The Regents of the University of California

COMMITTEE ON FINANCE
May 15, 2002

The Committee on Finance met on the above date at Covel Commons, Los Angeles campus.

Members present: Regents Atkinson, Davies, Hopkinson, Kozberg, Lee, Marcus, Montoya, Moores, Morrison, Parsky, and Preuss; Advisory member Ligot-Gordon

In attendance: Regents Blum, T. Davis, Johnson, Lansing, Lozano, Pattiz, Saban, and Seymour, Regents-designate Sainick and Terrazas, Faculty Representatives Binion and Viswanathan, Secretary Trivette, General Counsel Holst, Treasurer Russ, Provost King, Senior Vice President Mullinix, Vice Presidents Broome and Gomes, Chancellors Bishop, Carnesale, Dynes, Tomlinson-Keasey, and Vanderhoef, Acting Chancellor Warren, and Recording Secretary Nietfeld

The meeting convened at 2:23 p.m. with Committee Chair Preuss presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of March 13, 2002 were approved.

2. **UNIVERSITY OF CALIFORNIA RETIREMENT PLAN ASSET/LIABILITY STUDY**

It was recalled that at the January 2001 meeting, the Committee was presented with the results of a University of California Retirement Plan (UCRP or Plan) Asset/Liability Study prepared by the Plan's consulting actuary, Towers Perrin. The University's Human Resources/Benefits office has worked with Towers Perrin, the Office of the Treasurer, and Wilshire Associates to update the UCRP Asset/Liability Study. This study not only illustrates the effect of changes in the value of Plan assets and changes in capital markets on the Plans assets and liabilities but also shows the effect of UCRP benefit improvements being considered by The Regents.

The Committee was informed that in an asset/liability study, the baseline is set to equal the present conditions; future liabilities and assets are forecast over a ten-to-twenty-year period using stochastic modeling to create hundreds of discrete financial scenarios. The forecasting of liabilities and assets provides benchmark information to help assess the probability of achieving goals based on current policies, to gauge the reasonableness of assumptions, and to determine the probability of adverse results.

The success of an asset/liability project requires that the assets and liabilities be linked, capturing the fundamental dynamics of both the plan and real-world economic factors. In this modeling, decisions are made on the appropriate liability characteristics and sensitivities, customized to incorporate the plan's provisions and membership and the pattern of joint asset/liability movements over time as the capital market conditions change and those changes affect the plan's funded ratios. After the baseline results have been prepared, plan changes, asset portfolios, and economic scenarios are analyzed to determine the effect of these changes on the funded status of the plan and any contribution requirements.

Associate Vice President Boyette noted that there are some important issues facing the University relative to the retirement plan, including an aging workforce and projected enrollment growth which will result in the addition of new faculty and staff. The asset/liability study provides an analysis of any changes that might be made in the Plan in light of demographics, enrollment growth, and changes in the financial markets.

Ms. Catherine Cole of Towers Perrin, The Regents' consulting actuary, presented the **Summary of University of California Retirement Plan Asset/Liability Forecast Study - January 2002**, which had been mailed to all Regents in advance of the meeting. She noted that the primary objectives of the study are to demonstrate fiduciary due diligence and to determine the adequacy of assets in conjunction with liabilities. The Plan forecasts were developed using the assumption that active membership growth would be 2.5 percent per year through 2011 and 1.5 percent thereafter. Ms. Cole compared the present asset allocation policy for the UCRP with the new policy which is being recommended for adoption at today's meeting. The projected mean returns for the portfolio are similar under the two policies. The projected nominal return of 8.28 percent is higher than the 7.5 percent used in the annual actuarial study. Turning to Plan results, Ms. Cole reported that as of January 1, 2002 the funded ratio of assets to liabilities is 149 percent, based on assets of \$41.57 billion versus liabilities of \$27.9 billion. She presented a graph which projected performance of capital markets. The average expectation for assets is \$60 billion in 2011. She noted that the projections were lower than those presented in the July 2000 study due to the performance of the market.

Mr. Steve Nesbitt of Wilshire Associates discussed the data presented in the graph in greater detail, noting that the value of the stock market had declined by 25 percent since fiscal year 2000, resulting in a decrease in Plan assets from \$42 billion in 2000 to \$37.5 billion as of April 30, 2002. He stressed that this result is not outside the projected range of possibilities.

Ms. Cole discussed the funded status of the Plan through 2021, noting the assumption that no contributions will be made by the University during this time period. The funded status in 2006 ranges from 98 percent to 168 percent, with a mean value of 128 percent for the full range of probabilities. In 2016 and later, however, it is possible that contributions will be required using the current set of Plan provisions and growth projections. The current surplus will be needed over the next five to ten years to fund future growth as well as the increase in liabilities that result from the benefits earned by the membership. These liabilities increase annually by 15 percent of the covered payroll.

Ms. Cole continued that liabilities had also been forecast using the assumption that The Regents would approve a recommendation to extend retirement benefits to domestic partners. These projections indicate that such changes will have little impact on the forecasting.

In response to a question from Regent Parsky, Ms. Cole estimated that contributions to the Plan could be required sometime between 2012 and 2017 if the University retains the practice of requiring contributions when the asset-to-liability ratio falls below 100 percent. The Regents will need to consider this issue in the next four to five years if future studies show similar results. Regent Hopkinson suggested that The Regents may need to revisit the issue of contributions to the Plan earlier than the time frame referred to by Ms. Cole. Regent Parsky added that the issue of whether or not contributions will be required from Plan participants would need to be addressed well in advance of any action being contemplated.
Regent Moores pointed out that the data presented by Towers Perrin suggested that the University would be able to meet its responsibilities to Plan participants well into the future. Ms. Cole stressed that the level of funding required to fund the benefits paid to members will continue to rise over time. She believed that the current surplus of $14.5 billion could be gone in ten years. Senior Vice President Mullinix noted that one question to consider was whether or not earnings would cover the full cost of the Plan during that time period. He stressed that under most economic scenarios no contributions should be required over the next twenty years. Regent Parsky asked that the administration begin to address sooner rather than later what actions might be required.

The meeting adjourned at 3:00 p.m.

Attest:

Secretary