

Office of the President
November 6, 2003

TO MEMBERS OF THE COMMITTEE ON FINANCE:

ITEM FOR DISCUSSION AND ACTION

For Meeting of November 19, 2003

**DISCUSSION OF THE UNIVERSITY OF CALIFORNIA 2004-05 BUDGET FOR
CURRENT OPERATIONS AND APPROVAL OF PRINCIPLES FOR DETERMINING
PRIORITIES FOR THE 2004-05 BUDGET**

The President recommends that the Committee on Finance recommend to The Regents that the following principles for working with the Governor and the Legislature in developing the 2004-05 University of California state-funded budget be adopted.

BACKGROUND

The documents *2004-05 Budget for Current Operations* and *2004-05 Budget for Capital Improvements* were mailed on October 31, 2003. Vice President Hershman will make a detailed [presentation](#) on both budgets at the November 19 meeting of the Board of Regents. Attached to this item are displays taken from the Regents' budget documents that will serve as the basis for Vice President Hershman's presentation.

Given the context in which the Governor's Budget is currently being developed and the considerable uncertainty that exists associated with the transition to a new Governor, the size of the deficit the state is facing, and how the new Administration will address these issues, the University is not submitting a normal budget request to the state for 2004-05. Instead, the University intends to develop its spending plan for 2004-05 once the Governor's Budget has been issued in January. In the meantime, a set of principles has been developed that is intended to help guide negotiations on the budget. The principles express the University of California's priorities during this fiscal crisis for maintaining quality, access, and affordability. The Regents are being asked to adopt these principles at this time.

Principles for Developing the 2004-05 Budget

The Regents are committed to three primary principles that are to guide the University as negotiations proceed with the Governor and the Legislature on the development of the 2004-05 budget:

Primary Principles

- 1. Maintain and Enhance the Quality of the University—Quality is the most important asset the University of California offers the state.**
- 2. Maintain Access and Honor the Master Plan—The state needs the highly-skilled, well-educated graduates that are produced by the University of California.**
- 3. Maintain Affordability—Ensure that cost of attendance is reasonable and is not a financial barrier for needy students.**

These principles are supported by a discussion of the underlying considerations that together with the principles articulate the University's highest priorities for 2004-05. Reaching an understanding about the University's priorities is critical during this time of fiscal challenges and uncertainty.

The University has endured challenges and uncertainty before. However, the state is currently in the midst of a budget crisis unprecedented in magnitude and possibly duration. The University has already sustained \$424 million in base budget cuts, offset another \$230 million in cuts with increases in student fees, and foregone salary and other cost increase funding totaling \$424 million. The budget crisis shows no sign of abating in 2004-05. The state will begin the fiscal year with an ongoing structural deficit estimated to be at least \$7.9 billion—this estimate can grow higher if actions taken to balance the 2003-04 budget package are reversed. The state is also in the initial stages of a transition to a new Governor. Therefore, a great deal of uncertainty exists as development of the state budget for 2004-05 begins.

Difficult choices will have to be made by state decision-makers and by leadership in the University over the next year. Yet, the fiscal crisis will eventually subside and the state will return to normal economic growth. As in the past, the University can help the state achieve this growth. Weakening the University of California at the very time the state should benefit most from its investment in the University is unwise. The University must work to ensure that decisions made now to address the immediate crisis do not, in the long term, irreparably harm the University and its ability to maintain excellence as it carries out its three basic missions of teaching, research, and public service.

The principles embodied in this document are intended to guide the University during this time of challenge and uncertainty. They represent the basic values to which the University has long been committed and that must be preserved for the long-term success of the University.

Primary Principle: Maintain and Enhance the Quality of the University—Quality is the most important asset the University of California offers the state.

Background

- Students seek admission to the University because of its excellence. They are the brightest students in the state and they work hard to become eligible for UC because of the high value they place on attending one of the finest research universities in the world.
- Because the University is one of the finest higher educational systems in the world, it is able to attract eminent scholars whose teaching and research stimulate both educational opportunities and economic progress for the citizens of California. Faculty and students together create new knowledge that translates into emerging industry and technology, which in turn fuels the economy by creating jobs, promoting trade and commerce, and improving the well-being of those who live in California.
- The University's public service programs also help improve the quality of life for the state and stand as models for others in the country to follow. The Agricultural industry, consumers, and local communities rely heavily on the information and advice distributed through the University's Cooperative Extension programs. K-12 education is benefited greatly by the efforts of the University's outreach and K-12 teacher professional development programs. The University's programs are valuable to these external constituencies because they are based on research conducted by top scholars in their field and reflect the best thinking within the discipline for addressing problems and finding solutions.
- Any activity the University undertakes is born from an underlying principle of quality. It is what California has come to expect from the University of California. Surveys conducted several different times indicate that when Californians are asked what they think is most important about the University, a strong majority answers, "quality."

Supporting Principles

- The University will not allow quality to erode further. Quality must not be taken for granted. The University is deeply concerned about the ongoing effects of the budget reductions that have already occurred, for once lost, quality is not easily regained.
- Market lags in faculty and staff salaries must not deepen—the University must return to paying competitive salaries. A critical concern during the current budget crisis is the University's inability to pay competitive salaries. Faculty salaries currently lag the average of comparison institutions by 9% and there is a similar problem with respect to staff salaries. UC will be hiring 7,000 faculty over this decade as well as staff to support them. It is very difficult to recruit and retain high quality faculty and staff while unable

to pay salaries comparable to the market. This problem is exacerbated by unfunded health benefit cost increases. As those costs rise and are not funded, more of the burden must be borne by the employee. Increases in health benefit costs for 2003-04 are expected to cut deeply into paychecks.

- The University must continue to pay faculty merit increases. Paying faculty merit increases is key to maintaining quality. The University has a true merit system to reward the very best faculty and staff. Faculty are only eligible for merit increases every three years. Therefore, merit increases must be paid each year to avoid serious inequities from occurring among the faculty.
- The University will not permit the student-faculty ratio to deteriorate further. Another critical indicator of quality is the student-faculty ratio, which reflects the number of students to each faculty member funded by the state. UC's student-faculty ratio historically has been high compared to other research institutions in the country. During the budget cuts of the early 1990s, the student-faculty ratio deteriorated even further. The inability to pay competitive salaries already creates a significant recruitment and retention challenge for the University. It would not be reasonable or practical to ask faculty to receive less pay and also work more, particularly given the fact that UC workload policies are on a par with those at other comparison institutions. The University is instituting more freshmen seminars on its own initiative, and faculty remain committed to improving time-to-degree and getting students the classes they need to graduate. The University has a remarkable record in these areas and is doing all it can to continue making progress. The University cannot allow the student-faculty ratio to deteriorate further.
- Research support must be maintained in order to maintain quality in the University's academic program and to continue to help the economic recovery of the state. It is critical that UC maintain or even increase research support from all sources, for it is through the research enterprise that the University makes its uniquely valuable contribution to California. The entire state benefits from the products of UC research. Federal research grants to UC have been going up dramatically in recent years, which in turn creates jobs and income for the state, and thus helps the economy. For every state dollar invested in UC, \$4 more is leveraged from other sources. UC research has created whole industries for California and is a primary reason California leads the nation in biotechnology, aerospace, computer and information science, agriculture, environmental technologies and a variety of other fields. The *California Institutes for Science and Innovation* are world-class and will infuse research and development in the state with bold new discoveries that can lead to new frontiers, all of which will help fuel the economy.
- The core infrastructure of the University cannot sustain further budget cuts and continue to support the academic programs of the University. Maintaining the quality of the academic program requires maintaining support structures in the basic operations of the University. Continual reductions in non-instructional areas of the budget will weaken the infrastructure to the point that it will no longer be able to support the academic program.

- Base budgets have already been reduced by \$424 million. Reductions are occurring in programs that have a direct impact on the instructional program, such as instructional equipment and instructional technology. Historically, state funding has been inadequate for these programs and now with additional cuts they are losing their ability to keep up with fast-pace changes. With inadequate funding for maintenance and no funding for deferred maintenance, the physical plant is falling into greater disrepair. Costs in other areas of the budget, such as health benefits and energy costs, are increasing significantly but are not being funded by the state. Campuses believe administration budgets have been seriously underfunded for years, given all the increases in reporting and regulatory demands. Yet, with the current fiscal crisis, these budgets are being cut even more with no relief in workload. The need for adequate resources has always been great, but the pressure has built significantly due to the fact that budgets have been woefully short for several years in a row.

- The University will not further risk the quality of the institution. To do so would be to sacrifice the primary asset that makes UC valuable to the state. Preserving the quality of the University is in the best interest of all Californians.

Primary Principle: Maintain Access and Honor the Master Plan—The state needs the highly-skilled, well-educated graduates that are produced by the University of California.

Background

- For over forty years, the University of California has been committed to the tenets of the California Master Plan for Higher Education, which is the blueprint for higher education in this state. The Master Plan specifies the mission of each public higher education segment and defines the pool of high school graduates from which each segment is to admit its students.

- The Master Plan calls for UC to offer a place to the top 12.5% of graduating California high school seniors and all eligible California Community College students. Throughout its forty-year existence, UC has remained committed to the Master Plan and has accommodated all eligible students wishing to attend. The Master Plan also calls for the state to provide adequate resources to accommodate enrollment.

- However, language adopted as part of the 2003-04 budget package states the Legislature's intent that the Department of Finance is to include no funding for enrollment growth, salaries, or non-salary price increases as it develops the 2004-05 Governor's Budget for UC. This is consistent with instructions issued by the Department of Finance for developing the 2004-05 Budget.

- The state appears to be sending a signal that it may not honor its commitment under the Master Plan to provide adequate resources to fund enrollments. If that point is reached, it is unrealistic to expect that the University can continue to honor the access guarantee of the Master Plan in the same way it has done in the past without adequate resources from the state.
- Decisions about enrollment reductions cannot be made until more is known about the level of funding the University is to receive from the state in 2004-05.

Supporting Principles

- Enrollment levels in the University must match the resources provided. UC's enrollment has increased by 18% over the last three years while state funding for UC has declined by 14%. Enrollment is currently 12,000 over the level envisioned by the last enrollment plan (updated in 1999). The University has reached a point where taking more students without adequate resources will irreparably harm the University's ability to offer a high quality education to those who attend.
- If actions are taken to reduce enrollments, they should be implemented in such a way as to minimize the impact on UC's commitment to the access goals of the Master Plan and should be adopted on a temporary basis until the state is able to once again fully fund the University's basic needs. Implementation of enrollment constraints or reductions would constitute a major change in policy resulting in turning away potentially thousands of students who have worked hard to become eligible for UC under the expectation that if they achieved eligibility, they would be promised a place in UC. The University remains committed to the tenets of the Master Plan. The University intends to seek the state funding necessary to fulfill its commitments under the Master Plan. If the state ultimately decides not to fund the education of these students at UC, the University will endeavor to ensure that this is a short-term change and will mitigate as much as possible the impact on students.
- Access under the Master Plan includes a commitment to diversity and any actions to reduce enrollments should reflect that commitment. Just as major outreach efforts are undertaken to ensure students from disadvantaged circumstances have equal opportunity to attend UC when enrollments are expanding, any proposals for enrollment reduction must remain consistent with this commitment to diversity.

Primary Principle: Maintain Affordability—Ensure that cost of attendance is reasonable and is not a financial barrier for needy students.

Background

- Historically, student fees at the University of California have been very low, primarily due to the fact that the state has heavily subsidized the cost of education. Students currently pay 25% of the cost of their education.
- In good economic times, student fees have been frozen or reduced. For example, the most recent increases in student fees follow seven consecutive years of no fee increases and 10% reductions for undergraduates (5% reductions for graduates).
- As state support declines, the price students must pay has tended to rise. This happened in the early 1980s, the early 1990s, and is happening now. Contrary to recent news coverage nationally about the skyrocketing costs in higher education, the average cost of providing a UC education to a student has declined over 18 years by 12%. The state subsidy toward that cost has declined significantly—by 32% over an 18-year period between 1985-86 and 2003-04. As the state subsidy has declined, the price students must pay has tended to rise. The student's share of the cost was 11% in 1985-86; in 2003-04, that share is 25%. (Data are based on constant dollars.)
- Student fee increases have helped maintain quality during times of fiscal crisis. Student fee increases over the last 18 months have offset reductions that otherwise would have been targeted at instructional programs.

Supporting Principles

- The University's preference would be to have a fee policy accepted by both the University and those in state government that would provide for annual increases in student fees consistent with an economic measure, such as per capita personal income. Such a policy would be contingent upon the state being able to provide adequate support for the University's basic needs. The wide fluctuation in student fees tracks fairly closely with changes in the state's economy. In good years, fees were held steady or reduced. In years of fiscal crisis, student fees increased dramatically. If the state can afford basic support to ensure quality and access for the University, student fee increases should occur gradually, moderately, and predictably.

- As student fees rise, it is important to provide financial aid to mitigate the impact of fee increases on needy students. The University has an exceptional student financial aid program. Nearly 50% of UC undergraduates receive grant/scholarship aid averaging approximately \$6,500 per student; about 62% of graduate students receive such aid averaging about \$9,800 per student. The success of the University's financial aid program in helping to ensure access for needy students was illustrated in a study by the James Irvine Foundation published in March 2002, which examined enrollment of low-income students at the nation's top 40 public and private universities (as designated by U.S. News & World Report 2001 College Guide). This study showed that UCLA ranked number one among top universities in terms of enrolling low-income students, with 34.8% of its student body identified as low-income; UC Berkeley ranked second with 30.1% low-income students; and UC San Diego, with 28.7% low-income students, ranked third. These data were significantly above other public institutions included in the list, such as the University of Virginia (9%), the University of Wisconsin (11%), and the Universities of Michigan and North Carolina (both about 12%).
- The University would continue to use a portion of the revenue raised from an increase in student fees in 2004-05 to help ensure access for needy students. In the current year, the University provided grant aid to cover the full increase for low-income students and half of the increase for middle-income needy students. The University would do the same for student fee increases that occur in 2004-05.

([Attachments](#))