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October 24, 2013

Tito Guerrero, III  
Vice President  
Middle States Commission on Higher Education  
3624 Market Street  
Philadelphia, PA 19104-2680

Dear Dr. Guerrero:

The attached Monitoring Report is in response to Dr. Barbara Gitenstein's Middle States Commission on Higher Education letter, dated November 15, 2012. The Report focuses on the impact on the University's budget and identification of sources of funding to cover the requirements of the U.S. Department of Education report, the Freeh Report recommendations and NCAA Consent Decree; the developments associated with the revision of the Bylaws of the Board of Trustees and the dual report accountability of key positions to both the Board of Trustees and President. The report has already been uploaded as per Erin Mattson's directions.

Thank you for the opportunity to prepare this report. Please contact me if you have any questions.

Sincerely,

A handwritten signature in blue ink that reads 'Blannie' in a cursive, slightly stylized font.

Blannie E. Bowen

Enclosures

cc: Rodney A. Erickson  
Nicholas P. Jones

Monitoring Report to the  
Middle States Commission on Higher Education

From

**THE PENNSYLVANIA STATE UNIVERSITY**  
University Park, PA 16802

Rodney A. Erickson, President of the University

Nicholas P. Jones, Executive Vice President and Provost

Blannie E. Bowen, Vice Provost for Academic Affairs  
Accreditation Liaison Officer

October 24, 2013

Monitoring Report in  
Response to the Commission's Letter  
Dated November 15, 2012

“To request a monitoring report, due November 1, 2013, documenting (1) the impact on the University budget and the identification of sources of funding to cover the requirements of (a) the report of the U.S. Department of Education regarding the University's compliance with the Clery Act and associated penalties; (b) updated estimates of the projected costs and liabilities associated with related litigation and the implementation of the Freeh Report recommendations and the NCAA Consent Decree requirements; and (c) the recommendations that are articulated in the report of the external monitor called for by Recommendation 8.3 of the Freeh Report (Standard 3); and (2) developments associated with the revision of the Bylaws of the Board of Trustees to accommodate (a) the expanded involvement of faculty, staff, and students on Board committees and (b) the dual-reporting accountability to both the Board and the President of key positions, including that of the General Counsel and the Directors of Internal Audit and Compliance (Standard 4).”

## Table of Contents

EXECUTIVE SUMMARY .....	1
IMPACT ON THE UNIVERSITY BUDGET AND IDENTIFICATION OF SOURCES OF FUNDING TO COVER THE REQUIREMENTS .....	2
U.S. Department of Education Report Regarding the University’s Compliance with the Clery Act and Associated Penalties .....	2
Updated estimates of the project costs and liabilities associated with related litigation and the implementation of the Freeh Report recommendations and the NCAA Consent Decree requirements .....	2
Resources Identified to Cover Known and Anticipated Costs.....	3
Recommendations articulated in the report of the external monitor called for by Recommendation 8.3 of the Freeh Report (Standard 3) .....	4
DEVELOPMENTS ASSOCIATED WITH THE REVISION OF THE BYLAWS OF THE BOARD OF TRUSTEES.....	7
Expanded Involvement of Faculty, Staff, and Students on Board Committees.....	7
Dual-Reporting Accountability to Both the Board and the President of Key Positions Including that of the General Counsel and the Directors of Internal Audit and Compliance (Standard 4).....	8
CONCLUSION.....	10

## EXECUTIVE SUMMARY

Penn State appreciates the Middle States Commission on Higher Education's acceptance of the September 27, 2012, Monitoring Report, the removal of the warning, and the reaffirmation of the University's accreditation.

As requested in the November 15, 2012, reaffirmation of accreditation letter, this Monitoring Report is presented to ensure confidence that the University continues to be in compliance and to update the Commission on the impact on the University's budget and the identification of sources of funding to cover the requirements of the U.S. Department of Education's report on compliance with the Clery Act and associated penalties; give updated estimates of the projected costs and liabilities associated with related litigation and implementation of the Freeh Report recommendations and NCAA Consent Decree requirements; the recommendations articulated in the report of the external monitor [Recommendation 8.3 of the Freeh Report (Standard 3)]; and the developments associated with the revision of the Bylaws of the Board of Trustees.

Following this Executive Summary, the report will be divided into three sections. The first section, impact on the University budget and identification of sources of funding to cover the requirements, will cover the U.S. Department of Education's report regarding the University compliance with the Clery Act and associated penalties. We will also include the updated estimates of the project costs and liabilities associated with the related litigation and implementation of the Freeh Report recommendations and the NCAA Consent Decree requirements, and the resources identified to cover known and anticipated costs as well as the recommendations in the external monitor's report called for by Recommendation 8.3 of the Freeh Report.

The next section will review the developments associated with the revision of the Bylaws of the Board of Trustees, the expanded involvement of faculty, staff, and students on Board committees, and the dual-reporting accountability to both the Board and the President of key positions which includes the vice president for general counsel and the directors of internal audit and University ethics and compliance (Standard 4).

The final section will be concluding thoughts on the University's progress and continuing efforts to create a more transparent, accountable, and effective approach to governance, and safety and compliance; thus moving forward to make Penn State stronger and more accountable.

## **IMPACT ON THE UNIVERSITY BUDGET AND IDENTIFICATION OF SOURCES OF FUNDING TO COVER THE REQUIREMENTS**

### **U.S. Department of Education Report Regarding the University's Compliance with the Clery Act and Associated Penalties**

As of the September 2012 Monitoring Report

(<http://www.psu.edu/vpaa/pdfs/middle%20states/Monitoring%20Report%20September%2027%202012.pdf>), a program review of the University's compliance with the Clery Act and Drug-Free Schools and Community Act (DFSCA) was being conducted by the U.S. Department of Education. At that time the investigation was ongoing with the outcome uncertain.

On July 12, 2013, a preliminary report was received from the U.S. Department of Education. This preliminary report is part of the ongoing program review and the outcome continues to be uncertain. The Department of Education has also indicated that it will be issuing one or two supplemental, preliminary reports. With regard to these preliminary reports, and as required by statute, the Department of Education is maintaining the confidentiality of the preliminary reports in order to facilitate the ongoing program review. The University is fully engaged in the process and will also maintain the confidentiality of the preliminary reports. Once this process is complete, a final determination will be made at which time information about the Department of Education's program review will be made public.

The Department of Education's review team has been provided access to all requested records and information sources and has been working with the University's Clery Compliance Manager, Gabriel Gates. In addition to the unfettered access, Mr. Gates is working with leading national Clery Act organizations to standardize procedures, protocols, and guidelines for Campus Security Authorities and other individuals to follow, as well as instituting a mandatory Clery Act training program for Campus Security Authorities.

With regard to future costs associated with the U.S. Department of Education review, these are too uncertain to estimate but may include legal expenses and possible fines. Thus the "Resources Identified to Cover Known and Anticipated Costs" included later in this report does not include a line item for these costs.

### **Updated Estimates of the Project Costs and Liabilities Associated with Related Litigation and the Implementation of the Freeh Report Recommendations and the NCAA Consent Decree Requirements**

In the 2012 Monitoring Report, information was provided on incremental costs incurred by the University for legal defense and public relations efforts through June 30, 2012, as a result of the Sandusky matter. The data below provides an update of that information, with some of the fees and costs set forth below expected to be reimbursed under the University's insurance policies.

▪ NCAA Fine:	\$ 12,000,000
▪ Freeh Sporkin & Sullivan/Pepper Hamilton LLP:	\$ 8,171,177
▪ Independent Monitor:	\$ 1,944,968
▪ Board of Trustees - Legal Services, Consulting Services and Communications:	\$ 7,127,085
▪ University Legal Services/Defense:	\$ 11,474,838
▪ Externally Initiated Investigations:	\$ 842,042
▪ Indemnified Persons' Legal Defense:	\$ 6,780,790
▪ Other Institutional Expenses:	<u>\$ 2,118,928</u>
▪ Total as of July 31, 2013:	\$ 50,459,828

The above information is routinely updated and may be found at <http://progress.psu.edu/faqs> by referencing the FAQ: “*How much money is the University paying for legal fees, consultants and PR firms associated with the Sandusky matter?*”

Including the \$50.5 million referenced above, the University is currently estimating a total of \$172.0 million of anticipated one-time costs to manage the Sandusky matter, including costs of implementing recommendations of the Freeh Group report and the NCAA Consent Decree. The largest distinct amounts include \$60 million for the NCAA fine; approximately \$60 million for settlement of victim claims to date; \$40 million of legal and other expenses; and \$12 million of capital improvements to facilities to enhance security. In addition, the University is estimating on-going annual implementation costs of approximately \$1.3 million which will be incorporated into operating budgets as appropriate. This \$1.3 million includes costs such as salaries for compliance staff and training costs. There remain a few claims by individuals alleging to have been victims of abuse by Mr. Sandusky which are either not yet settled or are in litigation, and there may be others who have not yet come forward. The University is unable at this time to estimate the future cost of legal expenses, plus settlements or verdicts of those cases which are not currently resolved.

### **Resources Identified to Cover Known and Anticipated Costs**

The incremental costs surrounding legal defense and public relations efforts for the University associated with the Sandusky matter are not funded by student tuition, taxpayer funds, or donations. The University is currently reviewing these costs for insurance coverage and, in addition, has already identified an initial pool of approximately \$159 million to pay for any unrecovered costs including future legal costs and settlements.

This \$159 million pool of funds available represents interest proceeds repaid and anticipated from past internal loans to self-supporting units of the University, such as the Penn State Milton S. Hershey Medical Center and the Athletic Department. Approximately \$95 million of this pool has already been committed from existing funds while the remaining nearly \$64 million is to be accumulated over the coming years. The \$95 million already earmarked for this purpose represents approximately 3.4% of the University’s \$2.8 billion of unrestricted net assets in

excess of plant funds as of June 30, 2013. \$159 million would represent about 5.8% of those net assets. Alternatively, as a percentage of non-endowed cash and investments totaling \$2.5 billion, the \$159 million is relatively minor at 6.4%.

The University expects that insurance coverage and the existing pool of available funds will cover the large majority of the total incremental expenditures and settlements related to facts known as of this time. Further, similar sources of unrestricted funds have already been identified and, as appropriate, additional sources will continue to become available as the University's self-supporting units continue to repay internal capital loans and commitments over time. All of these repayments will be continuously evaluated in the future as facts and circumstances emerge with respect to litigation and settlement issues that may suggest further need.

The University has purchased Directors and Officers insurance coverage as well as comprehensive and commercial liability insurance throughout its history. This includes significant increases in general liability coverage limits beginning in policy years 1993 and 1996. The University annually benchmarks its insurance policies and limits against its peer institutions in the Big Ten and against other large higher education institutions. Consistent with its heritage of conservative financial management, the University has routinely noted that it carries among the broadest coverage of its peer group. While confidentiality precludes full disclosure of the coverage limits within the context of this written response, additional details were provided during the October 2012 visit of the Commission's assigned evaluators. The information regarding insurance coverage provided in the September 2012 Monitoring Report is largely unchanged. Information regarding insurance in the 2012 report may be found at <http://www.psu.edu/vpaa/pdfs/middle%20states/Monitoring%20Report%20September%202012.pdf>.

The best available evidence suggests that the resources discussed above will enable the University to cover the relevant costs. However, if necessary, the University is prepared to make additional modifications in its overall financial plans going forward. Specifically, as University management developed the five-year capital plan (2014-2018) with the Board of Trustees, much flexibility was programmed into the plan. For example, in acknowledgement of the need to provide up to \$60 million of bridge funding for payment of the NCAA fine, the new capital plan was reduced in scope by \$60 million. This can and will result in some reductions in deferred maintenance and other projects being requested by the self-supporting units of the University. The potential for additional accommodations has been built into the plan, allowing the University to deal with other unforeseen circumstances.

### **Recommendations Articulated in the Report of the External Monitor Called for by Recommendation 8.3 of the Freeh Report (Standard 3)**

Item 8.3 of the Freeh Report recommended that the University conduct a progress review 12 months from the acceptance of the report using internal and external examiners, and provide the findings to University administrators, the Board and the public.

Shortly after the issuance of the Freeh Report in July 2012, President Erickson appointed an “administration response team” composed of Thomas Poole, Vice President for Administration; Stephen Dunham, Vice President and General Counsel; and David Gray, Senior Vice President for Finance and Business/Treasurer; and charged that team with responsibility for developing the University’s responses and implementation plans for the Recommendations. The administration response team, with support from Paula Ammerman, then Director of the Office of the Board of Trustees, and Frank Guadagnino, outside counsel, met weekly starting in August 2012. Mr. Guadagnino served as the “project manager” for the overall implementation effort. Representatives of Senator George Mitchell, the independent monitor selected to oversee the University’s compliance with the NCAA Consent Decree and Athletics Integrity Agreement (AIA), were invited to, and regularly attended, the weekly meetings of the administration response team.

As its first step, the administration response team prepared a matrix which, for each Recommendation, had a column for a working title, the functional office or offices with responsibilities for the functional area, the executive or trustee leader proposed to be responsible for developing an action plan, the Board of Trustees committee with appropriate oversight for the subject area, the status of progress in implementing the recommendation, a color indicator reflecting the level of completion of the work and the date of completion. The matrix was then circulated to various administrators, deans and trustees to whom responsibilities had been assigned (“responsible persons”), with a request for a description of the current status of the topic addressed by each Recommendation assigned, a preliminary work plan, and an estimated completion date.

The administration response team began receiving input from responsible persons in September 2012. The information received was included in a revised draft of the matrix, which served as a “living document” and was continually updated by the project manager to reflect changes in the status of the implementation effort. The next step was to schedule meetings with each responsible person to review, in detail, the status, work plan, and estimated completion date of the implementation of the Recommendations for which each had been assigned. These meetings, which were attended by Senator Mitchell’s team, were used to discuss issues, review, and, in many cases, refine the implementation effort – and to ensure that the University’s efforts were on track. These meetings occurred weekly starting in August 2012 and continue to be held.

Separately, the University created an “advisory council” composed of the administration response team and representatives of a wide variety of University constituencies (students, faculty, administration, staff and trustees). This advisory council, chaired by Keith Masser, Chair of the Board of Trustees, met approximately every two weeks between September 2012 and June 2013 to review the progress being made by the administration response team and the responsible persons toward implementation of the Recommendations. Over the course of the last year, responsible persons were invited to attend the advisory council meetings to present the status of their implementation efforts, discuss issues and receive input from the council. Members of Senator Mitchell’s team were invited to, and were regular attendees of, these meetings.

Finally, the Board of Trustees formed an *ad hoc* group to oversee the administration's implementation efforts. This group, also chaired by Keith Masser, met with the administration response team and the advisory council on four occasions to hear reports on the status of the University's implementation efforts, to discuss issues, and to provide advice and guidance.

The status of the University's implementation efforts with respect to the recommendations was made public on a regular basis through a posting on the University's "Progress" website. An initial status report was issued in October 2012 with updated status reports being posted in November 2012, January 2013, March 2013, May 2013 and July 2013. The July 2013 report is available for review at <http://progress.psu.edu/resource-library/story/july-report-on-freeh-recommendations-shows-quick-action-by-penn-state>.

With the consent of the NCAA and the Big Ten Conference, the University engaged Senator Mitchell's firm, DLA Piper, LLP, to provide the external review referred to in Freeh Recommendation 8.3 of the University's efforts to implement the recommendations. Senator Mitchell's interim quarterly reports to the NCAA and the Big Ten Conference, issued in November 2012, March 2013 and May 2013 pursuant to, and in accordance with, the Consent Decree and the AIA, reported on the University's progress toward implementation of the recommendations.

Senator Mitchell's fourth quarterly report, issued in September 2013, reported more fully on the University's efforts to implement these Recommendations and, with the consent of the NCAA and the Big Ten Conference, constituted the 12-month progress review required by this Recommendation. Senator Mitchell's report was issued publicly on September 6, 2013. See [http://www.dlapiper.com/mitchell-ncaa-psu-release\\_4/](http://www.dlapiper.com/mitchell-ncaa-psu-release_4/). In his report, Senator Mitchell concluded that "Penn State has substantially completed the initial implementation of all of the Freeh Report recommendations and of its annual obligations under the AIA."

Senator Mitchell also observed that "[W]hile much has been accomplished, important work remains to be done. Penn State must maintain its focus on these ongoing initiatives while also fostering an environment in which its many undertakings will take root and thrive. By all indications thus far, the University has positioned itself well to meet this challenge."

Finally, Senator Mitchell noted that:

"While parties may continue to argue about the history that led to the Freeh Report and the AIA, a consensus has developed that the principles at the heart of these reforms are best practices for the governance of any large university. Penn State's Phase II plan of action assures the Monitor that the University has embraced the Freeh Report's recommendations as a roadmap supporting long-term enhancement. It demonstrates that, even after the December 31, 2013 deadline for completion has long since passed, Penn State plans to continue to be guided by the recommendations in its mission to establish effective ethics, compliance and governance programs, support the physical safety of all individuals on its campuses, and promote athletics integrity."

**DEVELOPMENTS ASSOCIATED WITH THE REVISION OF THE BYLAWS OF THE BOARD OF TRUSTEES**

**Expanded Involvement of Faculty, Staff, and Students on Board Committees**

As noted in the September 27, 2012, Monitoring Report, the Board of Trustees is the corporate body established, by charter, with complete responsibility for the welfare of the University, and all interests specific to students, faculty, staff, and alumni. In fulfilling that responsibility, the expanded involvement of these stakeholder representatives has been evident and assistive as the Board strives for continued communication and engagement with all aspects of the University community.

Standing Order IV(9)(a), effective May 3, 2013, provides that the Chair of the Trustees or President of the University is authorized to invite non-voting faculty representatives, non-voting student representatives or other stakeholder representatives to attend and participate in meetings of standing committees, subcommittees, and special committees. While the number of such representatives has evolved over time, as noted in the 2012 Monitoring Report, this current language eliminates numerical limitations on such invitations.

The current representatives, with corresponding committee assignments, are:

<b>Representing</b>	<b>Committee Assignment</b>
President, University Park Undergraduate Association	Academic Affairs and Student Life
Chair-Elect, University Faculty Senate	Academic Affairs and Student Life
Immediate Past Chair, University Staff Advisory Council	Academic Affairs and Student Life
Chair, University Faculty Senate	Finance, Business and Capital Planning
President, Graduate Student Association	Finance, Business and Capital Planning
Vice President, Council of Commonwealth Student Governments or University Park Undergraduate Association (alternate years by organization)	Governance and Long-Range Planning
Chair, University Planning Committee, University Faculty Senate	Governance and Long-Range Planning
President, Council of Commonwealth Student Governments	Outreach, Development and Community Relations
Secretary, University Faculty Senate	Outreach, Development and Community Relations
Chair, University Staff Advisory Council	Outreach, Development and Community Relations
President, Penn State Alumni Association	Outreach, Development and Community Relations

The Governor of the Commonwealth of Pennsylvania traditionally reserves one of six gubernatorial-appointed Board of Trustee voting positions for a student.

In May 2013, significant structural changes to the Board of Trustees and oversight procedures were approved by the Board of Trustees. A few of those reforms, particularly relevant to the request for this Monitoring Report, include:

- Both the governor of Pennsylvania and president of Penn State now serve as *ex officio*, non-voting members of the Board of Trustees. This change reduced the number of voting Trustees from 32 to 30.
- The president of Penn State no longer holds the position of secretary of the Board; rather, the secretary is now an elected position, currently held by the vice president for administration.
- The waiting period for former Penn State employees to serve as a member of the Board of Trustees was extended from three to five years.

An important example of Board engagement and involvement with various members of the University community is significantly evident in the composition of the University Presidential Search and Screen Committee. In January 2013, the Board named an 18-member committee to assist the Trustee Presidential Selection Council by screening, reviewing, and evaluating applications and nominations in order to develop and forward a short-list of names to the Trustee Presidential Selection Council for further consideration. The Committee membership includes nine faculty members, one staff member, two academic deans, one vice president, two undergraduate students and one graduate student, and one representative each from the Department of Intercollegiate Athletics and the Penn State Alumni Association.

#### **Dual-Reporting Accountability to Both the Board and the President of Key Positions Including that of the General Counsel and the Directors of Internal Audit and Compliance (Standard 4)**

Daniel Heist, the University's Director of Internal Audit, has a dual-reporting relationship to the Senior Vice President for Finance and Business/Treasurer and the Board of Trustees through the Board's Committee on Audit and Risk. That dual-reporting relationship provides for direct access to the Board of Trustees, typically through the Chair of the Committee on Audit and Risk. With Mr. Heist being responsible for conducting financial and information technology compliance and operational audits, as well as jointly overseeing (with the Director of University Ethics and Compliance, Regis Becker) the University's Ethics and Compliance hotline and conducting investigations into potential fraud and misuse of University assets, the dual-reporting relationship is critical to ensuring that Mr. Heist has unfettered access in order to address any issue regardless of the organizational level of such issue. Additionally, Mr. Heist serves as the administrative liaison to the Committee, thus ensuring that agendas include timely issues and topics critical for Board awareness.

As noted in the September 2012 Monitoring Report, Stephen Dunham joined the University on July 16, 2012, as Vice President and General Counsel. Mr. Dunham has a dual-reporting relationship to the Board of Trustees as well as the President. Since the date of the Commission's November 15, 2012, letter, the dual reporting relationship has been confirmed and institutionalized in the Charter and Guidelines of the Trustees' Committee on Legal and Compliance which was approved by the Trustee Committee. Given Mr. Dunham's role of providing advice to the Board and administration, as well as coordinating and monitoring legal actions and interpreting rules and guidelines affecting compliance with federal and state laws and regulations, a dual-reporting relationship provides that the position has immediate access to the Board as needed. This direct reporting to the Board of Trustees is effectuated both through reports to the full Board at every Board meeting and through regular reports to the Committee on Legal and Compliance. The Vice President and General Counsel serves as administrative liaison to the Committee. This provides another layer of communication and information exchange that is critical in forming the Committee's agenda and discussion topics. Finally, the Board has created a Legal Subcommittee which meets weekly with the General Counsel.

On April 1, 2013, Regis Becker was named as the University's first Director of University Ethics and Compliance. In his prior position, Mr. Becker was the Chief Compliance Officer at PPG Industries, a global Fortune 250 company. In his current role, Mr. Becker has a dual-reporting relationship to the Legal and Compliance Committee as well as to the Senior Vice President for Finance and Business/Treasurer. This dual reporting relationship is set forth in the Charter and Guidelines of the Committee on Legal and Compliance and approved by the Committee. Mr. Becker is responsible for overseeing all compliance issues and developing a comprehensive program of institutional ethics. Given the portfolio of Mr. Becker's responsibility, it is critical that the position has direct and immediate access to the Board, and this dual-reporting relationship to the Committee on Legal and Compliance ensures that unobstructed link as needed. Mr. Becker also meets on a regular basis with the President.

Also on April 1, 2013, Julie Del Giorno began her full-time employment with Penn State as the University's inaugural Athletics Integrity Officer. In her prior position, Ms. Del Giorno was the Chief of Staff at Moravian College and Moravian Theological Seminary. In her current role, she is responsible for development, implementation, and oversight of policies and practices within the University's Intercollegiate Athletics Department in accordance with the University's Athletics Integrity Agreement. Ms. Del Giorno reports to the director of University Ethics and Compliance, and has regular access to the President and Board of Trustees as well. Ms. Del Giorno provides regular updates to the Committee on Legal and Compliance of the Board of Trustees.

## CONCLUSION

As noted throughout this Monitoring Report, and in using the Freeh Report recommendations as a guide, Penn State continues to make significant progress in its efforts to embrace a more transparent, accountable, and effective approach to governance, and safety and compliance thus moving forward to make the University stronger and more accountable. The University is continuing to “foster an environment in which its many undertakings will take root and thrive” (Mitchell, DLA Piper News).

As a result of the progress that the University has made and continues to make, on September 24, 2013, the NCAA announced a gradual restoration of the football scholarships beginning next academic year (2014-15) and increasing until the full allocation is reached in 2015-16: “Due to Penn State University’s continued progress toward ensuring athletics integrity, the NCAA Executive Committee is gradually restoring football scholarships the university lost because of sanctions more than a year ago. These changes were endorsed by the Division I Board of Directors and based on the recommendation of George Mitchell, the independent Athletics Integrity Monitor for Penn State and former U.S. Senator.” Said President Rodney Erickson, “the action taken today by the NCAA, following its review of the positive report issued this month by Sen. George Mitchell, recognizes the significant efforts over the past year to make Penn State a safer, stronger institution. As we promised throughout this process, we are committed to continuing to improve all of our policies, procedures and actions.”

Continuing the positive momentum of the past 12 months, Penn State moves into Phase II of the implementation process to improve the governance, policies and procedures, and operations. The University remains committed to supporting the prevention and treatment of child abuse across the state and the nation, making continuous improvement, and taking advantage of synergies and lessons learned. The reforms that have been put in place make Penn State a safer institution, a national leader in terms of security, governance, human resources policies, and a benchmark for other universities.

As stated on the University’s Progress web site, “It is the actions of the many – not the few – that make up Penn State.” Education and research have been the foundation of Penn State for the past 158 years. It is with renewed focus we look ahead to educating our more than 98,000 students, continuing to lead the nation as a world-class academic and research institution, and to expanding our commitment to service.