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Office of the President

TO MEMBERS OF THE COMMITTEE ON COMPENSATION:

DISCUSSION ITEM

For the Meeting of November 14, 2007

UPDATE ON THE TRANSITION OF LAWRENCE LIVERMORE NATIONAL LABORATORY TO THE LAWRENCE LIVERMORE NATIONAL SECURITY, LLC AND THE AGREEMENTS WITH THE DEPARTMENT OF ENERGY REGARDING THE TRANSFER OF ASSETS AND LIABILITIES FROM THE UNIVERSITY OF CALIFORNIA RETIREMENT PLAN TO THE LAWRENCE LIVERMORE NATIONAL SECURITY, LLC DEFINED BENEFIT PENSION PLAN

EXECUTIVE SUMMARY

Effective October 1, 2007, the management of the Lawrence Livermore National Laboratory (LLNL) transferred from the University to the Lawrence Livermore National Security, LLC (LLNS). Of the nearly 7,300 former LLNL employees who were active members of the University of California Retirement Plan (UCRP), approximately 3,970 elected to transfer their UCRP benefits and service credit to the defined benefit pension plan established by LLNS (LLNS Plan), which is designed to be substantially equivalent to UCRP. Under the terms of management Contract No. W-7405-ENG-48 (Contract) between the University and the Department of Energy/National Nuclear Security Administration (DOE/NNSA) governing the transition to a successor contractor, the University is required to transfer the assets and liabilities associated with the UCRP benefits accrued by LLNL employees who have elected to participate in the LLNS Plan.

This item summarizes the results of the retirement plan elections made by the transition of LLNL employees and the actions that are expected to be proposed to The Regents as early as January 2008 to facilitate the transfer of assets and liabilities from UCRP to the LLNS Plan.

Previous Actions: **September 2007:** The Regents authorized the Associate Vice President, Human Resources and Benefits, to enter into discussions with the DOE/NNSA regarding the transfer of assets and liabilities from UCRP to the LLNS Plan and approved amendment of UCRP to provide an alternative method for supporting the timely payment of UCRP benefits to or on behalf of eligible members of the LLNS Plan who retire, die, or become disabled before the final transfer of assets and liabilities from UCRP to the LLNS Plan and their eligible alternate payees.

July 2007: The Regents authorized UCRP amendments to facilitate an effective transition of management to LLNS, including special provisions applicable to designated payees entitled to benefits pursuant to domestic relations orders, rehired retirees, and employees with split appointments at LLNL and another University location.

May 2007: Pursuant to the DOE/NNSA awarding the management contract for LLNL to LLNS, The Regents authorize UCRP amendments to facilitate the closeout of the Contract and the transfer of UCRP assets to the LLNS Plan at a rate sufficient to meet the LLNS Plan's cash flow requirements.

Future Action: Request for authorization to enter into agreements to implement the final transfer of assets and liabilities from UCRP to the LLNS Plan and confirm DOE/NNSA's ongoing funding obligation and to amend UCRP as necessary to carry out the intent of the agreements expected to be proposed for action as early as January 2008.

Relevant Policy: Plan document for UCRP and Contract.

Issues:

- Transfer of assets and liabilities from UCRP to the LLNS Plan;
- Confirmation of DOE/NNSA's ongoing obligation to fund UCRP benefits associated with LLNL service remaining in UCRP if a shortfall occurs; and
- Due to the similarity of the transactions at Los Alamos National Laboratory (LANL) and at LLNL, it is expected that the LANL Transfer Agreement and the LANL Funding Agreement will serve as models for the agreements regarding LLNL.

BACKGROUND

The University served as the prime contractor for the Berkeley Radiation Laboratory, the predecessor of LLNL, from 1943 to 1952 and then for LLNL through September 30, 2007. Under the prime contracts, DOE/NNSA reimbursed the University for contributions made by the University to UCRP to fund the benefits accrued by LLNL employees who participated in UCRP. The assets and liabilities associated with the UCRP benefits of University employees performing service at LLNL have been allocated to a segment within UCRP (LLNL Segment) and accounted for separately by The Regents' actuary each year since the early 1990s at the request of DOE/NNSA.

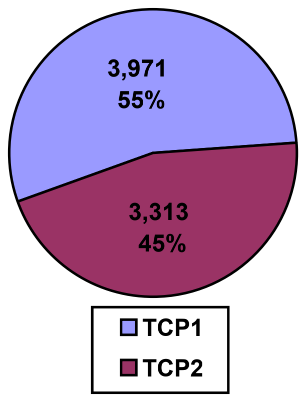
Upon the expiration of the Contract on September 30, 2007 and consistent with their elections required under the LLNL Request for Proposal issued by the DOE/NNSA, active LLNL employees who transferred employment to LLNS began participating in either Total Compensation Package 1 (TCP1) or Total Compensation Package 2 (TCP2). Employees who elected to participate in TCP1 receive retirement coverage under the

LLNS Plan, while those who elected TCP2 receive retirement coverage from the LLNS market-based defined contribution plan (DC Plan). The UCRP benefits and service credit of those who elected TCP1 must be transferred to the LLNS Plan under the terms of the Contract.[1] Vested UCRP members who elected TCP2 could either retire or become inactive UCRP members as of the transition date and remain eligible for a future UCRP benefit. No UCRP-associated assets or liabilities will be transferred for LLNL employees who elected to participate in TCP2.

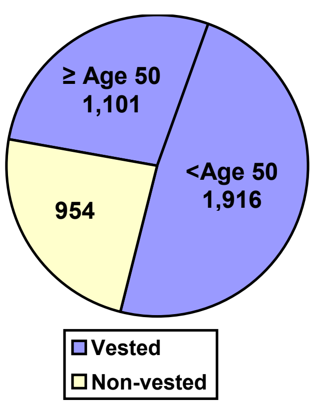
The following charts reflect the approximate LLNS retirement plan elections made by transferring LLNL employees, pending any final adjustments:

LLNS Transition Election Results

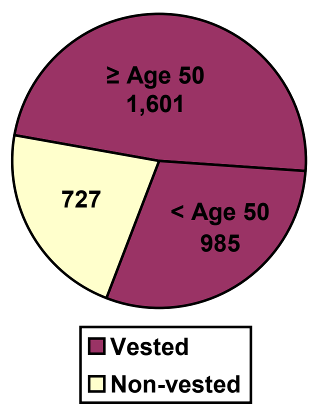
LLNS Total Plan Elections[2]



TCP1 Elections



TCP2 Elections[2]



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[1] UCRP will retain the assets and liabilities for a supplemental benefit, referred to as the Capital Accumulation Payment (CAP), for all LLNL employees, including those who elected to transfer their basic UCRP benefit to the LLNS Plan. All references in this item to the "UCRP benefit" of a LLNL employee refer only to the basic UCRP benefit.

[2] Note that approximately 570 employees who were not eligible for UCRP and thus not eligible for TCP1 are excluded from these charts; these employees were not required to make a retirement plan election as they are only eligible for TCP2.

As of July 1, 2007, the market value of assets attributable to the entire LLNL Segment was $5.527 billion, while the actuarial value of assets was $4.991 billion. The actuarial accrued liability for the LLNL Segment was $5.057 billion. The actuarial accrued liability for the benefits of members electing to participate in the LLNS Plan, as determined under the LLNS Plan provisions and the actuarial assumptions and methods used by the LLNS Plan's actuary, will almost certainly be different from the UCRP liability associated with these former UCRP members, because the LLNS Plan is subject to different legal requirements established in the Employee Retirement Income Security Act of 1974 (ERISA) that apply to the defined benefit plans of private sector employers.

In accordance with the terms of the Contract, the University is also required to transfer UCRP assets at a rate sufficient to meet the cash flow requirements of the LLNS Plan until the terms of the final transfer of assets and liabilities to the LLNS Plan are resolved with the DOE/NNSA (Final Transfer). Consequently, at its May 16, 2007 meeting, The Regents authorized the interim transfers of UCRP assets to the LLNS Plan to the extent necessary to satisfy the plan's cash flow needs. Any UCRP assets transferred, and related earnings, are to be accounted for in the Final Transfer.

At its September 19, 2007 meeting, The Regents authorized a contingent alternative method for supporting the timely payment of the UCRP portion of benefits payable to or on behalf of eligible members of the LLNS Plan who retire, die, or become disabled before the Final Transfer and to the alternate payees of members of the LLNS Plan named in a qualified domestic relations order, including former spouses, who request that their benefits begin before the Final Transfer (collectively, Eligible Payees). The alternative method will be invoked only if LLNS adopts a position similar to that taken by the Los Alamos National Security, LLC (LANS), namely, that it could not accept cash flow-based funding without jeopardizing the tax-qualified status of the LLNS Plan. Under the alternative method, benefits for an Eligible Payee, to the extent accrued under UCRP, will be paid directly from UCRP until the Final Transfer is accomplished. Any monies paid from UCRP to Eligible Payees under the alternative method will be accounted for in the determination of the amount of the Final Transfer.

Contract Formula

The formula outlined in the Contract (Formula) for determining the amount of assets to be transferred to the LLNS Plan is the same "A minus B" formula that applied to the transfer from UCRP to the LANS Defined Benefit Pension Plan (LANS Plan). Under the Formula, "A" equals the market value of the assets allocated to the LLNL Segment prior to transfer, and "B" equals the liabilities associated with the UCRP benefits that will be retained in UCRP in the LLNL Segment. That liability amount will reflect the value of the benefits accrued by former LLNL employees who elected inactive membership in UCRP, retired, died, or become disabled on or before October 1, 2007 as well as their eligible survivors and beneficiaries.

Agreements

Two agreements were reached with DOE/NNSA to complete the final transfer to the LANS Plan. The first was an agreement that established the process for determining the amount of assets and liabilities to be transferred and the supporting documentation required to be provided before the transfer could occur (Transfer Agreement). The second was a "Funding Agreement," which clarified the DOE/NNSA's obligation under the Contract to reimburse the University for any contributions made to UCRP to fund any existing or future funding shortfalls in UCRP associated with members' LANL service. It also established the methodology of calculating whether a current shortfall exists.

Due to the similarity of the transactions at LANL and at LLNL, it is expected that the LANL Transfer Agreement and the LANL Funding Agreement will serve as models for the LLNL agreements. As was the case with the LANL agreements, the substance of the agreements concerning the transfer of assets and liabilities from UCRP to the LLNS Plan will undergo regulatory review by the Internal Revenue Service (IRS) to insure compliance with applicable federal tax laws and will be modified as necessary to conform to such requirements. It is expected that the future recommendation for Regents' action will propose that the actual transfer of assets to the LLNS Plan occur as early as April 1, 2008. The LLNS Plan will then assume the liabilities transferred from UCRP determined as of October 1, 2007. The future recommendation is also expected to include the approval of an agreement confirming DOE/NNSA's obligation to reimburse the University for any contributions made to UCRP to fund the LLNL Segment remaining in UCRP if a shortfall occurs.

As authorized by The Regents at its September 2007 meeting, a University team led by Associate Vice President Boyette–Human Resources and Benefits has begun to hold regularly scheduled discussions with the DOE/NNSA team led by Contractor Human Resources Specialist Sanchez regarding the appropriate amount of assets and liabilities to be transferred to the LLNS Plan and related matters. Because of the complex legal issues presented by this transaction, the University and DOE/NNSA teams have agreed to seek guidance on the structure of the transaction from key regulatory agencies, including the Internal Revenue Service, the Department of Labor, and the Pension Benefit Guaranty Corporation. An early resolution will help LLNS satisfy the LLNS Plan's minimum funding obligations under ERISA by the applicable April 2008 deadline and thereby avoid significant economic penalties. UCRP's interests will be served by having the LLNS 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.

Consultation

University administrators have consulted with and will continue to engage in consultation with the appropriate representatives of the Academic Senate, including the University Committee on Faculty Welfare (UCFW) and the UCFW Task Force on Investment and Retirement regarding the issues described in this item.

Next Steps

It is expected that the proposal for the Final Transfer will be presented to the Committee on Compensation for action as early as the January 2008 meeting of The Regents. 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, if any such action is required.