

The Regents of the University of California

**COMMITTEE ON FINANCE**

November 19-20, 2008

The Committee on Finance met on the above dates at UCSF–Mission Bay Community Center, San Francisco.

Members present: Regents Blum, Garamendi, Gould, Hopkinson, Island, Kozberg, Scorza, Varner, Wachter, and Yudof; Advisory members Bernal, Nunn Gorman, and Croughan; Staff Advisors Abeyta and Johansen

In attendance: Regents Cole, De La Peña, Hotchkis, Johnson, Makarechian, Marcus, Pattiz, Ruiz, Schilling, and Shewmake, Regent-designate Stovitz, Faculty Representative Powell, Secretary and Chief of Staff Griffiths, Associate Secretary Shaw, General Counsel Robinson, Chief Investment Officer Berggren, Chief Compliance and Audit Officer Vacca, Interim Provost Grey, Executive Vice Presidents Darling and Lapp, Senior Vice President Stobo, Vice Presidents Beckwith, Broome, Dooley, Foley, Lenz, and Sakaki, Chancellors Birgeneau, Fox, and Kang, and Recording Secretary Johns

The meeting convened at 11:20 a.m. with Committee Chair Gould presiding.

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

Upon motion duly made and seconded, the minutes of the meetings of July 16 and September 18, 2008 were approved.

2. **AUTHORIZATION OF LEASES AND AGREEMENTS FOR VARIOUS STATE CAPITAL IMPROVEMENT PROGRAMS**

The President recommended that, subject to adoption by the State Public Works Board of a resolution authorizing the issuance of State Public Works Board (SPWB) Lease Revenue Bonds and authorizing interim loans from the State's Pooled Money Investment Account or General Fund for the following projects:

Berkeley campus

*Biomedical and Health Sciences Building*

Davis campus

*Veterinary Medicine 3B*

*California Animal Health and Food Safety Laboratory, Tulare/Fresno*

Los Angeles campus

*Hershey Hall Seismic Renovation*

Riverside campus  
*Environmental Health and Safety Expansion*

San Diego campus  
*Management School Facility Phase 2*

Santa Barbara campus  
*Arts Building Seismic Corrections and Renewal*

- A. The President or the Secretary and Chief of Staff be authorized to:
- (1) Execute an unsubordinated site lease from The Regents to the SPWB for each project named above, said lease to contain provisions substantially as follows:
    - a. The site shall comprise the approximate size of the footprint for each building named above. Said lease shall also include a license to the SPWB for access from campus roads to the site during the term of the lease.
    - b. The purpose of the lease shall be to permit construction of the project.
    - c. The term of the site lease shall commence on recordation of the lease or the first day of the month following the meeting of the SPWB at which the resolution is adopted authorizing the lease, the issuance of bonds, and interim financing for the project, whichever is earlier, and shall terminate on the date the bonds issued by the SPWB are paid in full, subject to earlier termination if such bonds have been retired in full.
    - d. The rental shall be \$1 per year.
    - e. The Regents shall have power to terminate the site lease in the event of default by the SPWB, except when such termination would affect or impair any assignment or sublease by the SPWB and such assignee or subtenant is duly performing the terms and conditions of the lease.
    - f. The Regents shall provide to the SPWB and any assignee of the SPWB access to the site and such parking and utility services as are provided for similar facilities on the campus.
    - g. The Regents shall waive personal or individual liability of any member, officer, agent, or employee of the SPWB.



- e. In consideration for occupancy during the term of the lease and after the date upon which The Regents takes possession of the facility, The Regents shall pay base rent in an annual amount sufficient to pay debt service on the bonds or other obligations of the SPWB issued to finance or refinance the facility and additional rent for payment of all administrative costs of the SPWB.
- f. The Regents covenants to take such actions as may be necessary to include in the University's annual budget amounts sufficient to make rental payments and to make the necessary annual allocations.
- g. During occupancy, The Regents shall maintain the facility and pay for all utility costs and shall maintain fire and extended coverage insurance at then current replacement cost or an equivalent program of self-insurance, and earthquake insurance if available on the open market at a reasonable cost.
- h. During occupancy, the Regents shall maintain public liability and property damage insurance, or an equivalent program of self-insurance, on the facility and shall maintain rental interruption or use and occupancy insurance, or an equivalent program of self-insurance.
- i. In the event of default by The Regents, the SPWB may maintain the lease whether or not The Regents abandons the facility and shall have the right to relet the facility, or the SPWB may terminate the lease and recover any damages available at law.
- j. The Regents shall be in default if the lease is assigned, sublet, or transferred without approval of the SPWB, if The Regents files any petition or institutes any proceedings for bankruptcy, or if The Regents abandons the facility.
- k. The Regents shall cure any mechanics' or materialmen or other liens against the facility and, to the extent permitted by law, shall indemnify the SPWB in that respect.
- l. The Regents, to the extent permitted by law, shall indemnify the SPWB from any claims for death, injury, or damage to persons or property in or around the facility.
- m. Upon termination or expiration of the lease, other than for breach or because of eminent domain, title to the facility shall vest in The Regents.

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

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

3. **UNIVERSITY OF CALIFORNIA FINANCIAL REPORTS, 2008**

The President recommended that the Regents adopt the University of California Annual Financial Report 2007-2008 and the June 30, 2008 audited financial statements for the University of California Retirement Plan, including the Public Employees' Retirement System Voluntary Early Retirement Incentive Program (PERS-VERIP); the University of California Retirement Savings Program, including the Defined Contribution, 403(b) and 457(b) Plans; and the University of California Health and Welfare Program, including the retiree health benefit trust and the five University of California Medical Centers.

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

Assistant Vice President Plotts began his presentation with a brief summary of the University's financial position as of June 30, 2008. The University had assets of almost \$42 billion, approximately \$900 million more than the previous year; liabilities of almost \$20 billion, \$1.15 billion more than last year; and net assets of slightly more than \$22 billion, \$243 million less than in 2007. In 2007, operating results showed an increase in net assets of slightly more than \$2 billion; this represents a year-to-year change of \$2.24 billion.

Mr. Plotts pointed out two factors that explained most of the change between 2007 and 2008. First, the value of investments in 2008 declined by \$192 million. He compared this to the appreciation in the value of investments in 2007 of \$949 million, a year-to-year change of \$1.14 billion. Second, there has been a change in the financial reporting rules for retiree health benefits. Governmental Accounting Standards Board (GASB) Statement 45 requires that the University spread the cost of retiree health care over the employee's years of service. This resulted in the University recording an expense of \$1.35 billion in 2008; under the previous rules, this had been an expense of \$175 million, a year-to-year change of \$1.18 billion in additional expenses. The change in the value of investments (\$1.14 billion) and the retiree health expense (\$1.18 billion) together total \$2.32 billion and account for most of the year-to-year change in net assets.

GASB 45 also requires that, to the extent that the University does not fund the retiree health benefit expense, it must record a liability in its balance sheets. This results in a new liability of \$1.08 billion for UC this year and accounts for most of the total \$1.15 billion increase in liability over the previous year. Last year there was no liability under the old accounting rules.

Turning to assets, Mr. Plotts noted that investments increased by \$600 million in 2008, but that the category of “other liabilities” increased by \$691 million. He explained that this was related to the timing of the July 1 payroll. The investment of cash collateral decreased by \$1.3 billion due to a declining demand at the end of the year by borrowers in the securities lending program. There is a corresponding \$1.3 billion decrease in securities lending collateral. Net capital assets grew by \$1.48 billion, accounted for by capital expenditures of \$2.6 billion and a depreciation expense of \$1.1 billion. The category of “other assets” increased by \$138 million.

In liabilities, UC’s debt in 2008 was \$10 billion. It increased by \$661 million from 2007. The obligations for retiree health, \$1.1 billion, now represent 6 percent of the University’s liabilities. This will grow under the University’s pay-as-you-go funding method.

Mr. Plotts noted two details in net assets. The amount invested in capital assets, net of related debt, increased by \$933 million. He accounted for this by the \$1.5 billion net increase minus the \$600 million increase in debt. This represents the University’s continuing investment in facilities. Unrestricted net assets declined by \$1.14 billion, mostly accounted for by the retiree health benefit expense recorded this year.

Operating revenues were \$15.45 billion, relatively flat compared to the previous year. The University lost \$1.14 billion in Department of Energy laboratory revenue with the termination of the contract for Lawrence Livermore National Laboratory (LLNL). Revenue in other categories closely offset this loss. Operating expenses increased by \$1.44 billion over the previous year. Expenses declined with the loss of the LLNL contract by \$1.13 billion, but other expense categories increased to offset this, including the retiree health benefit expense.

Mr. Plotts observed that the University will always show an operating loss because State educational appropriations are recorded as non-operating revenues. Non-operating revenues declined by \$926 million from the previous year. This decline is explained by the change in the fair value of UC investments. The category of “other changes in net assets” includes State capital appropriations and capital gifts and grants. The University received \$101 million more in State capital appropriations in 2008 than in 2007.

The campus foundations combined have assets of \$5 billion, liabilities of \$576 million, and net assets of \$4.47 billion. Net assets increased by \$100 million over the previous year. The increase in net assets is accounted for by operating revenues, primarily private gifts, of \$537 million; by grants to campuses of \$540 million; by non-operating revenues, such as investment income, of \$66 million, slightly down from 2007; and new permanent endowments of \$180 million which offset the \$143 million depreciation in the fair value of investments.

Mr. Plotts then presented a summary of the UC Retirement System (UCRS), comprising both the Defined Benefit Plan and the Defined Contribution Plan. UCRS net assets were \$56.18 billion in 2008, a decline of \$6.46 billion from the previous year. He analyzed this

decline. There were contributions of \$1.03 billion, predominantly in the Defined Contribution Plan, including employees' 403(b) contributions; investment income of \$1.88 billion, with a depreciation in the value of investments of \$4.98 billion; benefit payments and withdrawals of \$2.84 billion; and a non-recurring transfer of plan assets to the Lawrence Livermore National Security defined benefit plan of \$1.57 billion. All together this accounts for the \$6.46 billion decrease in net assets.

The new UC Retiree Health Benefit Trust, formed on July 1, 2007, has assets of \$53.4 million, consisting of investments of almost \$20 million, receivables of \$19 million, and prepaid insurance premiums of \$15 billion; liability of \$2.6 million; and net assets of \$50.8 million. During the last year there were contributions of \$243 million. This consisted of \$226 million from the University, including a one-time \$20 million contribution for working capital; \$17 million from retirees; and almost \$700,000 in investment income. Deductions consisted almost entirely of insurance premiums of \$193 million. This accounted for the increase in net assets of \$50.8 million.

Regent De La Peña asked if the \$1.35 billion change due to GASB 45 would occur only this year or would be repeated in coming years. Mr. Plotts responded that this expense would not be repeated. He explained that the \$1.35 billion expense is to be spread over employee years of service. GASB does not require funding of that expense; the University funds on a pay-as-you-go basis. The liability on the University's balance sheet will grow; each year the expense will be approximately \$1.35 billion to \$1.5 billion. He noted that this topic would be discussed comprehensively later in the meeting.

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

#### 4. **ANNUAL DEBT CAPITAL REPORT FOR FISCAL YEAR 2007-08**

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

Vice President Broome began her presentation by noting that the University had \$7.3 billion in outstanding debt as of June 30, 2008. She pointed out that the University is using new credit instruments as part of a long-term debt strategy to maximize capacity and minimize cost of debt, while older, less advantageous types of credit are being phased out, either through maturities or refunding. UC's average cost of capital is 4.48 percent.

Credit markets tightened in fiscal year 2008. There was a collapse of municipal bond insurers, which resulted in credit rating downgrades. There was also a collapse of the auction rate market. The University's credit ratings were upgraded by Moody's Investors Service, which reflects UC's strong financial position, its self-liquidity, and the management of the University.

During the year, the University issued \$1.2 billion in debt in new money and refinancing. Debt issuance of new money occurred on October 30, 2007 and January 31, 2008. On October 30, limited project revenue bonds were issued; on January 31, general revenue bonds were issued. On July 26, 2007 the University refunded \$197 million for UCLA, placing old, higher-rate debt into lower-rate debt in pooled revenue bonds. On April 23, 2008, auction rate bonds at UC Davis were refunded into pooled revenue bonds at terms favorable to the campus.

Ms. Broome then discussed market developments since the end of fiscal year 2008. There has been a severe dislocation of financial markets, extreme volatility, and short- and long-term credit markets have frozen. She recalled that, in July 2008, the Regents authorized an expansion of the University's commercial paper program. This is now taking place. Ms. Broome opined that the University is well positioned to weather the financial crisis, given its significant liquidity and strong credit ratings. She anticipated further new money debt issuance in the first quarter of the coming year, if conditions are favorable.

Finally, Ms. Broome discussed a chart showing the University's additional debt capacity over the next five years if it maintains its core credit rating at AA, or if it allows the limited project revenue bonds to drop to an A rating. She emphasized that this was a market view of capacity, not a campus-by-campus view.

President Yudof asked what the current debt capacity is in aggregate for the ten campuses and the Office of the President. Ms. Broome provided ranges for the University's debt capacity if it maintained its core general revenue bonds at a rating of AA and allowed its limited project revenue bonds to drop to an A rating, and its debt capacity if all bonds were kept at the AA rating.

President Yudof observed that the University's capacity for issuing bonds is not in question, but that the difficulty lies in the distribution and total magnitude of debt service. In the current unsettled markets the University must exercise caution in making a large bond offering. Even entities which are good credit risks are having trouble marketing their bonds.

Committee Chair Gould advised that the University should use its debt capacity very judiciously.

5. **ANNUAL REPORT OF EXTERNAL FINANCE APPROVALS FOR CAPITAL PROJECTS FOR THE FISCAL YEAR ENDING JUNE 30, 2008**

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

Vice President Lenz noted that the total for external finance approvals for capital projects for fiscal year 2007-08 was approximately \$1.254 billion for 33 projects.

6. **REVISED FISCAL YEAR 2008-09 BUDGET FOR THE OFFICE OF THE PRESIDENT AND UPDATE ON ONGOING RESTRUCTURING INITIATIVE**

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

Executive Vice President Lapp recalled that the 2008-09 budget for the Office of the President (UCOP) was presented to the Regents in March and approved in May. It included a 20 percent reduction in expenditures, or \$51.6 million, and a 23 percent reduction in FTE, or 405 FTE. Some reductions were in fact transfers of FTE out of the Office of the President. Review and assessment of UCOP continued after President Yudof's arrival.

Ms. Lapp recalled key elements of the UCOP restructuring initiative. Across-the-board reductions of ten percent were presented in May 2008. Programs were identified which were located at UCOP but better suited to the campuses. The most significant of these was the Continuing Education of the Bar program, which has been transferred to UCLA, in consultation with the UCLA School of Law. UCOP also undertook the Voluntary Separation Program, in which 155 employees participated, leaving by June 30. Sixteen of these individuals found jobs on campuses. UCOP reviewed the 155 vacant positions and made the decision to replace 80 of them. Ms. Lapp pointed out that most of the positions that were replaced were re-purposed to be more effective. There are currently 110 vacancies at UCOP. Seventy-five positions were eliminated. The first-year savings at UCOP, after payment of severance, was \$800,000. She anticipated that next year's savings will be approximately \$5 million.

UCOP then carried out a series of consolidations, identifying ways to merge units and save money in the administrative and business functions. All desktop support has been consolidated into one technology services unit. A budget office for UCOP has been created, bringing together seven employees who were previously scattered throughout the organization. Ms. Lapp anticipated resulting FTE savings of over 12. Business services have now been consolidated into one unit and this may bring about a reduction in headcount of 100. Communications are consolidated under Interim Senior Vice President Dooley. An institutional research unit is being created to maintain UCOP data for the President and policymakers. Legislative and policy analysis is also being consolidated in one unit which will report directly to the President. Significant savings are anticipated as a result of these consolidations. In addition, UCOP is continuing department-by-department reviews to determine low-priority activities which can be eliminated.

Ms. Lapp explained that headcount and expenditures were adjusted in the May budget, removing FTE and expenditures already supported, such as payroll work done at UCOP for the campuses and paid for by the campuses. President Yudof asked that these activities be returned to the unadjusted budget, which shows an increase in headcount of approximately 100. This different presentation does not change the reductions that were made. Since fiscal year 2007-08, UCOP FTE have been reduced by 27 percent, or approximately 501 positions. Forty-five percent of those reductions were the result of

transfers; the rest were due to the Voluntary Separation Program, 120 vacancies, and 78 layoffs. UCOP has offered support and outplacement services to employees who have been laid off. Further layoffs are anticipated at the end of January and March 2009. Since fiscal year 2007-08, the UCOP budget has been reduced by 21 percent, or \$60.5 million. This is an additional \$8.7 million reduction beyond that reported in May.

Ms. Lapp then distinguished between restricted and unrestricted funding. Thirty-eight percent of UCOP savings, \$23 million, are in unrestricted funds, which can be used to offset cuts at the campuses. There are \$37 million of savings in restricted funds, which can serve the programmatic needs of UCOP units.

Looking to the future, Ms. Lapp expressed the intention of UCOP to continue to reduce its budget and to achieve an overall reduction of 30 percent between 2007-08 and 2009-10. Reductions can be made not only in personnel, but also in non-personnel budget items, such as travel, consulting, and professional services. Controls have been implemented to curtail unnecessary travel and purchasing and to ensure that consultants are used at a minimum. UCOP seeks to reduce its FTE to approximately 1,100, a 43 percent reduction from 2007-08.

Regent Hopkinson noted references to appropriations requests for UCOP in the materials provided; in one instance a request for \$203 million and in another a request for \$230 million. Ms. Lapp explained that these amounts were related to the adjusted and unadjusted budgets. The adjusted budget in May removed some of the headcount and restricted funding. The dollar reduction from the budget is the same.

In response to a question asked by Regent Hopkinson, Ms. Lapp confirmed that the total budget reduction is ten percent.

Regent Hopkinson expressed serious concern about the use of the Voluntary Separation Program and continuation of the program as now designed. She observed that more than 50 percent of those who participated in the program were employees who will be replaced. There were approximately 80 positions for which UCOP will have to rehire, while 78 additional layoffs are expected. She questioned the moral justification for paying individuals to leave positions which will require rehiring. She would have preferred that the money be used only for positions the University decides to eliminate, rather than for a voluntary program.

Ms. Lapp noted that the deadline for the Voluntary Separation Program expired last year; there is no ongoing program. Many vacancies replaced at UCOP were re-purposed and have changed, with new job descriptions. She emphasized that, even if positions are re-purposed, they may still be eliminated.

President Yudof acknowledged that the restructuring process at UCOP has produced stress and anxiety for employees. He praised Ms. Lapp for her work. He expressed the hope for greater stability at UCOP in the future and for an improvement of morale. He outlined some of the reasons for re-purposing. UCOP had operations which were not

adding value and employees without the required skill sets. He suggested that this process is more revolutionary than it appears. It is not only a matter of financial savings, but functionally, UCOP is becoming a different organization.

Regent Scorza asked about the criteria used to determine which departments have value and need more or fewer personnel. He asked about the effect on campuses when certain UC activities are decentralized. Ms. Lapp responded that the activities of each unit are reviewed in order to determine whether they meet UCOP priorities. This process continues on a regular basis. The decisions are made by the President, informed by the vice presidents, provost, and others. In response to the second question, she stated that UCOP wishes to minimize any effect on the campuses. The campuses are currently benefiting from reductions at UCOP. UCOP is discontinuing activities which can be carried out on the campuses. In the longer term, UCOP will consider the effect on campuses if it reduces its activities even further.

Regent Scorza asked about the impact on academic and student affairs and about the community college transfer coordinator position. President Yudof responded that UCOP is actively examining this issue. He stated that the community college transfer coordinator position will be upgraded. He echoed Ms. Lapp's statement that many of the reductions at UCOP are in fact a way of getting out of the way of campuses; they result in less bureaucracy and appointments are not delayed. He stated that proposals are being prepared to improve the oversight of outreach activities aimed at K-12 and the community colleges and to improve the institutional research function. He observed that this evaluation cannot be carried out by the Board, but must be done office by office. The Academic Senate is involved in this process. He anticipated that academic positions will come under further scrutiny, since the business functions are those that have been reduced the most.

Regent Scorza expressed concern about possible loss of students and asked that campus communities be given appropriate information about UCOP actions.

Committee Chair Gould praised the presentation for its transparency and for its clarification of restricted and unrestricted resources and the net benefit to campuses. He asked that this be included in future presentations.

Regent Island expressed appreciation for the work done by Ms. Lapp and her team. He reminded the Committee that while they should be concerned about the goals and results of restructuring, they should not be involved in details of this work. Such interference would only impede the work of UCOP staff, especially in a climate of change and layoffs.

President Yudof introduced Ms. Lucero Chavez, president of the UC Student Association (UCSA).

Ms. Chavez began her presentation by reporting that UCSA succeeded in registering more than 40,000 students statewide to vote. She acknowledged the assistance of the

Office of the President and the campuses in this effort. She informed the Regents that UCSA's annual student of color conference would take place the following weekend at UCLA. More than 900 students have registered.

Ms. Chavez referred to the proposed freshman eligibility policy reforms and expressed the students' wish to participate in the discussion of long-term policy reform. She emphasized the importance of access for students. She applauded the University for completing contract negotiations with hospital workers and urged it to complete similar negotiations with service workers.

Ms. Chavez then discussed budget issues. She noted that students currently pay up to one-third of the cost of their education, not including cost of living and health insurance. Seven years ago students paid one-fifth of this cost. She recalled that the Governor's Compact with the University included a promise that student fees would not have to be raised to offset budget cuts and she expressed the hope that the University would continue this in the coming year. She expressed concern about reductions in student services.

Ms. Chavez reported that many students are unable to find sufficient loans and aid to offset continued fee increases. At the same time, there has been a decrease in the quality of a UC education, with larger class sizes and fewer sections available to students. She also emphasized that rising student fees have a negative impact on diversity at UC. She asked the University to partner and dialogue with UCSA.

Regent Garamendi stated that students are one of the University's most valuable assets in dealing with budget issues and in presenting its case to the Governor, Legislature, and public. He thanked the students for their involvement.

7. **APPROVAL OF UNIVERSITY OF CALIFORNIA 2009-10 BUDGETS FOR CURRENT OPERATIONS AND FOR STATE CAPITAL IMPROVEMENTS**

The President recommended that:

- A. The Committee on Finance recommend to the Regents that the expenditure plan included in the document, *2009-10 Budget for Current Operations*, be approved.
- B. The Committee on Finance concur with the recommendation of the Committee on Grounds and Buildings to the Regents that the *2009-2010 Budget for State Capital Improvements* be approved.

[Background material was mailed to Regents in advance of the meeting, and copies are on file in the Office of the Secretary and Chief of Staff.]

Committee Chair Gould noted the precarious financial circumstances California finds itself in and the question of the State's ability to pay bills and provide resources for essential programs. He emphasized this as the context for the University budget proposal.

Vice President Lenz recalled that the Governor signed a 2008-09 State budget on September 23, including \$24.3 billion in budget solutions. These solutions included reductions, some small revenue increases, and re-alignment of programs. The budget was assumed to be balanced with a \$1.7 billion reserve. However, dramatic change in the federal and State economies has changed revenue and expenditure assumptions. The Governor has called a special session of the Legislature, which will have until the end of November to act on his recommendation. The California Department of Finance estimates the State's revenue shortfall at \$24.2 billion over the next 20 months. The Legislative Analyst's Office estimates the shortfall to be closer to \$28 billion over the same period.

The Governor's special session budget recommendations include a request for \$4.7 billion in additional State General Fund revenue, \$4.5 billion in additional spending reductions, and no additional borrowing. The proposed \$4.5 billion reduction includes severe cuts to health and human services programs. Mr. Lenz pointed out the proposed cuts to higher education – \$2.5 billion for K-12, \$332 million for the community colleges, \$66.3 million for the California State University (CSU), and \$65.5 million for UC. This \$65.5 million is in addition to the \$33 million reduction the University absorbed at the end of the budget process. At the present time it is unclear if the Governor would have the necessary two-thirds majority to enact these special session recommendations.

This is clearly a multi-year problem. The Legislative Analyst's Office has indicated that, unless there is some corrective action, California may be faced with an annual budget deficit of \$22 billion through fiscal year 2013-14. If the State is unable to enact some mid-year budget solutions to address the deficit, the Governor will be forced to propose significant reductions in the 2009-10 budget which will have a severe impact on UC. In addition, without resolution by the Legislature, the State will be unable to pay its bills and will run out of cash by February 2009.

Mr. Lenz recalled that the Regents approved the final 2008-09 UC budget of \$5.36 billion four weeks previously. The University received no funding from the State for enrollment growth, health benefit increases, graduate student support, purchased utility deficits, salary commitments, academic merit increases, or funding for a buyout of the student fee. The net reduction for campuses, with the exception of the faculty salary plan, which will go unfunded in 2008-09, is \$148.7 million. If the Governor's special session recommendations are adopted, the campuses will have to absorb the additional \$65.5 million reduction.

Mr. Lenz noted that President Yudof has already requested that campuses make their best effort to protect instructional programs, but he has advised campuses to consider options such as implementing a hiring freeze, curtailing non-essential travel, reducing the amount of leased space, limiting the number of consulting contracts, deferring the purchase of equipment, expanding energy cost savings, initiating Staff and Academic Reduction in Time (START) programs for employees to work at less than 100 percent time, and other administrative efficiencies.

Mr. Lenz then presented a chart showing that approximately 70 percent of the University's operating budget covers compensation and health benefits for employees. Another chart displayed how the University has experienced a drop in inflation-adjusted spending per student over the last 18 years. During this period, State funds per student have declined by more than 40 percent. Increases in student fees have made up some but not all of the decline. Students now pay about 30 percent of the cost of their education.

Committee Chair Gould cautioned that delay by the Legislature will result in a more severe impact on the University in the coming year. The University should encourage the Legislature to work with the Governor to come to a prompt and sound decision. Absent such quick action, the University will be more vulnerable next year.

Regent Garamendi observed that this year's budget is affected, as well as the 2009-10 budget. He did not anticipate action during the current legislative session, which ends this month. He described fee increases for students as a tax increase and the only significant revenue increase. He emphasized that the budget deficit will continue for five years or more. He urged the Regents to take a strong stance that additional cuts in education are not appropriate. The University must convey the message that significant reform is taking place at UC. He described the accountability program established by President Yudof as extremely important.

Regent Hopkinson noted that the current circumstances are very discouraging, with a negative effect on the children of California. She stated that the University must face the reality of State funding and recognize that this problem will not be fixed by the State. She recalled that last year, the University issued a warning that if enrollment growth were not funded, it would not be able to admit new students. While such an action is difficult to contemplate, it must be seriously discussed. She also noted that the budget proposal examines only a little over \$5 billion of the University's expenditures; the University should consider the whole budget and seek creative solutions.

Committee Chair Gould noted that the proposal focuses on a subset of the budget.

Mr. Lenz explained that the entire budget was examined. He noted, in the materials provided, an outline of all revenue available to UC and the purpose of that revenue. He noted that some of the revenue is restricted. There may be creative ideas for the use of revenue, but Mr. Lenz stated that the Regents would have to receive a report on how revenue is currently used and then make a decision about re-directing it. He described the situation as a zero-sum game.

Regent Pattiz concurred with Regent Hopkinson that the University needs to make difficult decisions, and the sooner it does so, the better. He referred to the recent decision by the CSU Board of Trustees to limit enrollment. He suggested that the University can put pressure on the Legislature by some of the actions it may be forced to take.

















































