COMMITTEE ON FACULTY WELFARE
Report on the University of California Retirement Program

To the Academic Senate, Santa Cruz Division:

Introduction

Recent losses in the UC Retirement Program (UCRP) have emerged as one of the Committee on Faculty Welfare's (CFW) most urgent concerns this year. Assets in the UCRP, like investment portfolios generally, have decreased significantly in response to the recent downturn in global and national markets. At the same time, the UCRP has also been affected because neither UC employees nor UC itself have contributed to UCRP since 1990.[1] In the meantime, liabilities have continued to increase. These three factors--losses due to market forces, suspension of member contributions to UCRP (scheduled to restart in early 2010), and increase in liabilities–have had a powerful effect: ***UCRP liabilities now well exceed assets.***

In the face of this news, two assumptions have been made by UC's Office of the President (UCOP) to project the future UCRP funding situation: first, investment returns on UCRP are projected at 3.75% from January 1, 2009, to June 30, 2009, and at 7.5% every year for the following four years; second, total scheduled employer-employee contributions to UCRP will rise gradually to 16% of covered payroll in the next 4 years.[2] Even using these promising assumptions, however, ***UCOP has projected that the UCRP funding ratio***—that is, the ratio of assets to liabilities—***will decline to 61%*** (from well above 100% through mid-2008) ***by 2013***—a remarkable drop in a program once so robust that it ceased requiring member contributions at all.[3]

Health benefits for retirees are handled separately from the UCRP and are another area of serious concern. ***The ratio of assets to liabilities for retiree health benefits is a meager 0.4%,*** with a current unfilled liability (liability minus assets) of $13.3 billion that is projected to grow to $18 billion by 2013 (see the section on "restructuring retirement health benefits" later in this document). Thus two cornerstones of post-retirement benefits–the UC Retirement Program and retiree health benefits–are both in serious financial jeopardy.

This document has several interlocking purposes, all of them intended to enable UCSC Senate members to understand and participate meaningfully in major decisions about the UCRP and UC itself, currently being considered systemwide. CFW aims:

1. To inform our UCSC colleagues about the status of UCRP by highlighting key questions that UCRP's current and projected funding ratio and investment returns raise, and presenting and explaining the publicly available but difficult-to-

[1] Cessation of contributions began as a result of the excellent health of the UCRP.

[2] Proposal to Reinstate Contributions to UCRP presented to the UC Regents, February 2009. http://www.universityofcalifornia.edu/regents/regmeet/feb09/j3pp.pdf

[3] This 61% estimate is an estimate of the projected "ARatio," or Actuarial Value Funding Ratio, which smoothes out market fluctuations over the previous five-year period. See "Current Status of UC Retirement System," later in this document, for an explanation.

decipher information that gave rise to these questions. The bulk of the report focuses on these facts;

2. To provide information as context for a set of Resolutions that will be introduced at the May 20 Academic Senate meeting. These Resolutions, if endorsed, should enable UC employees to make informed decisions about their retirement futures and we hope to participate in the direction UC itself will take in the coming years;

3. To raise the important question of whether the state and the Regents recognize the UCRP as an obligation that must be honored in its current form;

4. To bring to Senate attention the larger context in which the strategy for restructuring post-retirement benefits is being formulated: because of the major, permanent budget reductions UC is undergoing, this larger context is nothing less than the shape of the UC system itself. In particular, CFW wishes to flag two important questions: (a) UC is launching several new initiatives even as some programs are being eliminated or merged with others. In this context, we ask whether UC has the capacity to meet existing obligations towards its personnel; (b) UC is already engaged in developing decentralization strategies. We ask whether UC has sufficiently employed its existing process for consulting on these issues with the Academic Senate, both at the systemwide and the individual campus levels, and whether it has communicated these processes effectively to its constituents.

CFW hopes that in providing information about UCRP and retiree health benefits to the Senate, faculty members will be sufficiently informed both to make individual retirement decisions and participate effectively in decisions about such potential changes.

Definitions

Defined Benefit vs. Defined Contribution
UCRP is a defined benefit pension plan, where benefits are determined not by contributions to the plan but by defined formulas that vary according to the types of benefits payable (for example, retirement or survivor benefits). The formulas are based on such factors as a member's age, years of service credit, and salary. UC's defined benefit plan has historically been its finest employee benefit.

In contrast, 403(b) plans, 457(b) deferred compensation plans, and DC plans are defined contribution plans, where the employee and/or employer contribute to the plan following the appropriate Internal Revenue Code guidelines. *This document is about UCRP defined benefit plan* and not about any of the defined contribution plans mentioned above.

Vesting
Vesting refers to a member's non-forfeitable right to receive UCRP retirement benefits upon leaving the University and reaching retirement age. A vested member is one who has earned five or more years of service credit (employees who became UCRP members on or before July 1, 1989, are vested regardless of service credit if they leave University employment after reaching age 62). Existing vestment refers to the benefits that a

member is already eligible for under the UCRP defined benefit plan, based on current formulas that take into account a member's age, years of service credit, and salary. For example, a 60-year-old member (with Social Security) and 20 years of service credit is eligible for a monthly retirement income of 50% of the highest average plan compensation (HAPC) less $133. For details, please refer to the UCOP benefits website.

Future vestment can be changed by changing the current formulas.

Cost Of Living Adjustment (COLA)
After receiving UCRP benefits for one year, UCRP members are eligible to receive an annual cost-of-living adjustment paid each July 1. COLA is based on the Consumer Price Index (CPI) and is designed to increase the benefit payments with increase in CPI. Please refer to the UCOP benefits website for further details and the formula used to determine the amount of COLA to be paid.[4]

California Public Employees Retirement System (CalPERS)
CalPERS is analogous to but separate from UCRP. CalPERS provides retirement benefits to California state and school employees, and to employees of contracting local public agencies. UCRP provides retirement benefits to retirees of the UC system only.

Presidential Steering Committee
The Presidential Steering Committee was appointed by UC President Mark Yudof to make recommendations on restructuring post-retirement benefits-most notably to UCRP and retiree health benefits.

Presidential Task Force on Post-Retirement Benefits
The Presidential Task Force on Post-Retirement Benefits was appointed by UC President Yudof to evaluate alternative options for restructuring post-retirement benefits and present the findings to the Presidential Steering Committee.

Current Issues for Individual Employees

The most pressing question for individual UC employees has to do with the reliability of their expectations about their UC retirement benefits. Bluntly: ***Will UC employees receive the benefits they expect when they retire?*** This breaks down into three more nuanced sub-questions related to: (a) the status of individual employees' already vested monies—for example, an individual's already vested 12 years of service credit; (b) the status of their future anticipated monies—for example, an additional 10 years of anticipated service prior to retirement; and (c) the status of vestment options for future employees—for example, possibly a new set of rules for future employees. UC President Yudof has publicly indicated that some restructuring of expected benefits must take place.[5]

In order to address the post-retirement benefits (UCRP and health), UC President Yudof has set up a Presidential Steering Committee charged with recommending a strategy

[4] http://atyourservice.ucop.edu/retirees/retirement_savings/ucrp.html
[5] James P. Sweeney, UC Pension System Faces Economic Reality, San Diego Union-Tribune. February 6, 2009. http://www3.signonsandiego.com/stories/2009/feb/06/1n6pension235823-uc-pension-system-faces-economic-/?uniontrib

based on the analysis and evaluation of various options developed by the Presidential Task Force on Post-Retirement Benefits. These committees are likely to address at least the two key issues noted below, about which CFW poses the following questions:

A. Restructuring Retirement Financial Benefits

1. Will the existing vestment of current and retired employees be honored?

2. Will future vestment of current employees be changed or redefined?

3. Will future UC employees receive the same benefit guarantees as current employees? What are the implications for hiring and retention, especially given UC salaries and California's cost of living?

4. How much will UC employees be asked to contribute to the UCRP, starting when? What sum will UC match? What sum will the state of California match? What expectations should we have for future contributions by UC? By California?

5. How effective will the projected contributions (by employees, by UC, by state) be in bringing the UCRP to healthy levels (defined as a funding ratio of 95-110%)? If the funding ratio remains low, how will the gap be covered? What percentage of covered payroll will be needed to return UCRP to a healthy funding ratio? Is this likely to be substantially more than 20% of covered payroll over an extended period of time? (On this point, the most worrisome scenario is one in which members start contributions but are denied the anticipated benefits or awarded reduced benefits at the time of their retirement.)

6. Will COLAs continue to be paid to retirees in the future? Are COLAs a contractual obligation of the UC Regents? Are they protected by law?

B. Restructuring Retirement Health Benefits

UC has taken a different approach to retiree health benefits than it has to retirement benefits generally. Instead of aiming for a robust funding ratio such as that previously enjoyed by UCRP, the plan for retiree health benefits has all along hinged on a "pay-as-we-go" approach. The viability of this approach is being called into question for the first time in view of rapidly rising retiree health costs. The current funding ratio for health benefits is 0.4%, with a current unfilled liability of about $13.3 billion, which is expected to grow to $18 billion by 2013 (Exhibit D).[6]

1. How will the shortfall between the assets and liabilities of expected retirement health benefits be covered? Is the pay-as-we-go basis for these health benefits viable? Will premiums significantly rise? Will retirees' health benefits be reduced/modified? Will there be different responses to this question for current retirees and future retirees?

[6] Retiree Health Benefits Report presented to the UC Regents on November 19, 2008. http://www.universityofcalifornia.edu/regents/regmeet/nov08/f11.pdf

2. Is there a contractual obligation on the part of the UC Regents to honor the anticipated retiree health benefits? Are retiree health benefits protected by law? Currently, after 20 years of service credit, Senate members are fully vested in retiree health benefits--that is, UC will cover the same premium for retirees as for current employees. Can this vesting period or accrual rate be changed for current or future employees? Can health benefits be modified for younger retirees such as those who are retiring at age 55?

Current Issues for the UC System

Responses to the key questions above about the potential restructuring of retirement financial and health benefits must take place in the larger context of the UC budget. In light of the significant underfunding of the UCRP and retirement health benefits, and of permanent reductions in the UC budget, structures we have come to see as unassailable suddenly appear less certain. Two in particular come up for scrutiny:

A. Is UCRP a state obligation?

UCRP is unquestionably an obligation of the UC Regents, a position reinforced in the Academic Council's January 2009 statement about the lump-sum cashout option, which asserts that "UC has a legal obligation to provide funding for UCRP", and that "Courts have consistently found that…public entities like UC cannot renege on those promises." [7] In view of the deteriorating situation of UCRP funding and the current budgetary climate, however, it is natural to ask whether UCRP is also an obligation of the state. This is an important question in part because of the impending return to employee and employer contributions to UCRP. Prior to the cessation of these contributions in 1990, fully a third of UC's 12% contribution came from the state.

During the recent state budget deadlock, the California legislative analyst's office recommended eliminating even the nominal $20 million allocation for UCRP in the state budget (UC's original request was for a $228 million allocation).[8] This recommendation raises doubt about whether UCRP is indeed a state obligation, and further challenges the UC budget by laying the burden of funding retirement largely on UC alone.

B. Will UC restructure?

Although the restructuring of UC is being considered, apparently, primarily due to reductions in UC's permanent budget, this restructuring is taking place alongside a serious decline in the UCRP funding ratio and the significant challenge of meeting retiree

[7] Academic Council Statement on Lump Sum Cashout, January 22, 2009.
http://www.universityofcalifornia.edu/senate/reports/Lump%20Sum%20Cashouts%2022JAN09%20Final.pdf
Note that this statement is an assertion of the Academic Council, not UCRP or the UC Regents, and that it refers to court decisions about public institutions "like UC" (emphasis added). By contrast, several CalPERS informational webpages unequivocally state that employees' benefits are "protected by law" or "guaranteed by law." (See
http://www.calpers.ca.gov/index.jsp?bc=/about/press/news/invest-corp/faqs.xml and
http://www.calpers.ca.gov/index.jsp?bc=/about/press/news/invest-corp/responds-financial-crisis.xml)

[8] 2009-10 Budget Analysis Series: Higher Education, January 29, 2009.
http://www.lao.ca.gov/analysis_2009/highered/highered_anl09.pdf

health costs. The official position presented in the recent UCOP "Report on Campus Budget Reduction Strategies" is that all campuses are eliminating or curtailing programs that no longer serve the identified priorities of the campus, and each campus is setting priorities to advance and launch new initiatives that continue to be important to the development of the institution.[9] This report appears implicitly to assume a decentralization strategy on many but not necessarily all of the following issues: differential budget cuts, layoffs, hiring freezes, salary cuts, furloughs, and student fees. However, no public dialogue or consultation with the Academic Senate seems to have taken place on the far-reaching consequences of decentralization on UC. The key questions are: (a) whether UC has the capacity to meet obligations towards its current and future personnel in launching several new initiatives currently being undertaken even when several programs are being eliminated or merged; (b) even when UC is engaged in developing decentralization strategies, whether UC has developed an engagement process to consult the Academic Senate both at the systemwide and the individual campus level on these issues and has communicated these processes effectively to its constituents.

Current Status of UC Retirement Program

To understand the impact UCRP is having on the UC system itself, it is helpful to understand how UCRP works and what its current and projected status is.

UCRP has three main components: assets, liabilities, and contributions.

A. Funding Ratio (assets/liabilities)

The status of the UCRP is commonly discussed in terms of the funding ratio, the ratio of assets to liabilities. For more than two decades, this funding ratio has been above 100%. However, the funding ratio has now dropped well below 100%.

We first define a few terms and introduce some abbreviations:
MVA= Market Value of Assets
AVA = Actuarial Value of Assets
AAL = Actuarial Accrued Liabilities

Market Value Funding Ratio (MRatio) = MVA/AAL
Actuarial Value Funding Ratio (ARatio) = AVA/AAL

MVA is reported quarterly by the UC Treasurer.

In the computation of AVA, only 20% (or 1/5th) of the current year returns are taken into account; the remaining 80% are distributed over the next four years, 20% each. For example, a loss of $6 billion this year will contribute a loss of only $1.2 billion to AVA in the current year, and the remaining $4.8 billion loss will be attributed to the AVA in the next four years. AVA smoothes out the fluctuations in assets by attributing 1/5th of investment returns of the past five years.

[9] Report on Campus Budget Reduction Strategies. http://www.universityofcalifornia.edu/regents/regmeet/mar09/f5.pdf

Computation of AAL is complex, taking into account several factors including potential salary increases, service credit, demographics, actuarial tables, probability of lump-sum cashouts, and an assumption of a 7.5% rate of return. Computation of AAL is done annually by the UC's actuary, Segal Company.[10]

The data below were reported as of July 1 of the corresponding year.[11]
MVA, AVA, and AAL are all reported below in millions of dollars.

	00	01	02	03	04	05	06	07	08	Dec 31/08
MVA	42,071	38,870	34,442	35,327	39,216	41,858	43,362	48,105	42,023	31,708
AVA	37,026	40,554	41,649	41,429	41,293	41,085	41,972	43,434	43,840	
AAL	24,067	27,451	30,100	32,955	35,034	37,252	40,302	41,437	42,577	43,854*
MRatio	1.75	1.42	1.14	1.07	1.12	1.12	1.08	1.16	0.99	0.72
ARatio	1.54	1.48	1.38	1.26	1.18	1.10	1.04	1.05	1.03	

*AAL estimated to increase 3% in 6 months

The actuarial funding ratio gradually decreased from 1.54 (54% surplus) in 2000 to 1.03 (3% surplus) on June 30, 2008. There has been a significant deterioration in the actuarial funding ratio since then. Reflecting the recent sharp drop in the market, as of December 31, 2008, the MRatio was 0.72, and as of the same date, there was an unfilled liability (i.e., liability minus assets) of more than $12 billion. Due to the five-year smoothing explained above, the ARatio changes more slowly than the MRatio. (The ARatio is typically used in most official communications and for planning purposes.)

The assets and liabilities data above are for all of UCRP including all of the five segments: campus and medical centers, Lawrence Berkeley National Laboratory, Lawrence Livermore National Laboratory, Los Alamos National Laboratory, and UC-PERS Plus 5 Plan. The latter plan, not related to CalPERS, is a frozen plan covering a closed group of members, all of whom are in retirement status, and no additional benefits will accrue for these members in the future. This plan is a very small percentage of the total UCRP plan. The five segments each have different funding ratios. Thus it would be useful to have separate tables for each segment, as well as having information on yearly benefit payments broken out separately. Although some data are available in graphical form for some segments,[12] overall this information has been difficult to obtain.

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[10] Segal Company, UCRP Actuarial Valuation Report as of July 1 2008, http://www.universityofcalifornia.edu/regents/regmeet/nov08/f10attach2.pdf

[11] Treasurer of the Regents, Quarterly Investment Information. http://www.ucop.edu/treasurer/invinfo/investment_info.html. Data for MVA, AVA, and AAL used in this were obtained from a report presented to UC Regents (Annual Actuarial Valuation Report presented to UC Regents on November 19, 2008. http://www.universityofcalifornia.edu/regents/regmeet/nov08/f10.pdf). December 31, 2008, data were obtained from UC Treasurer's Quarterly Investment Report (http://www.ucop.edu/treasurer/invinfo/investment_info.html). MRatio and ARatio were computed based on these numbers.

[12] Office of the Treasurer of the Regents, UCRP and GEP Quarterly Investment Risk Report, presented to Committee on Investments/Investment Advisory Group on February 24, 2009. http://www.universityofcalifornia.edu/regents/regmeet/feb09/i1attach2.pdf

B. Investment Returns on UCRP

The percent return below is reported for the one-year period from July 1 of the preceding year through June 30 of the corresponding year.[13]

	01	02	03	04	05	06	07	08	Dec 31, 08
% return	-5.5	-9.0	5.6	14.5	10.3	7.2	19.0	-5.6	-22.83
Annualized return starting 00	-5.5	-7.3	-3.3	0.98	2.78	3.50	5.58	4.11	1.11*

* The annualized return has been computed with the assumption of a one-year return of -20% (that is, assuming a slight recovery between January 1 to June 30, 2009). Please note the sharp drop between July 1, 2008 and December 31, 2008 due to global market turmoil.

The annualized return on UCRP assets as of June 30, 2008, has been 4.11% for a period of eight years. However, due to hefty losses in the current fiscal year, the annualized return on UCRP assets is projected to drop to 1.11% over a period of nine years.

CFW employs the year 2000 as a starting point for computing investment returns as there were major structural changes in managing UCRP assets starting late 2000. In 2000 the UC Treasurer of 28 years resigned. At the same time, the UC Regents created new structures for managing UCRP assets (both decision-making and advisory committees). The routine comparisons of UCRP performance with those of other pension plan funds in the Treasurer's report that appeared prior to 2002 were eliminated.[14] The UC Treasurer's Office has issued a statement stating the pitfalls of such comparisons.[15] That said, the Master Trust Report shows that as of September 30, 2008, the UCRP performance has been consistently in the bottom 25 percentile of all public funds with greater than $1

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[13] Data used in the table for investment returns are taken from a report presented to the UC Regents on November 19, 2008 (p.4) [http://www.universityofcalifornia.edu/regents/regmeet/nov08/f10.pdf]. This rate of return data is slightly different from the data reported in the UC Treasurer's report, where these returns are reported after the administrative expenses. The rate of return data for the years ending 2001, 2002, and 2003 (available from the respective annual UC Treasurer's reports) and from 2004 to 2008 (from the annual _Treasurer's report ending June 30, 2008) is listed below (Annual Investment Report ending June 30, 2008, by the UC Treasurer Office. http://www.ucop.edu/treasurer/publications/UCTreasurer_AnnualReport_2008.pdf).

Further information can be obtained from the quarterly (http://www.ucop.edu/treasurer/invinfo/investment_info.html) and annual investment reports by the Office of the UC Treasurer. Annualized returns (the bottom row of the table in section B, Investment Returns on UCRP) have been computed from the yearly returns shown in the previous row. Since some of the returns are listed with only one decimal digit accuracy, the annualized returns may be slightly off numerically. Using the data reported in the UC Treasurer's reports, the annualized rate of return since July 1, 2000, for a period of more than eight years (with the assumption of -20% return during the current year) is 1.02%.

Computation of investment returns is somewhat complicated due to cash flows in and out. Returns are computed using a standard methodology as mentioned in the UC Treasurer's report. As such, the annualized returns shown display a return on a dollar invested in UCRP that has never been taken out.

[14] UC Treasurer's Office. "Annual Investment Report ending June 30, 2002" http://www.universityofcalifornia.edu/regents/regmeet/nov02/601attach.pdf

[15] UCRP Peer Comparison by the UC Treasurer Office, February 13, 2009. http://www.ucop.edu/treasurer/updates/Peer_Comparison.pdf

billion for all time frames including 1 year, 2 years, 3 years, 4 years, 5 years, and 7 years [see Exhibit A].[16]

	01	02	03	04	05	06	07	08	09*
% return (regents' presentation)	-5.5	-9.0	5.6	14.5	10.3	7.20	19.0	-5.6	-20.0
% return (treasurer)	-5.6	-9.2	5.63	14.34	10.3	7.10	18.83	-5.74	-20.0
$100 on July 1, 2000 (following treasurer)	94.40	85.71	90.54	103.52	114.18	122.29	145.32	136.98	109.58
$100 on July 1, 2000 (following regents' presentation)	94.50	86.00	90.81	103.98	114.69	122.95	146.31	138.11	110.49

* assumption of -20% return during the current year

C. Expenses

Though it would be useful to include data on administrative expenses and service fees (to external managers) incurred in managing UCRP assets—indeed, this information is routinely provided for CalPERS, California's other major public employees' retirement system[17]--it is not provided for UCRP. Similarly useful would be data on the performance of external managers, which is compiled by State Street (the bank used by UC), and is available through the Office of UC Treasurer upon submitting a request each quarter.[18]

D. Contributions

UCRP members (faculty and staff) and UC have made no contributions to UCRP since November 1990.

Percentages are reported as covered payroll (more on this below).
Prior to November 1990, UCRP received contributions from both members and employer (UC) as follows:

- Members: 2.4 %
- UC: 12.0 %

The employee-to-employer ratio of contributions to UCRP was 1:5. UC's 12% contribution was made up approximately as follows: 36 % from the state of California, 24% from the Department of Energy Labs, and 40% from Contracts and Grants.

[16] UC Master Trust Report. September 30, 2008. Available from the UC Treasurer Office.

[17] CalPERS Annual Investment and Financial Reports, Comprehensive Annual Financial Report ending June 30, 2008. http://www.calpers.ca.gov/index.jsp?bc=/investments/reports/home.xml&rsns=99
See pages 72-81 for expenses (administrative, investment, consultant, and professional services).

[18] External Managers Performance Summary Report, September 30, 2008. Available from the UC Treasurer Office.

The current proposal is for members (employees) to contribute 2% starting April 15, 2010 and continuing through June 30, 2011.[19] These contributions are expected to increase 1% each subsequent year until they reach 5%. The suggested contribution by UC is twice the annual contribution by employees--thus 4% from April 15, 2010 through June 30, 2011 and increasing by 2% in subsequent years to 6%, 8%, and 10%, and then, finally to 11% annually. ***A total contribution of 16% (5 % by employees and 11% by employers) of covered payroll is being suggested after five years.***

This employee-to-employer contribution ratio of roughly 1:2 is similar to the ratio currently being used in CalPERS. In the current budgetary climate, it is difficult to expect the employer to contribute at a higher ratio. However, if UCRP remains chronically underfunded over a long period of time, a higher contribution from the employer may be needed. The UC Academic Council has supported the return of member contributions to UCRP for several years.[20]

Contributions are reported as a percentage of covered payroll. Currently, the covered payroll is \$7.47 billion,[21] while assets (as of September 30, 2008) are approximately \$37.3 billion. That is, the ratio of covered payroll to UCRP assets is approximately 1:5. ***Therefore, at the current level, a contribution of 2% by employees will add about \$150 million and make a difference of .4% (1/5th of 2%) in the assets***. A contribution of 16% of covered payroll will provide for about 3.2% of UCRP assets at current levels. In other words, the proposed new contributions will provide only a very small percentage of UCRP assets, and certainly not enough to restore UCRP to a healthy funding ratio. Nevertheless, it is a beginning.

The total benefit payment to retirees of UCRP campus and medical center segments in the past 3 years, during 2005-06, 2006-07, and 2007-08, has been approximately \$1.4, \$1.7, and \$1.8 billion respectively.[22] The reasons for the sharp benefit payment increase from 2005-06 to 2007-08 is not clear. In any case, the proposed 2% contribution by employees represents roughly 8.3% of annual benefit payments; a full employer-employee contribution of 16% after five years is roughly 67% of total current benefit payments. This will still fall short of the total benefit payments, and will thereby contribute to the increasing gap between liabilities and assets.

[19] Proposal to Reinstate Contributions to UCRP, presented to UC Regents, February 2009.
http://www.universityofcalifornia.edu/regents/regmeet/feb09/j3pp.pdf

[20] Academic Council Memorandum on Resumption of Contributions, May 25, 2006.
http://www.universityofcalifornia.edu/senate/reports/ucrp.0506.pdf

[21] Annual Actuarial Valuation Report presented to UC Regents on November 19, 2008.
http://www.universityofcalifornia.edu/regents/regmeet/nov08/f10.pdf

[22] Estimated from the bar graph data presented in "UCRP and GEP Quarterly Investment Risk Report," presented to Committee on Investments/Investment Advisory Group on February 24, 2009.
http://www.universityofcalifornia.edu/regents/regmeet/feb09/i1attach2.pdf

E. Projections

The projection of the funding ratio as presented to the UC Regents in February 2009 (Exhibit B) shows that the funding ratio (ARatio) will decline to 61% by 2013.[23] This decline will create an unfilled liability of $18 billion, assuming (a) a negative investment return of -20% during the current year (an assumption that has been met so far), (b) a return to positive returns of 7.5% annually during the subsequent four years,[24] and (c) employer and employee contributions increasing to 16% of covered payroll by 2013 as has been suggested above. This analysis also shows that the level of contributions required to bring UCRP back to 100% funding will exceed 35% of covered payroll by 2013 (Exhibit C). Therefore, even under promising assumptions, the level of contributions required to bring UCRP back to full funding seems both extraordinarily high and unsustainable.

F. Emerging Issues regarding UCRP

The above scenario raises serious questions regarding several underlying assumptions that have been taken for granted so far. These assumptions must be questioned and investigated afresh and an open democratic dialogue needs to be supported surrounding these issues. The issues include:

1. Asset Management Strategies (asset protection, investment allocation, governance structure for managing UCRP assets, internal benchmarking, and comparison of UCRP with other pension plan funds):
Are UCRP assets protected in a protracted downturn or long-term sideways movement of stock market? How do UCRP investment returns compare with those of other pension plan funds? Is UCRP moving towards higher-risk highly-specialized privatized investing?[25] Who should be making the investment decisions?

2. Liabilities Computation:
Are UCRP liabilities growing more rapidly relative to other pension plans? If so, why? Are there demographic reasons? Are the actuarial tables used reasonable?

3. Accounting and Planning Issues:
Is a 7.5% rate of return reasonable? What are the implications of using a different rate of return? Is there a tipping point on the funding ratio below which the contributions will have to be chronically overwhelming, such as 33% of payroll over an extended period of time?

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[23] "Proposal to Reinstate Contributions to UCRP", presented to the UC Regents, February 2009. http://www.universityofcalifornia.edu/regents/regmeet/feb09/j3pp.pdf

[24] In 2007, the Academic Council stated that "the assumption of a 7.5% rate of return in reasonable and slightly conservative" (Academic Council Statement on UCRP, July 25, 2007 http://www.universityofcalifornia.edu/senate/committees/council/ac.ucrp.0707.pdf). Although the view from 2007 is clearly different from the view in 2009, current investment projections, including the project ARatio of 61% for 2013, still employ the 7.5% projected return rate.

[25] Discussion on Revised Asset Allocation for UCRP at Committee on Investments, September 17, 2008. http://www.universityofcalifornia.edu/regents/minutes/2008/invest9.pdf

Conclusion

The UCRP funding situation has deteriorated significantly in the past year, raising anxiety and concern among UCRP members and retirees.

Some of the key concerns include whether the current, retired, and the newly hired UC employees will receive the expected UCRP and health benefits when they retire. Additional questions include the size of expected member contributions in the next five years—with or without salary increases, freezes, or even cuts—and whether these contributions will be sufficient to bring the UCRP back to sustainable levels.

Although the Presidential Steering Committee and Presidential Task Force on Post-Retirement Benefits have begun to look into these questions, it is important that the UC Regents adopt the best practices of the industry and strive to provide UCRP-related data in an easily accessible, transparent, and timely manner to all UCRP members so that members can take well-informed decisions, provide meaningful input to these committees, and have a better understanding of the decisions advocated later by the UC Regents.

Reductions in UC's permanent budget combined with the significant unmet obligations of the UCRP and retirement health benefits program is the backdrop against which UC has started formulating and implementing major structural changes at UC. These changes apparently include decentralization without sufficient engagement, consultation, or communication with the Senate, bypassing the processes already in place for such consultation, and evidently without creating new processes in their stead.

CFW hopes the UC Regents will assert their commitment to current employees to honor post-retirement benefits (UCRP and health) before campuses begin launching new initiatives and hiring new personnel associated with them. Such a statement will reassure current employees, help UC recruit and retain top quality faculty and staff, and preserve the integrity of our institution.

Respectfully submitted;
COMMITTEE ON FACULTY WELFARE
Maria-Elena Diaz
Isebill Gruhn *ex officio*
Joel Kubby
Suresh Lodha
Pete Raimondi (W, S)
Jennifer Reardon
Trish Stoddard (S)
Marilyn Westerkamp (S)
Elizabeth Abrams, Chair

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