

Office of the President

TO MEMBERS OF THE SPECIAL COMMITTEE ON COMPENSATION:

ACTION ITEM*For Meeting of March 16, 2006***CONSIDERATION OF FUTURE REINSTATEMENT OF CONTRIBUTIONS TO THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN****EXECUTIVE SUMMARY**

The President recommends that the Special Committee on Compensation recommend to The Regents that The Regents update the funding policy for the University of California Retirement Plan (UCRP or Plan) to incorporate a long-term targeted funding level of 100 percent; authorize the reinstatement of contributions effective as of July 2007, subject to funding and completion of the budget process; and provide for a multi-year contribution strategy under which contribution rates will increase gradually over time to 16 percent of covered earnings, based on UCRP's current normal cost.

Previous Actions: **October 1990:** The Regents suspended all University contributions to UCRP and redirected part of the UCRP member contributions to the Defined Contribution Plan (DC Plan), but reserved the right to reinstate member contributions in UCRP as necessary to maintain funded levels.
July 1993: The Regents suspended the remaining portion of UCRP member contributions.

Relevant Policies: UCRP and DC Plan documents.

Future Action: An advisory group to the President is evaluating alternative strategies for the reinstatement of contributions. It is anticipated that in May 2006, specific recommendations for action by The Regents will be made on the reinstatement of contributions to be effective July 2007, subject to funding and completion of the budget process.

Issues: • Sustaining the long-term viability of UCRP requires maintaining the Plan at or near a full funding level.
 • Barring extraordinary market gains in excess of UCRP's assumed rate of investment return, University and member contributions will be necessary to maintain the fully funded status of UCRP.
 • Implementation is subject to collective bargaining requirements, as applicable, and the availability of funding.

RECOMMENDATION

The President recommends that the Special Committee on Compensation recommend to The Regents that The Regents update the funding policy for UCRP to provide for:

- (1) A targeted funding level of 100 percent over the long term, and for University and UCRP member contributions at the rates necessary to maintain that level within a range of 95 percent to 110 percent.
- (2) A multi-year contribution strategy under which contribution rates will increase gradually over time to 16 percent of covered earnings, based on UCRP's current normal cost.
- (3) The resumption of UCRP contributions effective July 2007, subject to funding and completion of the budget process.

An advisory group to the President is evaluating alternative strategies for the reinstatement of contributions. It is anticipated that in May 2006, specific recommendations for action by The Regents will be made on the reinstatement of contributions, to be effective July 2007, subject to funding and completion of the budget process, to include:

- (1) A year-by-year schedule of total UCRP contributions through 2013.
- (2) The specific cost sharing of these contributions between the University and UCRP members through 2010.

The goal is for The Regents to take action on the recommended reinstatement of contributions strategy by May 2006. Implementation of member contributions is subject to available funding and collective bargaining requirements, as applicable.

BACKGROUND

Contribution History

Prior to November 1990, both University (employer) contributions and member (employee) contributions to UCRP were required. In 1990, The Regents suspended University contributions to UCRP after the actuaries and the auditors confirmed that UCRP was adequately funded to provide plan benefits for many years into the future. At the same time, The Regents directed that contributions from members participating in Social Security, and a portion of the contributions from members not participating in Social Security, and from Safety members, be redirected to individual accounts in the DC Plan, subject to The Regents' reservation of the right to reinstate such contributions in UCRP to maintain the Plan's funded status. Under the DC Plan, contributions from employees are held in accounts and invested at an employee's direction. DC Plan accumulations are available for distribution starting at retirement or termination of employment. In July 1993, The Regents suspended the remaining portion of UCRP contributions from members without Social Security and from Safety members.

The suspension of University contributions to UCRP and the redirection of UCRP member contributions to the DC Plan have continued unchanged since the early 1990s. The rates of member contributions to the DC Plan vary by membership classification, as shown in the following table.

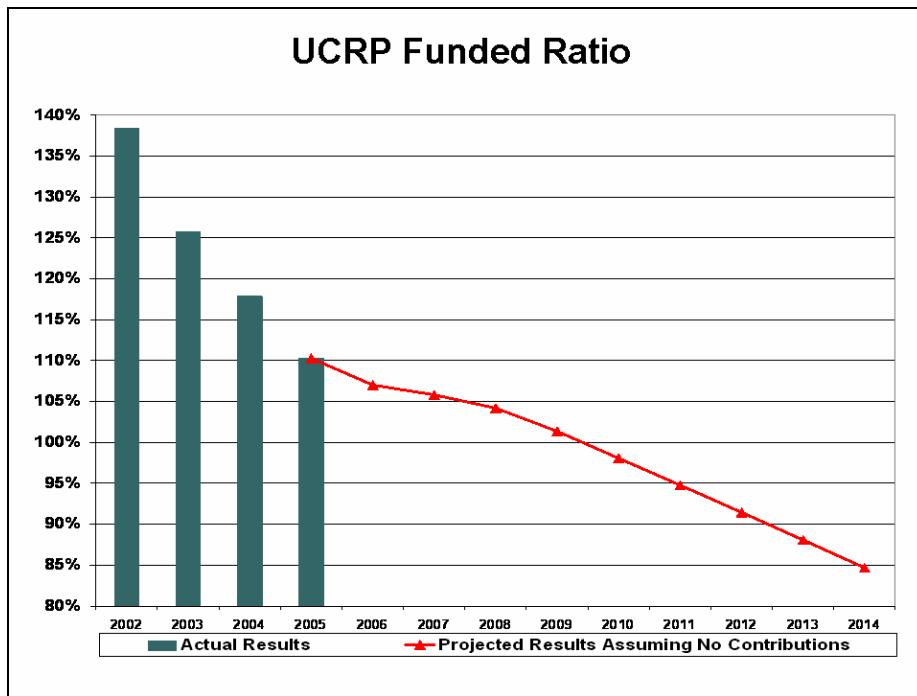
Member Contributions Redirected into the DC Plan since November 1990

Member Classification	Contributions as a % of covered pay below the Social Security Wage Base (\$94,200 for 2006) ¹	Contributions as a % of covered pay above the Social Security Wage Base (\$94,200 for 2006) ¹
With Social Security	2%	4%
Without Social Security	3%	3%
Safety	3%	3%

UCRP Funded Status

At the November 2005 meeting, the Regents were presented with the results of the July 1, 2005 UCRP annual actuarial valuation by The Segal Company, The Regents' actuary. This report illustrated that the funded status of UCRP is projected to decline well below 100 percent unless contributions are restarted or extraordinary market gains occur. A 100 percent target funded status for UCRP over the long term will sustain the viability of the Plan.

¹All contributions are reduced by \$19 per month.



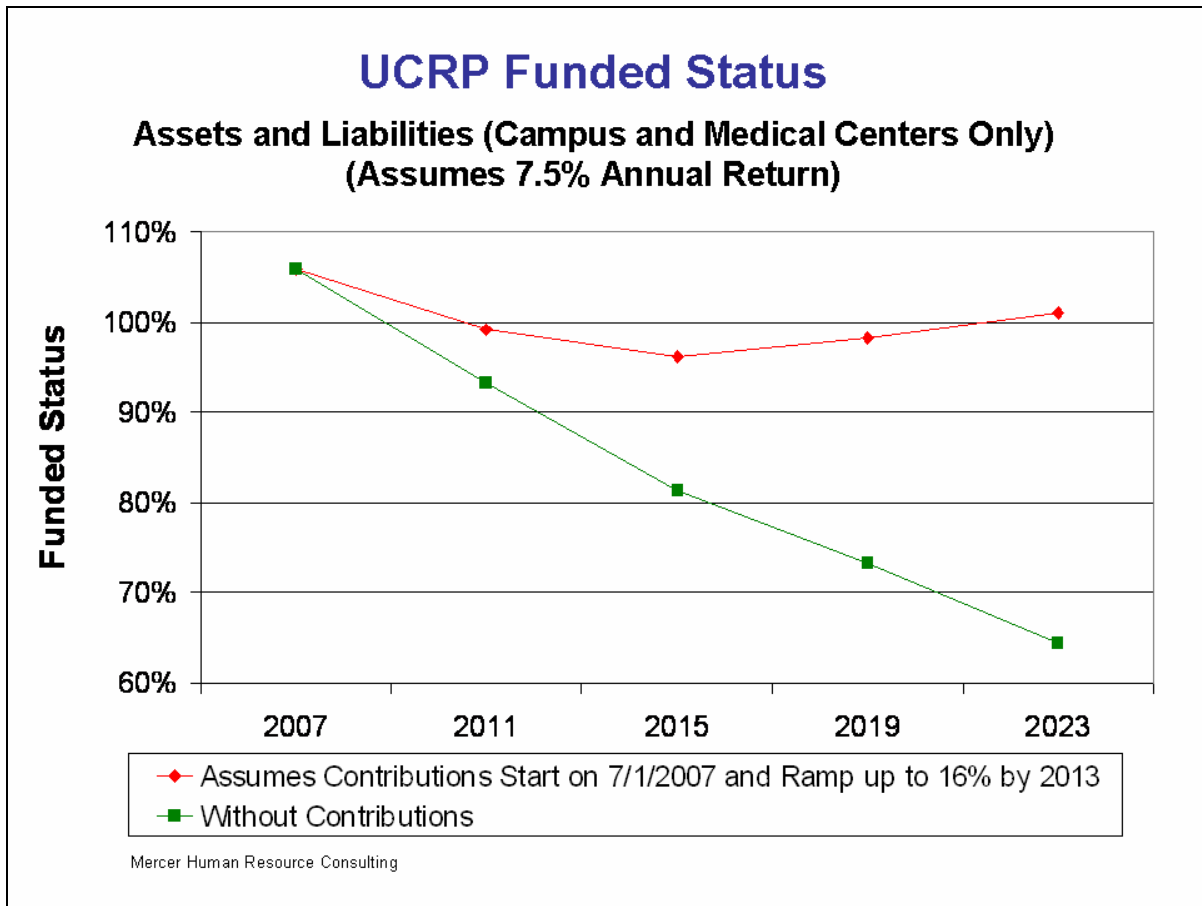
Recommended Funding Policy

The Regents' action in October 1990 did not include specific guidelines as to when University contributions should be resumed or when the redirected member contributions should be reinstated in UCRP. To clarify The Regents' intent, the President requests that the Special Committee on Compensation recommend that The Regents update its funding policy to incorporate, effective July 2007, a target funded status for UCRP of 100 percent over the long term, with University and UCRP member contributions established at the rates necessary to maintain that level within a range of 95 percent to 110 percent if actuarial expectations are met. The normal cost¹ of UCRP, as determined by the UCRP actuarial valuation report as of July 1, 2005, is 15.9 percent of covered payroll.² The President's recommendation proposes that contributions gradually increase to 16 percent of UCRP covered payroll by July 2013. The following chart illustrates the projected impact of this proposal.³

¹ The "Normal Cost" of the Plan, as defined under ERISA §3(28), is the annual amount, expressed as a percent of payroll (the "Normal Cost Rate") that must be accrued over the total career of each employee to provide fully for future UCRP benefits.

² 15.9% represents the Plan's normal cost calculated as of the middle of the 2005-2006 plan year.

³ These projections include the impact of catch-up pay increases and are based on employees hired before July 1, 2007.



An advisory group to the President is evaluating alternative reinstatement of contribution strategies. It is anticipated that in May 2006 specific recommendations for action by The Regents will be made on the reinstatement of contributions strategy that will be implemented effective July 2007, subject to funding and completion of the budget process, to include a year-by-year schedule of total UCRP contributions through 2013 and the specific cost sharing of these contributions between the University and UCRP members through 2010.

Once implemented, the UCRP contribution strategy will be a multi-year plan that will not be changed unless the funded status of UCRP increases or decreases significantly because investment returns, salary, or other factors differ significantly from actuarial expectations. If further analysis indicates that such variances are likely to cause the projected funded ratio of UCRP to fall outside a range of 95 percent to 110 percent for an extended period of time, the contribution strategy may be revised to the extent necessary to maintain the long-term viability of UCRP.

Guided by Total Remuneration Philosophy

The recommended funding policy was developed in consultation with an advisory group on retirement benefits that includes representatives from The Board of Regents and the Office of the President, and a member of the Academic Senate. Human Resources/Benefits has engaged Mercer Human Resource Consulting to serve as the lead consultant for advising the University in this process, with actuarial assistance provided by The Segal Company.

The advisory group is considering the strategic positioning of the University's retirement programs as part of the competitive total remuneration offered to faculty and staff. Regents' Item RE-61, adopted in November 2005, laid out the University's philosophy for total remuneration (defined as cash compensation, health and welfare benefits, pension benefits, and retiree health): "Our strategy is to attract and retain the highest quality academic, managerial, and staff talent by offering competitive total remuneration." With this philosophy as a key driver, a number of principles came out of the consultation with the advisory group to guide the development of the proposed funding policy and the consideration of alternative reinstatement of contribution strategies, including the following:

- Maintain current level of UCRP benefits for existing UCRP members.
- Target the UCRP funded level of 100 percent over the long term, and establish University and UCRP member contributions at the rates necessary to maintain that level within a range of 95 percent to 110 percent if actuarial expectations are met.
- Increase contributions over time to the Plan's Normal Cost.
- Share costs between the University and its employees.
- Employ a uniform UCRP contribution strategy for all existing employees (appropriately recognizing the differing benefit and contribution levels for safety members).
- Maintain total remuneration at market-competitive levels.
- Where possible, mitigate affordability concerns with an integrated approach to changes in total remuneration.
- Periodically review the UCRP contribution strategy and make adjustments if significant changes in funded status occur.

Future Action

The recommended funding policy is necessary to sustain the long-term viability of the Plan. The funded status of the Plan will continue to be monitored by reviews of the annual valuations performed by the actuary to UCRP that are presented to the Regents in November each year.

An advisory group to the President is evaluating alternative reinstatement of contributions strategies. It is anticipated that in May 2006, specific recommendations for action by The Regents will be made on the reinstatement of contributions to be implemented effective July 2007, subject to funding and completion of the budget process, to include:

- A year-by-year schedule of total UCRP contributions through 2013.
- The specific cost sharing of these contributions between the University and UCRP members through 2010.

As previously stated, the goal is for The Regents to take action on the recommended reinstatement strategy in May 2006. UCRP members will receive ample notice as the timing and level of UCRP contributions are determined. The University 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.