UCRS Advisory Board

MINUTES
UNIVERSITY OF CALIFORNIA RETIREMENT SYSTEM (UCRS)
ADVISORY BOARD MEETING
NOVEMBER 30, 2018
10:00 AM – 2:00 PM

BOARD MEMBERS PARTICIPATING: Chair David Brownstone, Vice Chair Henning Bohn, Chief Investment Officer (CIO) Jagdeep Bachher, Vice Chancellor Ronald Cortez, Interim AVC and CHRO Jo Mackness, Pharmacy Technician Naomi Nakamura (via telephone), Computer Resource Specialist Michael Fehr, CUCEA Chair Caroline Kane, and CUCRA Chair Marianne Schnaubelt.

BOARD MEMBERS ABSENT: Chief Operating Officer (COO) Rachael Nava and Vice President (VP) Dwaine B. Duckett

UCOP STAFF PARTICIPATING: Executive Director Gary Schlimgen, Sr. Counsel Luis Blanco, Director Cain Diaz, Director Marco Merz, Director Esther Cheung Hill, Director Ellen Lorenz, Director David Olson, Associate Director Anthony DiGrazia, Manager Ken Reicher, Manager Greg Ricks, Manager Scott Sylva, Manager Hyun Swanson, and Principal Analyst Robert Semple.

OTHERS PRESENT: DANR/Cooperative extension representative John Karlik, UCBEA representative Amy Block Joy, UCRAB representative Antonia Sweet, CUCFA representative Eric Hayes, CUCFA representative Joe Kiskis, AFSCME Local 3299 representative Claudia Preparata, Teamsters Local 2010 representative Alex Vermie, Retiree Paul Brooks, Actuary Paul Angelo (Segal Consulting), actuarial consultant Emily Klare (Segal Consulting, via telephone).

The meeting officially began at 10:03 a.m.

PUBLIC COMMENT PERIOD: CUCFA representative Joe Kiskis voiced objections to a letter sent by VP Duckett in late summer indicating that locations would soon lose access to AYSO due to the Redwood transition and would temporarily need to contact the RASC for data they formerly found on AYSO. He indicated that the locations need AYSO data for health and retirement issues, especially those locations still conducting their own retirement counseling. He was informed that another letter was sent to locations in October informing them that they would continue to have access to AYSO until it was replaced by the new system, UCRAYS. CUCFA representative Kiskis also stated that he received incorrect information from Fidelity regarding his first minimum required distribution (MRD). He said that information on Fidelity's website regarding MRDs is scant and needs improvement. Board member Fehr stated that comprehensive information regarding MRDs is important to all employees, regardless of age. Manager Swanson responded by noting that a MRD factsheet exists, although it is not easy to find. She stated that Vendor Relations Management would redesign the UC/Fidelity website and provide more information on MRDs.

John Karlik from DANR/Cooperative Extension noted that future market returns are expected to be lower and asked how UCRS intends to deal with such future returns. He was told that his question would be addressed by CIO Bachher as part of the CIO report a bit later in the meeting.

APPROVAL OF THE MINUTES: Chair Brownstone called for the approval of the minutes from the Board meeting of June 22, 2018. After noting a typo, the minutes were approved by acclamation.

COMMENTS FROM THE CHAIR: The Chair began by introducing and welcoming the Board's two new members, Jo Mackness and Dr. Caroline Kane. Jo Mackness, who is the Interim Assistant Vice Chancellor and Chief Human Resources officer at UCB, is a presidential appointee to the Board, replacing David Odato. She has over twenty years of Human Resources experience and an under-graduate degree from UCLA and an MBA from UCB. Dr. Caroline Kane is a new ex-officio member of the Board by virtue of becoming the new Chair of CUCEA, effective July 1, 2018. She is a Professor Emeritus of Biochemistry and Molecular Biology from UCB and earned her PhD from UCB.

OFFICE OF THE CHIEF FINANCIAL OFFICER – BUDGET UPDATE: Operating Budget Director Cain Diaz provided the budget update**.** He noted that for fiscal year (FY) 2018/19, UC received $350 million in new state funding, of which $252 million is temporary and $98 million is permanent funding. The additional funding allowed UC to avoid a tuition increase and enroll more undergraduate students, use Proposition 56 funds to enroll more medical residents, and partially address facilities issues. He stressed that the temporary, one-time funding would not fully support the cost of the additional undergraduates during their expected four-year enrollment. With respect to the FY 2019/20 budget, he indicated that UC would be asking for a 3.75% base budget increase to accommodate additional enrollment without resorting to a tuition increase. He also indicated that UC would be looking for additional (ideally permanent) funding to cover mandatory retirement contributions and salary increases for policy-covered staff. Finally, UC would be requesting additional funding for improving graduation rates. The use of such funding, if granted, would be at the discretion of each campus. For example, one location could choose to improve graduation rates by hiring more faculty while another might invest in technology.

CHIEF INVESTMENT OFFICER – REPORT: Chief Investment Officer (CIO) Bachher began by addressing questions raised during the public comment period concerning (1) UCRP's ongoing asset allocation in view of expected market volatility and lower returns and (2) UCRP's exposure to real estate. He stated that it is difficult to predict market returns amid periods of volatility so he prefers to remain a bit conservative by holding cash. During the last year, he stated that UCRP was overweight in cash, but also noted that cash holdings were invested in the UC Short Term Investment Pool (STIP) that provided a better return than most bonds. He conceded, however, that UCRS Advisory Board members and others had expressed concern over holding too much cash and that he has recently reduced UCRP's cash holdings. He indicated that he is comfortable with UCRP's current asset allocation of roughly 53% equities, 22% bonds, 5% cash and 20% other investments, which includes some real estate. He indicated that UCRP does not have the same exposure to real estate as some other pension funds. However, UCRP is better funded than most pension funds and he prefers to balance returns with risk. He also noted that a significant investment in real estate could potentially result in a liquidity problem for a pension fund. He concluded by noting that he remains cautious and does not wish to immediately invest too much of UCRP's cash into other investments that could be locked-in for many years. He stated that the Regents agree with his approach.

Director Merz provided an overview of the Retirement Savings Program (RSP), noting that the RSP had $25 billion in assets, with the 403(b) Plan accounting for 71%, the Defined Contribution Plan accounting for 18%, and the 457(b) Plan accounting for 11% of the assets. He noted that $9.2 billion was invested in UC Pathway (i.e., target date) funds, $14.1 billion in other UC Core funds and $1.7 billion invested through the Brokerage link. He then summarized changes that occurred over the past two years that reduced RSP costs by almost $8 million, such as updating the approach to management fees and institutionalizing funds. He also mentioned actions that improved investor comprehension, such as white-labeling fund names. He concluded by summarizing future actions under consideration for the RSP, such as offering an annuity feature, adding some socially conscious investment options, and gradually increasing equity amounts in the UC Pathway funds.

ITEM A. UCRP – ANNUAL ACTUARIAL VALUATION REPORT AS OF JULY 1, 2018 AND PREVIEW OF EXPERIENCE STUDY: For the benefit of the new members, Manager Reicher explained the concept of the annual actuarial valuation process, describing it as a check-up comparing UCRP's assets to its liabilities. He then described the purpose of the Experience Study, which occurs every 3-5 years, as a comparison of the UCRP's actual experience versus its assumptions.

Consulting Actuary Angelo proceeded to summarize the actuarial valuation report highlights. He noted that UCRP had a market value return of 7.8% and an actuarial value return of 7.9% for the last fiscal year (FY), exceeding UCRP's assumed rate of return of 7.25%. He also mentioned that UCRP's funded ratio increased from 85% to 87%, while the unfunded liability decreased from $11.08 to $10.3 billion. He stated that UCRP received $169 million from the state as well as $392 million in transfers (borrowed) from the STIP. These monies, along with employer and employee contributions, resulted in full funding of UCRP in line with policy for the fiscal year. He briefly explained the concept of five-year smoothing and concluded by summarizing various charts that illustrated projections of UCRP's future funded status under various scenarios and market returns. In particular, he cited slides showing that Savings Choice participation has little impact on UCRP's funded status due to the UC-paid Savings Choice surcharge that is applied towards UCRP's unfunded liability.

Turning to the Experience Study, actuary Angelo noted that the study is a review of both demographic and economic assumptions. Demographic assumptions include rates of retirement, disability, mortality and termination. Economic assumptions include price inflation, real wage inflation, salary increases and investment return. He concluded by noting that the current experience study is for the period from July 2014 through June 2018 and any adopted assumption changes will be used in the next actuarial valuation of UCRP.

ITEM B. UCRP – LUMP SUM CASHOUT REPORT: Manager Ricks began by explaining that the Lump Sum Cashout (LSC) is the actuarially equivalent of a member's lifetime basic retirement income, including assumed cost of living adjustments (COLAs). He then provided a summary of the LSC statistics, noting that LSC elections increased by 7% and the average dollar amount of LSC payments increased by 8% from FY 2016/17. However, he stated that the overall LSC take rate remained consistent at 20% annually. He also noted that the LSC form of distribution remained consistent; 26% of participants requested a direct payment, while the remaining 74% requested either a full rollover or a combination of rollover and direct payment. He closed by noting that 71% of participants who requested an LSC were not eligible for UC retiree health coverage.

ITEM C. UCRP – DISABILITY INCOME REVIEW – UPDATE: Manager Ricks stated that the RASC established a co-sourcing partnership with Liberty Mutual (now Liberty Life Assurance Company, a Lincoln Financial Group Company) in 2013 to manage the medical review of UCRP disability income cases more efficiently. The process has been streamlined so that a member works with a single case manager at Liberty for the medical management of both voluntary, employee-paid long-term disability and UCRP disability income claims. Due to active case management, processing time has been halved and the number of UCRP disability income cases has been reduced by 31%. Additionally, the annual cost for UCRP disability income has been reduced by 14%, from $35.2 million to $30.3 million. In response to a questions on (1) why the disability application approvals decreased significantly from FY 2015 to FY 2016 and (2) whether the number of complaints have increased or decreased during this co-sourcing partnership, Manager Ricks indicated that he would have to research these questions and respond at a later date.

ITEM D. UCRP – UPDATED METHODS FOR DESIGNATING A DOMESTIC PARTNER: Manager Sylva began by noting that, effective January 1, 2019, UC will expand eligibility for UC-sponsored health & welfare benefits to all opposite gender domestic partners of UC employees, retirees and disabled members so that one partner no longer need be at least age 62 and eligible for Social Security. The health and welfare eligibility provisions for opposite gender domestic partners will then align with those of same gender domestic partners, and with UCRP rules already in place that treat all domestic partners, regardless of gender, the same for purposes of UCRP survivor benefits.

He then described the current, separate practices for adding a domestic partner for purpose of UC health and welfare benefits versus naming a domestic partner for potential survivor benefits under UCRP. For health and welfare purposes, there is a family member eligibility verification (FMEV) process where a member submits documentation to an outside vendor. For naming a domestic partner under UCRP, a member must separately submit certain documentation directly to UC prior to his/her retirement (or death, if prior to retirement). Manager Sylva indicated that, effective January 1, 2019, a domestic partner verified through the FMEV process for UC-sponsored health and welfare benefits will automatically become the UCRP member's domestic partner under UCRP. He noted that separate documentation must still be submitted to UC for naming a domestic partner for purposes of UCRP under certain circumstances, such as when both partners are UCRP members and each are enrolled separately in UC-sponsored health and welfare benefits. He concluded by stating that naming a domestic partner under UCRP does not automatically make the domestic partner eligible for survivor benefits; they must still meet all the survivor eligibility provisions.

ITEM E. UCRP – REDWOOD RETIREMENT ADMINISTRATION RECORDKEEPING SYSTEM – UPDATE: In response to questions raised at the Board's June 2018 meeting, Executive Director Schlimgen stated that while UCOP issues 71,000 electronic pension distributions per month, it has only received three reported cases of identity theft in which a retiree's pension payment was re-routed to an unauthorized bank account (i.e., stolen). He indicated that UC's insurance has reimbursed the stolen pension payments for all three affected retirees. He concluded by noting that procedures have been put in place to help prevent such identity theft in the future; until the AYSO replacement (UCRAYS) with multi-factor authentication is implemented, the RASC will make outbound calls for all deposit changes (both on-line and paper) to verify that the change is being requested by the retiree.

Director Cheung-Hill addressed a comment made during the public comment period. She noted that UCOP has listened to and acknowledged comments from all UC stakeholders with respect to potential data disruptions resulting from the Redwood project. As mentioned earlier, she noted that all locations will continue to have access to AYSO and other data until the Redwood retirement recordkeeping systems and the AYSO replacement (UCRAYS) are in place. She then proceeded to summarize the Redwood timeline that had been distributed to the Board members. She stated that the main Redwood retirement recordkeeping system is still scheduled to go live in March 2019 but that UCRAYS would not go live until the summer of 2019. She noted that, unlike AYSO, UCRAYS would only contain retirement information. She also indicated that UCRAYS would incorporate a multi-factor authentication process for requested changes. She concluded by stating that additional Redwood testing needs to be performed and communications need to be developed for educating retirees on ways to protect their UCRAYS accounts and passwords. Director Ellen Lorenz then summarized the various trainings for UCOP personnel that will be undertaken prior to Redwood going live in March 2019. She also warned that she expects RASC service levels to drop slightly during the first few months that RASC staff are working with the new Redwood retirement recordkeeping system.

ITEM F. RETIREMENT ADMINISTRATION SERVICE CENTER – UPDATE: Director Lorenz summarized the FY 2017/18 RASC statistics for the Board. She noted that while calls to Customer Care decreased by 7% from the previous fiscal year (FY), there was a 4% increase in retirement elections processed. She also noted that that 90% of customers indicted that they were satisfied (or more than satisfied) with service they received from RASC, a 1% increase from the previous year. She mentioned that during the past FY, over 2,200 faculty and staff attended on site, in-person retirement presentations at the locations and another 500 were reached via monthly systemwide retirement webinars. In conclusion, she reminded the Board that RASC had contracted with International Customer Management Institute (ICMI) in 2016 to improve the RASC customer experience. She was happy to announce that ICMI would be at UCOP in January 2019 to perform the final assessment for awarding the RASC with the ICMI site certification. If awarded, the RASC will be the first California governmental agency to achieve ICMI site certification.

ITEM G. UCRS – AUDITED ANNUAL FINANCIAL REPORT FOR FISCAL YEAR 2017-2018: Director Olson noted that the primary UCRP and RSP financial figures had been presented as part of the CIO report and annual actuarial valuation item. He noted some changes to the annual financial report for the last FY, such as combining UCRP and the PERS Plus 5 Plan for reporting purposes, which saved on audit costs. He also noted that some of the financial reporting had been streamlined.

ITEM H. RETIREMENT SAVINGS PROGRAM – OPERATION AND EDUCATION REPORT: Manager Swanson began by noting that the RSP had 327,866 unique participants with 55% of active participants making voluntary contributions. However, she noted that participation rates tend to spike during the third quarter of each year. With respect to retirement readiness, she indicated that approximately 62% of career employees were on track to achieve an income replacement of 80% from the combination of their UCRP benefit and RSP assets (not including Social Security benefits). She then mentioned that the myucretirement.com site would be updated to make it less RSP centric and designed to serve employees during the different stages of their UC career.

ITEM I. RETIREMENT SAVINGS PROGRAM – DISCUSSION OF ADDING A ROTH FEATURE TO THE 403(b) PLAN: The Chair framed the discussion for the item, noting that contributions to a Roth feature would be made on an after-tax basis but there would be no taxes on either contributions or earnings upon distribution. He indicated that tax rates are likely to increase in the future and that a Roth feature for the RSP/403(b) would be very beneficial for younger employees. He also noted that the Academic Senate had requested a Roth feature as far back as 2012, at which time they were informed that a RSP Roth feature could be added when the UCPath conversion was completed. The Chair indicated that the Faculty

Welfare's Task Force on Investment and Retirement (TFIR) had recently requested that Director Merz and Manager Swanson look into implementing a RSP Roth feature as soon as possible.

Manager Swanson explained that a RSP Roth feature could not be added until the UCPath payroll conversion was completed, which would not be until late 2019. She also clarified that Roth earnings are tax-fee only if distributed five or more years after the participant established the Roth and if the participant is at least 59 ½ years of age. She then mentioned concerns that adding another RSP benefit could run counter to efforts to simplify the RSP benefits. She noted that the Retirement Choice Program implemented in July 2016 has caused confusion for many new members and added additional work and complexity for location benefits staff. She fears that adding a RSP Roth feature so soon after implementing the Retirement Choice program may overwhelm new employees and discourage them from enrolling in the RSP at all. She also noted that the City of San Diego added a 457(b) Roth feature and that participation has been very low. A brief discussion ensued in which the Chair, Vice Chair and other Board members stated that the addition of a RSP Roth feature would not add undue confusion for employees. Moreover, they felt that the benefits of a Roth feature outweigh any additional complexity or burden on location benefits staff; a burden that they felt was temporary in nature. They asked Hyun to continue to research the feasibility of a RSP Roth feature and, absent any significant obstacles, to implement one shortly following the completion of the UCPath conversion.

The meeting adjourned at 1:56 p.m.