**Minutes**
**Business and Finance Committee**
**Board of Regents of the University of Wisconsin System**
**October 4, 2001**

The Business and Finance Committee met at 1:37 p.m. in the Arrowhead Room at UW-Eau Claire, in a joint meeting with the Physical Planning and Funding Committee to discuss Systemwide Energy Conservation. The meeting concluded at 2:25 p.m. Details of that discussion are covered in the Physical Planning and Funding Committee minutes.

Following the joint meeting with the Physical Planning and Funding Committee, the Business and Finance Committee reconvened at 2:30 p.m. in the Potawatami Room at UW-Eau Claire. Present were Regents Gottschalk, Axtell, Jones, Klauser, and Krutsch.

**c. Building Our Resource Base**

Associate Vice President Kathi Sell made some introductory comments about the series of papers that will be presented over the coming months on "Building our Resource Base," noting that the month that certain topics are scheduled for presentation has been revised. In November there will be a discussion on federal fund raising and gifts, grants and contracts. The discussion of all tuition options will take place in December.

The basic goals of "Building our Resource Base" are: 1) flexibility/fungibility of the revenues we have at our disposal; 2) increasing interest earnings as the UW System relies on these sources; and 3) providing stability and predictability in our revenue base.

**1. Follow-up on National Higher Education Resource Strategies**

Terry MacTaggart, Chancellor, University of Maine System, was unable to present to the Committee due to his travel plans.

**2. Ability to Keep Investment Earnings**

Vice President Debbie Durcan noted that the issue paper exploring the ability to keep interest earnings is the second in a series of papers on financing options that will be explored over the course of the year. At present, the Board has statutory authority to invest surplus auxiliary funds and those gifts, bequests and devises that are received as Trust Funds. Under an investment agreement negotiated with the Department of Administration (DOA) auxiliary funds are invested by the State of Wisconsin Investment Board (SWIB) and earn the same interest as the state's cash fund. Trust Funds are invested through our contracts with investment managers. The interest earned on all other program revenue appropriations accrues to the state's general fund, not to the UW System.

The paper covers three options: 1) request statutory authority to keep investment earnings on selected additional program revenue funds including tuition, private gifts, grants and contracts, and federal indirect cost reimbursement; 2) amend the investment agreement with DOA to permit the investment of a portion of auxiliary funds in longer term investments; 3) ask the state to allow the UW System to be able to manage all of its cash in whatever investment vehicles it deems appropriate.

Vice President Durcan noted the advantages and disadvantages of each option:

Option 1—keeping investment earnings on select program revenue funds

- Requested in 01-03 biennial budget for tuition appropriation.
- Estimated tuition interest would be $4.9 million.
- Other three appropriations would provide $3.3 million of earnings.
- Treats all student-provided dollars the same (auxiliary funds and tuition).
- Private donors already probably assume interest goes to the UW on their gifts.

- Financial benefits lost if the state takes away corresponding GPR support.
- Would require a statutory change for all appropriations except for gifts. Historically, only long term gifts or gifts associated with bequests have been invested.

Option 2—investing auxiliary balances in longer term investments

- Estimated additional earnings could reach $5.5 million.
- Many auxiliary revenues are collected for long-term needs (facility renovation, deferred maintenance, etc.).
- Current statutory language provides that auxiliary balances can be invested in securities that are legal for trust fund investments.
- No statutory change is needed but the investment agreement with DOA would have to be amended to make this change.
- Because of the scrutiny given to auxiliary balances, others may interpret a move to longer term investments as meaning that these balances are in excess of need and therefore available for reallocation.

Option 3—Full cash management for all program revenue funds

- Estimated additional earnings of $11.1 million.
- Would require additional staffing to perform the full treasury management function including movement of funds among investment types based upon daily estimation of cash flows.
- Gives the UW full control over all cash balances.
- Would require statutory changes.

Regent Klauser asked whether UW System Administration retains a portion of the interest on auxiliary balances. Vice President Durcan reported that the full amount of the interest earned on auxiliary balances is distributed by UW System Administration to the institutions based upon their daily book balances in the auxiliaries appropriation.

Regent Krutsch asked whether the interest earned on any additional program revenue appropriations would be allocated to the institutions or retained to meet systemwide priorities. Vice President Durcan responded that the disposition of any new interest earnings would need to be reviewed. At a minimum, System Administration would recover the cost of cash management function before allocating interest to the institution or project that generated the interest.

Regent Axtell asked whether other state agencies earn interest on their program revenue appropriations. Vice President Durcan reported that UW System's auxiliary operations appropriation is the major appropriation within the state's General Fund that is credited with interest earnings. Regent Klauser pointed out that the interest earned on "segregated" funds such as the Transportation Fund and Natural Resources Fund accrues to the segregated fund and not to the General Fund.

Regent Klauser expressed the belief that the UW System should be able to attain the authority to retain interest earnings on its tuition appropriation.

**3. Seamless Management of Tuition and Non-allocable Auxiliary Revenues**

Assistant Vice President Freda Harris noted that "Seamless Tuition and Fee Management" is the third in a series of options for "Building Our Resource Base." Seamless tuition and fee management, unlike many of the other resource topics, does not provide increased revenue. Instead it provides the ability to maximize the use of existing dollars. It would allow managers to remove some of the barriers that currently exist between auxiliary revenue and tuition. Seamless tuition and fee management was suggested by some of our former chancellors who had experience at other institutions with more ability to "treat all dollars as green."

Currently, tuition and state funds (GPR) are pooled. They are treated interchangeably or "fungibly" in supporting the instructional mission of the UW System. The pooling of GPR and fees is an example of the seamless management of funds. In contrast, the revenues generated by auxiliary operations are, for the most part, retained for the exclusive use of the operation that generated those revenues.

Auxiliary resources are funds that are derived from user charges for services that provide a benefit to students, faculty, staff and the public. Some examples of auxiliary operations are unions, cafeterias, dormitories, athletic operations, golf courses, parking operations, and health services. Segregated student fees, funds generated from a separate charge to students for student related activities such as union fees, organized activities, health care charges, are also a form of auxiliary revenue.

Student segregated fees may be either allocable or non-allocable. Allocable funds are primarily managed by students. The use of allocable funds can be decided on an annual basis, such that students can decide to fund an activity in one year and not the next. Non-allocable funds represent that portion of the segregated fee that is required to fund the commitments previously made by students for specific operations including debt service and salaries of staff. For this reason, there is less student involvement in non-allocable segregated fee decisions.

Ms. Harris discussed dormitories as an example of the current UW System policy for the separate management of auxiliary funds and tuition. Residence halls are expected to be self-supporting and do not generally receive tuition funding. Likewise, residence hall fees are used for the exclusive support of the residence hall program and related administrative overhead and are not used to support the instructional program or other institutional purposes. In some cases, such as the placement of a computer laboratory in a residence hall, tuition funding from the student technology fee may be combined with residence halls funds to cover the specific costs related to the laboratory, but the tuition could not be used to fund any other dormitory need. There is a clear firewall that has been established by the state and the UW System to expend these funds for the purposes for which they are generated.

In the Board of Regent's 21st Century Study, the UW System made a small step towards breaking down the barriers between tuition and fees by requesting statutory authority to allow one-time transfers of surplus auxiliary funds for other student related activities. That flexibility has been used twice since it was attained in 1997. The limited use may be related to the restrictions on when the flexibility must be requested (during the annual budget review by the Board) and what funds may be used (surplus funds for one-time, fixed duration costs).

Regent Krutsch asked about the two instances where the transfers were made. Ms. Harris responded that the first instance was when the UW-Green Bay child care program was closed and the second was UW-Milwaukee's transfer of funds for the student information services program.

Ms. Harris explained that to reach the ultimate flexibility, seamless tuition and fee management would require all auxiliary revenue and segregated fees to be fungible. Chapter 36 of the state's statutes provides students with input into the disposition of funding for student related segregated fee funds. The UW System, the State, and the Board of Regents are strongly supportive of student governance, as demonstrated in the Southworth case. For this reason, we feel that this option is not a viable one. A variant on this would provide flexible management of tuition and auxiliary revenues, excluding allocable segregated fees but including non-allocable fees in the seamless mix. Non-allocable segregated fees are already committed to pay for other things but, under the seamless management philosophy, could be used for any student related purpose under the current board policy on one-time transfers if excess balances are accumulated.

Another option would be to seamlessly manage tuition and auxiliary revenues other than segregated fees. This option would eliminate concerns related to student governance and still provide institutions with more flexibility. This option would increase management flexibility on the campus but would require campuses to carefully plan so that needed auxiliary reserve balances are maintained. There is a fundamental difference between the management of tuition and GPR on the one hand and the management of auxiliaries on the other. Tuition and GPR are treated as just-in-time funding, available when needed, and not before that time. Auxiliaries are operated as businesses and reserves must be maintained to sustain operations when unanticipated expenditures are incurred or revenues fall short. In addition, auxiliaries must accumulate funds to cover planned expenditures that do not occur annually such as mattress replacement or building renovations.

Some campus business officers have expressed concerns about treating tuition and auxiliary revenues seamlessly. While institutions welcome greater flexibility in managing funds, the business officers are concerned that auxiliary funds being accumulated for expenditures that will not occur for 2-3 years may be seen as “available” to cover short term needs when combined with tuition and state funds. In addition, this year there was proposed legislation that would have used auxiliary reserve balances for the regular state budget. The UW System was able to point out that the reserves were planned for specific purposes and not just excess revenue. However, moving in this direction might send a contradictory message.

The final option is to change the current board policy for one-time transfers and loans. Suggested changes would be to: 1) allow changes during the year with a report back to the Board during the annual budget of any transfers/loans that have occurred; 2) delegate the authority to approve changes to the President; and 3) set up a working group of chancellors and business officers to recommend other changes that would increase the likelihood that the flexibility would be used.

**d. UW-Eau Claire presentation on Operating Budget Challenges**

Andrew Soll, Vice Chancellor, Business and Student Services, UW-Eau Claire, discussed operating budget challenges and initiatives facing UW-Eau Claire. Over 88% of the operating budget goes to fund salaries and fringes, and another 6% goes to fund non-discretionary items such as utilities and debt service. Only the remaining 6% of the budget is available for discretionary spending on supplies and services. Vice Chancellor Soll also discussed differential tuition at UW-Eau Claire. Now in its fifth year, differential tuition, approved by UW-Eau Claire students, enhances their educational experience. Students help to determine how the annual revenue of $950,000, resulting from the program, is spent. Finally, Mr. Soll discussed other UW-Eau Claire ideas such as faculty/student collaborative research, first year (freshman) experiences, capstone experiences, and service-learning programs.

**e. Committee Business**

**1. Approval of minutes of the September 6, 2001 meeting of the Business and Finance Committee**

Upon the motion of Regent Klauser and the second of Regent Jones, the minutes of the September 6, 2001, meeting of the Business and Finance Committee were approved as presented.

**2. Annual Sick Leave Report**

George Brooks, Associate Vice President of Human Resources presented the annual sick leave report to the Committee as required by statute. Due to a concern that UW faculty and academic staff report less usage of sick leave than other state employees, the State legislature established a cap, effective August 1, 1987, on the amount of unused sick leave that can be converted annually by faculty and academic staff to pay for group health insurance upon retirement. Faculty and academic staff earn 12 days of sick leave per year. However, annual conversion of sick leave credits is capped at 8.5 days for those with annual (52-week) appointments, and 6.4 days for those with academic year (39-week) appointments. The sick leave cap does not apply to classified staff. As permitted by statute, the cap has been waived by the Secretary of the Department of Administration, since certain specified conditions have been met by all UW institutions. However, the statute continues to require an annual review of sick leave usage.

**f. Trust Funds**

**1. Update On Private Capital Manager Search**

Doug Hoerr, Treasury Manager, noted that the deadline for accepting applications from private capital managers was extended to October 3, 2001. There were 46 responses, therefore the Trust Funds office will conduct a pre-screening of applications to ensure compliance with applicant requirements, and limit the number of applicants for the core evaluation team. Mr. Hoerr noted that the evaluation team would still attempt to select finalists by the end of the month, and they may be presented to the Committee during the November meeting.

**2. History of Quasi-Endowment**

Mr. Hoerr noted that the Business and Finance Committee asked that the history of the current quasi-endowment policy be reviewed and summarized, and that further thought be given to the appropriateness of the policy and/or further principles to be applied in the granting of exceptions to it. The current policy resulted from the Business and Finance Committee's action of October 4, 1990, where upon the Board of Regents passed resolution 5631. This resolution states that all new quasi-endowments (bequests where the donor remains silent as to the use of principal) greater than $50,000 be identified as designated endowments, with only income to be made available for expenditure. The resolution further states that should the receiving institution desire an exception to this rule (whether upon initial acceptance of the gift or subsequently), the request for exception with appropriate justification should be submitted for approval and be incorporated in any subsequent Regent resolution of acceptance.

Existing records indicate that the discussion leading to the current policy began at the Business and Finance Committee's meeting of July 12, 1990. The meeting minutes indicate that Legal Counsel Stathas presented for acceptance a bequest from the estate of W.G. Kirchoffer in the amount of $303,000. Although not perfectly clear from the minutes and the wording of Mr. Kirchoffer's will, it appears that this bequest was considered a quasi-endowment, with the donor not specifically restricting the use of principal. The meeting minutes go on to state: "The committee directed System Administration to prepare a report on the ability of the regents to place additional restrictions on the expenditure of principal on quasi-endowments."

A report regarding quasi-endowments from then-Vice President for Business and Finance, Fred Poellnitz, Jr., was sent to the Committee and all Regents on August 29, 1990. This report stated: "Based on a review of the Wisconsin Statutes, Regent Policies and Bylaws, in the absence of donor language to the contrary, there are no rules or regulations which would prevent the Regents from imposing restrictions on the expending of principal. A formal Regent resolution is not necessary, as the authority granted the Business and Finance Committee allows them to impose restrictions, which in their judgment are deemed appropriate." The report then concludes by recommending the current policy (exactly as it was later stated in resolution 5631). This report was then discussed at the Business and Finance Committee meeting of September 6, 1990. The meeting minutes state: "After discussion, the committee endorsed a practice which specifies that in the absence of donor language, all new quasi-endowments greater than $50,000 would be identified as designated endowments… The committee asked System Administration to develop a resolution to be presented at the October meeting which would make this practice regent policy." This resolution was then unanimously approved by the Committee on October 4, 1990, and adopted by the Board of Regents as resolution 5631.

Former Legal Counsel Stathas was recently asked what his recollection was as to the reasoning behind the Board's adoption of the current policy. Mr. Stathas stated that the Board adopted the policy to try to grow funds by limiting the spending to income only on larger bequests. Mr. Stathas further commented that since this policy is self-imposed and not donor-imposed, the Board should permit the spending of principal on quasi-endowments when requested to do so.

Regarding the origin of or reasoning behind the $50,000 level, only one item was found in Trust Funds files. This was a hand-written note (from then-Assistant Trust Officer David Konshak, presumably) indicating that $50,000 should be used since this was the level at which gifts are taken individually to the Board for acceptance.

It would seem that the intent of the Board in adopting the current policy was simply to designate large, unrestricted gifts to be used as "endowed" assets, which could meaningfully and perpetually support the benefiting program or need (either by itself or in conjunction with other endowed assets benefiting the same) through the spending plan distribution (5% per year), while still growing the endowed asset base so as to maintain and grow this perpetual support. This objective may be considered particularly relevant since University Trust Funds represent largely unsolicited gifts currently; therefore, the endowed asset base cannot be expected to grow as significantly through new contributions as it would if fundraising and solicitation were actively pursued.

In considering the $50,000 level again, it is important to note that a gift of this size would provide for only $2,500 in annual spending initially. Depending on the benefiting program, unless combined with other sources, this may not provide meaningful or sufficient support. Also, since this level was established eleven years ago, simply adjusting it for inflation would imply a current level of approximately $70,000, which would generate $3,500 per year initially. Establishing a new threshold of $100,000 could even make sense, as a gift of this size would generate $5,000 per year.

The Board may ask whether there are other principles that could be applied to the consideration of exceptions to this type of policy where any quasi-endowed gift for any program/need in excess of a certain level must become a designated endowment unless the benefiting institution justifies an exception. One possibility might be a principle based on the nature of the benefiting program/purpose. For instance, if the donor specifies that the gift be used for scholarships, fellowships, professorships, a certain minimum level could be set; if for research, art/library acquisitions, or at the discretion of the receiving institution, other levels could be established. In requesting exception to any such policies, the benefiting institution might also be required to demonstrate that the new gift could not be "combined" with other gift sources to provide the desired annual or near-term support.

Mr. Hoerr noted that other peer institutions have not yet been surveyed on their quasi-endowment policies. Mr. Hoerr did survey an estate planner and tax lawyer from Marshall and Ilsley Bank, who mentioned that the donor should always be encouraged to specifically address the use of principal in their gift language. Mr. Hoerr mentioned that if the donor remains silent, then the donor's relatives are often consulted, to better understand donor intent. If this is impossible, the donation should always be endowed.

Regent Gottschalk noted his concern for the UW System's goal of growing the endowment. Well meaning department's can always justify spending the funds in the short term, but they must understand that these funds are critical to the continued support of the UW System.

The Committee continued to discuss raising, or possibly lowering the $50,000 threshold, but concluded there was no compelling reason to change the current quasi-endowment policy.

**3. Investment Guidelines Related to Annual Meetings with Managers**

Mr. Hoerr noted that the Business and Finance Committee has historically met annually with each individual Trust Fund investment manager in the closed session portion of their monthly Committee meeting. (There are presently nine investment managers.) The Committee expressed interest in delegating the responsibility to regularly meet with the managers to the Trust Officers and/or Assistant Trust Officer(s), with the expectation that a report on such meetings would be provided to the Committee. The Committee further asked that Trust Funds investigate what current policies addressed this responsibility and what changes, if any, would be required to delegate it.

Trust Funds reviewed the promulgations that deal with the annual meeting requirement, or the ability of the fund trustees to delegate such fiduciary responsibilities. Nothing was found in Wisconsin Statutes nor Regent Bylaws that require the Board of Regents specifically, or trustees in general, to meet at least annually with managers given discretionary investment authority. Trust Funds also reviewed Board of Regent Policies regarding delegation of such fiduciary responsibilities. Policy 71-4, Management and Administration of Trust Funds, does not specifically address this responsibility, but does state that "the Business and Finance Committee is authorized, with the approval of the Board, to delegate such powers and responsibilities regarding the management and administration of university Trust Funds to the Trust Officer or other administrative officers or employees of the University as the Committee may in its judgment deem appropriate…" However, Policy 91-11, Investment Objectives and Guidelines, states in the "Reports" section dealing with what is expected of the managers: "Annual investment meetings (more frequently, as warranted) will be held with the Committee." Therefore, there seems to be no reason why the Committee could not delegate the responsibility of regularly meeting with investment managers to the Trust Funds' Assistant Trust Officer, pending an appropriate modification to Policy 91-11.

Regent Gottschalk noted the Committee's consensus that the annual investment meetings should be delegated from the Business and Finance Committee. Upon the motion of Regent Klauser and the second of Regent Axtell, the Committee directed that a resolution be brought before the Committee next month to vote on this change to Regent policy.

**g. Nonresident Undergraduate Tuition Increase for Spring 2002**

Assistant Vice President Freda Harris noted that the 2001 Senate Bill 55, the state's 2001-03 budget bill, was signed by the Governor on August 30, 2001, and became 2001Wisconsin Act 16. The bill, prior to the governor's signature, included legislation approved by both houses of the legislature that would have increased nonresident undergraduate tuition by 2.5% for the 2001-02 academic year, and another 2.5% for 2002-03.

The governor exercised his partial veto authority, and left a 5% nonresident undergraduate tuition increase in 2001-02 and another 5% increase in 2002-03. In addition to doubling the tuition increase, the governor also doubled the UW System's state funding (GPR) base cut associated with this tuition increase from $2 million to $4 million this year, and from $4 million to $8 million next year.

The resolution being presented merely ratifies an action already mandated by the state budget bill. While the Board has no practical option other than to approve the resolution, Ms. Harris noted the nonresident undergraduate tuition is increasing throughout the UW System to levels near the top among our peer institutions and that this could result in the UW System losing some nonresident students. This issue will be discussed further when the Committee reviews tuition options in December.

Upon the motion of Regent Axtell and the second of Regent Jones, the Committee approved Resolution I.2.g.

**[Resolution I.2.g.]**

That, upon the recommendation of the President of the University of Wisconsin System, tuition for nonresident undergraduate students be increased by 2.5%, starting with this spring semester to reflect the final legislative budget, Wisconsin Act 16, signed by the Governor.

**h. Report of the Vice President**

Vice President Debbie Durcan reported that the Governmental Accounting Standards Board (GASB), the organization that promulgates rules for the not-for-profit sector including public higher education, has released a new exposure draft on affiliated organizations and how they should be reported. Currently GASB requires incorporation of an affiliated organization only if the primary government controls or is accountable for the organization or if exclusion of the organization causes the reporting entity's financial statements to be misleading or incomplete. The proposed statement would require discrete presentation within our financial statements if all of the following three criteria are met:

- The economic resources of the separate affiliated organization entirely or almost entirely directly benefit the primary government, its component units or its constituents.
- The primary government or its component units are entitled to, or can otherwise access, a majority of the economic resources of the separate affiliated organization.
- The economic resources that the specific primary government is entitled to, or can otherwise access, are significant to that primary government.

The UW System is considered a "primary government" because we issue our own financial statements. Ms. Durcan noted that "ability to access" is not based on legal control but rather the historic record of providing resources. She has filed a comment letter with GASB opposing the Exposure Draft and has urged other public institutions to do so as well. The UW System has met with the state controller and the LAB audit director in charge of the University's audit. The comment period ends at the end of October.

Vice President Durcan noted the UW System's concerns with the proposal:

- The standard is too far reaching and would force inclusion of a number of organizations over which we exercise little or no control.
- These organizations are separate legal entities and their inclusion would be confusing and misleading.
- These organizations report their activities through their own independently audited financial statements and are accountable to their own board of directors.
- The UW System would have considerable difficulty in complying. A number of the UW System's affiliated organizations have stated that they will provide us copies of their independently audited financial statements, but will not open their records to us.

Vice President Durcan discussed the Tripp Trust Expenditure Plan. The UW System will be coming to the Board with this plan after the UW-Madison campus is able to conduct a facilities condition assessment. This involves entering all data into FACMAN for the various facilities and grounds at Brittingham. From this information, a long-range plan can be put together, including the appropriate funding sources. The UW System expects that this will be completed in early spring.

Linda Weimer, Vice President of University Relations reported that over $5,000 in contributions has been received for the President's Fund in connection with the 30th anniversary celebration. Also, information about fund raising by peer institutions will be brought before the Committee next month. Regent Gottschalk asked that this information include a list of other campuses that have their own foundations.

**i. Closed Session to consider trust fund matters, as permitted by s.19.85(1)(e), Wis. Stats.**

Upon the motion of Regent Axtell and the second of Regent Jones, the Business and Finance Committee adjourned to Closed Session at 4:25 p.m. Present were Regents Gottschalk, Axtell, Jones, Klauser, and Krutsch.

The Business and Finance Committee adjourned at 5:25 p.m.

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Eric Engbloom, Recording Secretary