UCRS Advisory Board

MINUTES
UNIVERSITY OF CALIFORNIA RETIREMENT SYSTEM (UCRS)
ADVISORY BOARD MEETING
THURSDAY, NOVEMBER 10, 2011
10:00 AM – 2:00 PM

BOARD MEMBERS PRESENT: Chair Ross Starr, Vice Chair Shane White, Executive Vice President (EVP) Nathan Brostrom, Vice President Dwaine Duckett, Chief Investment Officer (CIO) Marie Berggren, Vice Chancellor Meredith Michaels, CUCRA Chair Marian Gade, CUCEA Chair Ernest Newbrun, Associate Vice Chancellor Angela Hawkins, Assistant Researcher Catherine Brennan, Spectroscopist Paul Brooks.

STAFF PRESENT: Principal Counsel Barbara Clark, Senior Counsel Ina Potter, Executive Director Nancy Tanaka, Special Assistant to the Vice Provost Patricia Price, Director Kris Lange, Director David Olson, Director Gayle Saxton, Director Gary Schlimgen, Associate Director Maria Anguiano, Manager Bill Ryan, Specialist Ken Reicher, Principal Analyst Robert Semple.

OTHERS PRESENT: UCB Retiree Association representative Antonia Sweet, UCB Emeriti Association representative George Goldman, CUCFA representative Eric Hays, CUCFA representative Joe Kiskis (by telephone), UAW representative Maria Chen, CUE representative Anytra Henderson, AFSCME #3299 representative Nathaniel Johnson, UCRS Actuary John Monroe (The Segal Company), Aon-Hewitt consultant Ruth Schau.

The meeting officially began at 10:00 a.m.

COMMENTS FROM THE CHAIR: Chair Starr initiated the public comment period of the meeting, noting UCD Physics Professor and CUFCA representative Kiskis had asked to make remarks.

PUBLIC COMMENT PERIOD: With respect to Governor's pension proposal, CUCFA representative Kiskis noted that responsibility for UCRP rests with The Regents and not the state, which has not made any contribution to UCRP for years. He also stated that UC has a history of conservative and responsible investing and UCRP's current funded status was the result of the financial market downturn, not mismanagement. He questioned the potential cost savings of the Governor's proposed hybrid plan, since many studies show that defined benefit plans are less expensive than defined contribution plans. He concluded by noting that UC can't vie for talent in a competitive market with its current low salaries and feels that The Regents need to confer more with employees on issues such as salaries and retirement benefits.

EXECUTIVE VICE PRESIDENT, BUSINESS OPERATIONS - BUDGET UPDATE: EVP Brostrom stated that the legislature had approved a $500 million reduction to UC's budget in the spring of 2011 and reduced it by another $150 million by the summer, with a trigger for a further

$100 million reduction mid-year if state revenue targets were not met. UC also faces $362.5 million in unfunded mandatory costs. This $1 billion shortfall was somewhat mitigated as a result of tuition increases, leaving a budget gap of $750 million for 2011-2012. Since it is doubtful that the state will meet its revenue targets, UC's budget will likely be reduced by another $100 million early next year. Despite the possibility of a further budget cut, however, EVP Brostrom indicated that there are no plans for another tuition hike for 2011-2012. In response to questions about state funding for UCRP, he indicated that UC will be asking the state to contribute $87.6 million to UCRP for 2012-2013, which is a portion of the state's actual costs of roughly $256 million.

CHIEF INVESTMENT OFFICER - REPORT: Since third quarter investment results were not available, CIO Berggren provided results for the quarter ended June 30, 2011. She noted that UCRP had a return of 1.48% for the quarter and 22.45% for the fiscal year, 36 and 81 points above the respective benchmarks. UCRP rated in the top quartile of public plans with over $1 billion in assets for the fiscal year, per the Wilshire Trust Universe Comparison Service (TUCS). She noted that the key contributors were core bonds, absolute returns and real estate investments. Although second quarter returns were positive, they were impacted by the Japanese tsunami, unrest in the middle east, and confusion over the US sovereign debt. She concluded by noting that UCRP's 3 and 5-year returns were below its 7.5% assumed rate of return, but it had an average 20-year return of over 9%, which she attributed to investment diversification.

ITEM A. UCRP - EXPERIENCE STUDY: UCRS Actuary John Monroe from the Segal Company summarized the Experience Study for the period of July 1, 2006 through June 30, 2010, that was presented to The Regents in July. He noted that such a study is conducted every 3-5 years to compare expected to actual experience and to determine if the rates and assumptions used in the actuarial valuations are suitable. He stated that the approved recommendation with the most significant impact on UCRP costs and liabilities was the change in mortality rates, as UCRP experience shows that members (males in particular) are living longer. The use of new mortality tables will affect the UCRP Lump Sum Cashout (LSC) and monthly retirement option factors beginning July 1, 2012. Actuary Monroe also noted that UCRP's assumed rate of return will remain at 7.5%, which is lower than the rate maintained by most other public retirement plans.

ITEM B. UCRS ANNUAL ACTUARIAL VALUATION REPORTS: Actuary Monroe provided a summary of the UCRP valuation report as of July 1, 2011, which included the $1.1 billion transferred to UCRP in April 2011, but not the $935 million transferred to UCRP in July 2011. He noted that the adoption of a new mortality table increased UCRP's actuarial liability by $1.8 billion. While UCRP had a return of 22% on a market value of assets (MVA) basis over the last fiscal year, he stated that the return on an actuarial value of assets (AVA) basis was 4.6% due to factoring in losses from previous years (i.e., smoothing). He noted, however, that UCRP's MVA and AVA were moving closer together, which means that UCRP is not deferring larger amounts of past losses. In response to member comments, he indicated that UCRP's 5-year smoothing period was standard in California, although CalPERS uses a 15-year smoothing period.

ITEM C. UCRS – AUDITING ACTUARY OF UCRP AND THE UC-PERS PLUS 5 PLAN: Aon consultant Ruth Schau summarized the auditing work that Aon performed with respect to UCRP and the UC-PERS Plus 5 Plan, noting that auditing of retirement plans is a widely accepted best-practice. She indicated that Aon was totally independent of the Segal Company and used its own model for conducting the audits. Using the same data that UC provided to Segal, Aon performed the actuarial valuations for UCRP and the UC-PERS Plus 5 Plan and replicated the results reached by Segal with no major findings. She indicated that results of the audits will be available after they are presented to the Regents.

ITEM D. UCRP – ADDITIONAL CONTRIBUTIONS TOWARDS THE ANNUAL REQUIRED CONTRIBUTION – UPDATE: As a follow-up on the approved transfer of assets to UCRP, Associate Director Anguiano advised that the second transfer of assets, totaling $935 million, was effectuated on July 27, 2011 and was garnered from the issuance of general revenue bonds. She stated that the assessment on payroll funding sources for the latest transfer was .68%, as compared with the .8% assessment for the previous $1.1 billion transfer from STIP. She indicated that the combined transfers should lower the maximum expected UCRP employer contribution in 2019 and beyond from 20% to roughly 18.8%. She concluded by reviewing a graph on UCRP's estimated future funded status with the modeling of employee contributions ranging from 6.5% to 8%.

ITEM E. UCRP – PROPOSED UNIVERSITY AND MEMBER CONTRIBUTION RATES BEGINNING PLAN YEAR 2013-2014: Specialist Reicher stated that the recommendation was to raise rates incrementally, subject to collective bargaining as applicable. The proposed UC contribution rate beginning July 1, 2013 for all UCRP members, including those in the new UCRP tier, would be 12% and the proposed member rate in the current UCRP tier would be 6.5% less a $19 offset, with different rates for Safety and Tier Two members. The Regents had previously approved a member contribution rate of 7% beginning July 2013 for non-Safety members covered under the new UCRP tier (without the $19 offset). He noted that the proposed contributions for Plan Year 2013-2014, if approved, would cover Normal Cost for the first time since contributions were resumed. During the discussion of this item, it was noted that the Academic Senate had recommended a maximum employee contribution of 7% and that the trajectory of the proposed 6.5% employee contribution for 2013-2014 did not appear to be in line with their recommendation. It was also noted that the proposed contribution rates did not reflect the payroll assessments for the two transfers of assets to UCRP.

ITEM F. UCRS – AUDITED ANNUAL FINANCIAL REPORTS FOR FISCAL YEAR 2010-2011: Director Olson indicated that the reports followed the same format as the previous year and were presented in accordance with Government Accounting Standards Board (GASB) guidelines. He refrained from providing financial numbers, noting that they had already been reported by CIO Berggren and UCRS Actuary Monroe. In conclusion, he indicated that, as part of the reporting process, he must sign an affidavit attesting that no fraud had occurred that could impact the financial condition of the plans.

ITEM K. PROPOSED DEFINED CONTRIBUTION PLAN OPTION FOR CLINICAL ENTERPRISE NEW HIRES – FEASIBILITY STUDY: (*This item was presented out of order at the Chair's request*). Director Schlimgen noted that this feasibility study was suggested by the PEB Task Force and is at the request of Clinical Enterprise (CE). He stated that meetings have been held with CE Chief Human Resource Officers (CHROs) to document recruitment issues, discuss the types of plans offered by competitors, and to define the CE employees for whom the DC Plan could potentially apply. He stated that CE CHROs envision the proposed DC Plan would apply broadly to most new hires, including faculty members, and prefer a plan design in which employees must contribute to receive an employer contribution. CE CHROs also prefer a DC Plan with a 1-year vesting period for employer contributions. Citing the concern previously expressed by a Board member and some union representatives that a separate DC Plan for CE new hires could reduce funding to UCRP, he clarified that CE would still be responsible for the legacy liability in UCRP and would pay an additional assessment to UCRP. The Chair expressed concern regarding the proposed DC plan option for CE, saying it would still reduce UCRP's funding through the loss of employer contributions made on behalf of employees who don't vest and would encourage other groups to try to "opt out" of UCRP.

ITEM G. THE GOVERNOR'S PROPOSED TWELVE POINT PENSION REFORM PLAN: Since a description of the Governor's proposal was provided to the Board, Director Schlimgen did not summarize all its points. He noted that the Legislative Analyst's Office (LAO) made several references to UC in its summary of the Governor's proposed plan and that UC plans to participate in a public pension conference committee in Sacramento in December. The Vice Chair pointed out that the Faculty Welfare's Task Force on Investment and Retirement (TFIR) had issued a response indicating that UC already complies with or is initiating many of the reform measures proposed by the Governor. The TFIR response is available on the Academic Senate web site. A general discussion ensued on how best for UC to respond to the proposal, given the complexities of the issues.

ITEM H. RETIREMENT SAVINGS PROGRAM – VENDOR RELATIONS MANAGEMET REPORT: Director Lange provided highlights of the report, which covers record-keeping services as well as financial education provided by Fidelity Retirement Services. She noted that the UC's Retirement Savings Program (RSP) financial education campaign was recently recognized with two awards and that a new workshop "Women & Investing" was being rolled out. She also noted that a recent RSP communications campaign that was sent to 90,000 employees resulted in a 1.6% increase in RSP participation. She concluded by noting that Fidelity will be issuing minimum required distributions (MRDs) in late December and that an article on MRDs appears in the November issue of the New Dimensions retiree newsletter.

ITEM I. RETIREMENT SAVINGS PROGRAM – FEE DISCLOSURE REQUIREMENTS FOR DEFINED CONTRIBUTION PLAN PARTICIPANTS: Director Lange reminded the Board that the Department of Labor (DOL) had issued regulations concerning the disclosure of fees, expenses and investment performance to participants in defined contribution plans covered under the Employee Retirement Income Security Act (ERISA). She noted that while the UC Retirement Savings Program plans were not subject to ERISA, UC has historically complied with ERISA rules, as feasible, and that UC would be providing information on-line (with a print option).

ITEM J. RETIREMENT SAVINGS PROGRAM - FINANCIAL EDUCATION PROGRAM - UPATE: Manager Ryan stressed that the goal of the financial education campaign was to increase financial literacy and improve retirement readiness. He indicated that Vendor Relations Management is enhancing the UC Focus on Your Future web portal to allow employees to generate personalized retirement estimates, obtain a retirement readiness score based on their UCRP and/or RSP participation, and create a retirement strategy. The updated web portal should launch in February 2012.

ITEM L. PROPOSED DEFINED CONTRIBUTION PLAN CONTRIBUTIONS ON ADDITIONAL NEGOTIATED COMPENSATION EARNED BY FACULTY: Principal Analyst Semple summarized two proposals advanced by Academic Affairs to implement 3.5% employer and a 3.5% employee contribution to a defined contribution plan (DC Plan) based on additional negotiated salary earned by faculty which is not covered by UCRP or any other retirement plan. The intent is to improve the retirement replacement ratios for faculty by providing retirement benefits on all their types of pay. Specifically, the contributions for Health Sciences Compensation Plan faculty would be made on their additional negotiated "Y" pay, which many have received for years. For non-Health Sciences, ladder-rank faculty, the contributions would be based on additional negotiated compensation which is currently being considered for them, as described in the draft section of Academic Personnel Manual (APM) 668, which is currently out for system-wide review. The UC contributions would be attributable to the funding source of the negotiated compensation.