March 1, 2012

Director of Research and Technical Activities, Project No. 13-3
Governmental Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk CT 06856-0659

Dear Director,

We are responding to the GASB’s Invitation to Comment on Preliminary Views on Economic Condition Reporting: Financial Projections. We appreciate the Board’s interest in seeking comments on their Preliminary Views and the Board’s willingness to consider our perspective.

We do not support the preliminary view that financial projections should be included in the annual financial statement. We request that you consider our comments on certain issues outlined in the Preliminary Views. Specifically, we list three issues below that are of concern for the University of California:

**Issue 2.** The Board’s preliminary view is that financial projections should be (a) based on current policy, (b) informed by historical information, and (c) adjusted for known events and conditions that affect the projection periods. Current policy includes policy changes that have been formally adopted by the end of the reporting period but that will not be effective until future periods. Do you agree with this view? Why or why not?

The University receives a portion of its funding from the state of California. For the last fifteen years, the University’s budgetary planning has been guided by an agreement about funding and accountability reached with the Governor. These funding agreements were a comprehensive statement of the minimum resources needed for the University to accommodate enrollment growth and sustain the institution. These agreements were intended to provide the University with base budget adjustments to fund compensation, non-salary cost increases, and other programmatic needs related to its basic operations, enrollment funding, and funding for initiatives mutually agreed upon by the University and the state. These agreements were honored and often exceeded in years in which the state’s fiscal situation was healthy. However, in years in which the state was in the midst of fiscal crisis, the agreements were either only partially honored or suspended. Most recently, for 2006 through 2008, state funding increased by more than $550 million. However, for 2009 through 2012, the University experienced major budget reductions, including a reduction of $715 million in July 2009 retroactively for the year ended June 30, 2009. These circumstances will make it difficult, if not impossible, for the University to make financial projections.

**Issue 5.** The Board’s preliminary view is that annual financial projections should be made for a minimum of five individual years beyond the reporting period for the purpose of external reporting. Do you agree with this view? Why or why not?
We do not agree that annual financial projections should be required for a minimum of five years. Forward-looking information is subjective and creates significant risk for our organization. Our organization publishes the annual budget each year eight months in advance of the fiscal year. The budget is published before the state’s budget is finalized and is contingent upon achieving certain funding levels from the state. Information on state funding levels is not available until the final state budget adopted by the legislature and signed by the governor. The state budget has been volatile and difficult to predict in advance of the fiscal year. Projections any further in advance than the next fiscal year will be highly speculative and not useful to our readers. Projecting that state funding levels in future year will remain unchanged is also not realistic in our current environment. For example, our organization received cuts in state funding both mid-year through the fiscal year and after the end of the fiscal year in recent years. For example, in July 2009, the state of California finalized their State Budget Act that required the University to return $715 million of state educational appropriations after the end of the fiscal year. If a reader relied on financial projections in our annual reports when these recent state funding cuts were not anticipated, we believe our organization would be exposed to tremendous risk.

Issue 6. The Board’s preliminary view is that all of the components of fiscal sustainability information are essential for placing the basic financial statements and notes to the basic financial statements in an operational or economic context and therefore should be required and communicated as required supplementary information. Do you agree with this view? Why or why not?

We don’t believe that the reporting of financial projections is essential for placing basic financial statements and notes to basic financial statements in an appropriate operational, economic, or historical context. We don’t believe that financial projections should be required as part of the required supplementary information in the basic financial statements since the projections represent subjective assessments of the effects of reporting information on the organization’s future financial position. We question the cost-benefit relationship in reporting financial projections in the annual financial statements. Preparation of the annual financial statements for our organization is a significant activity requiring extensive efforts by many employees at in each department at all of our campuses, medical centers, foundations and laboratories to gather and report accurate and complete financial data. Preparing projections that would reasonably estimate future inflows and outflows would require similar participation and diligence throughout our organization. We believe this reporting standard would require us to add a significant number of staff throughout the University, outweighing the value of economic condition reporting.

If you have any questions regarding these comments, please contact Peggy Arrivas, Systemwide Controller, University of California, Office of the President at 510-987-9067 or peggy.arrivas@ucop.edu.

Best,

Peter J Taylor
Executive Vice President - Chief Financial Officer

Peggy Arrivas
Associate Vice President - Finance
Hello, my name is Peggy Arrivas and I am an Associate Vice President and the Systemwide Controller for the University of California.

Today we are commenting on Issue #2 regarding the GASB’s preliminary view on how organizations should prepare financial projections for economic condition reporting.

We are not in favor of GASB’s proposal for economic condition reporting because it increases the administrative burden and risk for our organization. We want to share some specific examples to explain our point of view.

The University of California, one of the largest and most acclaimed institutions of higher learning in the world, is dedicated to excellence in teaching, research, health care and public service. The University has annual resources of nearly $23.7 billion. The University operates ten campuses, five medical schools and medical centers and ten foundations. The University is also involved in the operation and management of three national laboratories for the U.S. Department of Energy.

The University does not have one common financial system. Each of the campuses, medical centers, foundations and labs has their own portfolio of financial systems. Information from all these financial systems is compiled at the Office of the President to prepare the annual audited financial statements.

While certain arrangements are established for the entire system by the Office of the President, most contracts are negotiated by the campuses, medical centers, foundations and labs. For example, the Regents of the University set undergraduate student tuition and pension contribution rates for all locations. However, many of our arrangements
and contracts are negotiated at each campus and medical center, such as research contracts and grants, arrangements for auxiliary enterprises and vendor contracts.

GASB’s preliminary view is that financial projections should be (a) based on current policy, (b) informed by historical information, and (c) adjusted for known events and conditions that affect the projection periods. While some of the assumptions in the budget for the University would be the same for economic condition reporting, there are many other assumptions used in our budget that would not meet these criteria, and therefore would be excluded from our economic condition reporting. One example would be the aggressive pursuit of new revenues and cost reductions. These are management initiatives that may be include in our budget however, would not meet the criteria to be included in the economic condition report under GASB’s standard. We share this viewpoint, not because we would suggest you modify the proposed standard, but to help you understand that your proposal creates the need to establish another framework for developing an additional set of financial data besides our annual budget and the actual results that are prepared now.

Because the University is decentralized and many of our contractual arrangements are overseen locally at our campuses and medical centers, we would need to start at the local level to prepare the data required for economic condition reporting as outlined in the preliminary view. Creating another parallel process to develop and report this data at each campus and medical center and then compile it for the system would be a huge administrative cost to the University. It would be difficult for the University to do bear this additional cost at a time of declining support from the state of California.
Additionally, publishing our different projections for our budget and economic conditions report will draw questions from our faculty, readers of our financial statements and the public. We would be forced to explain why different assumptions were used in the two reports, potentially affecting our credibility.

Appropriations from the state of California for the year ended June 30, 2011 were $2,651,000,000, representing 11.2% of the total operating and non-operating revenues for the University. Our current fiscal budget from the state is only 10% higher (in non-inflation adjusted dollars) than our 1990-91 allocation. During the last 20 years, enrollment has grown 51% and we opened a 10th campus. State appropriations for the last several fiscal years have been as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
<th>Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>$3,064</td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>2,932</td>
<td>4.3% decline</td>
</tr>
<tr>
<td>2004</td>
<td>2,640</td>
<td>10.0% decline</td>
</tr>
<tr>
<td>2005</td>
<td>2,463</td>
<td>6.7% decline</td>
</tr>
<tr>
<td>2006</td>
<td>2,573</td>
<td>4.5% increase</td>
</tr>
<tr>
<td>2007</td>
<td>2,793</td>
<td>8.6% increase</td>
</tr>
<tr>
<td>2008</td>
<td>2,975</td>
<td>6.5% increase</td>
</tr>
<tr>
<td>2009</td>
<td>2,415</td>
<td>18.8% decline</td>
</tr>
</tbody>
</table>

While we have experienced increases and declines in state funding between 2002 and 2008, we could not have predicted the state’s fiscal crisis and the 18.8% decline in 2009 by either evaluating history or the agreements in place with the state of California. The budget adopted by the state of California called for increased funding for the University. We were paid during the year based upon this increased funding level. The state retroactively reduced their allocation for the year ended June 30, 2009 in July 2009 by
$715 million, and we returned these funds to the state of California after our fiscal year-end.

We believe the preliminary view on economic reporting published by the GASB creates tremendous risk for our organization while increasing the administrative burdens for our organization and therefore are not in favor of these changes.

Thank you and we appreciate the opportunity to share our views with the GASB.