

**STATE SENATE EDUCATION COMMITTEE
AND SENATE BUDGET COMMITTEE SUBCOMMITTEE ON EDUCATION
INFORMATIONAL HEARING ON UC COMPENSATION**

**Gerald L. Parsky, Chairman of the Board of Regents
University of California
Wednesday, February 22, 2006**

As prepared for delivery

Chairman Scott, Vice Chairman Maldonado, and members: Thank you for inviting me here today to address the Committee on compensation practices at the University of California.

Joining me today are Regent Judith Hopkinson, Chair of the Regents' new Special Committee on Compensation, Speaker Emeritus Robert Hertzberg and Regent Joanne Kozberg, co-chairs of the Task Force on UC Compensation, Accountability and Transparency. I convened this task force to recommend how the University's compensation policies and practices should be changed.

I would like to focus on three fundamental questions this morning:

- First, what are the Regents' roles and responsibilities with regard to the University generally, and specifically, the University's compensation practices?
- Second, why did the University's compensation practices go away, little more than a decade after the executive compensation controversies of the early 1990s?
- Third, what are we going to do to ensure that with respect compensation, there is compliance with Regents' policy, including transparency to the public?

The Regents' Role

The Regents' roles and responsibilities are clearly spelled out in the California Constitution. As an independent institution, the University of California has a unique trust with the people of California, and the Regents are given the ultimate authority to oversee the University.

Most Regents are appointed, unpaid volunteers with extensive professional responsibilities beyond the University. As with any large organization, the President of UC and the 10 UC Chancellors, who are full-time, paid employees of the University, have been delegated considerable responsibility and authority over the years. At the same time, however, the Regents have set clear policies for the administration and faculty to follow, and we have never hesitated to provide oversight and to correct practices when it was warranted.

Let me give you a few examples:

First, the Regents have taken aggressive action to ensure the most effective management of the University's pension and endowment funds. We have made personnel changes, modified the reporting structure of the Treasurer's office and established asset allocation policies for the

University's investments. We remain vigilant and very “hands on” – to the extent that last year I testified here in Sacramento about the proposal to make changes in several public pension funds, including the University.

Another example is the Regents’ oversight of the three national laboratories that UC manages. To make the sweeping changes necessary at Los Alamos, we brought in independent auditors and other outside experts. When it came time to put together a bid to compete for continued management of the lab, Regents were intimately involved, including helping to recruit business partners with the expertise UC needed to more effectively manage the lab. The results speak for themselves: the Department of Energy recently awarded the contract to the limited liability corporation that I, as chairman of the Regents, now chair.

A third example involves UC compensation. The Regents recognized several years ago the need for greater oversight and accountability of executive compensation. After careful study, including consultation with independent outside experts, the Regents last November adopted a new policy governing University compensation. Regent Hopkinson, who led that effort, will describe in greater detail this new policy.

This leads to the second question – how did we get here?

For the answer to that, we must go back to 1992, when the Regents adopted a set of principles to guide executive compensation. By doing so, the board made a clear commitment to public access, awareness, knowledge, and understanding of the Regents' decision-making processes, as well as to public concerns about the Regents’ deliberations with regard to executive compensation.

That policy, as amended in 1993, has been distributed to you, but let me summarize a few key principles:

- First, it defined executive compensation broadly to include not just base salary, but also many other forms of compensation, including retirement, perquisites, deferred compensation and housing.
- Second, it required that all discussions of and actions on executive compensation programs occur in open session of the appropriate committee, with final action occurring in open session of the full board. It further required that any paid leaves of absence for most executives be reported to the board and that all actions affecting executive compensation be released to the public in a timely manner.

These principles remain the policy of the Regents today!

And yet the letter and the spirit of these principles have not been followed in every instance. For instance, we were not informed, in writing, of the full terms and conditions of MRC Greenwood’s appointment as Provost. As a result, we were not aware of the provision providing her paid administrative leave upon her resignation.

We were also not informed of the terms of Celeste Rose’s agreement to leave her position as vice chancellor at UC Davis and accept a new job, at an increase in salary, as senior adviser to the

Chancellor. Therefore, we were not aware of provisions that have made it difficult to assign her work.

And we were not informed of outside compensation arrangements and leave exceptions granted to some executives.

The failure to properly and consistently disclose these compensation arrangements to the Regents and to the public do not adhere to the principles established by the Regents more than a decade ago.

And, therefore, Mr. Chairman, we need to do something about this situation.

First, we need to look back and fully audit what has taken place. Then, we have to look forward and decide what additional policy changes need to be made. Part of the fact-finding that the Regents initiated is to understand whether other violations occurred, why they occurred, and who was responsible. In particular, we want to know whether exceptions to policy were properly authorized.

The answers to these and other questions will be provided by the independent audit that I commissioned last December.

The audit is being conducted by Pricewaterhouse Coopers. The objective is to summarize the employment arrangements and compensation for the 32 most senior administrators from 1996 through 2005. In addition, the audit will assess compliance with University policies, including whether the proper level of approval was received, and whether the arrangements were disclosed to the Regents and to the public.

The scope of work will examine 64 individuals who are either current incumbents or past incumbents of these 32 positions over this 10-year period of time.

The first phase covers the 32 current incumbents, including the President, Senior Vice Presidents, Vice Presidents, Chancellors, Officers of the Regents, Laboratory Directors and Medical Center CEO's, as well as five recent incumbents such as former President Atkinson and former Provost Greenwood.

The second phase of the audit covers 27 previous occupants of the same 32 positions, going back to 1996.

Although it took more time for the Administration to assemble than we thought, the University has provided most information to Pricewaterhouse Coopers about the current incumbents, and is providing it for the past occupants of these positions. This information includes a summary of the employment arrangements; details of each individual's W-2 compensation; and representations as to whether they have received, either directly or indirectly, any other potential compensation or personal benefits.

Finally, Pricewaterhouse Coopers has been provided the travel and entertainment reimbursements made to all the individuals who held the top 32 positions between 2003 and 2005.

Pricewaterhouse Coopers is now assessing the accuracy and completeness of all this material, as well as evaluating whether the employment arrangements and/or compensation was approved by the proper level of authority; whether it was paid or promised in accordance with University policies; and whether it was communicated to the Regents and to the public in accordance with policy.

The Pricewaterhouse Coopers report is expected to be presented to the Regents in preliminary form in mid-March and finalized by the end of March.

The Regents are going to continue to pursue this process until we are satisfied that we have fully addressed the problem. That includes fully cooperating with the Bureau of State Audits in its review of these same issues.

At the same time, we are looking forward:

We are going to carefully consider the full range of recommendations from the Hertzberg-Kozberg task force, including ways to strengthen accountability. Among other areas, I have asked the task force to recommend what policies should apply to then outside compensated activities, such as service on outside boards of directors.

(In light of the timing of the Pricewaterhouse Coopers audit report, I have asked the task force to delay their report until the audit is complete.)

As a further step, The Regents will consider how best to ensure future compliance with University policies and to improve Regents' oversight. The Regents will consider a number of alternatives to ensure compliance, such as:

1. Asking the University Auditor to hire separate auditors reporting to the Regents, whose sole responsibility would be to audit compliance with a range of crucial University policies.
2. Asking the University's outside independent audit firm to conduct a separate annual compliance audit.
3. Hiring an Inspector General or full-time audit staff reporting to the Regents.

In addition, we will hold people accountable. If that means disciplining or firing people, we will! But not without full knowledge of the facts, including an understanding of whether the matter arose due to error, poor judgment, or lack of organizational clarity.

In any event, it appears that the organizational structure and business practices of the Office of the President needs to be enhanced.

In brief, I am sure you would agree that ensuring due process is important to any discipline process.

Finally, it appears that the organizational structure and business practices of the Office of the President needs to be enhanced.

Therefore, the Regents will address, with the help of outside experts, how best to re-organize and staff the Office of the President and each of the Chancellors' offices to strengthen the management of the University in order to better complement the University's academic excellence.

Like many of my fellow Regents, and like many of you, I come from the world of business – and, I do not accept the argument that academia and business should not mix. However, I also believe that business practices should not detract from the quality of the academic enterprise.

On the contrary, as we learned at Los Alamos, sound management practices are necessary to support strong science. This is equally true for the broader University: we must improve our business practices so that they fully support – and not further distract us from, our primary mission to provide quality teaching, research and public service to the people of California.

Thank you for focusing on the University's compensation problems. I know you all join the four of us in being proud of the accomplishments of the University and in your deep commitment to the University – please all join with us in developing solutions to these current problems – as partners we can and will succeed!