United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6500

ANNOTATED RESPONSE

SMR

October 27, 2005

Thomas Gottschalk, Acting Chair of the Board
Office of the, President
American University
4400 Massachusetts Ave., NW
Washington, D.C.

Dear Mr. Gottschalk:

I am deeply troubled by reports about the recent actions of the American University's ("AU") board of trustees in regards to payments to former president Mr. Benjamin Ladner related to Mr. Ladner's departure. The Finance Committee has been engaged in a bipartisan review of charities and reform of charities and it appears the AU board could be a poster child for why review and reform are necessary.

The Internal Revenue Code ("IRC") provides charities very special treatment. Most important is the exemption from income tax and the ability to receive tax-deductible contributions. It is therefore particularly troubling when an organization receives preferential tax. treatment and then believes that it is proper to provide approximately $3.75 million in payments to an individual who has reportedly failed to pay taxes on nearly $400,000 in income (for the last three years) after the board terminated his employment. Such actions raise significant questions about what other things a charity that has such a cavalier attitude toward the tax laws might be doing, especially in light of escalating tuition increases.

To assist the committee its review of AU and the AU board's actions, the Committee requests the following.

1) IRC Section 4958 - Excess Benefit Transactions

a. Provide copies of Mr. Ladner's employment contract, deferred compensation and severance plans and any other compensation arrangements, including expense reimbursements.

Provided. (See AUSF 000001-000075, 009187-009279).

b. Provide all material, discussion, legal opinions, compensation studies and analysis or other related items used by the AU board, compensation committee or other relevant governing body when making its decisions regarding Mr. Ladder's employment contract, deferred compensation and severance plans and any other compensation arrangements, including expense reimbursements. Provide all material documenting AU's compliance with Internal Revenue Code ("IRC") section 4958 with respect to these items, including but not limited to copies of minutes of meetings from AU's board, compensation committee or other relevant governing body as well resolutions or written actions regarding such transaction. Provide a copy of any settlement agreement or release of claims entered into with Mr. Ladner and explain how any amounts paid under such agreement were determined.

Provided, with the exception of privileged materials.

c. Identify consultants, accountants, lawyers and or other outside advisors used with respect to the items requested in "a" and "b" above, and include names, addresses and total fees paid.

Provided.

d. Provide a list and brief description of all no-bid contracts issued by AU and its affiliates and subsidiaries over $100,000 for last 11 years. Explain how no-bid contracts are awarded.

There are three no-bid contracts with disqualified persons under IRC 4958 to disclose.

Lord Chadlington Peter Cummer was elected to the Board in May, 1999, and resigned in early 2001 prior to the February, 2001 Board meeting. He was employed by Shandwick International, a public affairs counseling firm. His firm was paid a total of approximately $287,000 for work related to raising the international profile of the University and Dr. Ladner in 2000 and 2001. (<u>See</u> AUSF 009284-009288).

Paul Wolff, Esq., a partner in the law firm of Williams & Connelly, served on the Board beginning May, 1996 through October, 2005. During the years 1999-2001, his firm was paid $301,749 for legal services related to litigation on adverse personnel actions. The Williams & Connelly attorney leading the work was Nancy Lesser, Esq., not Mr. Wolff. (<u>See</u> AUSF 009289-009290). This relationship was routinely reported to the Board during the General Counsel's regular reports. Attorneys are chosen by the General Counsel of the University.

Finally, Matthew Pittinsky, who is the Chairman and co-founder of Blackboard Inc. and an alumnus of AU, was elected to the Board in May, 2000 and continues to serve on the Board. AU began licensing Blackboard's teaching and learning software more than a year before his Board service began, and had licensed Blackboard's campus commerce system even earlier (the product was originally licensed from a company that was later acquired by Blackboard). AU has renewed its licenses to the Blackboard products -- specifically, the Blackboard Learning System and Blackboard Transaction System -- which are sold on an annual subscription basis. The annual amount spent on Blackboard's software products and related services has averaged approximately $160,000 over the past 5 years. The amounts paid to Blackboard result primarily from the annual fees arising from the subscription nature of the products licensed by AU. Blackboard is a leading provider of enterprise software applications to the education industry and has 2,200 educational institution clients, including, for example, Georgetown University and George Washington University. Mr. Pittinsky has never participated in sales meetings or activities with AU. Mr. Pittinsky disclosed Blackboard's business relationships to the first Board Chairman he served under at AU, and notified the entire Board of this issue on several occasions. He abstained on votes related to budget and funding that related to Blackboard's products. (<u>See</u> AUSF 009291-009343).

e. Provide copies of any conflicts of interest or similar policies as well as expense reimbursement and travel policies that have been adopted. Include an explanation of haw the AU processes expenses and requests for reimbursement. Please explain what, if any, changes to these policies AU is considering. Explain whether such policies were followed and enforced with respect to Mr. Ladder.

Provided. (See AUSF 009187-009279). The University's clear policies on expense reimbursement (copy provided) were followed, except with respect to Dr. Ladner. The Acting President is following the clear University policies. The next president of the University may deviate from any policies for other University officers or staff only with the written approval of the Board.

f. How did the board comply with its State law fiduciary duties in its actions regarding the hiring, retention, compensation of, and termination of, Mr. Ladner?

Please see the response in the accompanying letter from Gary M. Abramson and Thomas A. Gottschalk.

2) Board Governance & Transparency

a. Discuss whether you believe that there is sufficient transparency regarding your highly compensated officers, directors, trustees and employees. What do you to ensure numbers are transparent historically and in the future. Do you believe there was adequate disclosure?

Please see the response in the accompanying letter from Gary M. Abramson and Thomas A. Gottschalk. The IRS Form 990 discloses such compensation for top officers. Trustees are not compensated except for expenses relating to their service on the Board.

b. Provide descriptions of all transactions with disqualified persons (as defined in IRC section 4958(f)). Provide copies of legal opinions and minutes from board meetings discussing these transactions. Please provide this for the last three years for compensation, loans, property purchases/leases mid services for over $100,000.

Except for compensation paid to officers and as discussed above in response to question 1(d), the University did not engage in any transactions valued at over $100,000 with disqualified persons.

c. I understand that the AU audit of Mr. Ladner was for the most recent three years. However, Mr. Ladner's tenure was for eleven years. Given the extraordinarily troubling findings from the audit of the most recent time period, please inform me of your plans to conduct a complete audit of the entire 11 years.

The Committee is correct that the University audited the past three years of Dr. Ladner's tenure. At the present time the University is not planning to audit the prior years, a matter of practicality, prudence and law.

First, Dr. Ladner's relationship to the University has been terminated directly as a result of the three year audit.

Second, Dr. Ladner's expenses and imputed income are now under Department of Justice review. The Department of Justice has subpoena power, grand juries and other mechanisms to obtain Dr. Ladner's cooperation. In addition, the IRS, of course, can challenge Dr. Ladner's prior tax returns. Given this governmental power and interest, these matters are now appropriately between Dr. Ladner and these authorities, and the University

can and should stand aside and permit these procedures to address the prior years.

Third, the audit and investigation of the three years completed was very expensive to perform. While it resulted in a return of approximately $125,000 in items to the University plus interest, and the addition of approximately $400,000 in income to Dr. Ladner, the cost of conducting the audit and the related legal opinions is not financially proportionate to the funds returned. On a cost benefit basis, it is not financially prudent to continue the audit, due to the likelihood that the costs of further work will exceed the recovery.

Fourth, as we go back in time, it becomes more and more difficult for the University to find records sufficient to make sound business judgments. To be fair both to Dr. Ladner and the University, this is a matter best left to the federal authorities who are reviewing the matter.

Fifth, as a legal matter, the general statute of limitations that would be applicable to the assessment by the IRS of income taxes against Dr. and Mrs. Ladner is three years from the filing of their Forms 1040, according to IRC section 6501(a). The AU audit has covered to date all open years under the general statute of limitations.

Extending the audit back to eleven years would require auditing years already closed by the statute of limitations and would not be productive with respect to potential tax liabilities.

For all of these reasons, we believe the University's decision under these circumstances not to expand the investigation of Dr. Ladner's past expenditures earlier than 2002 is appropriate.

d. Provide your articles of incorporation, bylaws (in effect far past 11 years), application for exempt status, and the IRS determination letter. For the past 11 years, please provide a brief description of individuals who served on the board, a short biography, qualifications, how the board member was selected and how the board members serve the interests of the community.

Provided. (See AUSF 009344-009516).

3) Internal Revenue Service Filings

a. Please inform me of whether AU plans to amend mend its Form 990 for any year and whether it will be necessary for AU to amend Forms 990-T or 1120 of any affiliated or subsidiary organizations.

As we indicated in the accompanying letter from Gary M. Abramson and Thomas A. Gottschalk, AU has filed amended Forms 990 for 2002, 2003 and 2004. AU does not believe it is necessary to amend its Forms 990-T, which are accurate as filed. The University does not have any affiliates or subsidiaries.

b. Provide copies of all Forms 990-T and 1120 of affiliates and subsidiaries of AU for the last three years. Please provide all copies of legal opinions provided, created or received by AU for the past three years that discuss unrelated business income tax ("UBTT") implications, including debt-finance income as well as Real Estate Investment Trusts (REIT).

The University's Forms 990 are provided. No such Forms 1120 were filed There are no such opinions discussing UBIT or REIT issues. (See AUSF 009517-009666, 010463-010585).

c. Disclose the identity of all supporting organizations (as defined in IRC section 509(a)(3)) and provide copies of Forms 990s for such organizations for the most recent three years.

None.

d. Provide all correspondence with the IRS for the past five years.

We have provided all correspondence between the University and the IRS related to AU's Forms 990. AU's routine correspondence with the IRS (e.g., transmittal letters) is quite extensive and will be provided upon request. (<u>See</u> AUSF 009667-009669).

e. AU's 2003 Form 990 indicates $180 million in tax-exempt bond liabilities. Please explain in detail what the proceeds were used for, and how soon after receipt bond proceeds were obligated.

f. Provide a copy of all work papers from KPMG audits for the last three years.

Given that this request appears in the section relating to Internal Revenue Service Filings, we have interpreted this request as covering KPMG's work papers for AU's Forms 990. These work papers will be produced to the Committee under separate cover by KPMG. KPMG also prepares AU's audited financial statements. KPMG's work papers relating to such statements are available upon request. At the request of AU, KPMG has withheld two privileged documents, an October 5, 2005 legal opinion from Arnold & Porter LLP, and an October 7, 2005 legal opinion from Manatt, Phelps & Phillips LLP, both of which will be disclosed on the privilege log being provided to the Committee by the University.

4) Executive Compensation

For the past three years for individuals listed in Part V of form 990 "List of Officers, Directors, Trustees and Key Employees," and Part I "Compensation of the Five Highest Paid employees Other Than Officers, Directors and Trustees", please answer the following:

a. Explain how you established the amount of compensation and benefits.

<u>Officers, Directors, Trustees and Key Employees</u>.

The Trustees of the University are not compensated for their service. However, they may be reimbursed for reasonable business expenses incurred during activities related to their service on the Board.

<u>President</u>. The Board of Trustees is responsible for establishing the amount of the President's compensation and benefits. When Dr. Ladner, the former president, was hired in 1994, the University entered into an employment agreement with him. In setting Dr. Ladner's initial base salary, the Board collected compensation information from comparable educational institutions. Although no formal compensation study was done at the time Dr. Ladner was hired, in recent years the Board has formalized the process of setting the president's salary, including engaging compensation consultants to conduct compensation studies that consider every element of the president's compensation in comparison to his peers.

In late 2004, Arnold & Porter LLP, as counsel for the Board, retained Mercer Consulting ("Mercer") to conduct a review of compensation paid by like universities to their presidents. Mercer collected and reviewed compensation data (including base salary, cash

incentives, pension plan contributions and perquisites) for the presidents of comparable universities, based on four peer groups. The first peer group was compiled based on competition for students, enrollment, revenue, endowment, and organizational complexity. The second peer group was compiled based on universities with the same Carnegie Classification as the University: "Doctoral/Research – Extensive." The third peer group was compiled using a subset of the second peer group, selecting only universities with scope measurements similar to the University. Finally, the fourth peer group was compiled by Mercer using eight factors to determine similarity to the University. The peer groups together comprise forty-one universities, although there is overlap among the four groups. Mercer examined IRS Forms 990, published surveys of compensation data, and their own client database.

Based on Mercer's analysis of comparable data, the former president's longevity in his position, and the performance of the University under the former president, the Board targeted the president's proposed compensation at the 75th to 90th percentiles of the University's peer group.

After considering Mercer's analysis and other data regarding the former president's duties and performance, the Board reduced the former president's total compensation (consisting of base salary, a performance-based bonus determined by the Board, deferred compensation and a life insurance benefit) to no higher than $793,000, bringing it in line with the 75th to 90th percentile of compensation paid by his peers.

Vice Presidents. The President is responsible for establishing the compensation and benefits for each of the University vice-presidents, with the review and approval of the Board of Trustees Compensation Committee. Last year, Mercer Consulting was retained to evaluate the compensation of each of the University vice presidents on an annual basis, and to make recommendations as to the appropriate level of compensation and benefits for each of the vice presidents based on compensation data from comparable educational institutions. Many of the vice presidents are longstanding employees of the University, so that their initial compensation level was set many years ago when they were first employed by the University. The vice presidents' salaries and annual raises fit within the compensation structure and budget of the University, and are in line with salaries paid to their peers at comparable universities.

Deans. The Dean of the Washington College of Law, Claudio Grossman, and the former Dean of the Kogod School of Business, Myron Roomkin, have been among the top five highest paid University employees over the last three years.

Generally, the process for establishing the initial compensation for a new dean begins when the University establishes a committee and hires an executive search firm to seek out suitable candidates. The same search firm will often compile information on the compensation of deans at comparable universities. When establishing the incoming compensation level, the University also considers the salary history of the candidate, the current salary budgeted for the position, as well as how the contemplated compensation fits in structurally within the University budget and pay scale. In the case of both business schools and law schools generally, there is a highly competitive market for deans. AU's inability to match a salary offer was the most important factor in the departure of the business school dean in 2004.

Like all other University employees, the deans are eligible for merit increases on an annual basis. The pool for the merit increases is established and approved on an annual basis by the Board of Trustees as part of the budget process. The amount for merit increases is added to the salary base in the Office of the Provost The University does not make cost-of-living adjustments to any of the deans' salaries.

The merit increase pool is allocated using the following process. Each year the president, vice presidents, and provost work together to establish a set of goals for the entire campus. The president then solicits school-specific goals from the deans of each of the academic colleges that are consistent with the University's broader goals. The deans' goals typically include items such as enrollment, scholarly and professional achievements, teaching quality, and fundraising. At the end of the year, each dean must submit an annual report detailing the college's successes or failures in achieving the goals that were set at the beginning of the year. The standard guidelines for the deans' annual reports are enclosed as AUSFC 000001-000002, 000036-000039 (marked as confidential). The deans' annual reports are submitted to the provost, who then reviews the reports and meets with each dean to set his or her merit increase. Once the provost has made a determination regarding a proposed merit increase, the president reviews and approves the provost's proposed increase for each dean. After being approved by the president, the provost writes a detailed letter to each dean explaining the basis for the percentage increase.

Faculty. Washington College of Law Professors Peter Jaszi, Andrew Popper, and Robert Vaughn have been among the top five highest paid University employees over the last three years.

The three law professors listed above are long-term employees of the University. Each of their compensation was originally set at a level consistent with law professors of comparable experience. All three professors have increased their compensation by remaining at the University for an extended period of time, excelling in their fields, and earning merit increases on an annual basis.

Like the deans and other employees at the University, all faculty members are eligible for merit increases on an annual basis. The pool for the faculty merit increases is established by the Board of Trustees and fixed in the University's budget. As with the deans' salaries, the faculty does not receive any adjustment to salary for increased cost of living.

The merit increase pool for faculty members is allocated using the following process. Each faculty member is required to submit an annual report that details his or her achievements during the calendar year, including activities such as scholarly, creative and professional accomplishments, teaching effectiveness and external professional recognitions. The template for the faculty annual reports is enclosed as AUSF 009672-009673. Throughout the University, a detailed, multi-tiered process is followed in setting faculty determining merit increases. First, the dean of each school, with input from the faculty and final approval from the provost, determines merit increases for each faculty member in that particular school. The dean then makes a final recommendation to the Dean of Academic Affairs for the University. The Dean of Academic Affairs reviews the recommendations and makes a final determination regarding the allocation of the merit increase pool among the faculty. Finally, the merit increase for each faculty member is approved by the provost. Each school and college follows a different process in soliciting input from other faculty members. In the College of Arts and Sciences, each department establishes a committee to evaluate each faculty member and make a recommendation to the College's dean. Each department chair makes an independent recommendation to the dean for the faculty in the chair's department. In the School of Communication, a school-wide merit pay committee recommends merit increases to the dean; whereas, in the School of Public Affairs, the school's rank and tenure committee makes the recommendation. In the School of International Service, the Kogod School of Business, and the Washington College of Law, the senior faculty administrators form an advisory committee to the dean.

Chancellor of the American University of Sharjah ("AUS"). The chancellor has been among the top five highest paid University employees during the last three years.

AUS was founded in 1997 by Bin Mohammed Al Qassimi, Member of the Supreme

Council of the United Arab Emerites and Ruler of Sharjah, one of the United Arab Emirates. AUS is an independent, non-profit coeducational institution, based on American institutions of higher education.

AUS and the University have signed an affiliation agreement. Under this comprehensive agreement, the University provides the senior management personnel for AUS. The contract also calls for the University to certify the equivalency of AUS courses with those same courses as they are offered at the University. This ensures the transferability of AUS credits to American universities. The agreement also provides for exchanges of University and AUS students and faculty both in summer sessions and during the regular academic year.

The AUS chancellor is, in effect, the president of AUS. The chancellor's salary was originally set using the following process. The chancellor was hired after a search conducted with the help of a search firm. The search firm also collected comparability compensation data, which the University used to set the initial salary at a market rate. Salary increases thereafter are based on a review done by the AUS board (which includes members of the University's Board) and the president of the University. Salary increases are recommended and approved by the University president and AUS board. The chancellor has received a 4-5% salary increase each year. This is a cost-recovery item for the University because the Ruler of Sharjah reimburses the University for the salary of the chancellor. This salary fits within the University's overall salary structure, which is reviewed by Mercer and has been deemed to be consistent with the market.

Basketball Coach. The University's men's basketball coach, Jeffrey Jones, has been among the top five highest paid University employees over the last five years.

The basketball coach has an employment agreement with the University, which governs his compensation (AUSF 009699-009702). When the agreement was negotiated in 2002, the University set the coach's base salary by relying on comparable salaries for basketball coaches in the Patriot League, the athletic league in which the University's basketball team competes. The basketball coach is in the mid-range of coaches in the Patriot League – the third highest paid coach among the League's eight teams. In addition, the coach's employment agreement contains certain incentive payments, which are standard in the coaching industry, if the basketball team achieves certain goals. For example, there is an incentive payment in the employment agreement that is awarded if the basketball team wins the Patriot League championship. For a complete list of all possible incentive payments, a copy of the employment agreement is enclosed as AUSF 009699-009702. Other than the base salary and the industry-standard incentive payments, the basketball coach is eligible for merit increases on an annual basis. The pool for the annual merit increase is the same as the pool for other employees, which is established by the Board of Trustees and fixed in the University's budget. Like the deans and the faculty, the basketball coach does not receive any adjustment to salary for increased cost of living.

The method for allocating the merit increase pool, with respect to the basketball coach, is as follows. The Athletic Director, who is the head of the Athletic Department, makes recommendations to the Vice President for University Relations as to how the merit increase pool should be allocated among all athletic department employees, including the basketball coach. The Vice President of University Relations then reviews the recommendations and makes a final determination regarding the allocation of the merit increase pool.

b. Describe the nature of the components for each amount reported under compensation; contributions to employee benefit plans & deferred compensation; and, expense account and other allowances.

Officers, Directors, Trustees and Key Employees. The Trustees of the University are not compensated for their service.

At the time of his removal as president, the former president's compensation consisted of base salary of $500,000, annual incentive compensation up to 13% of base policy to be awarded by the Board based on its performance evaluation of the president, deferred compensation of $125,000 and a $103,000 contribution to a split-dollar life insurance policy. The president also received University-provided housing and residential staff, as well as health and welfare benefits, and qualified section 403(b) retirement benefits consistent with those provided to all University employees.

Similarly, each vice president's compensation includes base salary, an incentive bonus and deferred compensation. The vice presidents also participate in a qualified section 403(b) retirement plan and receive health and welfare benefits consistent with those provided to all University employees.

The former president, provost and the vice presidents also are eligible to participate in voluntary and supplemental deferred compensation programs, as set forth in AUSF 009263-6.

Deans, Faculty and Chancellor of AUS. The components of the compensation of the deans, faculty and AUS chancellor include base salary, contributions to a section 403(b) retirement plan, as well as health and welfare benefits consistent with those provided to all University employees.

Basketball Coach. The components of the coach's compensation includes base salary, any incentive bonuses awarded in a given year, contributions to a 403(b) retirement plan, as well as health and welfare benefits consistent with those provided to all University employees.

c. Describe the duties and responsibilities that each individual performed for you.

Officers, Directors, Trustees and Key Employees. Please see the enclosed job descriptions (AUSF 010439-010447) for a review of the duties and responsibilities of the president and vice presidents.

Deans. Please see the enclosed biographies (AUSF 010448-010450) for a description of the duties and responsibilities of the Dean of the Washington College of Law and the Dean of the Kogod School of Business.

Faculty. Please see the job descriptions attached (AUSF 010453-010458) for a review of the duties and responsibilities of Professors Jaszi, Popper, and Vaughn.

Chancellor of AUS. Please see the job description attached (AUSF 010451-010452) for a review of the duties and responsibilities of the chancellor of AUS.

Basketball Coach. Please see the job description attached (AUSF 010459-010461) for a review of the duties and responsibilities of the basketball coach.

d. Do the amounts reported represent the total economic benefits each individual received from you for the year? If no, please explain what other benefits were received, including the fair market value of those benefits.

Officers, Directors, Trustees and Key Employees. The Trustees of the University are not compensated for their service.

The University recently completed a thorough investigation of the former president's expenses over the last three years. During the course of the investigation, the University discovered that certain economic benefits that should have been reported on the former president's Forms W-2, as well as the University's Forms 990, had not been correctly reported. The University immediately corrected the error by submitting amended Forms W-2 and 990, reporting the correct amount of compensation. The University took these corrective actions on its own initiative, before any audit by the IRS. The amounts reported on the corrected forms represent the total economic benefits the former president received from the University for each of the three years in question.

For all other employees, the amounts reported on Forms W-2 and 990 represent the total economic benefits each individual received from the University for each year.

e. Did you establish the rebuttable presumption under section 53.4958.6 of the Foundation and Similar Excise Taxes Treasury Regulations as to the compensation and benefits reported for any of the individuals? If yes, please provide copies of all supporting documentation.

Prior to 2005, the University did not establish the rebuttable presumption under Treasury Regulations section 53.4958-6 as to the compensation and benefits reported for the officers or key employees. As part of governance reforms instituted in 2004, the Board relied on the rebuttable presumption in setting the president's compensation in April, 2005 and the vice presidents' compensation in November, 2005. The Board intends to continue to satisfy the requirements of Treasury Regulations Section 53.4958-6 for the president and vice presidents, and ensure that the compensation of other employees are within the University's overall compensation structure established and monitored by the Board.

f. If the answer is no to "e" for my of the individuals, do you have documentation supporting the reasonableness of the compensation and benefits reported? If yes, please provide a copy of this documentation.

Documentation supporting the reasonableness of the compensation and benefits reported for the former president, the vice presidents and other employees is enclosed. (See AUSF 000083, 000085-000170, 009674-009683, 009689-009698, 010414-010447).

g. Did the AU board approve the mount of compensation and benefits reported? If yes, please provide a copy of the approval for each individual.

Except for the personal expense items uncovered in the recent investigation conducted by the University's Audit Committee, the Board of Trustees approved the compensation and benefits reported for the former president in past years. The investigation conducted by the University of the former president's expenses revealed some gaps in the Board's approval process relating to personal expenditures by the former president. As a result of these findings, the Board severed ties with the former president and instituted an extensive program to reform the Board's corporate governance structures to ensure that any future employment agreements with a president, and compensation paid in benefits provided to a president, will be formally approved and closely monitored by the Board.

Until this year, the Board of Trustees did not approve the salaries of the vice presidents. The Board approves the annual University budget, which includes each salary. In addition, the Board's Compensation Committee reviewed and approved the vice presidents' salaries on an annual basis. Documentation of the approval of the annual budget for the last three years is enclosed as AUSF 010586-010606. Beginning in 2004, the Board put in place a process by which the full Board, rather than just the Compensation Committee, will review and approve compensation for the vice presidents. Based on data analyzed by

Mercer, the Board approved compensation for the vice presidents on November 11, 2005.

The Board of Trustees does not directly approve the salaries of the deans, faculty members, AUS Chancellor or other University employees. The Board approves the annual University budget, which includes each salary as well as the merit increase pool percentage. Documentation of the approval of the annual budget and merit increases for the last three years is enclosed as AUSF 010586-010606.

h. Did you have an employment contract or any other compensatory agreement with any of the individuals? If yes, please provide a copy of the contract or agreement.

The independent Trustees of the University are not compensated for their service, and the University does not have employment or other compensatory agreements with the independent Trustees.

The former president and the University entered into an employment agreement when the former president was hired in 1994. That original agreement lapsed after three years. A subsequent agreement was drawn up in 1997, but was never ratified by the Board of Trustees. The 1994 and 1997 agreements are attached as AUSF 000060-000072 to this letter.

The vice presidents, deans, faculty members and AUS Chancellor do not have employment agreements with the University.

The men's basketball coach has an employment agreement with the University. The agreement is enclosed as AUSF 009699-009702.

i. Does the amount of compensation and benefits reported agree with the amount reported on each individual's Form W-2 or Form 1099? If no, please explain the difference.

As explained in response to question 1(d), the University has submitted amended Forms W-2 and 990 for the last three years that correctly reflect the amount of the former president's compensation.

For all other officers and key employees, the amount of compensation and benefits reported on the University's original and amended Forms 990 correspond to the amount reported on each individual's Form W-2.

j. Did any of these individuals use any property that you owned or leased (such as an automobile, aircraft, real estate, credit card, etc..) for any purpose other than to further the organization's exempt purposes? If yes, did you include the value of this usage in the amount of compensation and benefits reported? Was the value included on the individual's Form W-2 or Form 1099? If your answer to either of these questions is "No" please explain.

The independent Trustees of the University did not use any property owned or leased by the University for non-exempt purposes.

During the course of the University's audit of the former president's expenses, the University discovered that the former president made personal use of certain University property and personnel. The University included on amended Forms W-2 issued to the former president the value of all personnel, use of University property and personnel that was authorized by the Board, even though the extent of such personal use was not known to the Board until the Audit Committee conducted its investigation. Before the University severed ties with the former president, the University required him to reimburse it for the value of all unauthorized use of University property, plus interest, identified in the Audit Committee's investigation. Because the value of such personal use was reimbursed by the former

president to the University, with interest, such amounts were not reported on the former president's amended Forms W-2.

To the best of the University's knowledge, no other employees have used any property that the University owned or leased (such as an automobile, real estate, credit card, etc.) for any purpose other than to further the University's exempt purposes.

Thank you for your time and assistance. Please provide the answers to these questions by . December 1, 2005. If you have any questions, please contact Mr. Dean Zerbe of my staff at (202) 224-4515.

Cordially yours,

Chuck Grassley

Charles E. Grassley Challis n

cc. Senator Baucus