UNIVERSITY OF CALIFORNIA ACADEMIC SENATE

UNIVERSITY COMMITTEE ON PLANNING AND BUDGET

Minutes of Meeting
October 7, 2014

I. Consultation with the Office of the President – Capital Projects

Nathan Brostrom, EVP/CFO and Interim COO

Update: EVP Brostrom reported that the model for financing capital projects is changing. The state has stepped back, and has not issued a General Obligation (GO) bond since 2006. A GO bond is unlikely this year as other bond measures are on the ballot. A GO bond may be possible in 2016, but allies in Sacramento and the other education segments need to be recruited. Lease-revenue bonds (LRBs) are issued by the legislature and carry a lower rating since they are subject to appropriations; the governor opposes additional LRBs at this time. UC has refinanced its LRBs, but some in Sacramento see only a wall of debt, no matter how well it is managed. Nonetheless, UC is near its debt capacity at its current credit rating. About $2.9B is available in AA general revenue credit. Medical center credit is rated AA-, and limited projects credit (for residential and dining facilities, e.g.) is rated AA. Unfortunately, about 8B in capital projects and improvements have been identified, so a new strategy is being developed. The new strategy may include components designed to:

1) Secure a GO bond on the 2016 ballot; UC would receive about 1B, with the rest going to K-12 and the other segments.

2) Use a portion of the state allocation to fund the most critical projects; UC can capture about 50M/yr in this manner by divvying up its block grants differently.

3) Explore greater use of other state sources of funds, such as Prop 39 or AB 32 funds; so far, all Prop 39 expenditures have gone to K-12 to shore up the Prop 98 guarantee. AB 32 funds are approximately 30B this year, and the total is expected to increase when transportation is added next year. AB 32 funds are not as flexible, but packaging improvements should be a workable option (HVAC upgrade in conjunction with seismic upgrades, for example).

4) Reorganize further internal asset management practices to free up capacity and reduce borrowing through:

- a) managing our own lines and refinancing limited projects and similar endeavors,
- b) moving some projects onto a single-A rating, which would lower coverage ratios,
- c) adding more variable rate debt to the portfolio while using STIP and TRIP to hedge against extreme fluctuations. This change would also allow UCOP to absorb high rates while passing the lower rates to the campuses.

5) Utilize new finance and governance structures to reduce UC liability and give vendors greater control over some projects; this option is more appropriate for commercial-type assets.

6) Reduce facility operating costs through space optimization, separate metering, and energy reduction.

7) Issue another century bond.

Discussion: Members asked who controlled AB 32 “cap and trade” funds, and EVP Brostrom indicated that both the legislature and the governor have some authority over the funds. Members also asked how UC’s cap and trade process was working, and EVP Brostrom said that so far, UC has been given waivers. Soon, UC will have to buy carbon allowances. He added that all AB 32 proceeds must go to increase energy efficiency, and not to the general fund.

Members then asked how a lower credit rating would impact UC. EVP Brostrom noted that some projects could see a higher cost, but that in aggregate, UC would benefit from the negligible rate gap between AA and A, which is currently only 20 basis points, and would benefit from freeing debt capacity. A preliminary estimate is that such a move could free up at least several hundred million in newly available funds. Projects funded in this way would have fixed interest rates.

Members next asked how STIP and TRIP could serve to hedge against variable interest rates. EVP Brostrom suggested that in an holistic balance sheet analysis, short-term assets can be used to cover the amount of variable rate debt.

Members asked what alternative revenue sources had been identified, given the state’s disinvestment trajectory. Members further wondered if cleverer asset management would free enough funds to meet UC’s needs. EVP Brostrom replied that a multi-faceted approach over a long time period is needed, and that campus real estate strategies can play an important part. Reducing lease expenditures, optimizing space per square foot, and metering electricity for departmental billing are all options under discussion.

Members suggested that the above strategies cannot address capital needs; EVP Brostrom concurred.

Finally, members recalled that the original discussions of this capital projects plan with Patrick Lenz had suggested that the base budget increase UC received last year for assuming some state obligations would be used for capital projects, and that this was presented as indicating a ceiling of approximately $10M in any one year for funding the finance charges for a program of approximately the size pursued in 2013/14. EVP Brostrom said that the deal with the state included some escalators, so it would not be appropriate to tie these funds to a fixed bond, thus suggesting that this was no longer viewed as the funding vehicle for this program.

II. Agenda Review and Announcements

Chair Leal

Update: Chair Leal reported on several items of interest from the Academic Council meeting of September 24:

- Governor Brown vetoed 50M in supplemental funding for UC. He also vetoed supplemental funding for CSU.
- The Regents in September approved the UC Ventures project.
- President Napolitano has appointed an Innovation Council consisting largely of venture capitalists.
- Several systemwide vice presidents will soon be or have recently retired: Steve Beckwith from Research and Graduate Studies, Patrick Lenz from Budget, Dan Dooley from External Relations, and Barbara Allen-Diaz from Agriculture and Natural Resources. A strategic operations review of the Office of the President continues.

- President Napolitano reported that her Mexico and Food Security Initiatives are gaining steam.
- President Napolitano will make a recommendation in November to the Regents on non-resident enrollments.

III. Consent Calendar

None.

IV. Consultation with the Office of the President – Budget

Patrick Lenz, Vice President (via phone)
Debbie Obley, Associate Vice President, Budget and Capital Resources

1. <u>15-16 Budget</u>

   Update: Vice President Lenz reported that spending assumptions were reported to the Regents last month and that revenue assumptions are still under development. The Governor's 5-5-4-4 plan assumed the University would not raise tuition, but UC never agreed. Worse, because the state funds only a portion of UC operations, the de facto budget increases were only 2.5-2.5-2-2; still worse, the first year's payment did not materialize, and the final two years' increases are now in doubt. Even if the promised funds do arrive, they are not adequate to cover costs absent additional revenue. Revenue option negotiations with the state continue on October 21, but there is a lack of agreement on priorities between the governor, the legislature, and the University.

   The expenditure assumptions include: (1) mandatory expenses (utilities, faculty merits) (approx. $200M), (2) high priority items (faculty COLAs, non-represented staff salary increases) (approx. $120-135M), (3) and reinvestment in academic quality (total remuneration for faculty and staff (approx. $50M), for a total of approx. $350-400M.

   The University also submitted 268M in capital projects to the Department of Finance. The specifics could change, and a final decision is not expected until the spring.

   Discussion: Members asked what the total spend would be for faculty COLAs, and AVP Obley replied that specifics were not available yet, but a $50M/yr investment over 4-5 years could accrue 250M for salaries; it is expected that campuses would be able to decide how to allocate their salary block locally. Members noted that some faculty could see their market competitiveness further erode depending on how funds are allocated locally, and noted that the salary scales have a long history and have driven UC's academic quality. AVP Obley noted that some assert that the scales are already nearly meaningless given the high numbers of off scale and above scale faculty. Members noted that the scales add transparency, which is useful at a public institution. Members further added that UC's policy of matching outside offers could discriminate against women and underrepresented minorities who typically have less freedom to relocate, and thus to pursue outside offers. Promotion by scale is peer-review merit driven; whereas salary negotiation with administrators is not subject to peer review and may be arbitrary. It was also noted that underperforming faculty are rare; previous studies place the number between 0.3-1% only. Nonetheless, some in the administration feel that automatic raises make it difficult to recognize outstanding faculty.

Members asked about the time frame for evaluation of the revenue assumptions. AVP Obley said the data would not be ready for 2-3 more weeks and suggested an off-cycle meeting to address them when they are final. Members noted that if the numbers are to be adopted by the Regents in November, that time frame does not allow for much consultation and revision. AVP Obley hinted that the revenue plans include continued cost savings from procurement and efficiency efforts, as well as aggressive philanthropic goals, which together could solve about 1/3 of the funding gap. Members speculated how the remaining 2/3 funding gap could be closed (see next item).

2. <u>3-year Sustainability Plans</u>

   Update: AVP Obley reported that the state has requested UC to generate three-year sustainable funding models; the models are not to include any tuition increases. The reports being developed will show two scenarios: one with no tuition increases that shows the resulting rollbacks in enrollment to funded levels only, along with other programmatic cuts and outcome impacts. A second report would illustrate the level of funding necessary to put UC back on solid fiscal footing vis-à-vis the state while maintaining and improving academics and the physical plant. The cost of instruction reports (see Item VII.2 below) will follow a similar pattern.

   Discussion: Members speculated if the University was prepared to back up calls for enrollment reductions or other drastic steps. It was observed that not all campuses are in a place to cull their unfunded students quickly. It was also suggested that a third plan should be assembled that indicates what UC really needs to address issues of quality, including total remuneration issues, rather than a plan that is limited to income projections based upon "potentially achievable" tuition increases. The latter leads to the dollar amount of $50M per year to address all issues of academic quality, which is viewed by some of the committee members as inadequate to address even the total remuneration problem, let alone other factors related to university quality.

V. Consultation with the Office of the President – Academic Affairs

Aimée Dorr, Provost

1. <u>Total Remuneration</u>

   With Susan Carlson, Vice Provost, Academic Personnel and Programs

   Update: Provost Dorr noted that the report shows clearly that circumstances have changed and that there are multiple variables in play. A plan for redress should only go to the Regents when it is final. Vice Provost Carlson added that she would meet with the EVCs next week to get their preliminary feedback. She noted that there are varying opinions among the vice chancellors regarding how much to spend for off scales and above scales.

   Discussion: Chair Leal asked if costs for various options could be modeled for evaluation. Provost Dorr added that a time line would also be necessary, since a multi-year plan would have different funding requirements. Vice Provost Carlson observed that a five year plan to close a 12% gap would require 400M plus benefits. Chair Leal noted that the 50M/yr available (see above) would not suffice. Vice Provost Carlson added that the EVCs all have different local priorities for the "quality" money.

Members asked if Academic Personnel tracked which faculty were more likely to receive outside offers. Vice Provost Carlson replied that the campuses stopped collecting that data a few years ago, and that the older data does not have breakdowns by discipline and such. It was observed that retentions are less expensive than recruitments. Members suggested a workgroup be formed with colleagues from UCFW and UCAP to evaluate carefully various options for planning a response to the Total Remuneration lag.

2. University-Industry Relations

With Bill Tucker, Interim Vice President, Office of Research and Graduate Studies

Update: Provost Dorr noted that this area too has many intersections, and that they are still being mapped out. President Napolitano is very enthusiastic about commercialization efforts: UC Ventures and the Innovation Council speak to this. At the same time, revised guidelines for university-industry relations are being edited, and a report on Conflict of Interest and Conflict of Commitment will soon be issued. At the Office of the President, a strategic operations review complicates the search for a permanent ORGS vice president as the new job duties are not yet known.

IVP Tucker spoke about creating an entrepreneurial environment at the University, as suggested in the Regents Report of the Working Group on Technology Transfer. In it, the Regents call for 1) improved communication, 2) streamlined processes, 3) more investment in individuals and technologies, and 4) more support for the process of commercialization. The immediate focus is on UC Ventures and the opportunities in our own back yards. UC already invests in various venture capital projects, and it makes sense to keep the money in-house as much as possible. UC can set its own metrics, direction, and time frames, and work to achieve a "double bottom line".

Discussion: Members noted a conflict in goals in the program: to make money and a strong return on investment or to create a new culture at the University. IVP Tucker indicated the goal of the Chief Investment Officer is to make money, but Chair Leal noted that President Napolitano at the Academic Council said the goal was to prime the pump. Provost Dorr noted that the President had stated both goals.

Members then asked about the replacement guidelines for university-industry relations. IVP Tucker said the rescission/replacement time lag was a simple accident. The review process started two years ago as part of a larger OP-wide policy review project, and in the mean time, other intersecting policies were enacted or amended. The revised guidelines are incorporating feedback from former Council Chair Jacob, and are being reviewed by contracts and grants, licensing, transaction managers, and the Technology Transfer Advisory Committee (TTAC). Provost Dorr added that the final version will have to cross her desk for approval. IVP Tucker noted that a 1996 policy frequently served as an exception to the equity prohibition, so the main changes from the rescission will impact incubators and accelerators.

Finally, members asked about the future of the Office of Research and Graduate Studies, noting that "Graduate Studies" seem to be left off the list of new projects and initiatives. Provost Dorr noted again that the President wants to elevate innovation, and that the reorganization question is about where to place graduate studies, not whether to include them. The strategic review should be complete by the end of the calendar year, so a new job description will follow thereafter.

VI. Consultation with Academic Senate Leadership

Mary Gilly, Academic Council Chair
Dan Hare, Academic Council Vice Chair

Update: Chair Gilly updated the committee on several items of interest:

- Academic Council meeting of September 24: President Napolitano agreed to more meetings with Senate leadership. The third ILTI RFP is forthcoming. The Regents in January will hear recommendations on doctoral student support, including non-resident supplemental tuition, stipends, and expanded professional development opportunities.
- Regents meeting of September 17-18:
    - The sexual assault task force presented their findings, and the Senate will be included in the next round of discussion and planning. One of the recommendations is for greater faculty sensitivity training; academic accommodation is a new issue.

      Discussion: Members noted that a stand-alone training on this issue might be valuable, even though the training onus has been lamented.
    - The lack of state support was discussed again, but the governor was absent. Of particular concern was the differential treatment between UC and CSU regarding retirement contributions. Some in Sacramento think that UCRP is more generous than CalSTRS and so does not deserve matching state support. Vice Chair Hare clarified that the provisions are largely similar, but CalSTRS has a lower compensation cap.

      Discussion: Members noted the importance of arriving at a saleable and yet meaningful Total Remuneration recommendation. How to arrive at such a recommendation is unclear: because the topic has been extensively discussed in recent years, there may not be many new ideas available regarding balancing on-scale versus off or above scale percent increases, minimizing disciplinary discrepancies, compensating for the loyalty penalty, etc.
    - The Innovation Council is expected to meet only three times per year, but they are establishing five working groups. The Senate has been invited to participate on two: Climate of Entrepreneurship and Rewards and Recognition. Senate participation has not been solicited for groups working on communications, streamlining processes, or evaluating investment options.

VII. Enrollment Management

Debbie Obley, Associate Vice President, Budget and Capital Resources
Todd Greenspan, Director, Institutional Research and Academic Planning

1. <u>Long-range Enrollment Planning</u>

Update: AVP Obley reported that her office was recently asked for more time by the campuses to revise their submissions; the current numbers are 1.5 years old. The revised numbers must be received by January for the 2015-16 allocations, and the campus requests will be merged with system goals to present a Universitywide plan.

Director Greenspan noted that there is not yet a cap on non-resident students, neither for the system nor for individual campuses. He added that the "compare favorably" standard may inhibit non-resident growth at some campuses. He stated that the current estimates for California residents are based on participation rates, not eligibility rates, especially as the state has consistently underestimated the number of Latino high school graduates for the past several years. It might also be necessary to disaggregate graduate student categories for more careful planning. AVP Obley noted that the average non-resident enrollment rate at AAU schools is 26%, while Berkeley and UCLA have only 22-23% in their most recent Freshman classes, and some campuses enroll as few as 4% non-residents. A cap on non-resident enrollments could be either for the system or by campus.

Discussion: Members noted that UC's statistics are muddied by having multiple AAU campuses, where other states have only one. Members speculated whether declining numbers for academic PhD students were attributable to poor financial support or less qualified applicants. AVP Obley noted that a balanced plan was unlikely to address all issues in a short-to-mid time frame. Members observed that a systemwide cap could freeze current non-resident distribution levels. AVP Obley reminded members that the agreed upon principles state that all campuses participate in the solution with regard to California resident enrollment. Members wondered if a "cap and trade" system could work for non-resident students, or if a cap could include escalators for out-years. What the overall rate of enrollment growth should be, though, is also a point of contention, given the current state of state support. Moreover, internal trade-offs are more complicated now that funding streams is policy, and the non-resident retention rate could benefit from additional analysis. The committee seeks more data upon which to base an opinion.

2. <u>Cost of Instruction</u>

   With Pamela Brown, Vice President, Institutional Research and Academic Planning

   Update: VP Brown reported that her office is not using the CSU report as a model, but is employing a blend of methodologies to arrive at the cost of instruction. Or rather, the cost of support for instruction, not the actual cost of instruction. Data will be divided into two categories, one narrowly defined to reflect costs directly associated with instruction (faculty salaries, physical plant maintenance, etc) and another broadly defined to capture costs associated with the "undergraduate experience" (intramural athletics and student health, for example). The narrow category has historically hovered around 16-18K. Partly, the final number includes a political calculation to adjust for saleability in Sacramento and the press.

   Discussion: Members asked if the weightings were different for graduate and undergraduate students. AVP Brown indicated that while full weights have yet to be determined, one idea was to include a portion of HSCP Y component in health sciences graduate student weightings to better reflect the differential cost of instruction.

VIII. Further Discussion

1. UCLA School of Music Preproposal
   Action: Members will confer with their campuses and report concerns electronically.
2. Investment Strategy
   Note: Item deferred.

Meeting adjourned at 3:55 p.m.

Minutes prepared by Kenneth Feer, Principal Analyst
Attest: L. Gary Leal, Chair