UCRS Advisory Board

MINUTES
UNIVERSITY OF CALIFORNIA RETIREMENT SYSTEM (UCRS)
ADVISORY BOARD MEETING
FRIDAY, NOVEMBER 21, 2014
10:00 AM – 2:00 PM

BOARD MEMBERS PRESENT: Chair Shane White, Vice Chair Meredith Michaels, Chief Investment Officer (CIO) Jagdeep Singh Bachher, Vice President (VP) Dwaine Duckett, Associate Vice Chancellor David Odato, Professor James Chalfant, Assistant Director Deborah McWilliams, Administrative Clinical Care Partner Monica Martinez (via telephone), CUCRA Chair Lee Duffus, and CUCEA Chair Roger Anderson.

BORD MEMBERS ABSENT: Executive Vice President (EVP) Nathan Brostrom

STAFF PRESENT: Associate CIO Arthur Guimaraes, Associate Vice President Debora Obley, Executive Director Gary Schlimgen, Principal Legal Counsel Barbara Clark, Senior Legal Counsel Ina Potter, Senior Investment Analyst Susie Ardeshir, Director Kris Lange, Director Ellen Lorenz, Director David Olson, Director Bill Ryan, Associate Director Tony DiGrazia, Manager Ken Reicher, Manager Richard Townsend, Coordinator Anne Wolf, Principal Analyst Mary Jenkins, Principal Analyst Robert Semple.

OTHERS PRESENT: CUCRA/CUCEA representative Adrian Harris (via telephone)**,** UCB Retiree Association representative Marian Gade (via telephone), UCB Retiree Association representative Amy Block Joy, CUCFA representative Eric Hays, CUCFA representative Joe Kiskis, AFSCME representative Claudia Preparata, Teamsters Local 2010 representative Mary Higgins, CUCSA representative Ken Feer (via telephone), UPTE representative Paul Brooks, UPTE representative Mike Fehr, SETC representative David Rogers, Actuary John Monroe (The Segal Company).

The meeting officially began at 10:04 a.m.

PUBLIC COMMENT PERIOD: CUCFA representative Kiskis had a number of questions. Based on comments from the Legislative Analyst's Office, he inquired if UCRP would possibly receive any money as a result of Proposition 2. He also asked for clarification on UCRP investments in private equity and hedge funds. Noting the improvement in UCRP's funded percentage, he questioned how much of the increase was attributable to employer and employee contributions and borrowing versus investment returns. Finally, he asked if there were any future plans to implement a Roth option in the UC Retirement Savings Program (RSP). UPTE representative Mike Fehr stated that reducing the options under the RSP would most likely result in a decrease in RSP participation. He also questioned whether the CIO would continue to invest in hedge funds in the wake of CalPERS' elimination of such investments. Based on best practices recommended by the Government Finance Officers' Association (GFOA), he suggested that a sensitivity analysis be conducted to determine how a change in UCRP actuarial assumptions would impact UCRP's funded status. For example, he noted that the Society of

Actuaries released a new mortality table in 2014 and wondered how members' increased longevity would impact UCRP.

APPROVAL OF THE MINUTES: Chair White called for approval of the minutes from the Board meeting of June 20, 2014. The minutes were approved by acclamation.

COMMENTS FROM THE CHAIR: Chair White began by introducing the new members, some of whom had attended prior meetings. He noted that the President had appointed Associate Vice Chancellor (AVC) David Odato from UCSF to replace Angela Hawkins, who retired last September. He mentioned that AVC Odato was the Chief Administrative and HR Officer at UCSF and had served on former President Yudof's Post Employment Benefits (PEB) Task Force as the chair of the pension committee. Chair White then introduced James Chalfant, a professor in the Department of Agricultural & Resource Economics at UCD who had been appointed by the Academic Senate to replace Professor Ross Starr. He noted that Professor Chalfant had also served on the PEB Task Force and currently served as chair of the Faculty Welfare's Task Force on Investment and Retirement (TFIR). Chair White next introduced staff representative Deborah McWilliams, an Assistant Director of Nursing Sciences at UCI, who replaced staff representative Paul Brooks who retired last July. Assistant Director McWilliams previously served as the Chair of the UCI Staff Assembly and had also served on a number of other UCI committees. Finally, Chair White noted that Roger Anderson, a professor Emeritus of Chemistry from UCSC, was the new CUCEA Chair, replacing Doug Morgan.

Chair White then mentioned that the Board's letter to President Napolitano regarding additional borrowing for UCRP and the response letter were available on the Board's pages of UCnet. He noted that the transfer of $700 million from the Short term Investment Pool (STIP) to UCRP in July 2014 was helpful, but that future borrowing for UCRP was still needed.

CHIEF FINANCIAL OFFICER/INTERIM CHIEF OPERATING OFFICER – BUDGET UPDATE: Since EVP Brostrom was unable to attend, the budget update was provided by AVP Debora Obley. The focus of her presentation concerned the Regents approval of President Napolitano's proposal to increase tuition by 5% over the next five years if UC does not receive the requested additional $100 million above its expected 4% base budget increase. She indicated that the request for additional funding seems acceptable to the legislature and actually represents only a 1.7% increase to UC core funds. She noted that UC enrollment has steadily been increasing and UC risks losing faculty, and thus maintaining quality, without more money. She stated that she disagrees with the accusation by Lt. Governor Newsom that UC is breaking its budget pact with the state by proposing to raise tuition. UC never agreed to the amounts in the current budget pact and had anticipated base budget increases of around 6%. Moreover, she indicated that state had broken its promise with respect to Proposition 30 proceeds, as UC had received only 3% (roughly $400 million) of the $13 billion generated by Proposition 30. In response to questions regarding UCRP, she indicated that some of the requested $100 million in additional funds, if provided, could be allocated to UCRP. There are no plans to raise the current UCRP employer contribution rate of 14% or the UCRP employee contribution rate. Based on projections, these contribution levels are expected to raise UCRP's funded status above 90% by 2022. The Chair noted that such projections still fall below the Regents policy of attaining a UCRP funded status of 100%.

CHIEF INVSTMENT OFFICER – REPORT: CIO Bachher began with an overview of UC's current situation with respect to investments. He noted that he believes equity returns will be decreasing in the future, providing between 5% and 7%, while bond returns will be only 1% to 3%. Consequently, it is going to be more difficult to achieve UCRP's assumed rate of return of 7.5% going forward. He noted that he is trying to build up cash (up to $2 billion) because UC will need to be nimble and flexible to take advantages of upcoming investment opportunities. He expects to discuss the rebalancing of portfolios with the Regents Committee on Investments in December 2014. He also plans to work with locations on how to best use proceeds from the Total Return Investment Pool (TRIP), which has had robust returns of late. Turning to public equities, he stated that he had inherited a portfolio of roughly 70 external managers who handle such investments, which he has subsequently decreased to 40 managers with an expected decrease to 35 managers by year's end. He believes UC's public equities are currently over-diversified and UC might want to invest more in index funds, which would lower costs, reduce complexity and result in similar or higher returns with the same risk. However, if equity returns steadily decrease, he sees a need for active management. Turning to hedge funds, he indicated that they have advantages by providing more flexibility with less regulation and they do not have a direct correlation with equities. He indicated that he is not concerned with the recent decision by CalPERS to eliminate its hedge fund investments. He stated that the challenge with hedge funds is transparency, but that it would be better to try and improve transparency with hedge fund investments than to simply dump them. (CIO Bachher distributed two documents, entitled "Why we invest in Hedge Funds?" and "University of California Defies CalPERS on Hedge Funds."). Turning to private equity, CIO Bachher indicated that he hasn't found many deals lately and has recently sold over $400 million of UC's private equity investments.

CIO Bachher closed by discussing personnel in the CIO's Office. Noting that Mel Stanton had retired, he introduced the new Chief Operating Officer and Associate CIO, Arthur Guimaraes. He also indicated that Randy Wedding, Senior Managing Director of Fixed Income, announced that he would be retiring in March 2015. He indicated that he will work with Senior Managing Director Wedding to find a new fixed income expert. He also praised Director Ryan for his passion and commitment to the RSP.

ITEM A. UCRS – ANNUAL ACTUARIAL VALUATION REPORT FOR FISCAL YEAR 2013-2014: UCRS Actuary John Monroe of the Segal Company noted that UCRP had a 2013-14 Fiscal Year (FY) return of 17.8% on a market value of assets (MVA) basis, but only a 12.3% return on an actuarial value of assets (AVA) basis due to 5-year smoothing. UCRP's funded ratio had increased from 76% to 80%, and its unfunded actuarial accrued liability (UAAL) had decreased from $13.8 billion to $12.1 billion, from the previous year. The UCRP funding policy had also decreased, from 30.3% to 28.8%. He noted that the $700 million transfer from STIP to UCRP had occurred on July 31, 2014, so it was not reflected in the FY 2013-14 valuation results. The $700 million transfer will serve to fully fund UCRP's modified annual required contribution (modified ARC = UCRP's Normal Cost plus interest on its UAAL) for FY 2014-15. He noted that the valuation was the first to include members of the UCRP 2013 tier. He closed by indicating that a UCRP experience study would be conducted in 2015 and recommendations for new actuarial assumptions may be made. However, he indicated that there was some controversy with the relatively new 2014 mortality table.

ITEM B. UCRS – AUDITED ANNUAL FINANCIAL REPORT FOR FISCAL YEAR 2013-14: Stating that much of the UCRP information had been covered by Actuary Monroe, and RSP information will be covered as part of the Vendor Relations Management Report (item F), Director Olson provided a brief synopsis of the report. He stated that, due to new Governmental Accounting Standards Board (GASB) provisions, the report included new information on net pension liability for UCRP and the PERS Plus 5 Plan. He also noted that several tables were updated to include information on both the UCRP 1976 and 2013 tiers. He informed the Board that UC had a new auditor this year, KPMG, but that there were no new audit findings that required reporting to the Regents. He closed by noting that assets in the RSP exceeded $20 billion for the first time.

Following Director Olson's summary of the financial report, Executive Director Schlimgen mentioned that Principal Analyst Jenkins had completed the annual, condensed summary of UCRP and RSP data for the Board and that a laminated copy (i.e., the "laminate") had been placed in each member's folder.

ITEM C. UCRS – RETIREMENT READINESS STUDY: Directors Bill Ryan and Kris Lange mentioned that, as in past years, the UC Retirement Readiness scores provided by Fidelity Retirement Services should be available to members early next year. These scores include projections of members' retirement income replacement ratio, based on their expected income from both UCRP and the RSP. Additionally, UC will be conducting a retirement readiness study based on members who have retired on July 1 over the past three years. The purpose of the study is to determine, based on actual data, how financially prepared theses members were at retirement and how UC can better educate its members. The results of the study should be available in spring of next year. In response to a question about lower retirement readiness scores for older members that had been previously reported to the Board, Director Lange noted that the UCRP benefit accounts for a very large percentage of the score. Since many older members joined UC late in their careers and have less time to build up a UCRP benefit, these folks tend to drag the average score down for their age group. The scores do not include expected Social Security income.

ITEM D. UCRP – LUMP SUM CSHOUT REPORT: Manager Richard Townsend noted that there was a slight decrease in the number of the lump sum cashout (LSC) elections versus monthly retirement elections over the past year. However, the dollar amount of the LSC payments increased by slightly more than 8%. Of the 949 LSCs elected elections in FY 2013-14, 48% were elected by active members and 52% were elected by inactive members. Roughly 70% of the members who elected an LSC would not have been eligible for continuation of retiree health coverage. In response to a question, he noted that the 2013 tier does not have an LSC option, but that some unions have negotiated a modified 2013 tier which does include it.

ITEM E. RETIREMENT SAVINGS PROGRAM – FUND MENU MANAGEMENT– UPDATE: Director Bill Ryan provided an update on phase 3 of the RSP Fund Menu project and the creation of a single Core funds menu with streamlined investment options, which is targeted for spring 2015. Participants with money in funds being removed from the menu who fail to take action will have their assets defaulted to an age-appropriate Pathway Fund. He clarified that RSP participants aren't losing investment options, as funds eliminated from the menu will be available under the Brokerage Link. He also stated that the $25 fee associated with the Brokerage Link is being eliminated. He stated that the purpose of phase 3 was to enhance value by providing the most cost efficient funds, to improve administrative monitoring and oversight, and to reduce duplication and complexity for participants. He noted that 71% of all RSP assets are currently in five funds, so a reduction in fund options should not have a dramatic impact for the majority of RSP participants. Director Kris Lange noted that the communication plan for phase 3 is underway and that impacted participants will be mailed personalized statements, a suggestion made by the Board that worked very well in phase 1 and 2.

ITEM F. RETIREMENT SAVINGS PROGRAM – VENDOR RELATIONS MANAGEMENT REPORT: Director Kris Lange provided highlights of the report, noting that the RSP currently had over 307,000 unique participants with total assets just under $20 billion. The 403(b) Plan had an average participation rate of nearly 50%, with an average deferral rate of just over 10%. However, almost 24% of 403(b) Plan participants, and nearly 76% of all DC Plan participants, had assets in only one fund (which was not a Pathway Fund). She noted that the default investment option had been changed from the Savings Fund to the age-appropriate Pathway Funds, which mostly impacts Safe Harbor DC Plan participants. The name of the UC Equity Fund was also changed to the UC Global Equity Fund. She also mentioned that the Easy Enroll application was launched, which allows participants to easily enroll in an age-appropriate Pathway Fund with a 3%, 5% or 7% contribution rate. In response to a question on voluntary RSP participation by age groups, especially younger employees, she noted that only 20% of employees under age 30 voluntarily contribute to the RSP, with an average contribution of 6%. She indicated that efforts were made, and will continue to be made, to better communicate the benefits of RSP participation to this age group.

ITEM G. RETIREMENT ADMINISTRATION SERVICE CENTER – UPDATE: Director Ellen Lorenz of the Retirement Administration Service Center (RASC) provided a brief review of RASC statistics and accomplishments. She noted that customer satisfaction with RASC remains high, even while total contacts increased by 31% during the past year (calls increased 28% and correspondence increased 54%). She noted that retirement elections increased 6% over the last year (LSC elections declined by 3%) and that there was an increase in retirement counseling. She confirmed that the increase in RASC retirement counseling was due, in part, to a loss of benefits personnel at some locations. However, she also attributed the increase to the proactive outreach by RASC to the locations. She also stated that RASC continues to partner with the Office of the CIO, Vendor Relations Management and other human resources personnel to further incorporate RSP information as part of the retirement counseling process. In closing, VP Duckett complimented the RASC on its efficiency and professionalism, especially in light of its increased workload.

The meeting adjourned at 1:57