THE REGENTS OF THE UNIVERSITY OF CALIFORNIA

April 13, 2006

The Regents of the University of California met on the above date at the following locations: James E. West Alumni Center, Los Angeles campus; 111-A University Complex, San Diego campus; 203 Mrak Hall, Davis campus; 909 Montgomery Street, San Francisco; 501 South Alta Avenue, Dinuba; 777 California Avenue, Palo Alto; 2220 Lodgepole Circle, Modesto; 1-Via Tornabuoni, Firenze, Italy; Keizergracht 384, 1016 GB Amsterdam, The Netherlands

Present: Regents Blum, Dynes, Gould, Island, Johnson, Juline, Kozberg, Lozano, Marcus, Moores, Parsky, Rominger, Ruiz, and Wachter (14)

In attendance: Regent-designate Coombs, Faculty Representatives Brown and Oakley, Secretary Trivette, General Counsel Holst, Senior Vice President Darling, and Recording Secretary Nietfeld

The meeting convened at 9:35 a.m. with Chairman Parsky presiding.

1. **READING OF NOTICE OF MEETING**

For the record, it was confirmed that notice was served in accordance with the Bylaws and Standing Orders for a Special Meeting of The Regents to discuss the report of the Task Force on Compensation, Accountability, and Transparency.

2. **PUBLIC COMMENT**

Chairman Parsky explained that the public comment period permitted members of the public an opportunity to address University-related matters. The following persons addressed The Regents concerning the item noted.

Task Force on UC Compensation, Accountability, and Transparency: Final Report

A. Professor Charles Schwartz, an emeritus faculty member on the Berkeley campus, observed that it was difficult to comment on the task force report as it had been released this morning. He noted that the University's response to series of newspaper articles had been to acknowledge the need for better oversight and suggested that the most important point had been overlooked, which was why UC executives should receive inflated pay packages. Mr. Schwartz recalled that a resolution adopted by the faculty at the Berkeley campus in 1992 called for a policy that would require that at any institution of higher education the total compensation paid to an executive officer should not exceed twice the average amount paid to a

full professor. He urged The Regents to restore public confidence in the institution by adopting such a resolution.

B. Ms. Norah Foster, a member of the Coalition of University Employees on the Berkeley campus, recalled that at the March meeting The Regents had approved the proposal to resume contributions to the University of California Retirement Plan in July 2007. She believed that the Plan was well funded through 2009 and saw no need for contributions until then at the earliest.

3. **TASK FORCE ON COMPENSATION, ACCOUNTABILITY, AND TRANSPARENCY: FINAL REPORT**

Chairman Parsky commented that today's special meeting had been convened in order to receive the final report of the Task Force on Compensation, Accountability, and Transparency, which had been released to the Regents and the public simultaneously. The issues raised in the report will need to be carefully evaluated. There will be another opportunity for the public to comment on the report at the May meeting.

Chairman Parsky recognized the two co-chairs of the Task Force, Mr. Robert Hertzberg and Regent Joanne Kozberg, and invited them to present the report. Mr. Hertzberg observed that the work of the Task Force had been a significant undertaking and expressed appreciation for the fact that the Task Force had been permitted to do its work independently. He recognized the members of the Task Force and expressed appreciation for their dedicated efforts, as well as for the contributions from individuals in the Office of the President. The Task Force was assisted in its efforts by Deloitte Consulting LLP. He reported that the Task Force had met ten times, with more than thirty hours of meetings, and there were numerous conference calls to discuss the drafting of the report. Mr. Hertzberg stressed that the members of the Task Force were the authors of the report, with Professor Duderstadt, the former President of the University of Michigan, serving as editor. He explained that the Task Force's support of the report had been unanimous.

The Task Force sought to take a long-term view of the problems associated with the University's compensation practices. The focus was to create a course of action which has been codified in a series of recommendations to The Regents and senior management. In addition to the efforts of the Task Force, The Regents' external auditor, PricewaterhouseCoopers, has undertaken an analysis of compensation practices over the past ten years, and the State is conducting an independent audit as well. University Auditor Reed is undertaking an internal review. Mr. Hertzberg noted that the report was limited to the information provided to the Task Force by internal and external sources, as well as by the

short time period devoted to the effort. The preliminary conclusions are set forth in the preamble to the report, which states in part:

> The University of California is a public institution and a public trust. Its foundation and future depend on the continuing support of the people of California.
>
> This support will only continue if the people – and their elected representatives – respect and trust those who lead the University system.

Mr. Hertzberg noted that the report has concluded that the decline in confidence in the administrative leadership of the University had resulted from failures to release compensation information in a clear and timely fashion and failure to comply with policies established by The Regents. The report states that the inappropriate incidents cited "…are all the more troubling when the University's history in this area is taken into account. In the early 1990s, in the wake of a public controversy regarding executive compensation, policies were put into place to prevent future problems in this area. At least some of the current problems would not have occurred if those policy reforms had been followed and enforced by the senior administrative leadership of the University system."

Mr. Hertzberg continued that the report contained the following findings:

- While the nature and scope of compensation-related problems in the University system will not be known conclusively until several current inquiries are completed, it is already clear that the current situation is wholly unacceptable. Necessary steps must be initiated immediately at all levels to remedy the problems. Outdated policies and practices must be replaced. Necessary and appropriate checks and balances must be put in place and rigorously adhered to.

- Neither the executives who lead the University nor the Regents who oversee it have done all they could or should to fulfill their respective or shared responsibilities.

- The Task Force underscores emphatically that no question has been raised about the academic leadership of the University of California system. Esteem for the University's students and faculty is undiminished.

- To be effective and accepted by the public whose trust and support are essential, accountably must include consequences, and the consequences must be consequential.

Mr. Hertzberg presented the **Findings and Recommendations** of the report with respect to **Disclosure and Transparency**:

1. **The Task Force finds that the University of California has failed to honor, consistently and comprehensively, its obligation of public accountability.**

   The University has not lived up to the responsibility to disclose executive compensation information, to file timely reports, to respond fully to information requests, or to ensure that compensation policies and practices are clear, accessible, and easily understood by the public.

2. **The Task Force finds that, over the years, UC and its leaders have failed repeatedly to inform the Regents about the total compensation of senior managers as required by the Regents' 1992 Principles for Review of Executive Compensation. This failure has hindered the ability of the Regents to perform their responsibilities of governance and oversight in this key area and make it impossible to disclose such information to the public and the Legislature.**

   The principles clearly state what elements of total compensation for senior executives must be disclosed to and approved by The Regents.

3. **The Task Force finds that UC's information systems are inadequate and unable to provide full and timely compensation information.**

   UC can establish the best disclosure policies and practices but still fail to achieve them without a modern, integrated human-resources information system that enables comprehensive analysis, monitoring, and reporting of compensation information. UC's antiquated and decentralized systems are inadequate to the task. The report details specific problems with the University's payroll systems that were identified by the Task Force.

Mr. Hertzberg outlined the recommendations in the report pertaining to Disclosure and Transparency:

Recommendation: The University should develop and broadly communicate a systemwide policy governing the disclosure of compensation information to the public. Such a disclosure policy must balance public access, personal privacy, and institutional competitiveness by defining what UC considers public versus private/protected information. UC must also provide ongoing training for its leaders

and managers about its compensation disclosure policies and practices.

Recommendation: UC must ensure that all relevant information about compensation packages is provided to the Regents in advance of approval. Following Regents' approval, compensation information should be disclosed to the public in a timely manner.

Recommendation: The University should invest in a modern, comprehensive, integrated human-resources information system that enables compensation data to be quickly examined and analyzed – at the campuses, medical centers, national laboratories, and systemwide – so that UC can meet its obligation of public accountability. Because the new systems will require a major investment of time, money, and staffing, the University should phase in implementation, beginning first with systems that track senior management compensation.

Recommendation: The University should establish clear protocols, procedures, and forms that allow for full and timely compensation reporting. These reports should include:

- Annual reports on total compensation for UC executives.
- Annual reports on outside compensated professional activities.
- Compliance with annual reporting requirements to the Regents and the Legislature.
- Regular reviews of compensation policies and practices.
- Regular reports on compensation actions taken by the Regents at Board meetings as well as compensation actions taken between Board meetings.

Recommendation:. The University should improve public information and ensure that this information is readily available, including creating a new, easily accessible Web site for posting UC compensation information

consistent with the other recommendations in this report.

Recommendation: The Regents should reaffirm the definition of "total compensation" in the Regents' 1992 Principles for Review of Executive Compensation and further clarify some missing elements to ensure consistency with accepted standards and practices.

Recommendation: The UC Office of the President should immediately assign to one person the Public Information Practices Coordinator role. This staff member should coordinate all Public Records Act requests and develop clear protocols and timelines for processing these requests.

Regent Kozberg presented the **Findings and Recommendations** of the report with respect to **Governance and Accountability**.

1. **The Task Force finds that UC's compliance with compensation policy is wholly inadequate and, in a number of cases, has failed or been circumvented.**

   There is confusion within the system as to who has the authority for compensation decisions. Many of the University's compensation policies are confusing, duplicative, overlapping, and at times conflicting. A glaring problem is the area of exceptions to policy. While there are legitimate reasons to grant an exception, they have become commonplace, and these exceptions are sometimes used to either ignore or circumvent policy. The Task Force finds that there are few, if any, real consequences for violating policy. The Regents' responsibility as fiduciaries to oversee compensation decisions is weakened by the sheer volume of the salaries they are asked to approve.

   Recommendation: The Regents should examine specific aspects of the University's compliance mechanisms and, if necessary, make changes or introduce new oversight mechanisms to ensure compliance. Specifically, the Regents' Compensation Committee should have primary responsibility for setting compensation policies and providing necessary oversight to ensure compliance. In order for the Committee to exercise proper oversight, the President should designate a senior official from the

Office of the President to serve as the administration's liaison to the Regents' Compensation Committee to implement the Committee's mandate. The University should also establish a compensation oversight committee to work with the administrative liaison to the Regents to ensure that recommendations reflect the needs of the campuses and the accountability requirements of the UC system.

These oversight mechanisms should help to address the failure to ensure that University policies and principles survive leadership changes in management and on the Board of Regents. Ignorance of policy cannot be used to excuse noncompliance.

2. **The Task Force finds that the point of responsibility for compensation decision-making is inadequate, confusing, and poorly documented. The result is inadequate oversight.**

Recommendation: The Regents should clearly delineate the respective authority of the Regents, the President, and the chancellors in approving compensation decisions. They should also specify which decisions can be delegated, the conditions under which decisions can be delegated, and the review and approval process for delegated decisions. Compensation decisions should be regularly audited to ensure that they are being made and approved at the appropriate levels.

3. **The Task Force finds that UC grants so many exceptions to policy as to render the policies ineffective. Furthermore, these "exceptions" have become a convenient way to circumvent policies.**

Recommendation: Compensation policies should include specific guidance about when exceptions to policy are appropriate, who may grant them, and through which mechanisms. Exceptions should be subject to rigorous review and advance approval by the appropriate higher authority. To monitor compliance, all exceptions should be reported to a central office or individual.

4. **The Task Force finds few, if any, consequences for violating policy.**

Recommendation: Policies must specify consequences for violations of compensation policy. Violations should be reported annually to the Regents' Compensation Committee and, where appropriate, sanctions should be issued.

5. **The Task Force finds that UC's executive compensation problems are exacerbated by confusing, duplicative, overlapping and sometime conflicting compensation policies.**

Recommendation: UC should immediately eliminate any conflicts in its compensation and related governance policies and clarify precisely which policies apply to different groups of employees.

The Task Force identified weaknesses in UC's compensation policies that limit the University's ability to ensure compliance. Compensation policies are out of date, and many of them duplicate or conflict with one another. Various aspects of compensation are addressed, not always consistently, in Regents' policy, in Presidential policy, and in faculty policies. The University should immediately revise its policies to eliminate conflicts among the various policies.

6. **The Task Force finds that the Regents' ability to provide oversight of compensation decisions has been has been weakened by the large number of compensation decisions they were expected to review.**

The Task Force believes that approval by the Regents of compensation for the top 32 positions, a Board action recently adopted on an interim basis, is too limited to allow for appropriate Board-level oversight and accountability.

Recommendation: The Task Force recommends that the Regents retain direct authority to approve compensation for the President, senior vice presidents, vice presidents, associate/assistant vice presidents, the University auditor, the University controller, principal officers of the Regents, chancellors and vice chancellors, national laboratory directors and deputy directors, medical center CEOs, professional school deans, and the top five most highly compensated positions at each UC location. This group comprises 264 individuals.

Regent Kozberg noted that this recommendation is consistent with national standards set by the Securities and Exchange Commission in the post-Sarbanes-Oxley era.

7. **The Task Force finds that the University has an established whistleblower policy and should continue its education efforts regarding whistleblowers and ethical conduct.**

Recommendation: UC leaders should vigorously promote standards of ethical conduct and UC should continue to broadly communicate its whistleblower and anti-retaliation policies.

Regent Kozberg then turned to the section of the report entitled **Specific Policies and Practices**.

1. **The Task Force finds that UC lacks clear guidelines on participation in externally compensated activities such as consulting or board service, which makes it impossible to ensure that outside activities do not interfere with the performance of UC duties.**

It is common at UC and other universities for senior administrators and faculty to engage in a variety of outside professional activities, from serving on corporate boards or national commissions to consulting. The Task Force recognizes that these pursuits add value to the University and to the individual. In fact, existing Regents' policy encourages UC's senior executives to serve on non-profit boards and public commissions. These activities are often seen as an extension of senior executives' academic work and university leadership; they provide opportunities for senior leaders to engage with and serve their local communities; they extend UC's influence, reach, and usefulness to the national and international arenas; and they are consistent with the practices at other public and private universities.

Notwithstanding these benefits, the Task Force strongly believes that senior executives' service on *externally compensated* boards should be limited. Institutional Shareholder Services recently recommended that corporate executives should be limited to serving on three outside boards and that CEOs should serve on no more than two. In the three years since the Sarbanes-Oxley Act took effect, the national trend among CEOs seems to be going towards reducing board service.

Recommendation: The University should adopt specific limits on externally compensated activities to preclude conflicts of commitment on the part of senior executives. Based on leading best practices in governance from the public and private sectors, UC senior executives should be limited to serving on no more than three externally compensated boards.

2. **The Task Force finds that existing UC policies governing senior managers' outside professional activities vary from those for faculty. This creates confusion for senior managers who also hold faculty appointments.**

Recommendation: Policies governing outside professional activities and board service for senior managers who also hold faculty appointments should be revised so that the senior manager policy prevails.

3. **The Task Force finds that 1) UC executives have not followed University policies in granting paid leaves to departing chancellors and others; and 2) the Regents have not been properly informed at the time of appointment about the terms related to these leaves.**

The Task Force is concerned about the following practices:

- The practice of paying year-long "administrative leaves in lieu of sabbatical" at the higher administrative salary rather than at the faculty salary and finds that these arrangements were not disclosed to the Regents.

- The practice of "honoring" faculty sabbatical credits earned at a prior institution.

Recommendation: The University should carefully review its policies on "administrative leaves in lieu of sabbaticals" for senior managers who also hold academic positions, especially chancellors, and revisit the provision that these leaves be paid at the higher administrative salary rate rather than the faculty salary rate.

The University must also revisit the questionable practice of honoring sabbatical credits earned at other institutions to ensure it is in accordance with both the letter and the spirit of sabbatical policies.

Furthermore, the Regents should eliminate the practice of making payments, at the commencement of employment, to compensate for forfeited sabbatical credits accrued at other institutions.

Mr. Hertzberg discussed the final section of the report, which pertains to **Competitive Compensation**.

1. **The Task Force finds that UC's compensation must be competitive if UC is to maintain its status as one of the great universities of the world.**

   For UC to best serve the people of California, the Task Force believes that the University must remain in the top tier of the world's research universities. To maintain this level of distinction, it must be able to provide its faculty, administrators, and staff a level of compensation that is competitive with that offered by universities in its peer group.

2. **The Task Force finds that UC has entered a period of intense competition and that it is currently at a competitive disadvantage relative to most of its peers in the top tier of universities.**

   By and large, UC employees are not overpaid. The Task Force addressed at great length the issue of competitiveness.

   Recommendation: The Regents should implement, in a vigorous and sustained manner, their compensation philosophy emphasizing the importance of competitive compensation as a means to maintain the quality of academic, management, and staff personnel.

3. **The Task Force finds that the composition of UC's compensation program needs to be examined to assess its overall competitiveness.**

   Recommendation: The Regents should examine the composition of UC compensation to determine if the balance between cash compensation versus health and retirement benefits is optimal for recruitment and retention purposes. The Regents should approach this examination with the understanding that the underlying issues may differ among employee groups and that some issues are subject to the collective bargaining process.

4. **The Task Force finds that regular benchmarking is the best way to ensure that compensation is competitive.**

   Recommendation: The Regents should regularly benchmark the University's compensation against peer institutions to ensure that UC compensation remains competitive.

5. **The Task Force finds that the Regents' Compensation Committee is the lynchpin to ensure proper compensation accountability, oversight, and competitiveness.**

   Recommendation: The Regents' Compensation Committee should identify and address as quickly as possible the key compensation challenges facing the University today, including the difficulties of competing with better-funded institutions for employees and the sometimes competing demands of market, merit, and equity.

Conclusion

The Task Force believes it essential that the University's leadership carefully craft its compensation policies and practices, rigorously implement and enforce them, and hold senior leaders accountable.

UC needs a sea change in current policies and practices, as well as in a University culture long accustomed to using exceptions to work around inadequate or obsolete policies rather than establishing and ensuring compliance with clear guidelines. To institutionalize and sustain the Task Force's recommendations, the University must focus simultaneously on disclosure and transparency, governance and accountability, and competitive compensation.

The Task Force challenges the University to hold itself accountable to the public that supports it. In approaching the tasks laid out in this report, the University must articulate its goals publicly, embark on a process that is appropriately open, and communicate the results to the public, the Governor and the Legislature, internal stakeholders, and other interested parties.

The Task Force urges the Regents to authorize, in three years, a similarly constituted, independent body to review and report back on the University's progress in these areas.

The Task Force takes this strong stance in order to protect the institution that is the crown jewel of California's higher education system and the envy of every

other state as well as countless nations. The University is a vital positive force in the everyday lives of the people of California.

Chairman Parsky thanked the members of the Task Force for their findings and recommendations, noting that they had been asked to fulfill a broad and ambitious charge in a very short amount of time. They have served the University of California and the State well by working so quickly to produce recommendations that will help the University address its problems with regard to compensation policies and practices.

These recommendations build on steps the Regents have recently taken to improve disclosure, accountability, and oversight, beginning with more timely and complete reporting of compensation actions taken by the Board. In addition, these recommendations complement other proposals, such as the creation of an independent compliance officer position that would report directly to The Regents. The Board will assess how best to organize and staff the Office of the President in ways that will strengthen the business practices and management of the University. The goal is for the University's business practices and management to rise to the same quality as its academic excellence.

The Regents will begin to act on these recommendations at the May meeting. While there is a sense of urgency to correct policies and practices that never should have been allowed to continue, violating both the letter and the spirit of the 1992 principles for review of executive compensation, the Regents will be deliberate in adopting these recommendations. Chairman Parsky urged that decisions be informed not only by the Task Force findings but also by the PricewaterhouseCoopers audit and the Bureau of State Audits report. The Regents remain steadfast in their determination to establish the University of California as a national leader in business practices in order to support the primary missions of research, teaching, and public service.

Chairman Parsky inquired about the Task Force's finding that UC employees in general are not overpaid and asked about the source materials used to make this determination. The problems with business practices and lack of public disclosure have not allowed the Regents' discussions to focus enough on the issue of competitiveness. He recalled that suggestions had been made in Sacramento that UC salaries should use government agencies as benchmarks. He observed that the Task Force does not share this opinion.

Regent Kozberg explained that one approach would be to give the California Postseondary Education Commission greater ability to conduct compensation surveys as a disinterested third party. The University has performed its own benchmarking against a well-defined peer group for a number of years. She emphasized that government salaries may not provide the right benchmark as UC

competes in a national marketplace. Regent Kozberg noted that this topic should be addressed by the Special Committee on Compensation.

Regent Blum complimented the Task Force for its excellent report, which addresses most of the major concerns that have been raised. He pointed out that the University has a large legal staff and asked what their role had been with respect to compensation actions. Mr. Blum believed that the Office of the General Counsel should be reviewing each hiring contract to make sure they are in conformance with policy. With respect to any violations of policy, it was his view that they must be dealt with immediately. Regent Blum suggested that the benchmarking of salaries should be viewed in the context of losing faculty and executives to private institutions over compensation issues.

Regent Marcus reiterated the fact that compensation for senior management is not an issue. Rather, the report focuses on how to improve transparency. He believed that the comparison institutions used by the University to benchmark salaries were appropriate.

In response to a comment by Regent Blum, Mr. Hertzberg explained that the annual report on violations was intended to be a catch-all to ensure that nothing is missed. With respect to UC's competitiveness in a global marketplace, the Task Force looked at issues such as local housing costs and other considerations. The Task Force is mindful of the fact that, as the top-rated public university in the world, UC must remain competitive.

Regent Kozberg observed that while the University of California had experienced considerable growth over the past 50 years, it still has an old model of management. The Regents intend to work with the President to reorganize his Office to achieve effective and efficient management. Checks and balances will need to be put into place.

Regent Moores referred to the section of the report that addresses competitive compensation, noting that Mr. Hertzberg had commented that one reason for nondisclosure had been the University's desire to remain competitive when recruiting executives. Mr. Hertzberg responded that in many instances, the desire to recruit the best people had resulted in a breakdown in the system. Regent Moores observed that the University had a history of non-transparency, both to the public and to the Regents. He emphasized that every Regent recognizes that the chancellors and senior executive are highly gifted, including President Dynes and Senior Vice President Darling. Regent Moores stressed that these individuals are underpaid in comparison to prestigious private institutions such as the Ivy League colleges, and he criticized the Office of the President for not informing the public that many candidates will not consider senior positions at UC because it does not pay competitive salaries. He believed that the strongest

recommendation in the report was contained in the Deloitte Consulting document, which indicated a need to integrate many of the University's IT systems and business processes across the campuses.

Mr. Hertzberg observed that, in the section Disclosure and Transparency, the Task Force recommends that the University invest in a comprehensive, integrated human-resources information system. Because currently there is only a payroll system on the campuses, there is no ability to analyze across campuses. Regent Kozberg saw the need to consider what information needs to be centralized, because it is costly to invest in human-resources systems. As a result of outdated systems, it takes the University a long time to respond to public records requests.

Regent Juline referred to the recommendation that UC leaders should vigorously promote standards of ethical conduct and asked whether the concept was that the standards would also be enforced. Regent Kozberg noted that the University should continue its education efforts regarding whistleblowers and ethical conduct. Regent Juline believed that the University's educational efforts must be expanded to change the culture over time. Regent Kozberg acknowledged that people had not been educated about policies that they were expected to enforce.

Turning to the recommendation concerning the limitation of service on outside boards, Regent Juline asked whether these appointments would need to be approved and whether judgment would be exercised at the appropriate level. Regent Kozberg noted that because chancellors often enter the UC system with pre-existing commitments, outside board service must be discussed at the time of hiring. There will need to be procedures to limit service to the appropriate number of boards. She believed that the Special Committee on Compensation would pay particular attention to this issue. Mr. Hertzberg added that the intention would be to avoid a conflict of commitment.

Regent Ruiz believed that the language could have been stronger in some areas of the report. Circumstances require more than a slap on the hand; the Office of the President must change its attitude on how it will do business. There must be serious consequences if these issues are not addressed properly.

In response to a further question from Regent Juline, Chairman Parsky noted that at the May meeting a significant amount of time will be reserved for a discussion of the report, with members of the Task Force invited to attend. There will be an opportunity to take action in May if consensus is reached among the Regents. In the interim, the Regents will receive an audit report from PricewaterhouseCoopers. If individual Regents have specific requests for agenda items for the May meeting, they should communicate them to Regent Hopkinson as Chair of the Special Committee on Compensation.

Regent Rominger observed that it is common for organizations to designate an individual in the general counsel's office who has the responsibility to review policies, practices, and ethical standards with every new senior executive. There typically is an annual review of the policies.

Regent Moores stressed that none of the recommendations should come from the Office of the President. Chairman Parsky believed that the Office should be given an opportunity to comment on any actions that are proposed. Regent Moores commented that the Regents do not have independent staff to analyze these issues. Chairman Parsky noted that at the May meeting there would be comment with respect to the reorganization of the Office of the President. The issue of ensuring compliance with policy will also be addressed.

The meeting adjourned at 10:55 a.m.

Attest:

Secretary