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July 26, 2012

Ms. Elaine M. Howle  
State Auditor  
Bureau of State Audits  
555 Capitol Mall, Suite 300  
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Dale Carlson, Project Mgr.  
Dan Andersen, Team Leader  
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Dear Ms. Howle:

This letter is the University's official 12-month progress report on recommendations included in the report *Although the University Maintains Extensive Financial Records, It Should Provide Additional Information to Improve Public Understanding of Its Operations*. Below is the University's response to each recommendation made in the report.

### **Chapter 1 – University Revenues and Expenses Have Undergone a Few Significant Changes Over the Past Five Years**

We note that this chapter did not include any recommendations.

### **Chapter 2 – The University Should Complete Its Reexamination of the Campus Base Budgets and Could Improve the Transparency of its Budget Process**

#### **The University's Allocation Process**

As described in the audit report and noted in our previous responses, the University established a systemwide work group, consisting of Chancellors and other campus leadership, faculty representatives, and leadership from the Office of the President, to examine variation in funding across the system. The effort by the Rebenching Task Force reviewed the base budgets and considered alternatives for adjusting distribution formulas, but did not attempt to "quantify" the existing variation, as suggested in the audit. The work group has completed its work and the summary of its findings has been sent to me for my consideration. Other University constituencies are also reviewing the documents. The report and the accompanying appendices are attached to this response. The core principles and recommendations offered by the Task Force create a framework that will form the basis for allocations of State General Funds going forward. Basically, the framework calls for allocations

Ms. Elaine M. Howle  
July 26, 2012  
Page 2

of State funds to be based on a per student calculation. The calculation considers the relative weights of various levels of students, without identifying actual costs associated with those levels, and makes several adjustments for a variety of considerations. Such adjustments include the new campus at Merced and the medical campus at San Francisco, programs that hold systemwide importance or that receive State-specific funding and therefore should not be funded on a per student basis. Other considerations are a recognition of a minimum level of fixed costs necessary to operate any campus, and acknowledgement of the need to fund graduate enrollment growth for those campuses that fall below the systemwide average, among others. The report of the Task Force and accompanying appendices have been posted on the following University website: <http://budget.ucop.edu/documents/rebenching-report-recommendations.pdf>.

Many issues will need to be resolved as these recommendations are implemented over time. The group recommended a six-year timeframe, which may or may not be achievable. In addition, because the formula relies on a per student calculation, it will be necessary for the University to develop a long-range enrollment plan upon which future allocations will be based. I am considering a number of issues that will need resolution before a final plan for rebenching State General Funds is completed, but it is my intention to begin the process of rebenching State General Funds in the 2012-13 allocations to those campuses that have the lowest State funding per student with the new funding provided in the University's 2012-13 State budget appropriation.

### **Transparency of Budget Process**

In our previous responses, we noted that for the 2011-12 fiscal year, the University has implemented changes to its budget process that result in individual campuses retaining all student tuition and fee revenue, research indirect cost recovery funds, and other campus-generated funds. These changes will increase the transparency of the University's budget. There is no further update to this response.

The Office of the President is developing a new budget manual describing current budget practices, which had been scheduled to be completed by July 2012. This work is still underway, but due to budget cuts and staff shortages, it is likely completion of this project will be delayed a year. When completed, it will be published on the University's website. Again, there is no further update to this response.

The University is reviewing the information about budget allocations currently available on the University's website, as well as other financial information made available on systemwide and campus websites. There is no further update to this response.

**Chapter 3 – Although the University Has Numerous Processes to Provide Detailed Accountability for Various Types of Funding, It Could Improve the Transparency of Its Financial Operations**

### **Transparency of University Funds**

We are continuing to analyze data and explore alternatives to consistently report unspent balances that are carried over to future years. We expect to include this information in fiscal year 2013 reports.

### **Campus Financial Information on Auxiliary Enterprises**

We gathered data for fiscal year 2011. After excluding revenues received for special programs, for example child-care grants from the State, and student fees designated by each Chancellor, there was \$1.4 million of campus unrestricted funds used to support non-hybrid auxiliaries. Two of these auxiliaries, which received \$0.9 million of campus support, were recently closed. For hybrid auxiliaries, the Chancellor has discretion over the source of funds that will be used for direct and indirect costs of the activities. We plan to continue to monitor this information annually.

### **Transparency of University Expenses**

Each campus implemented new procedures for fiscal year 2012, and we expect miscellaneous services will decrease by over 90 percent over the next two fiscal years as other, more appropriate accounts, are used to report the expenses.

### **Use of Revenues Generated from Student Fees Imposed by Referenda**

As noted in our previous responses, the University maintains that The Regents, and, by delegation, the President retain authority to make modifications to the terms of collection and the uses of revenue for all campus-based fees. At a future Regents' meeting, the University will request approval from The Regents for changes to policy that would clarify the University's position.

Compulsory campus-based student fees adopted by student referenda are guided by the University's *Policy on Compulsory Campus-Based Student Fees* (referred to as *Policy* below). Compulsory campus-based student fees may only be established following a student referendum adopting the fees, except as provided in Section 83.00, "Exceptions to the Referendum Requirement."

The passage of a referendum, however, does not mandate the imposition of a fee. The fee must still be approved by the Chancellor and the President. Approval of compulsory student fees adopted by student referenda, including fees for student-fee funded facilities, has been delegated to the President under The Regents' *Standing Order 100.4(g) – Duties of the President*, which can be found online at <http://www.universityofcalifornia.edu/regents/bylaws/so1004.html>.

In all situations, the Board of Regents, and by delegated authority, the President, retains ultimate authority pursuant to its Constitutional autonomy to impose or modify any and all student fees – including those established by campus-based

Ms. Elaine M. Howle

July 26, 2012

Page 4

referenda. Once a fee has been imposed by The Regents or the President, after possible modifications of the fee by The Regents or the President, the terms of its collection and expenditure are binding throughout the life of the fee. Typically, these terms are the same as those contained in the referendum. A referendum, however, may contain errors, unworkable terms, unacceptable provisions, or ambiguities that The Regents or the President may correct when approving the fee. Although The Regents and the President do not take such actions lightly, modifications to fee terms are well within their authority. The Office of the President (UCOP) and the campuses are collaborating on efforts to avoid the need for changes from referenda language. When student referenda for campus-based fees are in the planning stages on the campus level, campuses frequently send draft referenda language to UCOP prior to printing final language on student ballots. The draft language is circulated among Budget and Capital Resources, General Counsel, and Student Affairs staff for review and comment. Staff work closely with the campuses to clarify any potentially confusing language in the referenda, including, in the case of capital project fees, ensuring that the financial planning for building projects has been sound.

UCOP staff work with the campuses to ensure that referendum language is specific to the capital project(s) in question and to avoid leaving the door open to funding unnamed capital projects in the future. UCOP, however, may not want to restrict campus flexibility in the future. Campuses benefit from flexibility in their fund sources, future funding needs cannot always be anticipated, and it can be difficult to capture all potential uses of revenue generated by compulsory campus-based student fees. There is no further update to this response.

If you have any questions about this response, please do not hesitate to be in touch with me.

Sincerely yours,



Mark G. Yudof  
President

Attachment

cc: Executive Vice President Brostrom  
Chief Financial Officer Taylor  
Senior Vice President and Chief Compliance & Audit Officer Vacca