

Research & Occasional Paper Series: CSHE.7.08

CSHE | Center for Studies in Higher Education

UNIVERSITY OF CALIFORNIA, BERKELEY

<http://cshe.berkeley.edu/>

## EXECUTIVE COMPENSATION AT THE UNIVERSITY OF CALIFORNIA An Alternative View

May 2008

Patricia A. Pelfrey\*

Center for Studies in Higher Education UC Berkeley

*Copyright 2008 Patricia A. Pelfrey, all rights reserved.*

---

### ABSTRACT

The 2005-6 executive compensation controversy at the University of California has been explained as the result of a massive breach of compliance with the University's compensation policies by the Office of the President (UCOP). For more than a decade, the explanation goes, UCOP failed to comply with its own compensation policies, embodied in the 1992-93 Principles for Review of Executive Compensation, and engaged in a longstanding pattern of secrecy and policy violations. This paper argues that both assertions are wrong. It begins by analyzing the issues leading to adoption of the Principles and presents the evidence that the procedures for implementing them were consistent with prevailing understandings of presidential authority and Regental intent. With several exceptions that will be noted, this remained the case throughout the administrations of UC presidents J. W. Peltason (1992-5) and Richard C. Atkinson (1995-2003). The situation changed as the result of two developments early in the tenure of President Robert C. Dynes (2003-2008). First, executive offers began to include benefits that were not traditionally employed at UC, and the Regents as a body were not asked to approve them. Second, the board was not informed about these benefits because a report mandated by the Principles, the Annual Report on Executive Compensation, was not submitted in 2004 or 2005. These were significant departures from the Principles, but they were limited to two years, 2003-2005. The idea that non-compliance with the Principles was endemic in UCOP stems from media portrayals of the controversy and from an audit commissioned by the Regents in response to the controversy, the April 2006 PricewaterhouseCoopers (PwC) report. The PwC report failed to acknowledge the extent to which the Principles had been followed in the decade after their approval, and its interpretation of that policy was so different from the way it had historically been understood as to constitute a re-interpretation. Many of the putative violations in the PwC report reflect this re-interpretation of the Principles, not evidence of a longstanding failure in compliance or a culture of secrecy in UCOP. This major lapse of institutional memory has had serious consequences for governance and the future role of the Office of the President.

---

### Introduction

In November 2005, the *San Francisco Chronicle* launched a series of articles about the University of California, charging that UC had systematically awarded its highest-ranking officials everything from salary raises and bonuses to housing allowances and vacation leave

---

\* Patricia A. Pelfrey is a research associate at the Center for Studies in Higher Education at the University of California, Berkeley. From 1970 to 2002, she served on the immediate staff of five University of California presidents.

without the approval of its Board of Regents or disclosure to the public. The ensuing controversy, which unfolded over many months in the pages of the *Chronicle* and other publications, left the public with vivid images of a culture of entrenched bureaucratic secrecy, administrative excess, and willful inattention to the University's own policies. *San Francisco* magazine summed it up as "the explosive story of UC's secret practices of rewarding its top officials extravagant bonuses and perks—at a time when the system was in financial crisis."<sup>1</sup>

Behind the 2005-6 executive compensation controversy lay the shadow of another one, a dispute relating to the retirement arrangements for former UC President David P. Gardner. This earlier controversy erupted in 1992, engendered its own share of public and legislative outrage, and led to major changes in UC's compensation policies and practices. In February 2006, at a hearing on the executive pay issue held by the State Senate Education Committee and the Senate Budget Committee's Subcommittee on Education, state Senator Abel Maldonado reminded the UC officials present that their predecessors had been called upon to explain UC's compensation practices at legislative hearings more than a decade earlier. "Why are we here again?" he demanded to know.

At the heart of the issue were the Principles for Review of Executive Compensation, adopted by the Regents in 1992 and revised in 1993. The Principles were the Regents' policy response to the Gardner controversy, and they laid out how executive compensation was to be defined, discussed, approved, and disclosed. Blame for the events of 2005-6 has been laid at the door of the UC Office of the President (UCOP), which, the explanation goes, ignored, forgot, or misunderstood the Principles until the *San Francisco Chronicle* uncovered a hidden history of administrative lapses and policy violations. The Task Force on UC Compensation, Accountability, and Transparency put it this way: "In the early 1990s, in the wake of public controversy regarding executive compensation at the University, new policies were put in place by the Regents to prevent future problems in this area. At least some of the current problems would not have occurred if those policy reforms had been followed and enforced by the senior administrative leadership of the University system."<sup>2</sup>

Yet the UC presidents who served in the decade immediately after the Principles were adopted—J. W. Peltason (1992-95) and Richard C. Atkinson (1995-2003)—believed they were in compliance with them. Throughout these two administrations, the Regents seemed to agree, and this paper will present the evidence that they did. The issue is of more than strictly historical interest. The story that UCOP had spent more than a decade violating its own executive compensation policies led directly to a decision by the current Board of Regents to undertake a major review of the University's system of governance, beginning with the role of the Office of the President, that is still underway.<sup>3</sup>

The alternative view presented here is based on archival research in the Office of the President and the Office of the Secretary and Chief of Staff of The Regents, and on interviews with former UC Regents, presidents, officers, and staff; several current UC administrators and staff also responded to questions and requests for information. My analysis argues that the events of

---

<sup>1</sup> Diana Kapp, "The Scandal, the Scapegoats, and the Suicide," *San Francisco*, March 2007, pp. 53-72.

<sup>2</sup> "Report of the Task Force on UC Compensation, Accountability, and Transparency," April 2006, p. 1. This task force was appointed by the Regents.

<sup>3</sup> A January 18, 2008 letter from Regent Sherry Lansing et al. to Ralph Wolff, President and Executive Director of the Western Association of Schools and Colleges, notes that ". . . the Board itself understood that the executive compensation issue was illustrative of a broader governance problem and took action to initiate a process to review and respond to that broader problem." Available at <http://www.universityofcalifornia.edu/senate/committees/council/ac.wasc.report.0108.pdf>.

2005-6 were not caused by a deliberate or inadvertent failure to implement the Principles in the decade following their adoption. They were the outcome of several much more recent developments. The first dates to 2003 when, in response to an increasingly competitive higher-education marketplace, a number of offers made to prospective executives began to include benefits that were not standard practice or addressed in policy at UC—payment for sabbatical credits earned at other universities, for example. The Regents as a body were neither asked to approve these non-standard benefits nor informed about them. For two years in a row, in 2004 and 2005, the administration failed to send the Regents an annual report on executive salaries and benefits mandated by the Principles—a bureaucratic oversight with serious consequences.

These developments were transformed into a story of longstanding administrative mismanagement not only through media accounts, but also through a report issued by the University itself—the PricewaterhouseCoopers (PwC) audit of April 2006. This audit of UC compensation policies and practices, commissioned by the Regents in response to a growing chorus of media and legislative criticism, was based on an interpretation of the Principles that differed in important respects from the way they were implemented in the years following their adoption 1992. Under the auditors' re-interpretation of the Principles, scores of administrative actions that would have been considered routine in earlier years were instantly redefined as policy violations.

The first two developments—the change in recruitment packages for some high-level positions and the lapses in informing the Regents in 2004 and 2005—created the executive compensation controversy of 2006. The third—the re-interpretation of the Principles in the PwC audit—became the basis of an official narrative claiming that, from the beginning, the Principles had never really been implemented. And this, in turn, served to validate media accusations that the Office of the President was an administration steeped in secrecy and out of control, even though the PwC audit never alleged either.

This paper explains the implementation of the Principles in terms of the challenges faced by the Regents of 1992 and what they hoped to accomplish by articulating the principles that would govern the University's executive compensation policies and practices. It concludes that the Principles were indeed followed between 1992 and 2003; that their implementation was based on a mutual understanding between the administration and the Regents about the authority of the president; and that the PwC interpretation misread the Principles because it did not take into account the context in which they were developed. The Principles for Review of Executive Compensation were written in the middle of a crisis, which means that, more than most official documents, they need to be read in light of their history.<sup>4</sup>

### **The 1992 Controversy**

During a meeting at UCLA in March 1992, the Regents of the University of California approved certain financial arrangements related to the retirement of President David P. Gardner. These included a three-month paid leave of absence and almost \$738,000 in deferred compensation. The \$738,000 figure was the total of five separate agreements under a program known as the Non-qualified Deferred Income Plan (NDIP) and two Special Supplemental Retirement (SSR)

---

<sup>4</sup> For a more detailed account of the history of the Principles, see Patricia A. Pelfrey, "Origins of the Principles for Review of Executive Compensation, 1992-3," May 2008, Center for Studies in Higher Education Research and Occasional Papers at <http://cshe.berkeley.edu/publications/publications.php?s=1>.

agreements.<sup>5</sup> All of these agreements contained a forfeiture provision that made Gardner ineligible to receive the funds if he retired before the various vesting dates, which he planned to do. However, in recognition of Gardner's exemplary service and the unusual circumstances of his decision to retire—his wife had died prematurely some months earlier—the Regents voted to waive the forfeiture provisions and change the vesting dates of these agreements, which ranged from 1993 to 1998. An outside law firm engaged by the University's General Counsel determined these actions to be legally valid.

Gardner's two SSRs and several housing-related perquisites had been approved by the chair of the Subcommittee on Officers' Salaries and Administrative Funds—a subcommittee of the Committee on Finance—and several other Regents, under delegations of authority that did not require reporting these actions to the full board. Among them was reimbursement for the property taxes on the president's personal residence, apparently as a way of recognizing his contributions without raising his salary. News of these benefits, and of the detailed compensation information available to the subcommittee but not to the board as a whole, came as an unpleasant surprise to many Regents when Gardner's retirement arrangements were discussed.

It was a time of fiscal duress for the University, which was struggling with one of the worst budget crises in its history, and the Regents were uncomfortably aware of the negative light in which all of these actions would be viewed by the UC community and the public. After an intense debate, the Regents issued a routine press announcement after the March meeting which noted only that they had approved several items related to the president's retirement, including changes in vesting dates for several compensation agreements.

Within days, the *San Francisco Examiner* and other newspapers were churning out headlines about the story behind the press release. In response, the University held a widely attended press conference that laid out all the details of the president's retirement arrangements. The explanation came too late to quell the crisis. Sensational revelations about the benefits Gardner received, and the board's process in approving them, created an extended public-relations nightmare for the Regents and the University. Some of these revelations had been leaked to the press by at least one disaffected member of the board.

It quickly became clear to the Regents that the most pressing problem was staunching the hemorrhage of bad news that was damaging the University's credibility and good name. Under hostile scrutiny from the media and threats of budgetary retaliation from the legislature, the Regents turned their attention to drafting a new policy statement that would restore public confidence and rectify the errors of the past. On May 15, 1992, just eight weeks after the March meeting at UCLA, the Regents unanimously adopted the Principles for Review of Executive Compensation.

The Principles were revised eighteen months later to conform with California legislation concerning open meeting procedures. In a move that would prove to be significant later, one of the revisions incorporated into the Principles was a new definition of the term "compensation." The revision was approved by the Regents at their regular meeting in November 1993, without discussion or comment.

---

<sup>5</sup>The Special Supplemental Retirement Program was adopted by the board in 1985 to compensate for retirement benefits executives would forfeit by moving from another institution to UC in mid-career; it was also used as a retention tool. A second SSR was approved in 1988 to offset benefit limitations imposed by the Tax Reform Act of 1986.

### **The Principles and Their Goals**

The Principles had two goals. The first was to deal with the allegations of secrecy that had inflicted serious damage on the University's standing with the public. The Principles begin by asserting the Regents' commitment to "public access, awareness, knowledge, and understanding of The Regents' decision-making processes" and noting that "public concerns . . . require a response." A number of Regents were convinced that the secrecy problem was a direct result of the operations of the Subcommittee on Officers' Salaries and Administrative Funds and the delegations of authority to its chair, which had made the allegations of secrecy plausible to the public and the legislature.

The Regents' second goal was to ensure that future deliberations on executive compensation would be based on more and better information than had been the case in the Gardner controversy. It was not just a question of better information about the compensation of the president or other high-level executives. The overwhelmingly negative public reaction to deferred compensation had come as a surprise, for example, and some Regents felt they had voted to approve the NDIP program without a full grasp of the implications of their decisions or of the magnitude of the sums involved. They wanted more regular, more timely, and more comparative data about UC's executive compensation programs, including the overall executive salary structure at the Office of the President and on the campuses.

Accordingly, the major requirements of the Principles were the following:

- Open meetings of both Regental committees and the full board when executive compensation programs were discussed.
- Sufficient information about executive compensation programs to give the Regents an understanding of what was being proposed. For executive appointments, agendas were to include "all compensation elements relevant to each individual officer under consideration."
- Executive compensation actions approved by the Regents were to be disclosed to the public "in a timely manner," and administrative mechanisms for doing so were to be "coordinated, strengthened, and refined."
- A yearly report—the Annual Report on Executive Compensation—was to be submitted to the board and then sent to the state's higher-education coordinating agency—the California Postsecondary Education Commission—as well as to "the relevant policy and fiscal committees of the Legislature and the Governor."

At the same meeting, the Regents also withdrew the delegations of authority to the chair of the Subcommittee on Officers' Salaries and Administrative Funds. One month later, in June 1992, they abolished the subcommittee altogether.

### **Interpreting the Principles: 1992-93**

As the choice of the word "principles" indicates, the Regents of 1992 wanted to articulate the fundamental values and expectations governing the board's relationship with the administration and the public. The Principles were therefore interpreted and implemented in light of the painful experience of the 1992 crisis, but also in terms of existing administrative practices and understandings about the authority of the president.

The Standing Orders of The Regents assign considerable latitude to the president in how the responsibilities of his office are carried out, including the appointment and compensation of

employees.<sup>6</sup> In terms of the daily implementation of executive compensation policy, this meant that the president was assumed to possess the responsibility and the authority to apply executive benefit policies in individual cases once those policies had been approved by the board, as long as his actions were consistent with Regental policies and the board was informed about them. The president's authority was understood to extend to granting exceptions to executive compensation policy as well.

The 2006 PwC audit challenged this broad view of presidential authority, for reasons that will be discussed later on. The report's conclusion that only the Regents could approve executive compensation had an important procedural corollary: All elements had to be listed in every executive appointment item. This is not how the Principles were understood during the years that spanned the Peltason and Atkinson administrations. Since the president was assumed to have authority to approve most compensation elements, appointment items sent to the Regents for their approval routinely contained only those elements of compensation the president did *not* have the authority to approve—such as base salary, special payments such as additional salary and bonuses, and non-standard benefits.

The administration's reasoning for not including standard executive benefits—such things as automobile allowances, eligibility for mortgage loans, and executive life insurance, for example—was twofold. First, the Regents had already approved standard executive benefits as policies or programs, so bringing them back in every appointment item was to ask for approval twice. Second, there were several ways in which the board was routinely reminded of the standard benefits offered by UC—through regular presentations on market data and comparison studies of UC chancellorial and other executive compensation, for example, and through annual reports on executive compensation in California's public colleges and universities prepared by the state's coordinating body for higher education, the California Postsecondary Education Commission (CPEC).<sup>7</sup>

Most important, there was the yearly summary mandated by the Principles: the Annual Report on Executive Compensation. This report listed the University's highest-ranking executives in the Office of the President and on the campuses. It included each officer's perquisites and benefits, as well as any exceptions to UC policy. The Principles directed that the Annual Report also be sent to the California Postsecondary Education Commission, several legislative committees, and the governor. It was therefore a public document, as the PwC audit noted.<sup>8</sup>

The Annual Report gave the Regents comprehensive information about the compensation of the top leadership and the University's salary and benefit structure, all in a single document. A 1996 Regents' item about board procedures cited the Annual Report's role in keeping the Regents "fully informed on the overall structure and range of all Officers' salaries" and noted

---

<sup>6</sup> Regents' Standing Order 100.4(a) read in part: "The President shall be the executive head of the University and shall have full authority and responsibility over the administration of all affairs and operations of the University, excluding only those activities which are the responsibility of the Secretary, Treasurer, and General Counsel of The Regents. . . ." Standing Order 100.4(c) states that "The President of the University, in accordance with such regulations as the President may establish, is authorized to appoint, determine compensation, promote, demote, and dismiss University employees, except as otherwise provided in the Bylaws and Standing Orders and except those employees under the jurisdiction of the Secretary, Treasurer, and General Counsel of The Regents."

<sup>7</sup> CPEC did not publish an annual report in 2003 because of budget cuts.

<sup>8</sup> The PwC report, in summarizing the various ways executive compensation was disclosed following adoption of the Principles, describes the Annual Report on Executive Compensation as "Distributed at Regents' meetings, provided to legislative bodies and available upon request." PricewaterhouseCoopers, "University of California Findings and Observations: Examination of Compensation and Other Employment Arrangements," April 21, 2006, p. 4.

that it could be “slated as an item for discussion at any time by any Regent who thought it was warranted.”<sup>9</sup> It is considered one of the most complete disclosure statements in American higher education, and its role in public disclosure was key.

In sum, two fundamental differences between the 1992 and 2006 PwC interpretations of the Principles are the scope of the president’s authority and the form in which compensation information must be conveyed to the Regents. The PwC report assumes all elements of compensation for individuals must be detailed in the appointment item. Under the 1992 interpretation, appointment items were commonly used to seek Regental approval of base salary and unusual or non-standard benefits, recognizing that the Regents had multiple sources of information about standard benefits. The Annual Report on Executive Compensation, which gave comprehensive information about *all* elements of compensation, including exceptions to policy, was not the only way in which the Principles’ twin goals of informing the Regents and the public were met. But it was by far the most important. For ten years, from 1993 to 2003, these reports were sent to the Regents and made available to the public.

What is the evidence that the board understood and acquiesced in these administrative assumptions about implementation of the Principles?

- *The authority of the president was not an issue in the 1992-3 controversy:* The only delegations of authority the Regents withdrew were those related to the operations of the Subcommittee on Officers’ Salaries and Administrative Funds. The PwC audit read the Principles as if they were about presidential authority, when in reality they were about Regental information. The Regents wanted more information from the administration, but not a change in the president’s administrative powers to implement compensation policies.
- *The definition of “compensation” in the original version of the Principles:* The document that the Regents approved in 1992 defined compensation narrowly, as base salary plus “all forms of deferred compensation, supplemental retirement, and all components of housing allowances.” These were exactly the benefits that had proved troublesome for the Regents and the University in the Gardner controversy. This definition is significant as an indicator of Regental intent at the time the Principles were adopted—i.e., the Regents’ concern focused on ensuring they were informed about unusual benefits, not those that all or most executives routinely received. This may be an additional reason why the practice from the beginning was to limit information in the item to certain non-standard benefits.
- *The consistency of administrative practice:* A review of fourteen chancellorial and vice presidential appointment items from the Peltason and Atkinson administrations shows that, from the beginning, they routinely included the same kind and amount of information.<sup>10</sup> The same is true for the Annual Reports on Executive Compensation. All of which suggests that the administration and the Regents were operating on consistent and mutual assumptions about presidential authority and about which compensation elements required Regental approval and public disclosure.
- *The actions of the Regents themselves:* For more than a decade, no serious question was raised by the board about the authority of the president to approve various aspects of executive compensation or about how the Principles were applied. In fact the Regents

---

<sup>9</sup> SP-9, “Amendment of Bylaws, Standing Orders, and Policies Related to Board Practices and Procedures,” Special Committee on Regents’ Procedures, January 18, 1996.

<sup>10</sup> Presidential appointment items—those for Peltason and Atkinson, for example—differed in that they contained detailed information about benefits associated with the position, while chancellorial items did not. It is an exception that tends to prove the rule, however, since the Regents would have seen both and could have required comprehensive information in all executive appointment items if they so desired.

proceeded to expand presidential authority in the years immediately after the Principles were approved, including his authority over routine compensation matters—hardly an indication the board was unhappy with the procedures used to implement them.<sup>11</sup>

This is not to claim that compliance with the Principles was perfect. There was a serious departure from the Principles during the Atkinson administration, when a UCOP administrator simultaneously received a temporary housing allowance and two housing-related loans that were not approved by the board or included in the Annual Report on Executive Compensation. In terms of general practice, press releases on executive appointments issued after Regents' meetings were inconsistent in the amount of information they contained, though base salary was always included. Full details were disclosed in the Annual Report on Executive Compensation, but the Principles called for information to be released "in a timely manner," and it can be argued that a yearly report does not meet that standard. This exception aside, adoption of the Principles clearly gave the Regents more information about the compensation offered to the University's top executives, more time to consider it, and better public disclosure.

If the Principles were implemented appropriately, why did the 2006 controversy happen? There are several answers to this question. They include a return of the University's budget troubles; a decision to increase the competitiveness of UC's executive compensation; a rupture in communication between the administration and the Regents; and the redefinition of the term "compensation."

### **The 2006 Controversy**

The *San Francisco Chronicle's* coverage of UC administrative expenditures began in mid-November 2005. It included several articles which claimed, based on UC payroll records, that in the previous fiscal year UC had given out \$871 million in bonuses, stipends, relocation allowances, and the like, implying that most were awarded to high-level administrators at a time of budget stringency and exploding student fees. In reality, executives received less than one percent of this sum; almost all of it was spent on payments to doctors, clinical faculty, and other UC hospital employees for patient care, stipends for faculty for teaching and research during the summer, and vacation or severance pay for departing employees. All of this was in full accord with UC policy and standard practice. The University was slow to respond, however, and took nearly two months to release a complete explanation of how the \$871 million was spent—a function of understaffing and inadequate payroll and personnel systems, according to the Office of the President. In the meantime, the *Chronicle* article about the \$871 million caused state legislators to schedule hearings on UC's "hidden compensation" and alleged lack of transparency.

From there the *Chronicle*, and later other newspapers, moved into the compensation of individual executives—the renovations on the official residence of the chancellor of UC Santa Cruz, for example, and the relocation allowance given to the universitywide provost. The Office

---

<sup>11</sup> The Regents' decision to delegate more authority to the president in compensation matters was part of a broader effort to lessen the large number of routine transactions on the board's agenda; the September 1993 Transition Team Report estimated that "each agenda item presented for Regental consideration requires 75 to 100 hours of staff and management time at the campuses and in the President's office for research and preparation [The University of California Transition Team Final Report, Volume 1, p. 6]." Among other changes, SP-9 (cited in footnote 9) reduced the number of administrators whose appointment required Regental consent and raised the threshold at which administrative and faculty salaries must be approved by the board from \$136,700 to \$150,000, with future increases tied to the Consumer Price Index. These two changes cut the number of required Regental approvals in the compensation area by half, from roughly eighty to forty.



of the President was vulnerable in some of these examples, and not simply because of the lack of centralized compensation data.

Competition for administrative talent had become more difficult throughout the 1990s as a result of nationwide changes in the higher-education marketplace. The new president, Robert Dynes, was eager to improve UC's competitiveness for top-level managers. As he told the Regents in May 2006, he had a number of executive vacancies to fill when he took office three years earlier, and he found it increasingly necessary to resort to non-salary compensation elements to attract chancellors, laboratory directors, and other executives—more generous administrative leaves with pay, for example, accelerated eligibility for health benefits, additional vacation leave, and larger relocation allowances. Some of these executives came from outside the UC system, and making them whole—that is, giving them benefits equivalent to those they had received at other institutions—also required offers that were not standard at UC and not covered by regular compensation policy.

Executive recruitment is, by design, a confidential process. To protect the privacy of individuals, the practice was to limit information about the identity of candidates and the details of the proposed appointment to a few people in the Office of the President directly involved in recruitment. This did not include the General Counsel's office, which was not asked to review offers made to candidates or appointment items submitted to the board. Individual Regents serve on high-level executive search committees and offers are usually vetted with the Regents' senior leadership, so it is likely that at least some Regents knew about these non-standard benefits. Nonetheless, under the Principles many of these compensation elements would have normally been submitted to the entire Board of Regents for approval or included in the Annual Report on Executive Compensation for the board's information.

For a variety of reasons, however—the transition to a new president and its attendant workload, changes in personnel and organization in UCOP—the Annual Report on Executive Compensation was not sent to the Regents for two years in a row, 2004 and 2005. Given the growing number of non-standard compensation offers, what would have been an oversight in more normal times became a serious breakdown in communication between the administration and the Regents. As in 1992, therefore, stories began to crop up in the press about executive compensation agreements the Regents as a whole had not known about. For the second time in little more than a decade, the Regents and the Office of the President found themselves facing the challenge of explaining what had gone wrong to the public, the legislature, and the University community.

### **Interpreting the Principles: 2006**

By the following spring, the official response to the executive compensation controversy included three audits, the most comprehensive of which was conducted by PricewaterhouseCoopers at the Regents' request. Its April 2006 report looked at the compensation and employment arrangements for the thirty-two UC executives covered by the Principles over ten years, from January 1, 1996 to December 31, 2005. The auditors' conclusions about the intent of the Principles turned the prevailing interpretation on its head. Based on a legal analysis of the Principles and the Regents' Bylaws and Standing Orders, PwC argued that the president has no authority to approve any element of compensation for the officers covered by the Principles. This authority belongs to the Regents, which means that every executive appointment item from 1992 onward should have included not just base salary but also a complete list of the benefits each officer would receive, however routine, so the board could approve them.

This was a dramatic departure from the earlier assumption that the president had broad authority to apply executive compensation policies (policies already approved by the Regents), including the authority to allow exceptions in some cases, as long as the board was informed of these actions. To understand how the auditors reached these conclusions, it is necessary to take one last detour into the history of the Principles: the revisions of 1993. These were critical to the auditors' interpretation of 2006.

One of the fallouts of the Gardner controversy was state Senator Tom Hayden's SB 504, an expression of legislative displeasure about the overtones of secrecy in the Gardner controversy and its aftermath. Signed into law by the governor in October 1993, SB 504 was principally concerned with making Regental consideration of compensation actions more accessible to the public, not with defining compensation. But the bill's definition of compensation was incorporated into the Principles, along with several other revisions mandated by the bill, at the November 1993 meeting of the board. Unlike the earlier 1992 definition, this one was comprehensive:

Executive compensation shall be defined as including base salary, retirement and other benefits, perquisites, severance payments (except those made in connection with a dismissal or a litigation settlement), all forms of deferred compensation, supplemental retirement, all components of housing allowances or any other form of compensation applicable to the Officers of the University and the Principal Officers of the Regents, as currently and as may subsequently be described in the Bylaws and Standing Orders of The Regents.

From the perspective of the 2006 interpretation, this revision is a turning point in the reading of the Principles. In conjunction with Standing Order 100.3, which says that the Regents must approve compensation for senior University executives, including the president, the vice presidents, the university auditor, the chancellors, and the laboratory directors, this apparently simple wording change can be construed to deny the president authority to approve executive benefits; only the Regents have that authority. This is why the 2006 auditors found scores of violations of the Principles that would not have been violations had the word "compensation" not been redefined.

The interpretation of the Principles employed by the PwC auditors in 2006 is based on a legal analysis of the 1993 revision, and it turns on a single word: compensation. It is an ahistorical reading that poses a key historical question: Did the Regents of 1993 understand or intend that the new definition of "compensation" would result in shifting the division of authority between the board and the president and thus the way the Principles had to be implemented?

The written record does not tell us. The best evidence we have about Regental intent is the board's actions. If the Regents had wanted to reclaim authority from the president, it is unlikely they would have chosen this indirect route to accomplishing it, or that they would have done so without discussion or consultation of any kind. If they were dissatisfied with how the Principles had been implemented in the eighteen months since their adoption, the November 1993 revision was a perfect opportunity to make that clear. Yet there is nothing to suggest that they or the administration saw the 1993 redefinition of compensation as altering the authority of the president or as requiring that the Principles be implemented differently.

Nonetheless, it was a short step from the premise that the Principles had been imperfectly implemented, or not implemented at all, to the conclusion that the events of 2006 occurred

because the University—specifically, the Office of the President—had failed to learn the lessons of 1992. Especially the lesson about secrecy.

### **Explaining the Controversy**

The various audits and official statements presented three basic rationales for events. One was the statement by the Task Force on UC Compensation, Accountability, and Transparency, cited at the beginning of this paper, blaming the controversy on administrative negligence in carrying out the Principles. A second rationale was summed up in a February 2006 statement by President Dynes, who was quoted in the *San Francisco Chronicle* as saying that “the real tragedy” of the compensation controversy was that “similar events” had occurred in the early 1990s but that while “Policies were put in place . . . there was no system implemented to make the policies effective.” A third, also articulated by President Dynes, was the existence of “an overactive secrecy gland” and a “culture of secrecy” in the Office of the President—a culture of “trying to get away with as much as possible and disclose as little as possible.”<sup>12</sup> These and other official statements reinforced public perceptions that violations of the Principles were of long standing and that they were symptomatic of a pattern of administrative secrecy within the Office of the President.

As this paper has sought to show, the argument that implementing measures were never taken ignores the history. The Principles are mentioned by name in only one written executive compensation policy—the one on paid administrative leaves—but that does not mean they had no influence on the University’s day-to-day compensation practices; quite the contrary. Regulations derived from a particular law often do not cite the law that generated them. And if administrative laxness were indeed the problem, you would expect to find that compliance was strict in the beginning but fell off over time, as the pressures of the controversy faded. There would be a difference in the amount of information provided in individual appointment items, in the Annual Report on Executive Compensation, or in both—more in 1993, less in 2003. This was not the case.

Perceptions of endemic secrecy and non-compliance in the Office of the President stem from two sources besides the comments by the president quoted earlier. One was UCOP’s delay in reacting to stories about UC compensation—the \$871 million, for example—because of difficulties in accessing payroll data; like most bureaucracies, UC was hampered by the sheer size and complexity of its own operations. Another and more important reason—because it came from the University itself—was the PwC audit and its alleged multiple violations of the Principles from 1993 on. Most of these violations, as this paper has argued, were not violations at all under the interpretation of the Principles that prevailed for at least a decade. And even if you assume the administration was at fault in not recognizing the implications of the revised 1993 definition of compensation, the fault is an instance of administrative oversight, not administrative secrecy.

The extent to which the auditors’ conclusions reflected a re-interpretation of the Principles, not “the explosive story of UC’s secret [compensation] practices,” was entirely lost on the media. So was the difference between the kind and number of executive compensation offers made before and after 2003, however much those differences were a response to market forces. Anyone reading major California newspapers in 2006 could easily conclude that, as far as secrecy was concerned, little had changed at the University of California since 1992. This was an entirely unsurprising outcome, given the official explanation of events, but also entirely inconsistent with the history of the Principles.

---

<sup>12</sup> Remarks to the Regents, May 17, 2006.

By the time the 2006 controversy broke, however, none of the Regents who had adopted the Principles remained on the board, and many of the executives and staff who had implemented them had retired or gone elsewhere. The PwC audit recognized the existence of the Annual Report on Executive Compensation but not its significance, the significance of the missing reports of 2004 and 2005, or the earlier rationale for interpreting the Principles. All of these factors contributed to transforming what could have been seen as a series of bureaucratic missteps into a crisis of governance and a story about a hidden history of policy violations. And linking the compensation controversies of 1992 and 2006 only reinforced the negative image the Office of the President was seeking to combat.

### **Conclusion: Governance and Institutional Memory**

Whatever the similarities between the two controversies, there is one striking difference. In 1992, the Regents changed their policies and procedures but not their basic relationship with the president and the administration; indeed they went on to increase the scope of presidential authority. In 2006, the Regents mandated an extensive restructuring of the Office of the President, including the establishment of an office of compliance and audit headed by an executive vice president reporting directly to the Regents. They also engaged an outside consulting firm, the Monitor Group, to study the organization of the University system. Its initial report, released in fall 2007, was a harsh critique of the performance of the entire Office of the President. The consultants' study raises the prospect of a major realignment of authority and responsibility among the Regents, the Office of the President, and the campuses. The executive compensation controversy has already had large consequences for governance. It could have even larger consequences in the future.

This discussion of the executive compensation controversies of 1992 and 2006 has focused primarily on the relationship between the Board of Regents and the Office of the President. Other issues raised by the recent controversy—the overall clarity and coherence of UC's compensation policies, for example, and the adequacy of the University's data systems—are beyond the scope of this paper. So are the changes in compensation policy and procedures enacted by the Regents in the wake of the events of 2006. My purpose has been to present the evidence that the Principles were not forgotten, ignored, or circumvented in the decade after their adoption, and that the practices that grew up around them were not an exercise in secrecy.

The Principles were a broad policy statement about the University's commitment to openness and the Board of Regents' expectations regarding the information it needed to exercise its stewardship. But they were also the product of a particular set of issues and a particular historical moment, and that fact is crucial to understanding their original meaning and intent. If there is a lesson in the history of the Principles for Review of Executive Compensation, it is surely the importance, and the fragility, of institutional memory. The University of California lost a great deal in terms of public trust and confidence through the executive compensation controversy of 2005-6. It also lost a chapter of its own history.