

Memorandum

TO: UC Regents and Chancellors

FROM: Mark G. Yudof, President
University of California

RE: 2009-10 State Budget

DATE: January 5, 2009

In an unprecedented move last week the Department of Finance (DOF) released the narrative portion of the 2009-10 California State Budget. This was 10 days prior to the constitutional deadline for submitting a state budget to the Legislature. The release of the DOF analysis does not provide a complete detail of what will be present when the budget is actually released next week. However, I have highlighted the major issues regarding the state budget and issues specific to the 2009-10 budget for the University of California.

Overall State Budget

The 2009-10 State Budget assumes a General Fund budget deficit of \$14.8 billion in 2008-09 that will increase to \$41.6 billion in the 2009-10 fiscal year unless action is taken to implement both expenditure reductions and revenue increases proposed by the Governor. The Governor is proposing to address the budget gap with current year and budget year recommendations that include \$21 billion in expenditure reductions; \$15.8 billion in additional revenues; \$5 billion shifting lottery revenue from state funded programs to balancing the budget; \$358 million in borrowing; and \$4.7 billion from Reimbursement Warrants that will be used to meet the cash flow needs of the state through the 2009-10 fiscal year. The Governor budget assumes these actions, or comparable recommendations, will allow the Governor and the Legislature to balance the state budget and achieve a \$2 billion reserve by the end of the 2009-10 fiscal year.

2009-10 University of California Budget

2008-09 UC Budget – You will recall the 2008-09 UC budget was initially reduced by \$97.6 million when the Governor proposed the state budget in January 2008. The Governor subsequently restored this funding in his May Revise, however when the final budget was enacted in September, the Governor and the legislature reduced the UC budget by \$33.1 million. As part of the special session budget reductions, the Governor and the legislature proposed to reduce the rest of the May Revise restoration or \$65.5 million. As reflected in the 2009-10 state budget released last week, the Governor proposes to restore the \$33.1 million (treating it as a one-time reduction in 2008-09) and permanently reduce the UC budget by \$65.5 million.

2009-10 UC Budget - The Governor's 2009-10 State Budget assumes a total funding of \$20.2 billion for the University of California. Of this amount, \$3.2 billion is from state General Fund; nearly \$2 billion is from student fee revenue that includes a 9.3 percent increase in mandatory systemwide student fees; and \$610 million is from UC general funds. The DOF fully funded the UC and CSU Compacts, as they did in the 2008-09 budget, but took a similar action as last year's budget to reduce the entire amount of Compact funding as an "unallocated reduction" to the UC and CSU budgets. This action will severely constrain the University's ability to fund student access, compensation increases, or funding augmentations for health benefits, energy costs, or other instructional budget priorities.

The Department of Finance provided \$209.9 million to fund the UC under the Compact for Higher Education. By funding the Compact, the DOF recognized the University's need for 4 percent to support general operating costs; 1 percent for core academic needs (instructional equipment, libraries, technology and facilities maintenance) and 2.5 percent for enrollment growth. While the DOF built in these funding assumptions to the UC budget they subsequently deleted this identical amount as an "unallocated reduction" of \$209.9 million. The \$209.9 million augmentation and subsequent reduction to the UC Budget is in addition to the \$65.5 million permanent budget reduction. Thus, there is no funding to support the Higher Education Compact in the 2009-10 fiscal year. (The Governor's budget treats the California State University in the same manner by funding \$217.3 million under the Compact and then deleted \$217.3 million as an unallocated reduction.)

There is a small change in state General Fund of \$72.1 million for the following costs or shift of funds in the UC budget:

- Replace state General Funds for deleted lottery funds \$29.8 million
- Fund the debt service for lease purchase agreements \$28.4 million
- Funding for annuitant retirement benefits \$11.3 million
- Restoration of General Fund for Subject Matter Projects (One-time Federally Funded in 2008-09) \$5.0 million
- Reduction of UC Merced funding (\$10 to \$5 million) (\$5.0 million)
- Support for 57 additional MD's in the PRIME program \$1.5 million
- Funding for an additional 50 undergraduate and 42 graduates in the nursing program \$1.1 million

Student Fees - The Governor's budget also recognized an increase in mandatory systemwide student fees for the UC (9.3 percent) in the 2009-10 academic year. The 9.3 percent is an average of the education fee (10 percent) and the registration fee (4.2 percent). These two fees, in addition to professional fees that will increase from 5 to 24 percent, will generate \$166.1 million for the UC in 2009-10, of which approximately 35 percent would be set aside for student financial aid. This action would raise resident undergraduate fees from \$7,126 to \$7,788. (The budget also recognized a 10 percent increase in CSU student fees.)

Medical Centers - The UC Medical Centers are now assessing the impact of the proposed reductions to state and federal funded healthcare services. The proposed budget includes significant reductions in Medi-Cal payments and eligibility -- a state and federal health care program for low-income Californians. The rate reductions alone will impact the UC Medical Centers by approximately \$14 Million. Most significant are the reductions to program eligibility which would increase the number of uninsured Californians thereby increasing the cost of unreimbursed care at the UC Medical Centers. While a complete analysis is in progress, a conservative estimate is an additional program impact to the UC Medical Centers of \$11 Million.

UC Retirement - In the General Government portion of the State Budget, the Governor provided \$20 million to restart the state employer contribution to the UC Retirement System. This represents the first time in 19 years that the state has provided funds for this purpose. This amount is insufficient to fund the State's full year cost under most restart scenarios being discussed by the University. Options for when and by how much employer contributions will be started will be addressed at the February meeting of the Board.

UC Capital Outlay – The Regents 2009-10 Budget for Capital Improvements requested \$842.4 million in State capital funds. This amount included funds for projects that were included in the University's 2008-09 Budget, but could not be funded because a new higher education bond act was not proposed by the legislature. The 2009-10 Budget proposes capital funding for the University at the reduced amount of \$480 million from two sources—Lease Revenue Bonds and previously approved General Obligation Bonds.

Lease Revenue Financing totaling \$451 million is proposed for the following nine projects:

- \$62.3 million for the Campbell Hall Seismic Replacement at Berkeley
- \$14.9 million for the Music and Recital Instruction Building at Davis
- \$39.4 million for the Business Unit 2 at Irvine
- \$75.2 million for the Science and Engineering Building 2 at Merced
- \$65 million for the Engineering Building Unit 3 at Riverside
- \$81.2 million for the Biological and Physical Sciences Building at San Diego
- \$2.3 million for equipment for the Structural and Material Engineering Building at San Diego
- \$64.7 million for the Davidson Library Additional and Renewal
- \$45.9 million for the Coastal Biology Building at Santa Cruz

General Obligation Bond financing is available in the amount of \$28.6 million for the following three projects:

- \$0.5 million for equipment for the Telemedicine Facilities Phase 2 at Davis
- \$25.3 million for the Telemedicine and PRIME Facilities Phase 2 at Los Angeles
- \$2.8 million for the Telemedicine and PRIME-US Facilities Phase 2 at San Francisco

Cal Grant Funding – The Governor’s budget proposes various reductions in the Cal Grant program as follows:

- (1) Freeze the income ceilings (estimated \$1-2 million impact on aid levels to UC students)
- (2) Reduce maximum award at independent institutions (no impact on UC students)
- (3) Eliminate new Competitive Cal Grant program awards (estimated \$6 million impact on aid levels to UC students)
- (4) Partially decouple awards to public institutions from fee increases (estimated \$9 million impact on aid levels to UC students). Details about the partial decoupling are absent, but we think the proposal is to increase UC Cal Grant awards by only 2/3 of the 9.3% fee increase, rather than by the full amount. The rationale is probably tied to a perceived lack of necessity for the state to cover the 1/3 of the fee increase that augments our own institutional aid programs.

Collectively, the impact (given duplication) is estimated to be from \$14-16 million, which would increase loan/work burden on students by about \$200. The budget proposal also calls for a \$2 million savings from decentralizing Cal Grant program administration to the segments, a major undertaking that UC has long supported exploring but which would probably not generate any savings in the conversion year.

Once the actual detail of the Governor’s budget is released at the end of the week we will provide you with any additional information or funding assumptions that may be different from budget assumption provided in this memorandum.