Minutes
Business and Finance Committee
Board of Regents of the University of Wisconsin System
December 4, 1997

The Business and Finance Committee met in Room 1511 Van Hise, Madison, at 10:10 a.m. Present were Regents Hempel, De Simone and Marcovitz. Also attending were Regents Randall, Smith and Staszak.

I.2.a. Closed Session to Consider Trust Fund Matters, as Permitted by s. 19.85(1)(e), *Wis. Stats.*

Upon the motion of Regent De Simone and the second of Regent Marcovitz, the Business and Finance Committee adjourned to Closed Session at 10:12 a.m., to consider Trust Fund matters as permitted by s. 19.85(1)(e), *Wis. Stats*.

The Committee recessed at 11:45 a.m. and reconvened in Open Session at 1:10 p.m. in Room 1820 Van Hise Hall. All Regents were invited for the Education Committee presentation of the 1997 Accountability Report and Item I.2.b. of the Business and Finance Committee. Present were Regents Barry, Benson, Boyle, Brandes, De Braska, De Simone, Hempel, James, Lubar, Mac Neil, Marcovich, Mohs, Orr, Randall, Smith and Staszak.

I.2.b. Kick-off for 1999-01 Biennial Budget Planning

President Lyall stated that last biennium the Regents' 21st Century Study provided clear guidance on Systemwide needs and Regent priorities. Many of those priorities will continue, but it is also important to take a fresh look at where the UW System is, following the current biennium, and where the System needs to go.

The Strang report confirmed that the UW System is a major force in Wisconsin's economy. The System provides an excellent return on the State's investment–$.8.2 billion per year, a tenfold payback. While employing 40,000 staff directly, the System's purchases from Wisconsin businesses generate an additional 145,000 jobs for State citizens. The average UW undergraduate will recover his/her cost of education in about three years, while the State benefits further from increased State and local taxes paid by these graduates.

The 1997-99 budget had many successes. It reversed severe cuts of the previous biennium and will allow some important improvements. In information technology, it will allow the System to join BadgerNet, train faculty and staff in use of technology and help the public schools. Also, it funds Allied Health to increase the supply of physical and occupational therapists. In addition, it increases financial aid to help meet tuition increases since 1994. It also provides a pay plan which, though only partially funded, keeps faculty and academic staff compensation from eroding further.

While the UW remains the State's largest agency, Wisconsin has had to balance multiple priorities. The State's priorities have shifted to property tax relief, Corrections and Medicaid. Since 1990, the UW System has declined from the second largest State commitment to the fourth. If these trends continue, in year 2002, Wisconsin will spend more on Corrections than on the UW System. However, while it costs $19,500 GPR to incarcerate a prisoner for a year, a UW student can be supported for $6,800.

At the same time, other states are once again reinvesting in higher education. Wisconsin GPR funding for higher education has not kept up with national increases over the past two years. While State appropriations increased 9.8% nationally over the last two years, Wisconsin increased by only 3%, ranking 43rd out of the 50 states. Despite an excellent and growing economy, Wisconsin has fallen behind nationally in higher education support for students. GPR support for a senior who entered the

UW System four years ago has increased less than inflation (7% compared with 11% inflation), while other Midwestern states were increasing their investment in higher education over the same four years by an average of 21%. Within Wisconsin, the UW share of State GPR expenditures has declined from 14.4% at the time of merger to a low this year of 9%. Not only has the operating budget shown dramatic declines, but the UW System capital budget's share of State funding also has fallen from a high of 88.4% in the 87-89 biennium to 26.5% of the State's new GPR bonding this biennium. In part, these declines reflect the State's priority for funding prisons.

The System has managed these declines by paying faculty and staff salaries below our competitors' average, by substituting instructional academic staff for faculty as retirement vacancies occur, by deferring building maintenance, by carefully managing enrollments, by slashing administrative costs and services to a level that is half of our peers, and by increasing private contributions. Also, the student share of cost has increased from 25% in 1974 to 36% in 1997. Tuition has had to increase to help maintain sections and to fund investments in computing and other technology.

Since 1989, the UW System has lost $87 million in State funding reductions and lapses, including the $33 million cut last biennium. These reductions have caused serious erosion in meeting our commitment to students. Students tell System Administration they are seeing larger classes and less access to faculty. They say they don't have enough technical support with technology and are experiencing less access to lab and library resources. Student also express concern that class offerings have been reduced.

In most states, ongoing needs such as inflation and workload increases are automatically funded through formula or standard budget adjustments and then new initiatives can be requested above these amounts. By contrast, in Wisconsin, these ongoing needs are not funded and must compete against our own new initiatives within the State's fiscal target, and the University rarely receives full funding for these needs. Most universities are able to control creation/deletion of all positions and have determination of compensation levels. They are able to issue tax exempt bonds for capital needs and can exercise full tuition authority. Our Board needs these additional authorities in order to deploy our scarce resources most effectively.

At the beginning of the 1999-01 budget process, it is important to plan strategically for a more reliable fiscal environment which, hopefully, does not include further general and administrative cuts and lapses, and which will continue to provide access for qualified students. If the expected new student enrollments are realized, the GPR share of cost must be funded. In addition, the Board must have the ability to more independently manage existing resources as suggested by best business practices.

As the UW System looks at where it is going and where it needs to go to ensure quality education and service to Wisconsin students, three key questions should be addressed: (1) What is necessary to deliver on the Regents' promise to students that "quality always comes first?" (2) In an era when State budgets and budget planning processes have very short horizons, are there ways to make support for higher education more reliable and more supportive of long-term strategic plans? and (3) How can we better serve the future needs of the State with the University assets at our disposal?

Starting with a presentation on libraries this month in the Education Committee, staff will be presenting one or more reports on areas which are candidates for inclusion in the next budget request. Reports on collaborative programs, building maintenance, management flexibilities, student services and financial aid, supplies and expenses, instructional technology, research, outreach and diversity are planned for upcoming meetings. Board members should submit any additional suggestions by the end of December. When guidelines are received from the Department of Administration, they will be reviewed with the Board. In May, staff will seek the Board's direction on which themes to include in the draft budget document and what priority to attach to each. In August, the Board will be asked to adopt a final budget. As in the past, the Board will determine the Compensation request separately in November or December.

The Joint meeting recessed at 1:52 p.m. and the Business and Finance Committee reconvened at 2:00 p.m. in Room 1920 Van Hise Hall. Present were Regents Hempel, Brandes, De Simone, Marcovitz and Lubar.

I.2.c. Approval of Minutes of the November 6, 1997, Meeting of the Business and Finance Committee

Upon the motion of Regent Lubar and the second of Regent Brandes, the minutes of the November 6, 1997, meeting of the Business and Finance Committee stood approved.

I.2.d. Principles for An Optional Retirement System

Senior Vice President Olien stated that the Legislature is considering a measure which would mandate that the Board provide for an alternative to the Wisconsin Retirement System to be offered to UW faculty and academic staff. Of all the proposed legislation affecting faculty and staff benefits, creating an Optional Retirement System (ORS) is by far the most significant and complex. Discussion of the ORS is in a very early stage, but staff believe it is important that the Board be provided with as much information as possible on ORS issues.

Sue Chamberlain, Director of Staff Benefits and Payroll Policy, noted that retirement plans generally fall into one of two categories–a defined contribution plan or a defined benefit plan, and she briefly highlighted the differences between the two. She also indicated that currently all University staff participate in the Wisconsin Retirement System (WRS). The WRS is one of the largest public retirement systems in the nation, with over 423,000 employes and retirees covered and assets of $34 billion as of December 31, 1996. The WRS is a hybrid plan, incorporating elements of both the defined contribution and defined benefit plans. A unique feature of the WRS is the post-retirement dividend process where each year, based on favorable investment experience, retirees are awarded a dividend, which last year was 6.6% of the current monthly benefit.

Professor Emeritus Jim Hickman, former Dean of the UW-Madison School of Business, stated that an ORS could assist in recruiting and retaining high quality faculty and staff, but it would seldom be decisive. An ORS is best for early withdrawals. Sponsors of the ORS believe that defined benefit plans, such as the WRS, are too risky. Taxation and accounting regulations have increased expenses and decreased flexibility in defined benefit plans; and high real rates of interest compared to low rates of real salary growth favor defined contribution plans. The spirit of the age is in accord with individualistic values, making the addition of an ORS appealing to faculty and staff. Other considerations are: (1) administrative costs are small; (2) there would be an additional expense for pension counseling, if it was deemed necessary; (3) a disability income plan would need to be designed; and (4) there must be assurance that the ORS remains truly an option. Because faculty and staff are a small part of the WRS, any effect on WRS would be small.

Associate Vice President Wright indicated that the eleven proposed principles for an ORS being presented to the Board for consideration have been developed by the Office of Human Resources in consultation with a wide variety of interested committees, staff and individuals, faculty and academic staff representatives and institutional administrators. The principles were then reviewed, modified and approved by senior System and institutional administrators.

The principles were designed to ensure that an ORS: (1) meets IRS requirements for a tax preference/tax deferral; (2) protects the interests of the employer and employes in maintaining a sound retirement system; (3) provides the Board maximum flexibility in designing, offering and managing an ORS; (4) provides equity among employe groups relative to benefits provided by the State; and (5) continues State funding of the retirement program whether it is the Wisconsin Retirement System or an Optional Retirement System. As legislation develops, the Board may wish to add to the eleven principles.

In response to Regent questions, Associate Vice President Wright indicated choices for an ORS would be similar to the TSAs, but with a smaller number of products, and that the real benefit of the ORS is that accounts vest immediately.

Regent Lubar noted that investment returns will be lower than what employes might be expecting and there will be complaints. Currently, the State assumes the risks, but the employe assumes the risk with an ORS. Therefore, it's vital to make certain employes understand the risks involved. Regent De Simone also indicated the need for counseling because most employes do not understand how to invest.

UW-Milwaukee Professor Randy Ryder, Chair of the Faculty Fringe Benefits Advisory Committee, stated that committee is not hearing demands to increase the options, but that faculty are more concerned with immediate vesting and not waiting six months for health insurance coverage. He also shared a story that Minnesota had initiated a defined contribution plan for K-12 teachers and then spent a large sum of money to return this group to a defined benefit plan. That committee is also concerned with the need for a permanent disability plan and with the potential for adverse selection.

Associate Vice President Wright indicated that, prior to 1986, there was immediate vesting in WRS, and that the Senate has now approved a bill to return to immediate vesting in the WRS. In response to a question from Regent Brandes, he also indicated that a rollover provision is being considered for the ORS.

Regent Hempel noted that, in the future, lifetime careers will be uncommon and there is a need to provide portable plans. Regent Brandes agreed, noting that experience in the private sector is employes will chose a defined contribution plan over a defined benefit plan.

Regent De Simone questioned if fiduciary responsibilities would fall on the Board, and Associate Vice President Wright responded that they would.

Regent Lubar inquired if there were other negative factors to approval of an ORS and indicated he would have preferred to have an option paper for this issue. Senior Vice President Olien indicated an option paper could be provided to the Board when, and if, the issue becomes an actual decision. However, at this time, staff are only asking for direction in preliminary discussions.

Upon the motion of Regent De Simone and the second of Regent Brandes, the Committee approved Resolution I.2.d.

Resolution I.2.d.

That upon the recommendation of the President of the University of Wisconsin System, the Board of Regents (Board) declares that it could support a bill authorizing an Optional Retirement System (ORS) for any unclassified University staff providing that the bill –

1. Authorizes the Board to establish an ORS as a qualified plan pursuant to 401(a) of the Internal Revenue Code at such time and incorporating such plan provisions as it deems advisable for the good of the University and its employees, including the provisions that the ORS must be established and maintained solely for the benefit of participants and their beneficiaries and that the contributions to the ORS are held in trust for this purpose and cannot be refunded to the employer or otherwise diverted;
2. Authorizes the Board to retain oversight and control of the ORS;
3. Authorizes the Board to determine the number of vendors in the ORS and the types of products offered by the vendors;
4. Guarantees the contractual rights of ORS participants to benefits accrued under the Wisconsin Retirement System (WRS);

5. Authorizes the Board to provide long-term disability insurance for ORS participants by deducting from the retirement contribution the cost of participants' long-term disability insurance;
6. Authorizes the Board to charge to ORS participants and/or ORS vendors any new administrative costs directly related to the ORS;
7. Authorizes the Board to ensure equity in employer-paid retirement contributions among all employee groups;
8. Authorizes the Board to modify or to terminate any vendor contract;
9. Authorizes the Board to allow new staff to elect to participate in the ORS or the WRS; to determine whether current staff may also elect prospective participation in the ORS, and to determine the irrevocability of any such election;
10. Acknowledges the University's interest in preserving the excellence of the WRS by permitting the University to consider the potential impact of plan provisions on the ability of the WRS to meet its current and future liabilities and on the State Investment Board's investment of assets in the State of Wisconsin, as determined by a state-funded actuarial study; and,
11. Continues full state funding of retirement plans.

The Board further declares that its purpose in providing an ORS will be to enhance the University's efforts to recruit and to retain faculty and academic staff of the highest quality.

I.2.e. Salary Policy for UW System Senior Executives – Amendment to Delegate Authority

Item I.2.e. was postponed until a future meeting.

I.2.f. Report on Management and Staff Positions

Associate Vice President Wright reported that the biennial budget act had placed a new annual reporting requirement on the Board, directing the Board to categorize each position in the UW System as either a management position or a staff position and to submit an annual report to the Joint Committee on Finance by January 1 of each year beginning in 1998. The report must include: the definitions of "management" and "staff" used by the Board; a list of the position titles in each category; the criteria used by the Board to categorize the positions; and the current number of authorized positions in each category at each campus.

All employes in the University System are assigned to an official title for payroll and budget purposes and each title is assigned to categories established for compliance with the federal mandate for affirmative action reporting. For purposes of reporting management and staff positions to the Joint Committee on Finance, acceptance of the definition of the AA/EEO category of Executive, Administrative and Managerial would appear to meet the legislative intent to describe "management." All other job titles assigned to categories described as faculty, professional nonfaculty, clerical and secretarial, technical and paraprofessional, skilled craft and service/maintenance would appear to represent a reasonable definition of "staff" for reporting purposes.

Upon the motion of Regent Brandes and the second of Regent Marcovitz, the Committee approved Resolution I.2.f.

Resolution I.2.f.

That, upon recommendation of the President of the University of Wisconsin System, for the purposes of reporting on management and staff positions pursuant to s. 36.11(33)(b), *Wis. Stats*., the Board of Regents accepts as the definition of "management" the description of the Affirmative Action/Equal Employment Opportunity category for Executive, Administrative and Managerial positions and accepts as the definition of "staff" all other AA/EEO categories. The Board relies on established position title definitions as the criteria for placing positions in the appropriate AA/EEO category. The System President is directed to submit the required report to the legislative Joint Committee on Finance before January 1, 1998, and annually thereafter, based on the most recent available position data.

Because Special Assistant Takemoto was out of the room, Item I.2.g. the Committee agreed to discuss Item I.2.g. later in the meeting.

I.2.h. UW-Madison Mainframe Computer Report

Vice Chancellor Torphy asked if the Regents had any questions on the UW-Madison Mainframe Computer Report. Regent Hempel noted that it is a very positive report. Highlights of the report are that the overall mainframe costs decreased by 14% in 1996-97. Despite the decrease in costs, usage increased in all areas. The combination of higher volume and decreased costs resulted in the following improvements in the effectiveness measures: (a) cost per 1000 transactions decreased 11%; cost per batch job decreased 9%; cost per session decreased 27%; and cost per administrative function decreased 15%. DoIT continues to realize hardware and software savings resulting from practices of purchasing used equipment and sharing hardware and software among several computers, as well as the discounts received as an educational institution and because of negotiation efforts.

Upon the motion of Regent Marcovitz and the second of Regent De Simone, the Committee approved Resolution I.2.h.

Resolution I.2.h.

The Board of Regents authorizes the transmittal of UW-Madison's report on mainframe computing services to the Joint Committee on Finance, the Joint Committee on Information Policy and the State Auditor.

I.2.i. Differential Tuition Proposal – UW-Madison MBA Program

Business School Dean Policano stated that the Executive Masters of Business Administration (MBA) program is designed to meet the needs of individuals who are at or near the top of their organization's management structure. At present, the UW-Madison School of Business does not offer an MBA program appropriate for employed individuals who do not qualify for the Executive MBA program (employes from diverse backgrounds with less than ten years of work experience and with little formal education in the business disciplines). UW-Madison is proposing creation of an Evening MBA program to meet this need, with a tuition rate of $584 per credit which is based on the cost of the program and is roughly equivalent to tuition in similar programs at peer institutions. Tuition rates will increase at the same rate as the regular MBA tuition rate as determined by the Board.

Last fall, the UW-Madison School of Business initiated a market research study to obtain an estimate of the demand for an evening of part-time MBA program. Information from the survey indicated a substantial demand in the price range that can support the program's cost, and the seven companies participating in the focus group all indicated they would offer employes some form of tuition reimbursement. The primary difference between the night program and the daytime MBA will be that students will take all classes together, including "electives" which will be chosen by the Business School. This actually may be a benefit to the evening program because of the networking and teamwork which will occur.

The evening MBA program intends to enroll between 45-50 students each fall. The current plan is to offer from 12-16 credits of course work each year, which implies a three- to four-year program. To add a new program with this number of students will require a separate teaching, advising and support staff.

Regents agreed the program will be beneficial both to the campus and the business community.

Upon the motion of Regent Lubar and the second of Regent Brandes, the Committee approved Resolution I.2.i.

Resolution I.2.i.

That, upon the recommendation of the President of the University of Wisconsin System and the Chancellor of the University of Wisconsin-Madison, the UW-Madison Evening MBA Differential Tuition, beginning in academic year 1998-99 be approved, with specific tuition rates for this program established in June 1998 as part of the 1998-99 UW System Annual Budget.

I.2.g. Annual Broadcast Station Report

Special Assistant Takemoto explained that the Board is licensee to 12 radio and one television station located on the System campuses. The stations are staffed by faculty, staff and students. System Administration prepares an annual report to update the Board on any major changes and to assure that the broadcast stations are in compliance with FCC regulations. The report is based on information provided by each station manager. Major ongoing developments since last year's report are:

- All stations with towers and antennas over 200 feet have just been reregistered on December 1 with the FCC and in compliance with FAA determinations.
- In compliance with a mandate of the 1997-99 biennial budget, the UW System, the Educational Communications Board and the Milwaukee Area Technical College will be engaged in a six-month study looking at possible new scenarios for Wisconsin's public broadcasting enterprise. Regent Boyle will represent the University on the Commission.
- WHA Radio is celebrating its 80th anniversary this year, marking its beginning with Physics Professor Earle Terry's first transmission from Sterling Hall in 1917 under the call letters 9XM (9 marked the section of the U.S., X stood for experimental and M represented Madison).
- With the resignation of Jack Mitchell, Director of Wisconsin Public Radio, a national search for his replacement will occur this spring, with hopes to fill the position by the summer of 1998. After serving for 21 years, Dr. Mitchell will be joining the faculty of UW-Madison's Department of Journalism and Mass Communications.

- Work continues on the technical and financial aspects of the State's conversion to digital transmissions, which are mandated by the FCC to be operating in a simulcast mode with analog in 2002, and to be solely operational by 2006.

Regent Lubar expressed concern of the cost of the digital conversion. Ms. Takemoto stated that the total estimated cost is $50 million statewide for both television and radio. There is some optimism that the Federal government will fund some portion of each state's conversion.

I.2.j. Report of the Vice President

(1) Agreement with Private, For-Profit-Making Organization UW-Madison Contractual Agreement with Pfizer, Inc.

Upon the motion of Regent De Simone and the second of Regent Marcovitz, the Committee approved Resolution I.2.j.(1).

Resolution I.2.j.(1)

That upon recommendation of the President of the University of Wisconsin System and the Chancellor of the University of Wisconsin-Madison, the Board of Regents accepts the agreement with Pfizer, Inc., entitled, "Data Analysis Center for the WIZARD trial."

I.2.k. Additional Items Which May Be Presented to the Business and Finance Committee with Its Approval

No additional items were presented to the Committee.

I.2.l. Trust Funds
(1) Endowment Spending Plan

Vice President Bromberg noted that the small fraction spending plan adopted July 12, 1990, calls for an annual review of the small fraction rate. The current plan sets the distribution at 5% and that earned income, reserved balances or realized gains will be utilized to maintain the 5% rate. The fraction is applied to a trailing three-year moving average of endowment valuations and any income earned in excess of the fraction is added to endowment principal in a Stabilization Reserve.

At this time, there does not appear to be a need to alter the current spending plan of 5% annually. This allows for departmental funding to remain stable and predictable, but at the same time ensures the growth of the endowment funds. The spending fraction is slightly below that observed at other Big 10 Universities, but is above the median as reported in the June 1996 NACUBO endowment study. The realized gains maintained in the Stabilization Reserve account, at over $70 million, continue to grow.

(2) Modification of Investment Guidelines for Custodial Short Term Investment Fund

Treasury Manager Mills stated that Trust Funds currently utilizes the State of Wisconsin Investment Board (SWIB) cash management fund for all short-term investments. The result is that for every trade executed by the managers and settled by the custodian, Trust Funds is forced to liquidate SWIB short-term fund holdings, initiate a transfer to its account at Firstar and then wire the funds to Mellon for settlement of the trade.

By using Mellon's vehicle, Trust Funds will greatly reduce this processing effort. In addition, after comparing with quarterly results over the past three years, it appears Trust Funds will pick up around 13 basis points on the switch, or approximately $18,000 annually.

Due to an OCC rule change, all bank commingled funds are now required to observe the guidelines imposed by SEC's rules for 2A-7 funds. Therefore, most of the changes between the old CTFI guidelines and the new documentation are a result of this ruling change. The changes of eligible investments generally serve as more appropriate disclosure of the securities already being utilized in the fund and are not a cause for concern.

The guidelines are substantively the same as those used by SWIB to manage their short-term cash fund. Since this is the current short-term investment vehicle used by UW Trust Funds, the approval of Mellon's CTFI will not represent the acceptance of any incremental risk, but will allow for improved processing and enhanced revenues.

Upon the motion of Regent Marcovitz and the second of Regent De Simone, the Committee approved Resolution I.2.l.(2).

Resolution I.2.l.(2)

That upon the recommendation of the Regent Business and Finance Committee, the modification of Investment Guidelines for Custodial Short Term Investment Fund be approved.

(3) Modification of Investment Guidelines to Update Definitions/Restrictions

Treasury Manager Mills noted that some portions of the Investment Objectives and Guidelines have become outdated and need revision. In order to maintain the spirit of the original wording, but removing the unnecessary restriction requiring a five-year operating history, staff are recommending using "financially sound" in place of "well established" as a more appropriate phrasing in the Investment Policy sections of both the Principal Fund and the Income Fund. This will ensure the Board is expressing a desire to limit default exposure but will allow for investments in small cap (startup) companies.

The glossary changes in the Principal Fund are made to reflect the growing equity market. By targeting definitions to respective benchmarks, the Board will ensure the definitions are not outdated as quickly in the future.

Upon the motion of Regent De Simone and the second of Regent Marcovitz, the Committee approved Resolution I.2.l.(3).

Resolution I.2.l.(3)

That upon the recommendation of the Regent Business and Finance Committee, the modification of Investment Guidelines to Update Definitions/Restrictions be approved.

I.2.m. Closed Session to Consider Trust Fund Matters, as Presented by s. 19.85(1)(e), *Wis. Stats.*

Upon the motion of Regent Brandes and the second of Regent De Simone, the Business and Finance Committee adjourned to Closed Session at 3:15 p.m., to consider Trust Fund matters as permitted by s. 19.85(1)(e), *Wis. Stats*.

The Business and Finance Committee adjourned at 3:30 p.m.

Donita R. Zintz, Recording Secretary