UCRS Advisory Board

Meeting of June 22, 2018

AGENDA ITEM B

UCRS - Cost-of-Living Adjustment for 2018 and Measurement of Annuitant Purchasing Power

July 1, 2018 COLA

The July 1, 2018 annuitant Cost-of-Living Adjustment (COLA) for the University of California Retirement Plan (UCRP) and the UC-PERS Plus 5 Plan is based on the February 2017 to February 2018 increase in the Consumer Price Index (CPI) for All Urban Consumers averaged over the metropolitan areas of San Francisco and Los Angeles.

The CPI increase was 3.59%, resulting in July 1, 2018 COLAs as follows:

Retirement Date	UCRP COLA	UC-PERS Plus 5 COLA
On or before July 1, 2007	2.00%	2.00%
July 2, 2007 up to and including July 1, 2008	2.30%	N/A
July 2, 2008 up to and including July 1, 2017	2.00%	N/A

Eligible UCRP members who separate from active service no later than June 28, 2018 and retire on or after July 1, 2018 will have their Highest Average Plan Compensation (HAPC) increased by 2.00%.

COLA Methodology

UCRP provides an annual COLA that generally matches the increase in the CPI up to 2%, plus 75% of the CPI increase in excess of 4%, to a maximum COLA of 6%. Effective July 1, 2011, this methodology is also applied to determine the COLA for the UC-PERS Plus 5 Plan. The COLA is payable to the extent that the UC-PERS Plus 5 Plan has sufficient funding to pay the increased benefits as of the previous July 1st. Since the funded ratio as of July 1, 2017 was 223.5%, the full annual COLA is payable on July 1, 2018.

Each annuitant's COLA percentage for a specific year depends not only on the CPI increase that year, but also on the cumulative increase in the CPI since the Member retired. For this purpose, two banks are maintained, an "inflation bank" and a "COLA bank", which are then used to determine the total COLA amount that an annuitant is entitled to in a given year.

The inflation bank accumulates in years in which the CPI increase is greater than 2%. The inflation bank represents the portion of the cumulative increase in the CPI since the Member's Retirement Date for which the annuitant has not received a COLA. For example, the annual CPI increase as measured in February 2013 was 2.34%, but based on the UCRP COLA formula, the July 2013 COLA was only 2%. The remaining 0.34% is adjusted for compounding, resulting in an inflation bank of 0.33% for UCRP annuitants who were first eligible in July 2013. The inflation bank can be used to increase the COLA that would be payable in years in which inflation is less than 2%. For example, the inflation bank was used to provide UCRP annuitants who retired on or before July 1, 2006, a 2% COLA on July 1, 2014, even though the increase in the CPI average was less than 2%. After awarding the July 1, 2018, COLA, all annuitant with retirement dates prior to July 2, 2017 will have a remaining balance in the inflation bank.

The second bank is the COLA bank. In years in which inflation is less than 2%, the difference between 2% and the CPI increase is accumulated in the COLA bank. The COLA bank represents that portion of the potential COLA which has not been paid to the annuitant due to low inflation. For example, the annual CPI increase as measured in February 2009 was 0.58%. UCRP annuitants who received a 0.58% COLA on July 1, 2009 accumulated 1.42% in their COLA bank. The CPI increase measured in February 2012 was 2.55%. Those UCRP annuitants with nothing accumulated in their COLA bank were entitled to receive a 2.00% COLA on July 1, 2012, based on the formula. However, those annuitants who had a balance remaining in their COLA bank were entitled to receive a COLA above 2.00% up to 2.55%. The annuitants who received a 0.58% COLA on July 1, 2009 still had the 1.42% accumulated in their COLA bank and were entitled to receive a 2.55% (2% + 0.55%) COLA on July 1, 2012. After awarding the July 1, 2018, COLA, there are no annuitants with a balance in the COLA Bank.

Both banks accumulate from the Member's initial eligibility for a COLA. Therefore, when economic conditions warrant using either of the banks, it is possible to pay different annual COLA amounts in the same year to different Retired Member groups depending on the year in which the Members retired and the resulting amounts in the inflation bank and COLA bank. Attachment 1 shows the current level of the COLA and inflation banks as they apply to each group of UCRP annuitants, just after the July 1, 2018 COLA is credited. Attachment 2 shows the same information for UC-PERS Plus 5 Plan annuitants.

Measurement of Annuitant Purchasing Power – UCRP Annuitants

Once the annual COLA is determined, the "purchasing power" of annuitants' benefits may then be measured. Since the 2018 COLA amount at most matches or is generally less than the actual increase in the CPI, purchasing power has either remained the same or decreased slightly from last year. Attachment 1 shows that purchasing power remains above 75% for all annuitants as of July 1, 2018.

Historically, the Regents has striven to protect annuitants' benefits from being significantly eroded by inflation. However, this is not a guaranteed contractual benefit. Rather, in February 1988, the UCRS Advisory Board passed a resolution indicating its intent to recommend, from time to time and, subject to the availability of funds, adjustments to approximate a 75% minimum level of purchasing power for UCRP annuitants. One-time "ad hoc" COLAs were given in January 1986 and July 1988 to restore annuitants' purchasing power to a 75% level. In January 1991, an ad hoc COLA was given to restore

retirement benefits to a floor of 80% of purchasing power and in January 2001 another ad hoc COLA was given to restore retirement benefits to a floor of 85% of purchasing power. The 85% level was recommended so that it would not be necessary to provide additional ad hoc COLAs as frequently to restore the 75% purchasing power level.

Measurement of Annuitant Purchasing Power – UC-PERS Plus 5 Plan Annuitants

Unlike UCRP, the Regents originally approved the provisions of the UC-PERS Plus 5 Plan to specifically exclude an annual COLA provision, even though these annuitants have received periodic COLAs on their primary retirement benefit from CalPERS. Prior to July 1, 2011, ad hoc COLAs of 25% on July 1, 2002 and 15.19% on April 1, 2011 were given to restore the purchasing power of these annuitants' benefits at the time to 96% and 91% respectively. The April 1, 2011 ad hoc COLA restored the purchasing power of PERS Plus 5 Plan benefits to a level equivalent to that for UCRP members who retired at the same time. Attachment 2 shows the retained purchasing power of PERS Plus 5 Plan annuitants is approximately 90% as of July 1, 2018.

Attachments