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Office of the President

TO THE MEMBERS OF THE COMMITTEE ON COMPENSATION:

DISCUSSION ITEM

For the Meeting of January 18, 2007

UPDATE ON UNIVERSITY OF CALIFORNIA RETIREMENT PLAN/LOS ALAMOS NATIONAL SECURITY, LLC DEFINED BENEFIT PLAN ASSET TRANSFER

EXECUTIVE SUMMARY

This item summarizes actions that were approved under Interim Authority in December 2006 and the plan amendments that are expected to be proposed as an Action Item in March 2007 to facilitate the transfer of assets and liabilities from the University of California Retirement Plan (UCRP) to the defined benefit plan established by the successor contractor at the Los Alamos National Laboratory (LANL).

Future Action	UCRP amendments to facilitate the final transfer of assets and liabilities to the Los Alamos National Security, LLC (LANS) Defined Benefit Pension Plan (LANS Plan) expected to be proposed for action in March 2007.
Previous Actions	**December 2006:** Under Interim Authority, benefit payments, to the extent attributable to UC service, are authorized to be made to or on behalf of eligible LANS Plan members from UCRP prior to the final transfer of assets and liabilities from UCRP to the LANS Plan. **September 2006:** The Regents revise the authority to transfer UCRP assets granted at the May 2006 meeting and instead permit initial and interim transfers of UCRP assets to satisfy the liquidity needs of the LANS Plan up to a total amount of $50 million. **May 2006:** The Regents authorize the transfer of UCRP assets to the LANS Plan on a monthly basis, but only to the extent necessary to fund benefit claims and administrative expenses under the LANS Plan.
Relevant Policy	Plan document for UCRP

Issues Amendments to UCRP to implement the transfer of UCRP assets and liabilities, as authorized by The Regents, on behalf of former UC employees at LANL who elected to participate in the LANS Plan.

BACKGROUND

In accordance with the terms of UC's former management contract for LANL (Contract W-7405-ENG-36 or Contract) governing the transition of LANL to a successor contractor, UC is required to transfer UCRP assets at a rate sufficient to meet the cash flow requirements of the LANS Plan until the terms of the final transfer of assets and liabilities to the LANS Plan are resolved with the Department of Energy/National Nuclear Security Administration (DOE/NNSA) (Final Transfer). Consequently, at their meeting of May 18, 2006, The Regents authorized the transfer of UCRP assets to the LANS Plan on a monthly basis, but only to the extent necessary to satisfy the plan's liquidity needs. Any UCRP assets transferred, and earnings at the agreed-upon rate, were to be accounted for in the Final Transfer.

Following the May 18, 2006 Regents' meeting, LANS reported that approximately 10,200 active UCRP members employed at LANL had accepted an employment offer from LANS, and approximately 6,500 of those had elected to participate in the LANS Plan, which is designed to be substantially equivalent to UCRP. The actuarial accrued liability for those members electing to participate in the LANS Plan has been estimated by The Regents' actuary, The Segal Company, to be approximately $1.4 billion. Note, however, that the liability for the LANS Plan members as determined under the LANS Plan provisions and the actuarial assumptions and methods used by the LANS Plan's actuary will almost certainly be a different amount because that amount will be determined under different legal requirements established in the Employee Retirement Income Security Act of 1974 (ERISA) that apply to defined benefit plans sponsored by non-governmental entities.

At the September 21, 2006 meeting, at the request of the DOE/NNSA, The Regents authorized an amendment to the methodology approved in May for determining the amount of funds to be transferred from UCRP to the LANS Plan prior to the Final Transfer to better accommodate the ongoing administrative needs of the LANS Plan. It was expected that the transfers would facilitate the timely payment of benefits to former UC employees and their beneficiaries who became entitled to benefits from the LANS Plan prior to the Final Transfer. The changes also were intended to assist the fiduciaries of the LANS Plan to secure more favorable fee arrangements with service providers as well as cover other administrative and related costs payable from the LANS Plan trust. To that end, The Regents authorized an initial transfer of UCRP assets to the LANS Plan as a single sum not to exceed $10 million and, to the extent necessary to address the ongoing administrative needs of the LANS Plan, supplemental interim transfers not to exceed a combined total of $50 million.

Subsequent to the September meeting, LANS reported that, based on advice by its legal counsel, it would not accept assets on a cash flow basis as authorized by The Regents and consistent with UC's obligations under the Contract due to the uncertainties that such transfers might introduce regarding the tax-qualified status of the LANS Plan. Instead, LANS stated, if a LANS Plan member announced his or her intent to retire, the LANS Plan would need to receive the present value of the member's entire accrued benefit as of May 31, 2006, and any assets transferred to fund that benefit could be used only to pay the benefits of the identified member. Since that was outside the scope of the authority delegated by The Regents and the terms of the Contract, no assets have been transferred to date. Also, UC's internal and external counsel have advised against proceeding with the present value transfers until the Internal Revenue Service (IRS) provides a clearer indication of its position on the rules that will apply to the Final Transfer.

Interim Authority Item

LANS recently reported that two LANS Plan members have applied to retire effective December 1, 2006 and that several more members are expected to retire in the following months. In order to pay benefits to retiring LANS Plan members and survivors of deceased members before the Final Transfer, the DOE/NNSA requested that the University consider amending UCRP so that benefits could be paid from UCRP to or on behalf of a LANS Plan Member to the extent attributable to service with UC as of May 31, 2006. The part of the benefit attributable to service with LANS from June 1, 2006 forward would be paid from the LANS Plan. In order to ensure that the LANS retirees could be timely paid on January 1, 2007, the DOE/NNSA's requested changes were presented and approved under the Regental Policy on Interim Authority effective as of December 31, 2006. Thus, UCRP now permits such payments provided the retiree (or the retiree's beneficiary or alternate payee) elects payment in one of the distribution forms available under the LANS Plan and the amount, form and start date is memorialized in the LANL appendix to UCRP. In return, the DOE/NNSA has confirmed in writing that UC's obligations under the Contract with respect to meeting the LANS Plan's cash flow needs have been modified to reflect the interim payment arrangement; costs, expenses, penalties and other losses incurred in connection with such payments will be treated as reimbursable costs; UCRP will receive credit for all such payments, and related earnings, in calculating the Final Transfer amount; the DOE/NNSA will use its best efforts complete the Final Transfer as quickly as possible; and the UCRP plan administrator reserves the right to terminate the interim payment arrangement if the plan administrator determines the arrangement imposes an undue administrative burden on UCRP.

Proposal to Accomplish the Final Transfer

The UC team led by Associate Vice President Boyette, Human Resources & Benefits, continues to hold regularly scheduled discussions by telephone or in person with the DOE/NNSA team led by Roberto Archuleta regarding the appropriate amount of assets and liabilities to be transferred to the LANS Plan and related matters. The legal issues presented by the transaction are complex because the transfer will require moving assets and liabilities from a governmental plan, which is subject to provisions in the Internal Revenue Code and California law, to a private employer plan governed by the extensive statutory regime established by ERISA. Because of the lack of guidance on public-to-private plan transfers, and the significant fiduciary obligations at stake, the UC-DOE/NNSA teams have agreed to seek guidance on the structure of the transaction from key regulatory agencies, including the

IRS, the Department of Labor and the Pension Benefit Guaranty Corporation, so that the transfer can be accomplished as quickly as possible. An early resolution will help LANS satisfy the LANS Plan's minimum funding obligations under ERISA, and thereby avoid significant economic penalties. UCRP's interests will be served by having the LANS Plan assume the obligation to pay the benefits accrued under UCRP as quickly as possible, and thereby make the interim payment arrangement no longer necessary.

The teams have targeted April 2, 2007 as the proposed date for the Final Transfer. In order to meet that date, UC and the DOE/NNSA will need to resolve as quickly as possible the amount of assets and liabilities to be transferred to the LANS Plan and a number of related issues. The teams agreed to make their best efforts to come to agreement in January on the proposed methodology for determining the asset/liability split for the Final Transfer so that UC will have time to consult with faculty leadership regarding the specifics and both teams can discuss the proposal with their various constituencies. Such discussions will also cover the following elements:

- The Contract formula states that UCRP will retain sufficient assets to cover all liabilities associated with the benefits of individuals employed at LANL while under UC management who retired or became inactive UCRP members prior to June 1, 2006 (Retained Segment). That formula will be followed to the maximum extent possible, but adjusted as may be necessary to satisfy concerns of the regulators (i.e., the IRS, the Department of Labor, and the Pension Benefit Guaranty Corporation).

- The DOE/NNSA will confirm its existing obligation to fund any shortfalls attributable to the Retained Segment in clear and unambiguous terms.

- The Retained Segment will remain in UCRP, provided, however, that commitment is co-extensive with the DOE/NNSA's commitment to be financially responsible for maintaining the funded status of the Retained Segment. Should DOE/NNSA be either unable or unwilling to meet its financial responsibility, UC will take whatever actions with respect to the Retained Segment that are prudent and necessary with respect to all UCRP members.

- The Final Transfer is anticipated to take place no later than April 2, 2007, subject to potential adjustment to reflect regulatory requirements identified subsequent to the transfer.

- The Final Transfer will be in-kind to the maximum extent practicable in order to minimize transaction costs and will mirror the UCRP portfolio, as determined by the Office of the Treasurer, at the time of transfer.

- UC will provide an annual actuarial valuation of the Retained Segment at the DOE/NNSA expense.

- The agreement will be subject to regulatory review, and the final amounts of transfer, and enforceability of terms, are subject to adjustment to conform to the orders of such regulatory entities, or in the event of litigation, to the orders of a court of competent jurisdiction.

Next Steps

It is expected that the proposal for the Final Transfer will be presented to the Committee on Compensation as an Action Item at the March 2007 meeting of The Regents. The Office of the Treasurer and Associate Vice President Boyette, Human Resources & Benefits, will continue to engage in consultation with faculty leadership and meet with the various UC constituencies to discuss the elements of the proposal to implement the Final Transfer. UC will take appropriate action concerning proposed changes that may trigger notice, consultation, and meeting and conferring obligations under the Higher Education Employer-Employee Relations Act.