resulted because the University had a workforce that could be mobilized rapidly. It would be difficult to launch such a response under the present situation. In environmental education, the University was a central actor in defusing a volatile situation in the Klamath basin, where unbiased science was used to show how fish and farming could coexist. He commented that air quality regulations have endangered the existence of the state's dairy farming industry. University representatives have worked with farmers to develop methods that reduce sediment and run off, that meet regulations, and that save money. Obesity is epidemic; in adolescents it has tripled in the last 35 years and is expected to replace tobacco as the leading cause of preventable death and to catch cancer as the leading cause of death in the U.S. by 2005. The University is addressing these issues through research on the Berkeley and Davis campuses, through expanded food and nutrition education, food stamp nutrition education programs, and targeted programs within 4-H. Nine positions have been lost in these areas, and further losses are expected.

Mr. Gomes reported that California's stakeholders are concerned about the loss of University people, particularly people in the field, where problems can be addressed first hand. The University is receiving hundreds of requests a month asking that cuts be stopped and spending expanded in sustainable agriculture, integrated pest management, and small farm research. The populace does not understand the degree to which funds are decreasing.

Chancellor Córdova discussed programmatic impacts caused by budget cuts at the Riverside campus. She reported that one reason for the success in containing the glassy-winged sharpshooter mentioned by Vice President Gomez was that the University had the flexibility provided by State resources to address the problem early on. Since 1989, State-funded UC Riverside scientists have been in Temecula, where they were positioned to mount a strong response. Although full containment has not been achieved, UC research and outreach programs have prevented widespread devastation of the grape industry. Ms. Córdova commented that for every dollar the State invests in agricultural research, UC researchers generate an additional four dollars. In the case of the glassy-winged sharpshooter, State support was followed by allocations of $125,000 each from the County of Riverside and the City of Temecula in recognition of the seriousness of the threat. This, in turn, prompted a USDA allocation of $115 million over four years for research, control, and eradication.

Ms. Córdova observed that the State's investment in research is also buying the ability to integrate new fundamental knowledge with immediate applications. She cited, as a recent example, the State's citrus industry–a $1 billion-per-year enterprise–that is awaiting UCR's release of a new variety known as the Australian Finger Lime, the latest in a long line of citrus varieties studied or developed by the campus. Notable other examples of UCR research and its examples, not only to production agriculture but also the State economy, to the environment, and to health, include the science of biological control, which was pioneered by UCR in the early 1990s. Since then, UCR has developed biocontrol methods to help manage many insects, including the silverleaf whitefly, which has caused $1 billion in damage nationally. With recent budget cuts, UCR has lost 40 percent of its biological control specialists. Cuts to State-funded research will also hamper efforts to apply discoveries from genomics and proteomics, fields that are expected to provide the scientific and technical foundation to increase agriculture's competitive advantage and support development in alternative fuels, plastics, and pharmaceuticals. If cuts to State-funded agriculture are sustained, discoveries may not advance from the laboratory to the field. Particularly affected has been the field development of new technologies, as many technical staff who conducted this work have been laid off or redirected. In the area of human health, UCR's insectary and quarantine facility have been affected by cuts to the research budget. Using the quarantine facility, entomologists are developing molecular-based strategies for genetic control of mosquitoes. Research on the sequencing of the genome of the mosquito that transmits West Nile virus, which has been detected in 46 states, is threatened, which in turn affects research on the development of a transgenic mosquito that cannot transmit deadly diseases such as malaria. These projects hold great promise for managing some of the world's most serious public health problems, but only if funding is available to extend the discoveries to application.

Ms. Córdova commented that UCR's most successful product may be its alumni. She described two who had been trained by its agricultural experiment station faculty. Dr. Tina Nova made the discovery that led to the PSA test for prostate cancer. Since then she has founded four biotech startups in San Diego. Mr. Mike Mellano, who received his Ph.D. in plant pathology, runs the largest flower-growing operation in the nation. His ranch is the site of extensive UCR research studies.

Chancellor Córdova concluded her presentation by noting that UCR's agricultural research, extension, and teaching programs demonstrate how California's economy, health, and quality of life depend on the University. The cuts already sustained have seriously eroded UC's ability to address the challenges facing California. In the long term, the state will suffer, as opportunities to enhance its national and international competitiveness are lost.

Regent Johnson commented that it was distressing to hear the report. She asked whether the President's Advisory Commission on Agriculture and Natural Resources had offered helpful suggestions. Vice President Gomes responded that the commission, campus groups, and many others last year were very supportive in efforts in Sacramento and elsewhere. He believed that their lobbying had convinced the Governor not to cut the Cooperative Extension budget further this year. Regent Hopkinson stressed the need to publicize the impact the University has on this incredibly important component of the state's economy.

Senior Vice President Mullinix and Vice Chancellor Relyea presented the final topic, "Accelerating the New Business Architecture." Mr. Relyea recalled having informed the Regents in 2000 about the work of a task group comprised of campus vice chancellors and representatives from the Office of the President to recommend a restructuring of the way in which the University conducts its business operations. The main goals were to contain and reduce costs, prepare the infrastructure to support growth, and enhance productivity.

Mr. Relyea described the new business architecture, beginning with the business portal, a way of replacing labor- and paper-intensive processes and bringing them together in an on-line system in order to reduce costs. The business portal provides integrated access to business transactions, policies, and training, but in order to establish the University as a competitive employer, employees must be given the tools and training to be more productive and successful. Having the best-trained people and a solid infrastructure will not help if a weighty bureaucracy of policies and processes obstructs the attainment of the desired goals; processes must be redesigned to improve efficiency and effectiveness. In order to accomplish this, investment must be made in technology. The financial systems and reporting component of the new business architecture is improving the management of the institution's finances on the campuses and is transferring paper-based processes into an on-line system in order to provide better financial information to managers. Finally, Mr. Relyea reported, organizational performance and controls enable an assessment of whether students, faculty, and staff are being served with the most appropriate infrastructure and whether appropriate controls are in place to minimize risk to the institution.

Senior Vice President Mullinix reported that an assessment of how well individual campuses had implemented the new business strategy indicated significant improvement, particularly given the budget situation in recent years. He listed the following concerns as the focus for 2004:

- *Managed risk*: Address the increasing risks associated with long-term underfunding of institutional support.

- *Cost savings*: maximize the return on institutional support investments.

- *Collective solutions*: recognize the need to solve campus problems once rather than ten times.

- *Greater leverage*: leverage the University's size and purchasing power.

- *Flexibility*: accelerate New Business Architecture solutions which enable the University to accommodate both growth and downsizing without compromising service levels.

- *Regulatory burden*: lessen the cost and administrative affects of regulatory compliance.

Mr. Mullinix noted that the University budget had grown substantially since 1986-87, particularly in research, but the percentage of institutional support had declined proportionally. An objective is to reduce the proportion of administrative cost relative to total budget expenditures.

Mr. Relyea observed that, because of their specialized work, much of the administrative costs in research universities lies in departments where teaching, research, and clinical care are conducted. It may be necessary to make investments in central offices in order to reduce costs in department administration. He discussed some examples of streamlining initiatives on individual campuses.

Mr. Relyea reported that a good strategy for reducing costs is to move labor- and paper-intensive processes to the internet in terms of not only creating websites but also managing content and workflow. For instance, the business portal methodology is being extended to student portals for information delivery to students, parents, and alumni. Similarly, many employee benefits, human resources, employee training, and financial reporting processes have been moved to the web. Advances in employee self-service have reduced the amount of time employees must spend getting information, and their satisfaction has increased. By placing personnel benefits information on line, open enrollment costs have been reduced by $125,000 per year. An annual savings of $700,000 is expected to result if it becomes permissible to put W2s and direct deposit statements on line.

Mr. Relyea commented that, when faced with workload challenges and increased regulations, a first course of action is to try leveraging the size of the institution to develop common solutions. Corporate partners have provided ideas for consolidating the reporting of federal contracts and grants, procuring on line, and developing business content.

Mr. Mullinix reported that in order to reduce the cost of operating and maintaining facilities, the University is collectively procuring utilities and storing thermal energy. The University has not received funding for ongoing building maintenance for two years, however, and there does not appear to be an opportunity for further savings in this area. In order to focus on leveraging the University's size and strength, a program is under way to examine the University's ability to procure jointly in order to save resources. Twenty commodity groups were identified where aggressive savings targets have been established, and the strategy is being extended to consulting contracts. Debt restructuring using General Revenue Bonds also offers opportunities for substantial savings.

Mr. Mullinix emphasized that the University has been subjected to an increasingly heavy regulatory burden. The University is working with the State to identify areas in which improving the University's efficiency may eliminate unnecessary requirements, some of which could result in substantial savings.

Mr. Mullinix believed that in the longer term the University is making a large disinvestment in its staff by not providing adequate salaries. It is no longer competitive in most areas, and the gap is growing. At some point, the University must reinvest in its staff and its facilities. In closing, Vice President Mullinix stated that the administration is relatively lean, but he noted that there are always opportunities for increasing efficiency.

Regent Connerly asked about the process for reviewing the business architecture of faculty operations, for example courses that may have lost relevance. President Dynes recalled that an extensive analysis of teaching loads throughout the University had been completed in order to eliminate courses systemwide. Faculty Representative Pitts observed that faculty are at the forefront of their fields and typically offer courses that reflect the latest issues. Provost King added that the process of culling courses is continual at the departmental level. Acting Chancellor Chandler reported that at the campus level programmatic reviews are done for undergraduate and graduate programs that review the curriculum for relevance. These are followed by reviews up to the systemwide level. Regent Hopkinson suggested that it may be appropriate to focus on the contemporary environment at a given time in order to make decisions regarding the curriculum. Regent Montoya requested that the President provide a report to the Regents on how teaching loads have been reevaluated on the campuses.

Commenting that she was particularly interested in business technology, Regent Kozberg noted that teams are examining individual State departments as part of the Governor's California performance review. She believed that, while constitutionally separate, there are areas experiencing rising costs, such as technology and construction procurement, where the University is governed by State laws. She suggested volunteering to form a team with the State on programs such as procurement in order to put forward the University's issues about regulatory requirements. Mr. Mullinix responded that the State administration has been approached in an attempt to promote some of the University's business reforms, but he observed that many activities are governed by legislation that has a long and complex history and will be difficult to change.

Regent Hopkinson noted that challenging times can produce opportunities. She complimented the faculty, staff, and Regents, who are committed to maintaining the University's quality and are approaching issues aggressively.

Secretary Trivette drew attention to the report that had been distributed pertaining to communications received concerning this item.

[For speakers' comments, refer to the March 17 and March18, 2004 minutes of the Committee of the Whole.]

3. **AMENDMENT OF THE UNIVERSITY OF CALIFORNIA STUDENT FEE POLICY TO INCLUDE CONSIDERATION OF THE FULL COST OF ATTENDING THE UNIVERSITY WHEN SETTING ANNUAL STUDENT FEE LEVELS**

Regent Murray requested that the Committee consider amending The University of California Student Fee Policy to include consideration of the full cost of attending the University and comparable institutions when setting annual student fee levels.

Regent Murray observed that student fee levels play an important role in ensuring that the University has adequate resources to fulfill its mission. Fees also have a direct impact on the affordability of the institution. Fees are not the only costs that students attending the University must pay, however, and for the University to ensure that attendance remains affordable, the President and the Regents should take into consideration all the costs of attending the University when setting annual fee levels.

The University's current focus on comparing student fees with student charges at comparable institutions incites criticism from students and others who know that students face differential costs in other areas, including housing, transportation, and supplies, and who perceive the University as attempting to ignore those costs. The UC Student Association prepared a critical report in 2002 titled, "Dispelling the Myths: The True Cost of Attending the University of California," to bring attention to the need to consider more than just fee levels when evaluating the affordability of the University.

Regent Murray suggested that the perspective of the University's affordability that derives from fee comparisons which ignore other costs of attendance invites calls from other commentators that the University should increase fees substantially so that they match charges at comparable institutions. Pressure for substantial fee increases based on limited information damages the University's overall budget prospects. The University and the State of California will be served best if decisions regarding annual fee levels are made after consideration of all relevant factors so that those decisions are as fully informed and justifiable as possible.

He recalled that at the January 2004 Regents meeting, The Regents agreed in principle to eight priorities to direct the Office of the President in negotiations with the State regarding the University's budget. The third short-term priority stated that, "Graduate student quality and ratios that exist today shall be maintained. That means that the net cost to attend and related financial support shall be maintained." This priority recognizes that the "net cost to attend" is the critical component of affordability.

At the January 2003 Regents meeting, Provost King gave a presentation on "Financing the Cost of Attending the University of California" which addressed the total cost of attendance at the University.

Regent Murray believed that consideration of the full cost of attendance at the University should be a routine, integral part of fee discussions at meetings of the Board of Regents, rather than the topic of occasional presentations.

Regent Hopkinson supported the concept of considering, when setting fees, the full cost of attendance, but she believed it should be one element rather than the only element in that consideration. Regent Murray noted that the policy has four elements, to which this fifth element would be added.

Regent-designate Anderson commented that the proposal would enable the Regents to have access to information that would help in their deliberations about student fees and that would be useful to provide to the general public as well.

[For speakers' comments, refer to the March 17, 2004 minutes of the Committee of the Whole.]

4. **APPOINTMENT OF CONSULTING ACTUARY FOR THE UNIVERSITY OF CALIFORNIA RETIREMENT SYSTEM BY THE REGENTS AS TRUSTEE**

The President recommended that:

A. The Segal Company (Segal) be appointed the Consulting Actuary for the University of California Retirement System (UCRS) on behalf of The Regents as Trustee for the period April 1, 2004 through December 31, 2005, with the ability to renew annually.

B. The Secretary of The Regents be authorized to execute necessary documents effecting the appointment and subsequent calendar year re-appointments.

C. The Request for Proposals (RFP) process continue to be undertaken every five to seven years or as necessary.

It was recalled that Towers Perrin had been the Consulting Actuary for UCRS since the 1970s and was most recently approved by The Regents as Consulting Actuary as a result of a bid process conducted in 2000, with an initial appointment for the period January 1, 2001 through December 31, 2001. Generally, an RFP process for the Consulting Actuary is undertaken every five to seven years.

An annual renewal of the Towers Perrin contract for the period January 1, 2002 through December 31, 2002 was subsequently executed. For the 2003 calendar year contract, Towers Perrin attempted to modify the agreement by introducing language limiting its potential liability. Such a limitation contradicts The Regents' Standing Order 100.4(dd)(9), as well as long-standing University contracting policy prohibiting the University from entering into agreements that can result in the assumption of liability for the conduct of other parties. After extensive negotiations, the Towers Perrin contract was extended under current terms through March 31, 2004. A bid process was initiated to appoint a Consulting Actuary for the period April 1, 2004 through December 31, 2005.

The RFP was designed to attract actuarial firms with experience in the public and private sectors related to both qualified and statutory defined benefit and defined contribution plans. An advertisement was placed in the *Wall Street Journal*, October 13-15, 2003, inviting qualified actuarial firms to obtain the bid specifications for their proposals. Pre-qualification packets and invitations to bid were sent to six firms. Two additional firms requested pre-qualification packets in response to the advertisement. The deadline for receipt of the pre-qualification packet was November 3, 2003.

Six firms met the pre-qualification criteria and submitted bids by the November 26, 2003 deadline. The bid proposals were reviewed and scored by an evaluation committee. The results were compiled, and the three top-ranking firms, Segal, Towers Perrin, and Mellon Financial Corporation, were selected for final interviews on January 7, 2004. The total scores given to each bidder by the evaluation committee, along with a comparison of the firms in critical areas, were provided in an executive summary for review and consideration by the selection committee. On January 20, 2004, the three firms were invited to make a presentation to, and be interviewed by, a selection committee consisting of the Senior Vice President–Business and Finance, Associate Vice President–Human Resources and Benefits, Executive Director–Human Resources and Benefits Policy and Program Design, Treasurer, Assistant Vice President–Financial Management, University Counsel, Director–Retirement Policy and Planning, and Associate Director–Retirement Policy and Planning.

The goal of the RFP process was to identify and select a firm that is capable of meeting the actuarial consulting needs of UCRS and, in accordance with University contracting policy, does not propose to limit its liability. The Consulting Actuary awarded the contract in response to this bid process will have an initial appointment beginning April 1, 2004 through December 31, 2005, with the ability to renew annually. In accordance with past practice, a bid process will continue to be undertaken every five to seven years or as necessary. As with all consulting contracts, the University retains the right to terminate the relationship upon 90 days' written notice.

The Segal Company received the highest overall rating from the selection committee based on a number of criteria, including its strong performance in all phases of the RFP process, its growing presence in the public sector market, and its conformance with University of California contracting policy. Segal is a privately-held, well-regarded national firm that carries $10 million in Errors and Omissions insurance coverage. The incumbent actuary proposed an overall limit of $25 million to its liability, in violation of University of California contracting policy. While it may be possible to obtain a larger settlement of a potential claim from a firm such as the incumbent actuary which has higher insurance, Segal will commit to a contract term including no limitations on its liability through December 31, 2006.

While Segal proposes slightly higher fixed fees for the annual actuarial valuation than the incumbent, Segal's proposed hourly rates are lower than the incumbent's for its most senior consultants. This means that the University can expect cost savings with Segal, because the majority of the University's annual expenses are the result of hourly rates charged for ad hoc and special projects. Segal received favorable recommendations from its clients and positive feedback from a site inspection conducted by UC HR/Benefits staff. Segal proposes a locally-based UCRS consulting team, led by Messrs. Paul Angelo and Drew James.

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

5. **UNIVERSITY OF CALIFORNIA POLICY ON CONFLICTS OF INTEREST CREATED BY CONSENSUAL RELATIONSHIPS**

This item was deferred by the President.

6. **UNIVERSITY OF CALIFORNIA POLICY ON SEXUAL HARASSMENT AND PROCEDURES FOR RESPONDING TO REPORTS OF SEXUAL HARASSMENT**

This item was deferred by the President.

7. **REPORT ON NEW LITIGATION**

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

The meeting adjourned at 1:10 p.m.

Attest:

Secretary