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Office of the President

TO MEMBERS OF THE FINANCE AND CAPITAL STRATEGIES COMMITTEE:

ACTION ITEM

For Meeting of March 14, 2018

APPROVAL OF UNDERGRADUATE NONRESIDENT SUPPLEMENTAL TUITION AND ADJUSTMENTS OF THE EMPLOYER CONTRIBUTION TO THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN

EXECUTIVE SUMMARY

The Regents are being asked to approve two components of the University of California operating budget plan for 2018-19: a proposed increase to undergraduate Nonresident Supplemental Tuition (NRST) and a proposed rescission of previously approved increases to employer contribution rates to the University of California Retirement Plan (UCRP). Other recommended actions related to the 2018-19 budget plan will be presented to the Board in May. The Regents are asked to approve the two actions addressed in the current item in March because ongoing discussions with the State are unlikely to change the need for either action, and campuses and students would be better equipped to plan for 2018-19 if they had greater clarity about the level of undergraduate NRST and the budgetary impact of UCRP contributions effective 2018-19.

Both requested actions are important components of the University's 2018-19 budget plan, which represents a balanced funding proposal to support expanded access for California resident students, enhance UC affordability for students with financial need, and allow for investments in student success such as improving the student-faculty ratio, increasing course availability, expanding access to student mental health services, and addressing the University's most critical capital needs. The plan also addresses funding needs associated with employee and retiree health benefits, faculty and staff compensation, and employer contributions to the University of California Retirement Plan, among other important areas.

RECOMMENDATION

The President of the University recommends that the Finance and Capital Strategies Committee recommend that the Regents:

A. Approve the increase in undergraduate Nonresident Supplemental Tuition shown in Display 1, to be effective with the 2018-19 academic year.

B. Rescind the prior Regents' approval in the July 2017 action, *Authorization to Increase the University Employer Contribution Rate and Make Additional Contributions to the University of California Retirement Plan*, to increase the University's contribution rate for the Campus and Medical Centers segment of the University of California Retirement Plan ("UCRP" or "Plan"), effective July 1, 2018, to 15 percent (from 14 percent) for all member classes and tiers, other than Tier Two and 7.5 percent (from seven percent) for Tier Two members.[1]

C. Rescind an increase in the employer assessment to seven percent (from six percent) for Savings Choice Participants in the Defined Contribution Plan.

DISPLAY 1: Proposed Increases to Undergraduate Nonresident Supplemental Tuition

	2017-18 Charges	*Proposed Adjustment*	*Proposed % Change*	Charges Effective 2018-19
Nonresident Supplementation Tuition				
Undergraduate	$28,014	*$978*	3.5%	$28,992

BACKGROUND

A broad outline of the University's 2018-19 budget plan for core funds was brought to the Finance and Capital Strategies Committee for discussion in September 2017, and a specific budget plan was presented to the full Board in January 2018. The budget plan represented a balanced funding proposal to support expanded access for California resident students, enhance UC affordability for students with financial need, and allow for investments in student success such as improving the student-faculty ratio, increasing course availability, expanding access to student mental health services, and addressing the University's most critical capital needs.

In January, the Board decided to table full consideration of the 2018-19 budget plan until May. Between January and May, the Board asked for complete presentations of the University's cost structure and financial aid programs. In addition, further discussions with the State were sought in the event that additional levels of State support for the University's budget could avoid the need for increases in student charges that were proposed in the budget plan.

Presentations related to the University's cost structure and financial aid are on the agenda for the March 15, 2018 meeting of the full Board, and discussions between the University, students, the State, and other stakeholders are ongoing. Within this context, the Regents are asked to approve two components of the 2018-19 budget plan – a proposed increase to undergraduate Nonresident

[1] The UCRP member class known as "Tier Two" is a frozen group. As of July 1, 2017, it had three active members.

Supplemental Tuition (NRST) and a proposed rescission of previously approved increases to employer contribution rates to the University of California Retirement Plan (UCRP) – because ongoing discussions with the State are unlikely to change the need for either action, and campuses and students would be better equipped to plan for 2018-19 if they had greater clarity about the level of undergraduate NRST and the budgetary impact of UCRP contributions effective 2018-19. Each component is described in greater detail below.

PROPOSED INCREASE IN UNDERGRADUATE NONRESIDENT SUPPLEMENTAL TUITION

The University's proposed 2018-19 budget plan includes revenue of $34.8 million from a proposed increase of $978 (3.5 percent) in undergraduate NRST. These additional revenues are critical to 2018-19 campus operating budgets. Campuses that are especially reliant on NRST revenue – Berkeley, Los Angeles, and San Diego – are also among the campuses that have seen relative declines in their share of the University's State General Fund appropriation as the University has moved towards a more enrollment-driven model for allocating State support. NRST revenue has helped these campuses bridge that transition. For example,

- At UC Berkeley, revenue from NRST has been used to support the campus's Student Learning Center, which provides academic support and advising to 9,000 Berkeley undergraduates. It has also enabled the campus to invest in the "Common Good Curriculum," expanding access to foundational courses in writing and math as well as high-demand lower-division courses that are critical to students' ability to enter and complete their majors on time.

- At UCLA, State General Funds fell from 64 percent of the core funds that support undergraduate education to 30 percent between 2007-18 and 2016-17. Despite that decline in State funds, UCLA was able to increase seats in primary sections of key undergraduate courses by 26 percent (compared with an overall enrollment increase of 18 percent).

- At UC San Diego, the campus has used NRST revenue to fund a new Teaching and Learning Commons that provides advising support for all students and leverages technology. Other uses include programs to support student diversity and improve graduation rates such as the Chancellor's Associates Scholarship Program, recruitment, outreach, student success coaches, summer on-boarding programs, and alcohol- and drug-free programming and education.

As funding for campus services and programs is shifted to NRST, the need for moderate and predictable increases to that revenue source becomes more important. The University does not expect the State to provide additional support in 2018-19 to buy out the proposed NRST increase of $978 that was included in the University's 2018-19 budget plan.

As a group, nonresident students who are admitted to UC have exceptional academic qualifications, are highly sought by competing institutions, and have multiple offers of admission from which to choose. As a result, campuses have requested greater clarity regarding the level of undergraduate NRST to be charged in 2018-19 prior to the May Regents meeting, by which time students will have already made their enrollment decisions. That clarity would provide a more stable basis for students' enrollment decisions and campuses' planning efforts this spring.

ADJUSTMENT TO THE EMPLOYER CONTRIBUTION TO THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN (UCRP)

Background

At the July 2017 meeting of the Board of Regents, in the *Authorization to Increase the University Employer Contribution Rate and Make Additional Contributions to the University of California Retirement Plan*, the Regents approved increases in the University contribution rate for the Campus and Medical Centers (C/MC) segment of UCRP, effective July 1, 2018, to 15 percent (from 14 percent) for all member classes and tiers other than Tier Two and 7.5 percent (from seven percent) for Tier Two members, and an increase in the employer assessment to seven percent (from six percent) for Savings Choice Participants in the Defined Contribution Plan, to help pay down the UCRP unfunded liability.

The Regents also approved the transfer of funds from the Short Term Investment Pool (STIP) and/or external financing to UCRP in fiscal year (FY) 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22 in amounts equal to the difference between the approved total UCRP contribution and the projected ARC. These transfers will not exceed $500 million in FY 2018-19, $500 million in FY 2019-20, $600 million in FY 2020-21, and $700 million in FY 2021-22.

The University now anticipates that the State will provide only a three percent budget augmentation for the University in 2018-19, which is one percent lower than expected in July 2017. As a result, State funds next year will likely fall short of expectations by over $30 million. While the University continues to discuss State funding proposals that would avoid the need for increasing tuition or the Student Services Fee next year, provide one-time funding for deferred maintenance, and fund enrollment growth, additional funding to fully fund the planned increase in UCRP contributions is not likely. As a result, the President of the University and the Chief Financial Officer recommend maintaining the current employer contribution rate at 14 percent for the C/MC segment of UCRP. Such action will save roughly the same amount for the University in terms of contributions from core funds.

Given the alternatives – not investing in student resources, worsening the faculty salary gap, etc. – rescinding the planned increase in the University's employer contribution is a prudent strategy. The University would, however, remain committed to the goal of bringing the total annual contribution to the "Annual Required Contribution" (ARC) level in each of the next four years. This is consistent with the University's strategy to improve the Plan's funded percentage by augmenting UCRP funding with internal borrowings from STIP to meet the ARC. The University also benefitted this year from strong investment performance that was not yet known when the increase to 15 percent was proposed. This investment performance was more favorable than the 7.25 assumed rate and so improved the funded percentage of UCRP to approximately 85 percent on both a market value of assets basis and on an actuarial (smoothed) value of assets basis as of July 1, 2017.

Projected Financial Impact on the Campus and Medical Center Segment of UCRP

Under the University contribution rate increase to 15 percent beginning July 1, 2018, and including the funds transferred from STIP and/or external financing to UCRP to bring the total annual contribution up to the ARC in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22 as approved by the Regents in July 2017, the C/MC segment was projected to be 90 percent funded by July 1, 2023.

If instead the University contribution rate remains at 14 percent and including the STIP transfers and/or external financing to UCRP approved by the Regents in July 2017 mentioned above, the C/MC segment is still projected to be 90 percent funded by July 1, 2023.

All of the actuarial projections are based on current assumptions, including the 7.25 percent assumed earnings rate. The projections indicate that if the University contribution remains at 14 percent, there will be a $44 million shortfall to fully fund the ARC in the fiscal year beginning July 1, 2018. However, for the three fiscal years from July 1, 2019 through June 30, 2022, the internal transfers needed to fully fund the ARC will be less than the approved “up to” limits even if the University contribution rate remains at 14 percent, as noted in Display 2. This is why the projected funded ratios under both scenarios described above reach 90 percent in the same year.

DISPLAY 2: Projected Utilization of STIP Transfers to UCRP

	FYs With Approved STIP Borrowing			
	2018-19	**2019-20**	**2020-21**	**2021-22**
UCRP Employer Rates: UCRP / Savings Choice	14% / 6%	14% / 6%	14% / 6%	14% / 6%
STIP Transfer Needed to Fully Fund Projected ARC	$ 544	$ 478	$ 486	$ 461
STIP Transfer Amount Approved in July 2017	$ 500	$ 500	$ 600	$ 700
(Projected ARC Shortfall)	$ (44)			
Amount of Approved STIP Transfers Not Needed to Fully Fund Projected ARC		$ 22	$ 114	$ 239

Amounts in $millions
C/MC segment only; July 1, 2017 valuation assumptions including:
7.25% rate of return, 0.7% active population growth, 20% election rate for Savings Choice

Consequently, rescinding the increase in the employer rate from 14 percent to 15 percent would not have a significant impact on the C/MC segment funded percentage over the short term as discussed above.

Related Prior Actions by the Board

March 2016: In the *Recommendation for New University of California Retirement Program*, the Regents approved the Retirement Choice Program effective July 1, 2016 for newly hired faculty and staff and certain rehires and newly eligible employees. Pensionable earnings are limited to the Public Employees' Pension Reform Act (PEPRA) limit, which is $118,775 effective July 1, 2017.

July 2017: The Regents approved the *Authorization to Increase the University Employer Contribution Rate and Make Additional Contributions to the University of California Retirement Plan*, which included:

- Increases in the University contribution rate for the Campus and Medical Centers segment of the University of California Retirement Plan (UCRP), effective July 1, 2018, to 15 percent (from 14 percent) for all member classes other than Tier Two and 7.5 percent (from seven percent) for Tier Two members, and an increase in the employer assessment to seven percent (from six percent) for Savings Choice Participants in the Defined Contribution Plan, to help pay down the UCRP unfunded liability.

- The transfer of funds from STIP to UCRP in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22 in amounts equal to the difference between the approved total UCRP contribution and the ARC. Should STIP have insufficient funds, funds will be transferred from the Total Return Investment Portfolio (TRIP) to STIP. External financing may be obtained in lieu of or in addition to the STIP transfers if it is expected that this option could be accomplished at a lower cost or is more practical for the University. These transfers shall satisfy certain requirements and will not exceed $500 million in FY 2018-19, $500 million in FY 2019-20, $600 million in FY 2020-21, and $700 million in FY 2021-22.

Key to Acronyms

ARC	Annual Required Contribution
CFO	Chief Financial Officer
C/MC	Campus and Medical Centers
FY	Fiscal Year
PEPRA	Public Employees' Pension Reform Act of 2013
STIP	Short Term Investment Pool
UCRP	University of California Retirement Plan

ATTACHMENTS:

Attachment 1: 2018-19 University of California Budget Plan for Core Funds
Attachment 2: 2018-19 Budget for Current Operations Summary