UCRS Advisory Board

Meeting of June 20, 2014

AGENDA ITEM J

UCRS – Cost-of-Living Adjustment for July 2014 and Measurement of Annuitant Purchasing Power

July 1, 2014 COLA

The July 1, 2014 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 average of the increases in the Consumer Price Index (CPI) for All Urban Consumers in the metropolitan areas of San Francisco and Los Angeles from February 2013 to February 2014. This average CPI increase was 1.50%; therefore, the July 1, 2014 COLA will be:

Retirement Date	UCRP COLA	UC-PERS Plus 5 COLA
On or before July 1, 2006	2.00%	2.00%
July 2, 2006 to July 1, 2008	1.50%	N/A
July 2, 2008 to July 1, 2009	1.98%	N/A
July 2, 2009 to July 1, 2011	2.00%	N/A
July 2, 2011 to July 1, 2012	1.84%	N/A
July 2, 2012 to July 1, 2013	1.50%	N/A

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 UC-PERS Plus 5 Plan has an additional constraint, requiring that plan's funded ratio to exceed 100% as of the previous July 1st in order to award a COLA. The UC-PERS Plus 5 Plan funded ratio for this purpose as of July 1, 2013 was 175.4%.

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, 2014, COLA, all annuitant groups have a balance in the inflation bank, except for the three groups with retirement dates during the period July 2, 2006 through July 1, 2009 and the two groups with retirement dates during the period July 2, 2011 through July 1, 2013.

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.

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 inflation and COLA banks as they apply to each group of UCRP annuitants, just after the July 1, 2014 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 20143 COLA matches or is greater than the actual increase in the CPI, purchasing power has either remained the same or increased slightly from last year. Attachment 1 demonstrates that purchasing power remains above 79% for all annuitants as of July 1, 2014.

Historically, the Regents have 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. “Ad hoc” COLAs were given in January 1986 and July 1988 to restore annuitants’ purchasing power to a 75% level. In January 1991, a one-time ad hoc COLA was given to restore retirement benefits to a floor of 80% of purchasing power and in January 2001 a one-time 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 UC-PERS Plus 5 Plan benefits to a level equivalent to that for UCRP members who retired at the same time. Attachment 2 demonstrates that the purchasing power of UC-PERS Plus 5 Plan annuitants’ benefits is 90.86% as of July 1, 20143.

Attachments