University of California

Stricter Oversight and Greater Transparency Are Needed to Improve Its Compensation Practices

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University of California's response as of May 2007

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits review the compensation practices of the University of California (university) and to identify systemwide compensation by type and funding source. In addition, we were asked to categorize the compensation of highly paid individuals receiving the most funds from state appropriations and student tuition and fees, and to determine whether they receive any additional compensation or employment inducements not appearing in the university's centrally maintained records.

The audit committee also asked us to determine the extent to which university compensation programs are disclosed to the Board of Regents (regents) and to the public, including the types of programs that exist, their size and cost, and the benefits that participants receive. Finally, we were asked to survey other universities about their compensation disclosure practices and the number of participants and expenses for those programs. Our survey found that the University of California' disclosure practices were similar to those of other universities.

Finding #1: Lack of consistency within the Corporate Personnel System (CPS) limits its usefulness.

The personnel information reporting system used by the university, the CPS, contains inconsistencies and overly vague categorizations. For example, we found a number of instances in which campuses included specific types of compensation, such as housing and auto allowances, in other categories not related to such allowances or in broad nondescriptive categories. Consequently, we could not determine the reliability of the amounts recorded in various compensation and funding source classifications contained within the CPS. In addition, the weaknesses of the CPS limit its usefulness as an oversight tool for the Office of the President (president's office) to monitor campuses' compliance with compensation policies. However, because the CPS is the most detailed and centrally maintained source of this information, our report presented several tables summarizing that total pay to university employees in fiscal year 2004–05 was $9.3 billion, of which $8.9 billion was regular pay and $334 million was additional compensation.

To improve its ability to monitor campus compliance, we recommended that the president's office issue clear directives prescribing consistent use of the CPS and require campuses to consistently classify compensation into standard categories. We also suggested that the president's office consider developing additional automated controls and edits within the CPS to ensure that expenditures are properly charged and to help avoid the possibility of errors.

Audit Highlights . . .

Our review of the compensation practices of the University of California (university) revealed the following:

- *The Corporate Personnel System (CPS) used by the university's Office of the President (president's office) to track the pay activity of university campuses contains inconsistencies and overly vague categories that did not allow us to determine the reliability of various compensation and funding source classifications contained within it and that limit its usefulness as an oversight tool.*
- *Despite these problems, the CPS is the most detailed and complete centrally maintained source of information, and in fiscal year 2004–05 it reflects that university employees earned approximately $9.3 billion—comprised of $8.9 billion in regular pay and $334 million in additional compensation.*
- *The president's office appears to regularly grant exceptions to university compensation policy. In a sample of 100 highly paid university employees, 17 benefited from an exception to compensation policy.*
- *Some university campuses circumvented or violated university policy, resulting in a $130,000 overpayment to an employee and improper increases to others' retirement covered compensation.*

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» *The university did not consistently disclose its officers' nonsalary compensation, such as housing allowances, to the Board of Regents as required by policy.*

University's Action: Pending.

The university states that by August 2007 it will issue guidance clarifying the proper use of transaction codes within the CPS and, in the future, will restrict the assignment of new codes to the president's office. After putting in place guidance to provide greater clarity about the intended use of CPS categories, the university indicates it will develop appropriate edits and analysis tools to screen for anomalies. Additionally, the university states it has developed an automated system to make compensation data for the senior leadership group available for querying and reporting, and is in the process of improving the accuracy and consistency of the data in this system.

Finding #2: The president's office regularly granted exceptions to the compensation policy.

The president's office regularly granted individuals exceptions to the university's compensation policy. University policy authorizes the president's office to approve policy exceptions that provide employees with benefits for which they otherwise would not be eligible. Seventeen of the 100 individuals in our sample benefited from an exception to policy, such as housing or moving allowances above established limits, auto allowances, or participation in the university's senior management severance pay plan.

To preserve the integrity of its compensation policies, we recommended that the president's office limit the number of exceptions to policy it allows. We suggested accomplishing this objective by the regents requiring the university to track and annually report exceptions to compensation policy that various university officers and officials grant during a fiscal year and provide justification for each exception.

University's Action: Partial corrective action taken.

The university states it has issued an interim policy requiring campuses to document the basis and rationale for all exceptions to existing compensation policies and to report them to a newly created position of Senior Vice President–Chief Compliance and Audit Officer. As of May 2007 the university indicated that it will soon be interviewing final candidates for this position. The new position will evaluate exceptions to policy to determine if they were made in accordance with the intent of existing policy, and report any concerns to the president and the regents. In addition, the university also states that this position will be responsible for developing additional monitoring and oversight activities.

Finding #3: The circumvention of policy caused a significant overpayment and inappropriate increases in retirement-covered compensation.

Some campuses circumvented or violated university policies, resulting in an overpayment to a university employee and questionable forms of compensation provided to others. These instances included an employee at the University of California at San Diego (San Diego) who received an overpayment of $130,000 and a San Diego vice chancellor who continued to receive a $68,000 administrative stipend and an $8,900 auto allowance despite being on sabbatical. Our review also revealed that some campuses violated the university's retirement plan policy by including inappropriate forms of compensation, such as housing and auto allowances, in three employees' retirement-covered compensation, a percentage of which they may receive when they retire.

We recommended that the president's office improve its oversight of campuses' compliance with university policies by developing a mechanism to annually identify unauthorized exceptions to policy. We also recommended that the president's office determine if it is appropriate to require repayment of university funds for the instances we identified and if so, develop a repayment plan with each employee. We further recommended that the president's office remove the inappropriate forms of retirement-covered compensation we identified from the employees' retirement earnings and establish a mechanism to detect such violations.

University's Action: Partial corrective action taken.

To address our recommendation that it annually identify unauthorized exceptions to compensation policies, the university states the president's office has identified arrangements that may be exceptional in nature by taking a more active role in the oversight of the preparation of executive compensation reports. Further, it indicates that its efforts to improve the clarity and consistency of recordkeeping will allow the university to more easily identify transactions that may be exceptional in nature. In addition, the university indicates that the newly created position of Senior Vice President–Chief Compliance and Audit Officer, will be responsible for developing additional monitoring and oversight practices for the campuses' compensation actions. The university states it has resolved most of the exceptions identified in our audit report by either obtaining the regents' approval of those exceptions or notifying the regents about them. The university indicates that a small number of matters were referred to the university's office of the General Counsel or to the appropriate campus in circumstances where the regent's approval would not be appropriate. A few of those issues are still pending. Additionally, the university asserts it corrected all inappropriate forms of retirement-covered compensation we identified and states that its efforts to clarify the use of codes within CPS and increase its audits of retirement-covered compensation should reduce the risk of similar errors occurring in the future.

Finding #4: The university consistently violated policies the regents established to ensure adequate review of executive compensation.

The regents' policies require them to approve all forms of compensation for officers of the university. Although the university consistently obtained approval for officers' salaries, in a sample of 10 officers we found that the university violated its policy by failing to disclose eight auto allowances, four housing allowances, two transfers of sabbatical credits, and an acceleration of health insurance contributions when the regents considered the individuals' appointment. Additionally, we found that the usefulness of the university's annual report on compensation to the regents was limited because the fiscal years 2003–04 and 2004–05 reports contained errors and were submitted late.

We recommended that the regents require the president's office to disclose all forms of compensation for university officers and for all employees whose compensation exceeds an established threshold. We further stated that this disclosure should occur when the regents approve the employees' salaries and at least annually in an accurate and timely report to the regents. Finally, the university should ensure that its annual report on compensation is accurate and timely.

University's Action: Partial corrective action taken.

In September 2006 the university developed two policies regarding how it will ensure better disclosure of employee compensation to the regents and the public. These practices include specifically identifying the elements of employee compensation to disclose in its annual report on senior management compensation and recent hires of executives and those earning an amount that requires the regents' approval, and the methods it will use to disclose this information. Additionally, the university has developed a compensation checklist, which it indicates the regents receive when approving employee compensation. To ensure the accuracy of the annual report, the university states that campus internal auditors will audit the data and campus administrators must certify the data's accuracy.