Minutes*

Senate Committee on Finance and Planning
Tuesday, October 22, 2002
2:00 - 5:00
238A Morrill Hall

Present: Charles Speaks (chair), Prince Amattoe, Brittny McCarthy Barnes, Stanley Bonnema, Bruce Brorson, Charles Campbell, Tom Gilson, Gary Jahn, Abu Jalal, Cynthia Jara, Joseph Konstan, Michael Korth, Richard Pfutzenreuter, Thomas Stinson, Terry Roe, Sue Van Voorhis, Warren Warwick, Susan Carlson Weinberg

Absent: Jean Bauer, David Chapman, Tim Church, Robert Cudeck, Thomas Klein, Marvin Marshak, Timothy Nantell, Daniel O'Connor, Laurie Scheich, Michael Volna

Guests: Senior Vice President Frank Cerra (Academic Health Center), Gerald Fischer, Doug Gorence, (University of Minnesota Foundation), Mark Rotenberg (General Counsel), Gail Klatt (Department of Audits), Vice President Kathleen O'Brien (University Services)

[In these minutes: (1) new facilities for the University of Minnesota Physicians private practice clinics; (2) report on the endowment; (3) University construction practices; (4) stadium update]

1. Private Practice Clinics

Professor Speaks convened the meeting at 2:00 and turned to Dr. Cerra to lead a discussion of private practice clinics.

Dr. Cerra began by saying that University of Minnesota Physicians (UMP) needs new clinics for several reasons. First, UMP has over 600,000 patient visits per year, up from 400,000 two to three years ago. The number of patient visits has increased 8-10% per year, which is a positive increase. Second, the facilities in Phillips-Wangensteen and Moos are now quite old and were not designed for the volume of patients now visiting the facility. Access to the facility by patients is also a source of complaints. This results in negative experiences for both patients and physicians.

They are also hospital-based clinics, which means they are connected to hospitals and owned and operated by hospitals; the significance of this is who actually controls the clinic and what happens in it. The reimbursement rate (the amount of money they receive for seeing a patient or performing a test) is higher for hospital-based clinics. In addition, in terms of services (x-rays, labs, and so on) the physicians are working in clinics where they cannot control scheduling, function of personnel and space. The ancillary services, particularly radiology, are mismatched to the equipment. The result is that the in-hospital services are overloaded with outpatients while the outpatient clinics are under-utilized. All of this makes it very difficult to meet the mission of health professional experiential learning and to provide the service environment that is essential in the marketplace of health care that exists in the state. The physicians compete for provider contracts with all the other providers in the state and region and receive no special attention or treatment as the principle teaching and research facility. The premium for health care services does not contain a component for education and research.

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Third, each of the health professional school faculty is now developing a private practice plan (Veterinary Medicine, Nursing, Dentistry, etc.). Nursing, for instance, will assume an increasingly prominent role as the primary providers in situations of chronic disease management. The evolving paradigm of health professional education, a component of the accreditation process, is to move from hospital to non-hospital settings and more into community settings. The AHC cannot educate and train all its health professional students in settings where regular faculty practice. It is highly dependent on community practitioners--and will become increasingly so as the community partnerships develop.

UMP cannot practice modern healthcare effectively, and cannot effectively compete in the marketplace, without efficient and effective facilities over which they have sufficient control to manage personnel, space, and services. The practice plan continues to finance a significant part of the education of students and the performance of research in the Medical School and other AHC professional schools.

There has been a phased change in that UMP is moving in a series of steps toward owning and operating their own clinics. The clinics UMP works in have always been part of the hospital--first University Hospital and now Fairview-University Medical Center. The relationship was renegotiated with Fairview in 2001 so that in January, 2002, UMP began to manage the clinics. This was the first step toward UMP owning and operating its own clinics. This transition was a planned part of the affiliation agreement with Fairview Health Services that started in 1997. At this time, negotiations are ongoing with Fairview to increase management authority over the clinics by UMP. This increased authority is planned to begin in January of 2003. The next step will be to own and operate the clinics, over the next five years. All of this needs to be accomplished within an environment of complex state and federal regulations. Staged over a period of time and accompanied by a programmatic and business plan, the outcome of owning and operating the clinics can occur in a way that will enhance the mission.

Also part of the discussion in moving toward a new clinic facility is the participation of nursing, pharmacy, and perhaps dentistry. Interdisciplinary activity to promote health and to prevent and treat disease requires that the provider disciplines have proximity to each other. This outpatient facility would also support chronic disease management and clinical research. In effect, it would become the physical location for clinical research and education for the health professions. This emphasis is critical for the future of the health enterprise of the Academic Health Center. Its reputation is quite dependent on the connecting of the basic and clinical sciences directly to prevention and to the treatment of disease.

How do you finance the new clinic building? UMP can have a certain amount of responsibility in financing but will have a very limited capacity to issue debt. UMP can also borrow but will be limited in the amount, and will not be able to support the cost of the facility on its own. When President Yudof was here, the question was asked if there was a way for the University to participate in the financing of this mission. UMP has cash flow but it does not have a balance sheet with assets to support debt.

UMP, by Regents' policy, is a legal entity outside the University and exists for the sole support of the mission of the Medical School. This structure is in place so that the faculty who practice have benefits in addition to University benefits, which are paid for from practice income, and there is limitation of the practice liability for the University. The dollars earned by the practice plan pays UMP overhead, pays the clinical practice portion of the physician's compensation, and the remainder is used to support the research and education mission of the Medical School. This revenue is part of the University IRS tax.

Dr. Cerra at this point turned the conversation over to Mr. Pfutzenreuter.

They have had discussions with a consultant, Mr. John Augustine, who has assisted in developing financing for academic clinics around the country that have similar problems. The models have run the gamut of physicians pledging salary dollars if there was a default on the payment to the University backing it 100%. For this to happen, and it is important from the standpoint of the money from the private practice, how can the financing package be structured so the University is not at total risk for a possible loss but shares the risk with the Medical School or Medical Foundation or physicians. The University would not be first in line but rather second or third in the event of non-payments.

What kind of assessment of risk potential do they have at this point, Professor Speaks asked? Dr. Cerra responded that they basically have not figured that out yet. The project is still in the formative stage; it is pre-pre-design, he said.

Professor Konstan suggested that if this venture is seen as income-producing, which is the plan, one opportunity might see this as an investment process. Own the clinic itself and allow it to be built as investment. Have those scenarios played out as they are talking about that financing? Dr. Cerra replied that there are real estate trusts that are on the table. The Medical Foundation Board has begun to entertain the possibility of being an investor in the building, but has not gotten to the point where it is willing to issue debt.

Mr. Pfutzenreuter said that Medical Foundation debt affects University debt. New accounting rules are going to bring the affiliated organizations onto the University's financial statements. Those debts are consolidated (the medical foundation, the arboretum) and even if they were not, the debt issued by affiliated organizations is counted in debt ratios. It is thus difficult to insulate the University from implications of possible debt.

Dr. Cerra said that the board deliberations have included the model where they are willing to make an investment but they have not gotten to the point where they are willing to invest in the whole building, using themselves as banker. Their concern is that they are afraid their fiduciary responsibilities would be violated. Mr. Pfutzenreuter said that if this does happen, the risk has to be shared among all parties and the last risk should be on the entire University as a whole. Dr. Cerra said he thinks everyone agrees with that.

Mr. Pfutzenreuter added that they can help with credit and a strong balance sheet, which will help get a better interest rate. They could help lower how much money has to be borrowed.

Dr. Cerra said the first debt payer would have to be the physicians. Probably the foundation would be second. The University, or some piece of it, would be the third. Dr. Speaks added that there is a provision for some form of partnership with the Foundation and the University. Dr. Cerra agreed. He added that another player, an unexplored avenue, is Fairview. Ultimately, Mr. Pfutzenreuter said, the difficult spot for the institution is how much the Medical School stands to lose if it cannot pay its bills.

Dr. Cerra said that this brings up an important point, which is two-fold. The first is that because of the Regents' policy, the practice plans have not been able to accrue assets; they can only have cash on hand in a reasonable amount. The second point is that the practice plan supports a very large percentage of the compensation of the faculty who practice medicine and teach. They receive only about 10% state money for their education activities but they are teaching about 35% time. There is also a substantial amount of money, in the range of $20-25 million dollars, that goes to the education of medical students. The Medical School is leveraged on private practice revenue. The struggle is about how much should be diverted to pay for assets directly or by putting it at risk--but there are no data to guide that decision.

Dr Cerra mentioned briefly that there is potential for a fifth investor, a private one or two, but it has not been explored. There has been some interest. It would lower the risk for the others.

Revenues would be earmarked for costs, salaries, and then the debt, Professor Roe asked? Dr. Cerra replied in the affirmative, adding that some of the money will be for support of Medical School student programs. Professor Roe wanted to know who determines the rules or the governance of the process, as reasonable people could argue about where resources should be allocated. Dr. Cerra said that has been worked out already; there is a Regents' policy on private practice plans and a procedure manual that regulates the practice. Decision authority resides in the office of the Dean of the Medical School and the board of practice plan with oversight by his (Dr. Cerra's) office. It is tightly regulated, he said. The goals of the UMP are set by a bottom-up process with the faculty of UMP, who are also the faculty in the clinical departments; there is also a relationship with the dean's office. There is constant cross-talk so the missions of the two entities stay in sync.

Professor Korth wondered about authority and fiscal responsibility. UMP is legally distinct from the University but subject to Regents' Policies. How is that distinct? Dr. Cerra said they are two different entities. By Regents' policy the tenured faculty of the Medical School receive state money to teach--but they are also full-fledged members of a 501(c)(3) non-profit, tax exempt foundation called UMP, that exists for the sole support of the Medical School but delivers clinical care by faculty. The budget is set like a funnel: dollars come in the top and out the bottom. Those that are taken off the top include the Dean's tax, then University taxes, then overhead and salaries of the physicians. What comes out the bottom goes back into departments; use of that money has to meet the mission of the school. This is codified in the yearly compact.

If this moves forward, how do physicians become convinced that it is a good idea to have one more outlet in this funnel that will be paying off debt, and who decides how big that outlet is relative to the others? The first example is the push-pull. The push is the doctors and patients don't like the clinic but like each other. The pull is having a new clinic that has the doctors, nurses, pharmacists, and clinical research associated with it. Their mission is to educate the next generation in the best way possible. Ultimately, if they are responsible for the debt, it will come off high in the funnel.

Professor Konstan asked about Nursing and Pharmacy--they don't report to the Dean of the Medical School. What happens to the structure when UMP is tightly woven into the Medical School? Dr. Cerra said this is an evolving structural issue. The survival of the AHC and schools directly depends on leveraging mutual strengths in the marketplace, one of which is contracting for care. They do not have a governance structure to deal with that yet but it is in the work plan.

If the clinic is built, is there space in Moos and Phillips-Wangensteen that can be reclaimed for other University academic purposes, Professor Konstan asked? There is, Dr. Cerra said, and they have a task force working on that issue. They have an architect and an engineering crew looking at possible uses for the two facilities.

Mr. Jalal asked what happens if the clinic is built and there is not money at the bottom of the funnel after debt is paid. Who kicks in the money for the Medical School? Dr. Cerra said that they do not have a business plan to support any of this at this point. This development is in the talking stage with a long way to go.

Ms. Van Voorhis asked if these facilities are anticipating making classes smaller. Dr. Cerra said they are; that is built into the design.

Professor Campbell expressed interest in the Medical School timeline. Dr. Cerra said it is listed in the 6-year plan. Probably around 2005-07, but there is an enormous amount of work to be done.

Mr. Pfutzenreuter underscored one of the discussions with President Yudof before he left for Texas: President Yudof felt it important to keep the clinic on the campus rather than moving it to another site. The public comes away with a good feeling about the University and it does not want to lose that; it is important to the identity of the University.

Professor Speaks thanked Dr. Cerra for his report.

2. Report on the Endowment

Professor Speaks then turned the discussion over to Gerald Fischer from the University Foundation. Mr. Fischer was accompanied by Doug Gorence, who oversees the daily management of the endowment.

The first slide showed the combined endowments that benefit the University, located in three different legal entities: the Minnesota Medical Foundation, the University of Minnesota, and the University of Minnesota Foundation. The combined endowments were $1.5 billion at June 30, 2002. The University ranks 25th nationally among all public and private universities; it ranks 7th among public universities. The University of Texas system ranks first due to oil royalties. The others ranking higher than Minnesota are places such as the University of California system, Michigan, and Virginia.

Where does the drop of about 16 percent over the last two years put us in relation to comparable universities, Professor Konstan asked? The University lost one ranking point. It is not that schools raised that much more money, but more likely the investment performance. The University is also in the middle of a capital campaign.

The total endowment was declining but there was a slight increase in the Foundation; they have been roughly able to hold stable. Mr. Gorence said that the gift flow that they have been receiving is a result of past pledges and new gifts; it has just about offset the payout and spending to the University. This is more the effect of investment return.

Mr. Fischer then discussed total return on the foundation's endowment of the last 1, 3, 5, and 10 years, ranked at the 6th, 9th, 30th, and 39th percentiles, respectively, among the top 400 endowments in the country. The Foundation tries to earn 6 points over inflation to maintain long-term permanent value of the endowment. At ten years, the 10.9% performance compared favorably to a market benchmark with asset allocation that matched what the Foundation was doing in its portfolio. When the 6 points are added to 2.5% inflation, the result is 8.5%, so the University is well ahead of the benchmark. This is important because the Foundation is trying to maintain highest levels of payout possible to the University. Exceeding the goal during periods of excellent performance and positive market conditions during the 1990's, for example, provided the Foundation a reserve so there aren't radical drops in payout because of the negative performance in the market in the past few years.

At five years, 7.8% was well ahead of the benchmark and slightly short of the goal. The last three years the Foundation has been proud to have had a positive return in extremely difficult markets. Last year was an extraordinarily positive performance in that they had a positive return when so many other foundations around the country were experiencing negative returns of 10-15%, some as low as -17%. The rankings are of 400-500 universities and major non-profits. The 6th percentile rank last year was strong performance. The sample is a broad one that includes large funds like Harvard and smaller funds which are not run the same way. There are always issues with data. The fairer benchmark is investing in the market, but everyone likes to see how they did versus other schools.

Professor Konstan asked about the policy benchmark—is that a dynamically changing thing as asset allocation is adjusted? Is this basically saying how well they are executing the policy as compared to others? It is.

Why does the Foundation have so little invested in real estate? It is more where we are in the investment cycle, Mr. Gorence said. He arrived in 1999 and started building the real estate and other alternative investment programs from zero. The Foundation uses limited partnership structures. Mr. Gorence puts money with outside managers, but there are not always opportunities to invest it productively. The target allocation for real estate is 5% and it will take several years to get there.

The Foundation created the subsidiary, University of Minnesota Foundation Investment Advisors (UMFIA) with a board made up of experienced professionals. The UMFIA Board hired Mr. Gorence as CIO who reports to the same board. The UMFIA Board of Directors includes people such Fred Friswold, former head of Dain Bosworth; Mr. Winton, an experienced venture capitalist; and Dale Olseth, the CEO of Surmodics. Mr. Fischer came from Ford and US Bank, which gave him a lot of investment experience.

There is a clear understanding of roles and responsibilities. Mr. Gorence keeps the UMFIA Board focused on asset allocation strategy. The Board decides the Foundation's risk tolerance and modifies policy accordingly. It looks at likely returns for the long-term. Mr. Gorence then focuses on manager selection and monitors those managers.

Do your results include all of the costs of the Foundation as well as the costs of the external management, Professor Konstan asked? The returns are net of all investment expenses, Mr. Gorence said, including custodian and consulting fees. They do not include the three-quarter percent charge that the Foundation uses to support its business.

If there is a donor who wants to give money to the endowment, does the donor's preference for how the money is invested control the investment? A key underlying principle is that when donors make a gift they release control of that asset to the Foundation. The donor can specify how the money is used but not how it is invested, said Mr. Gorence.

Is the Foundation entering into partnerships with real estate? Real estate in the Foundation's portfolio is not consciously aligned with the University's mission; the Foundation has not developed student housing, for example, Mr. Gorence said. They hire expert managers who invest in several projects—the Foundation does not make these decisions directly. UMFIA hires managers and then manage the managers. UMFIA may invest in a project to build multi-family complex that would be leased out or sold to another for profit, Mr. Gorence said.

The policy is that assets the Foundation receives, if they are in the form of securities, are sold as soon as practicable and turned into cash. There is enormous wealth in private equity and commercial real estate but the Foundation does not accept gifts that have ongoing liability.

With respect to real estate, should there be a provision in the policy such that if a unit of the University needs a facility and the facility would have a strong revenue stream, the Foundation could consider whether or not it would be worth investing in it so that instead of the University issuing bonds the Foundation makes an investment with the expectation of decent return, Professor Konstan asked? Mr. Gorence said he thought the Foundation would be open to such a proposal if it were to meet investment standards and criterion. The participants discussed ties and conflicts. Mr. Fischer said that any such investment must meet return objectives. When there are opportunities to invest in University and commercialized discovery it is very inviting because it could hit two mission goals, but the project would have to meet the investment return and risk requirements of the Foundation.

Would there be any instance where the Foundation and the Minnesota Medical Foundation would become partners in a venture? Mr. Gorence and Mr. Fischer indicated that anything is possible. They did work together on the McNamara Center. But 99% of gifts are designated for specific purposes. More unrestricted money is always desirable.

Professor Konstan noted that the University of Minnesota endowment is not invested by the University of Minnesota Foundation. Is there any sharing of resources and knowledge, he asked, or is there potential inefficiency in that the University has two large pools of money (three if the medical foundation is included), each of which is trying to accomplish the same goal and managing a smaller amount of money and therefore being willing to accept lower risk? Are they spending more money to parcel it out to managers? They have quarterly interaction, Mr. Fischer said. There is not a strong bond; they ultimately report to different boards. They do tend to have coordination problems and everyone wants control over their piece of the pie. From a practical standpoint they are limited in how much they can work together, Mr. Fischer said.

From what they have seen, have the investment objectives differed during the coordinating meetings, or are they the same but different views on how to accomplish them, Professor Konstan asked? There is a little of both, Mr. Gorence said. The medical foundation, given that it is smaller, is a more conventional investor. They have a different board with different opinions. The University has a larger staff and it has a different governance structure. Ultimately, all decisions go to the Regents but there are different processes and different outcomes. These different approaches have likely benefited the University, he said.

Mr. Fischer commented on payout. Given the markets the Foundation has had and the outlook of the Board, it is far more likely the returns will be positive but in the single digits in the next ten years, rather than the double-digit returns the Foundation got used to. A year ago the UMFIA gave the Foundation a strong message: They felt that to maintain the 5.5% payout rate would force them into a level of risk with which they were uncomfortable. The Foundation analyzed different strategies to lower the payout rate and did lower the payout rate from 5.5% to 5% but the Foundation is migrating over a five year period to reduce the pain on the University beneficiaries. They have built up the reserve to smooth it over years, but there is still a concern that the payout may be too high. Goldman Sachs did a study suggesting the payout should be well below five percent.

Beyond the 5% payout, the Foundation takes three-quarters of a percent administrative fee for support of the Foundation’s operations, including the stewardship it provides to donors. It was noted that the 5% rate is still more generous than most Universities according to a third party analysis. In addition, the payout rate is high in relation to the long term results outlook. For the long-term sake of the endowment, UMFIA would still like the Foundation to consider further reductions in the rate.

Professor Konstan asked if one of the things that might cause a further fee reduction was the anticipation that the endowment would grow to over a billion dollars. Has the Foundation been looking at the question of whether this three-quarter percent needs to remain as high as it gains some economy of scale from having a larger amount? The long-term hope is that the endowment would grow faster than the operating budget and therefore permit a reduction in that fee, Mr. Fischer said. They are, however, ending the capital campaign (there are actually nine months left), but they have more identified potential than they did at the beginning, even though they have raised $1.457 billion so far. The Foundation cost to raise a dollar is 10 to 12 cents but they are getting a return $8-$10 for every dollar it is spending. The Foundation Trustees are asking how to invest more to seize more potential and get a 10 to 1 return on investment. Community foundations are at about 1%; many banks are over 1%. The Foundation does not want donors to go somewhere else because they view the Foundation as inefficient, Mr. Fischer said.

The present capital campaign is taking three-quarters percent from University funds. When the capital campaign is finished does that go away, a committee member asked? He is recommending it continue, Mr. Fischer said. They provide stewardship; it is a legitimate fee. In the spirit of figuring out how to raise more money it is a source that helps them.

Professor Speaks thanked Mr. Fischer and Mr. Gorence for joining the meeting.

3. Construction Practices

Professor Speaks now introduced Gail Klatt, Director of Audits, Mark Rotenberg, General Counsel, and Vice President Kathleen O'Brien from University Services.

Ms. Klatt explained that when they audit construction they do not audit specific projects; for example, auditing all of the costs associated with Riverbend Commons. That function is housed in Facilities Management's Construction and Design Services unit. The Department of Audits' charge is to audit the control processes established over construction activities (such as whether change orders are being properly controlled) using a sample of construction projects.

In December of 2000 they issued an audit for which most of the projects sampled followed the design-bid-build methodology. This was not intentional but simply reflected the fact that this method was the one most used at that time. The audit reported in April, 2002 involved mostly projects using the design-build method, which again reflected the method most in use at that time. They offered no opinion about which was better. The controls that need to be in place are similar but vary in how they are accomplished.

The primary difference between design-bid-build and design-build is the role of the architect. In the design-bid-build process the University would contract directly with an architect. The architect would draw the plans and the University would then ensure that the plans met requirements. The University would put the project out on bid to construction firms. The architects are contractually obligated to the University as its representative; they serve as its agent. In the design-build process, the construction firm will usually use an architect as a partner to develop a proposal to design and build. In that case, the University contracts with the construction management company, which is partnered with the architect--the architect's relationship is with the contractor, not the University. The design-build process shifts responsibility for guarding the University's interests and seems to require more oversight on the University's part. Ms. O'Brien added that design-build is a competitive process; design-build also has a guaranteed maximum price whereas design-bid-build does not.

Committee members were curious to know if there was any difference in the risk to the University between these two processes. The response was that the risk is limited by how good the contracts are as well as the quality of contract management. Design-build generally proceeds faster because they can go in parallel with design and build where design-bid-build is more serial. Design-build expedites the construction process.

Professor Campbell noted that it seems that with design-bid-build the University knows what it is getting but with design-build it has to make compromises and raise prices. People who advocate for design-build say that when unforeseen circumstances arise they can be remedied more quickly because the contractor and architect are working together and it is to their benefit to finish quickly. But does one trade timeliness for price, he asked? Both Ms. Klatt and Ms. O'Brien agreed. Vice President O'Brien added that the University will end up with a better product if it has a clear definition of what it wants; change orders cause the same problems in either process. The project delivery method is not really the cause; it is the way the process is used, she said.

Professor Konstan noted that if a project is under-funded compared to the program's ambition, it will save time, effort, and money by discovering that gap in a separate design process before going into bidding or building. Design-build seems to work best if the amount of funding matches ambitions.

Vice President O'Brien observed that the guaranteed price in design-build puts a limit on the project. But if the University changes its expectations, when the occupants decide they want to modify something, the change will be expensive with either process. That is part of the control mechanism: Who provides direction to contractor in terms of subsequent changes.

Professor Roe inquired which of the two methods are most common. Design-bid-build is the traditional; design-build is relatively new but gaining popularity, Ms. Klatt said; Vice President O'Brien agreed. There is no rule about which is best.

Mr. Rotenberg next informed the Committee that the General Counsel did two things in order to inform the Board of Regents and President about these projects. The General Counsel's office does not typically conduct a review or audit of a whole area of University concern, but because there was over a billion dollars involved and there were concerns about contracting and delivery method, the General Counsel's office decided to conduct a review of the contracting in response to the issues raised in the December, 2002, audit. The public document that was discussed at the Regents' meeting in June produced 13 recommendations which address how the University contracts for construction services and manages the projects once they are delivered, because it can receive all kinds of guarantees with design-bid-build and the same with design-build. They do have inherent differences; design-build is generally speedier and problems that arise incidentally can be worked out more quickly and with less conflict--the architect and construction company have no economic interest in blaming each other (as they may in the design-bid-build process). One design-bid-build advantage is that architects may be more zealous in defending the University's interests because they have no economic connection with the contractor. Mr. Rotenberg emphasized that how these things play out depends a great deal on the project "owner" (unit or department) and project.

Mr. Rotenberg then offered two recommendations. One was in the area of design supervision. Irrespective of which delivery method is used, he said, the best way for an owner to ascertain design quality is peer review. In current and prior situations, when specifications were defective the primary recourse was litigation or arbitration. But, he said, even an excellently-litigated result will not deliver a better project. In the future, Facilities Management will obtain independent peer review of the plans and specifications in those cases when projects costs exceed $1 million. The University, in order to be economical, has not had inspections of projects in a way that would determine good workmanship and conformity to plans and specifications. Although it does employ independent testing firms to test soil and building codes, it usually does not have comprehensive inspection processes on major construction processes.

Facilities Management should provide for construction project inspections on projects over $1 million in value. The General Counsel's office does not have an opinion on the delivery method; neither is necessarily disadvantageous from a legal liability standpoint or risk exposure standpoint. They have been reviewing and revising contract forms for Facilities Management so that the contracts will better address the University's interests. The recommendations were directed at improving the overall project delivery so that the University's legal interests are best protected.

Professor Konstan mentioned that the Committee had just heard from the Foundation that in portfolios approaching a billion dollars, it was seen as prudent to farm things out to outside managers. Is that the scale that the University is in with respect to construction? Should it have a set of outside construction experts as opposed to trying to supervise with staff from inside the University? Vice President O'Brien said there are two or three answers to that question. First is that the volume of work in the last four to five years was extraordinary in the University's history; that volume is declining and will not likely return in the near future. The second answer is that yes, when the University has an extraordinary volume of work it is not prudent to increase staff to the level of that extraordinary volume. For example, she said that when she oversaw the doubling of the size of the Minneapolis Convention Center, they hired an external construction manager. A third answer is also yes, the University did use some external managers.

The questions the University really needs to ask are these: Are we getting what we designed? Is it safe? Are we getting what we paid for? Audits raise those issues. University Services plan to improve construction oversight and management services.

Ms. Klatt said this gets back to the view that neither of the methods is inherently better or worse; the issue is how they are managed. One of the things they determined from the audit was that the University's contracts with the external owner's (the University's) representatives were identical whether it was design-bid-build or design-build arrangement. Theoretically, the external University representative should have had additional responsibilities under design-build, which raises the question about the expectation of the oversight they would provide. In terms of the use of internal or external owner's representative, one is not necessarily better than the other.

Professor Konstan inquired about the two reports, one of which was a public report delivered to the Regents. What, if anything, could Mr. Rotenberg tell the committee about the other report which was not publicly presented? Mr. Rotenberg said there was a nonpublic report which is protected by attorney-client privilege with respect to certain allegations of wrongdoing related to some of the construction activities of the University. The only thing he could disclose was what he disclosed in the public meeting in December: There was no evidence found to warrant discipline of a University employee. The General Counsel's office did not refer any issues to the county attorney.

Professor Jahn asked if the visitors could comment on the current status of Andersen Library. Mr. Rotenberg said that they have studies with respect to environmental issues at or near the library. They believe that the environmental issues from a legal standpoint (OSHA and protection of the workforce) have been successfully addressed. With respect to the cause of certain leaking and pollution in the area, the General Counsel's office had a long dialogue with Minnegasco. It is the University's position that Minnegasco is responsible for a lot of issues related to groundwater and subsurface pollution on that side of the campus.

Professor Jahn followed up by asking if they had any inspections from outside inspectors during the construction of Andersen Library. Ms. Klatt said that Andersen was mostly done when they began their audit effort but she believed it would have followed the same process--the University did not do inspections themselves. It does not have an inspections staff.

Ms. Van Voorhis said that what happens usually is that the architect designs a wonderful building but forgets about the classroom technology and equipment and furniture needed--and then change orders occur. By the time it gets to her to purchase the furniture and technology there is no money left. Is there any way to can avoid this problem? Vice President O'Brien replied that she is aware that one of her major tasks as Vice President for University Services is restoring trust and confidence in the design and construction processes. The issue that has been raised is not one where the University can change one part of its process to make it better. As a new person in this position, she is conducting a systematic review of how they develop the building programs and who makes decisions. The University will end up with the right product if it spends time at the front end, she said; her job is continuously to improve the process. The University can do a better job than it has. She noted that she would be happy to report back to the Committee in the future.

Professor Speaks said he believed Ms. Van Voorhis raised an important point. As there are new classroom facilities being built on campus, how frequently are Ms. Van Voorhis or Mr. Fitzgerald, Director of Classroom Management, consulted? Normally, not until later, Ms. VanVoorhis said. The technical people need to be involved from the beginning to address issues related to acoustics, lighting, and classroom technology.

Professor Speaks thanked Ms. Klatt and Mr. Rotenberg for their report.

4. Stadium Update

Professor Speaks then turned the subject to the update on the stadium. It will go before the Board of Regents for discussion in November and for action in December. Professor Speaks noted that one of the metropolitan newspapers reported that things are moving well on the Vikings side but are very complex and slow at the University. The Committee would like to know where the University is with respect to the predesign and the Memorandum of Understanding (MOU).

Mr. Rotenberg said that design elements have been worked on intensively by Ms. O'Brien's and Mr. Pfutzenreuter's people. An enormous amount of work has been done. The legislation provides that all material aspects will be worked out in a bargain between the University and the Vikings franchise.

There are several ways to achieve the objectives that the Regents have set out; nothing is going to satisfy everyone. For example, the campus look and feel is obtained from something standing on the ground. With the respect to the objective that we obtain a substantial financial benefit from the project, is that a contribution of one professorship a year from Red McCombs, is it balancing the athletics budget, is it $1 million in cash for rent payments? To reasonable people, these are all things that could be considered substantial benefits. These things have to be compartmentalized in a document and they must figure out what can be achieved.

The macro-negotiation posture can be envisioned as a three-legged stool. One is the requirements of the University of Minnesota, which are described in the principles. The University must have a limit on its capital contribution, it must make sure the stadium can support itself on an ongoing basis because it will be on campus for many years, and it must make sure the stadium fits well with the University's academic agenda, the neighborhood, and campus life. The second leg is the Vikings, which are part of a large entertainment business; they have their requirements. Most important, they need to make a lot of money playing football in the stadium. The third leg is the public--and the legislature, which represents the public. In order to finance the gap between the Vikings contribution to the project and what the University will contribute to the project, the legislature needs to be assured there will be revenues that will support the stadium. They are trying to be sensitive to every one of those concerns, Mr. Rotenberg said.

It is not clear that all these objectives will be realized. It may happen, and if it does the MOU draft and pre-design materials will be forwarded to the Board of Regents by the President, presumably with the recommendation that the Regents approve it, recommend it, and forward it on to the legislature. If the agreement and the understandings cannot be reached in time, then there might be another resolution that will be appropriate for the Board to vote on. The instructions from the President and Board of Regents are to achieve as best they can implementation of the principles adopted by the Board. If that goal cannot be achieved, the University is not necessarily under pressure to deliver a document that the Vikings will find acceptable.

Professor Speaks asked if Mr. Rotenberg anticipated having a draft of the MOU for the November Board meeting? He did not, Mr. Rotenberg replied. The Regents will be updated at the November meeting. Materials are to be distributed late in November, presumably including a draft MOU draft so people could see some of the operational, governance, financial, and other parameters. There will be a series of public discussions with various constituent groups, including and especially the faculty and students on campus. The Regents would have an opportunity at their December meeting to vote and decide how the University is going to transmit it to the legislature.

The last one or two presentations the Committee heard included a parking facility that the University would pay for at a cost of about $60 million, Professor Speaks recalled. At one point that ramp was projected to lose about $3 million annually. It has now been said that the size of the parking facility has been scaled back. Is that correct, and if so, how much was the cost reduced and does the reduction have any effect on the projected annual deficit? Mr. Rotenberg and Mr. Pfutzenreuter said that is still under discussion.

Professor Campbell said that he was interested in knowing what happens if the University and Vikings agree. The MOU is between the Vikings and the University. Does this mean the University has now made a commitment to the stadium and the legislature goes along with it and agrees to the funding? Mr. Rotenberg said that it depends what is contained in any resolution the Board passes in December--if it even passes anything. It will depend on what the documents say. For example, if the negotiations are successful the Board could pass a resolution that endorses this project as defined by the accompanying materials (MOU, predesign, and so on). There would be various conditions in the document that would specify when the University and Vikings would be prepared to go forward. It will not say that the University is committed to the stadium under any and all circumstances. Even under the most sanguine hypothesis for the project there would be conditions, which if not met would destroy the possibility of going forward. Most obvious, if the legislature does not fund it appropriately, in which case the Vikings will not be committed to doing anything and neither would the University.

If in fact the MOU is successfully executed, is it possible that everything in there would be agreed to, and in that sense, it could be a go based upon the Regents accepting or executing this MOU, Committee members asked? Mr. Rotenberg said it could be but the devil will be in the details

Professor Campbell asked where Mr. Rotenberg saw a role for the constituents--the faculty, students and staff--in having an impact on the decision? Is it just a matter of getting the conditions right in order to get the stadium here and paid for or is there a place in this decision-making process for the attitudes and opinions of the University community? Mr. Rotenberg said he was under the impression there was a lot of consultation occurring. The faculty has articulated in writing its concerns through the Faculty Consultative Committee. And consultation is virtually a nonstop activity around the University.

Professor Speaks agreed that there has been a lot of consultation but if everything is right in the MOU, if University decision-makers are happy with it, and if the Vikings are happy, but the faculty, staff, and student say they do not like the concept and want it stopped, can it be? Mr. Rotenberg said that faculty, student, and staff views should be expressed as forcefully as possible to the Board of Regents and President. It is not improper to say "we don’t really care about the principles being implemented, we don't want to have a building like this." It is absolutely appropriate to make your case, Mr. Rotenberg told the Committee. Additionally, the President has not publicly said that he will favor the project.

Professor Speaks said that individually Committee members all have opinions, even if it is one of uncertainty. Collectively the Committee has never tried to decide how it weighs in on the issue. Partly this is because it wants to be able to do so at an appropriate time--if or when it decides is has an opinion. The Committee also wants to avoid taking a position at a point that might adversely affect the negotiations. At the last meeting, the Committee decided it wanted to continue to be informed and to express its concerns--rather than a final opinion--and defer to FCC and SCC. At some point, the Committee needs to make its opinion known, if it knows what it is.

Professor Warwick noted that the question that comes to mind is the marriage between two unequal groups. On the one hand, there is an institution 150 years old; on the other is an individually-owned, commercial company that could take the team away. If the University owned the team, he said he would feel very differently. But the University has unanswered questions and it must have answers in the MOU between this volatile, uncertain group and the University, which has a different charter.

Mr. Rotenberg said that this is a foundational problem: the University not moving any place and can't be sold. Nothing the University can do in a document can prevent the Vikings from being sold. On the other hand, the University can make it all but legally impossible for the owners to remove the team from this facility for a period of years. The University could also seek to have the NFL bound by that obligation. He said he thought it would be impossible to imagine the legislature would fund a stadium in the absence of such a guarantee. At the same time, the volatility of the industry cannot be contractually or legally be whisked away. But certain things can be assured; that includes keeping the team here and playing football in the stadium.

Ms. McCarthy Barnes noted that the University has a set of criteria identifying what it wants and it will negotiate those criteria with the Vikings. Will the University move forward if the Vikings cross off any of the criteria? Mr. Rotenberg said they are not authorized to move off the principles adopted by the Board of Regents. But there are lots of ways to skin the cat, so to speak: There are many ways to implement the principles, and that is the content of the discussions.

Ms. McCarthy Barnes next asked if the MOU could go back to the Board of Regents with some adjustments to the criteria, which the Board could approve? Mr. Rotenberg said that has not been offered as an option to the Vikings; none of them would be comfortable going to the Board with such a proposal. The MOU and pre-design are going to have to comply with the principles the Regents sent them to implement, Mr. Rotenberg said.

Ms. McCarthy Barnes asked if the Vikings were coming to the table with the same idea that they will not make any adjustments. Mr. Rotenberg said the Vikings have a very different set of objectives. They are at the table to get a stadium that will make them a lot more money on an annual basis and which will presumably put them in the top quartile of NFL in terms of annual revenue. The current owner also wants the value of the asset to appreciate and they believe that will not occur without a new stadium.

Ms. McCarthy Barnes said that students may have something to say above and beyond the criteria adopted by the Board of Regents. But conversation seems to be lacking about what would make it acceptable or not acceptable to have a Gopher/Vikings partnership on campus.

Professor Konstan asked what would happen if in December there is no agreement with the Vikings--would Mr. Rotenberg ask the Board of Regents to consider a statement releasing the University's last offer in the negotiations so the University can make the case with the public and the legislature that it made a reasonable attempt to come to terms with the Vikings? Mr. Rotenberg said he did not know the answer; he has not discussed the option with the Board or the President.

Has the fact that there is no resounding outcry for the stadium from the University helped the University in negotiation with the Vikings, Professor Konstan inquired? It has, Mr. Rotenberg said.

Professor Konstan asked how far from a contract the MOU would be--if legislature went along with everything, does the University have a chance of being burned in the contract details? There would be a lot of work to implement the MOU, Mr. Rotenberg said. Because of the compressed time frame the MOU will not contain enough detail to implement it as a legally effective instrument. A stadium project of this magnitude will take well in excess of 40 different contracts to be drafted, negotiated, and executed. That’s a lot of lawyer and negotiation time, Mr. Rotenberg said.

Professor Jahn agreed with Professor Campbell and Ms. McCarthy Barnes about the appropriate time and place for faculty, staff, and student views. The basis of the problem is that there has been no invitation for such participation; there is the impression that the decision has already been made so people feel that they can only whine from the sidelines. There are things that are virtually agreed upon and some that are very contentious, Mr. Rotenberg said. Money is an issue in these kinds of deals. Who is going to establish the firewall to protect the University from financial exposure to the operation? The cash flows and liability are very important issues.

Professor Korth said that part of the difficulty is that everything the University is doing is defensive. If the University is trying to minimize the negative impact of something that is apparently being pushed on it, it is not a positive situation to which people can contribute; it is all negative and it is unclear how the Committee can make its voice heard. He was puzzled at the apparent reluctance to come out and say that this is not in the best interests of the University.

Professor Speaks noted that he will, at any time between now and when the issue goes to the Board of Regents in December, entertain a motion of any form for this committee. He sensed last time the Committee met that it was not prepared to make a statement and that it wanted to let the FCC be the point committee.

At the FCC retreat in August, there was a conversation with the Provost and a chair of the Board of Regents; it was said that one reason why the University must continue to be a player in a joint stadium is that if there is no joint stadium, there is not likely to be a Vikings stadium; if there is not a Vikings stadium, the Vikings will leave town--and the University doesn’t want to be blamed for it. Ergo, the University should continue to participate. Professor Speaks said he did not agree with that reasoning.

If everything gets approved by everybody, including the legislature, by some date in March, then the NFL makes a contribution to the project of $51 million. Is that a real deadline that is helping set the University's timeline or is that something that can be negotiated with the NFL? Is that a real gift or is it a loan? Finally, for six Gopher games and 10-11 Viking games why are we talking about a retractable roof, Professor Speaks asked?

Mr. Rotenberg said that it was his understanding the NFL contribution is phrased in terms of a loan to the franchise. It is up to the franchise to pay it back but even the owners describe it as a gift. Everything they do is to make money. They will invest in a new stadium if they think it will make them more money. The NFL loan program is supposed to expire this spring; the owners will meet and make new decisions. There could be a new plan after March, or there may not be. Some revenues go to franchises, some go to the owners. By having a stadium that generates tens of millions of dollars more in revenue, both the franchise owner and other owners can reap big financial benefits. As for the retractable roof, the Vikings will not consider any other option than a roof because the Super Bowl and other events cannot be played out-of-doors in this market.

Professor Speaks asked if there is $151 million on the table, $51 loaned to the franchise from the NFL and $100 contributed by the franchise to the project. When revenue starts flowing to the University and the franchise, the franchise does not start making money until they recoup the $151? Technically speaking, the $51 million is a loan from the league to be paid back by visiting team television receipts, Mr. Rotenberg said.

According to what he read in the newspaper, Professor Campbell said, the value of the Vikings increases $300 million dollars if they have a new stadium--so they put in $100 million and their value goes up $300 million? If the total cost is $500 million, $151 million of that is in effect a loan that gets paid back, should the legislature fund the other part, a contribution that does not paid back? That is not accurate, Mr. Rotenberg said; the bonds would be paid off over a period of time. The University would have some legal assurance that the team would stay in the stadium until the bonds are paid off.

Professor Konstan said that there are good reasons people are not speaking publicly about how wonderful this is. The Committee must exercise caution in making statements representing faculty and students. Those who are interested in serving in governance are probably less interested in sports than the average student on campus. The Committee should think about whether there is a role for a larger forum to obtain a broader representation of views. In all these negotiations the lease would lock the Vikings in as long as bonds remain to be paid. But teams often spend a great deal of money before the lease is up in order to get lease forgiveness so they can move. Professor Konstan said he hoped the University can find a way to negotiate an agreement so that the bonds are repaid if the team does not need or like this stadium anymore.

Ms. McCarthy Barnes agreed with Professor Konstan. She felt the University has created forums for the expression of views. As a student she feels she can say things that maybe administrators cannot. The Committee can challenge things that others cannot. She said she was concerned about the University entering a partnership with people who are involved in the franchise just for the money--and that the Committee should put these opinions on paper. She said the Committee will have done an injustice to students and faculty if it does not say anything. If the Committee is uncertain, it is important to communicate that, too.

Mr. Amattoe said that most members of the Committee have passionate ideas about the stadium and Vikings. He moved a motion to make the stadium as a subject of discussion at the next meeting with more information, come to a conclusion, and make a statement. Professor Konstan said that he thought it perfectly reasonable for someone to circulate drafts of statements to see if the Committee can agree; the Committee should also spend energy on all the other things it has let slide.

Professor Roe asked about the status of an MOU. Does it mean that the University has already made a decision? He said he hoped that was not the case. It seemed to him that the faculty know where they stand relative to the MOU. Professor Campbell agreed. He recalled that there was some mention of the FCC statement which addressed details; he said had a feeling of grand uneasiness and then people begin to find little reasons to object. He said that Ms. McCarthy Barnes comments go beyond those reasons, that FCC or SCC should lead a "future of the University" discussion which deals with the grander notions of how a stadium enhances or detracts from its missions, in addition to the details. That must come from the leadership of SCC, perhaps in conjunction with some hearings where people can express their opinions. There are both sides of the issue: if the stadium happens the University wants to make sure it happens right. If there's no choice in the matter, the University will want to optimize its position. Is there a choice? Professor Campbell said the Committee's role is to look at the bigger picture, the forest instead of the trees--or in addition to the trees.

Mr. Rotenberg reiterated that he encouraged the Committee to make its views known in proper form and they will try to get as much as they can for the University and defend its interests as zealously as possible.

On Mr. Amattoey's motion, there were two in favor and four opposed. The motion failed but will be discussed again at an appropriate time.

Professor Speaks had had to leave the meeting before it ended. Professor Campbell assumed the chair; on vote taken, he adjourned the meeting at 5:00.

-- Katie Derdoski & Gary Engstrand

University of Minnesota