

# Post Employment Benefits

**Presentation to  
Assembly of Academic Senate  
October 14, 2009**

Peter Taylor, Chief Financial Officer  
Robert Anderson, Chair, TFIR

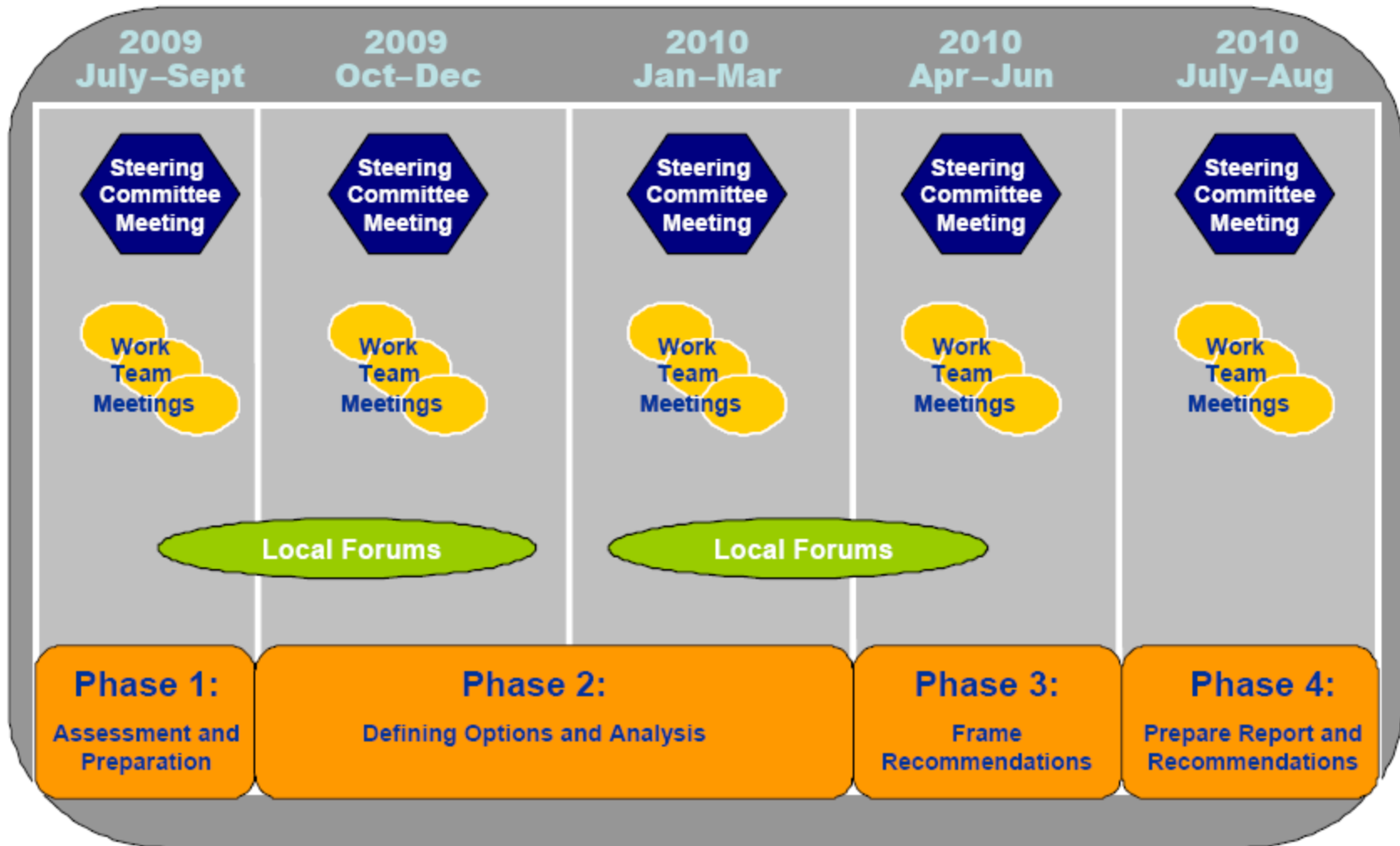
# PEB Task Force Background

- February 6, 2009 Regents approved the restart of contributions to UCRP.
- Also authorized the President's Task Force on Post Employment Benefits to develop a comprehensive, long-term approach for all post employment benefits.
- Task Force will make recommendations to the President for his review and endorsement before subsequent submission to the Regents.
- The President and Regents are the final decision-makers.
- President's charge: engage in a robust consultation and communication process.
  - *Local Forums with stakeholders and advisory groups*
  - *Meeting all HEERA obligations with unions*
  - *State of California*
  - *Website: <http://www.universityofcalifornia.edu/news/ucrpfuture/>*

# PEB Task Force Charge

- **Consider the impact of:**
  - **Market competitiveness,**
  - **Talent management, work force development and renewal, work force behavior,**
  - **Affordability and sustainability**
- **Analyze:**
  - **Cost and cash flow**
  - **Long-term funding options & impact on UC financial integrity**
- **Complete work within a reasonable timeframe**
- **Make recommendations which allow the Regents to meet:**
  - **Fiduciary obligations**
  - **Educational responsibilities**

# PEB Task Force Process Timeline



# University's Legal Obligation for Post-Employment Benefits:

- **The University is legally obligated to pay all pension benefits that have been accrued to date, and cannot escape that obligation.**
- **The University *may* be able to reduce future accrual of pension benefits by current employees; would certainly result in litigation.**
- **The University has more freedom with regard to reducing retiree health benefits.**
- **The University *clearly can* reduce pension and retiree health benefits of newly hired employees.**

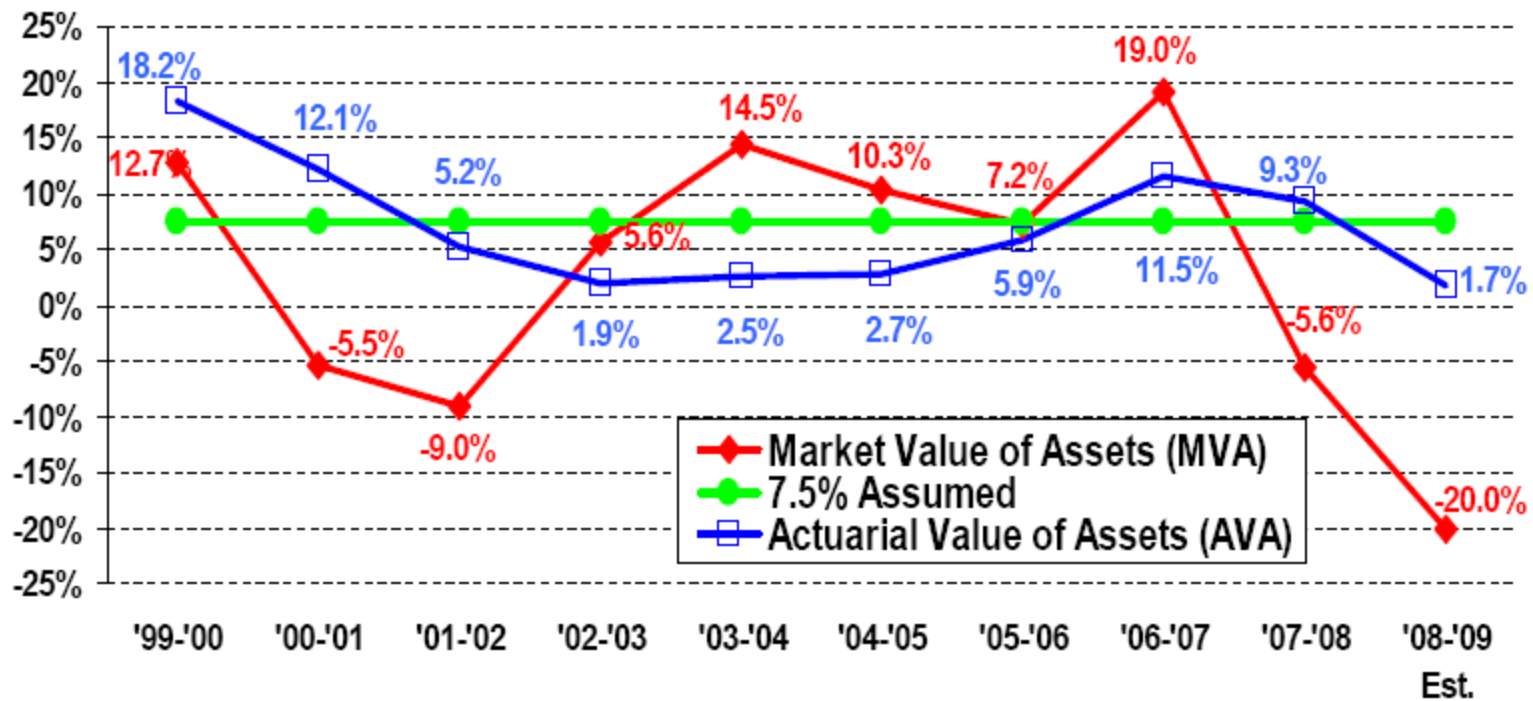
# Devastating Effect on Budget

- **UC has been subsidizing its budget by promising pension benefits, paid for by drawing down the UCRP surplus.**
- **That surplus is gone, and the subsidy cannot continue. UC must now make contributions to cover the ongoing accrual of benefits.**
- **UCRP has a substantial unfunded liability. UC must make additional contributions to amortize that liability.**
- **UC has a substantial unfunded liability for retiree health, and no assets have been set aside.**

# **UCRP was 100% Funded on June 30, 2008**

- **100% funded means that if assumptions are exactly right**
  - **earn 7.5% return compounded**
  - **everyone cooperates by dying when expected.**
- **UCRP will have just enough money to pay pensions accrued based on service credit earned in the past.**
- **No provision for pension based on service credit earned in the future.**

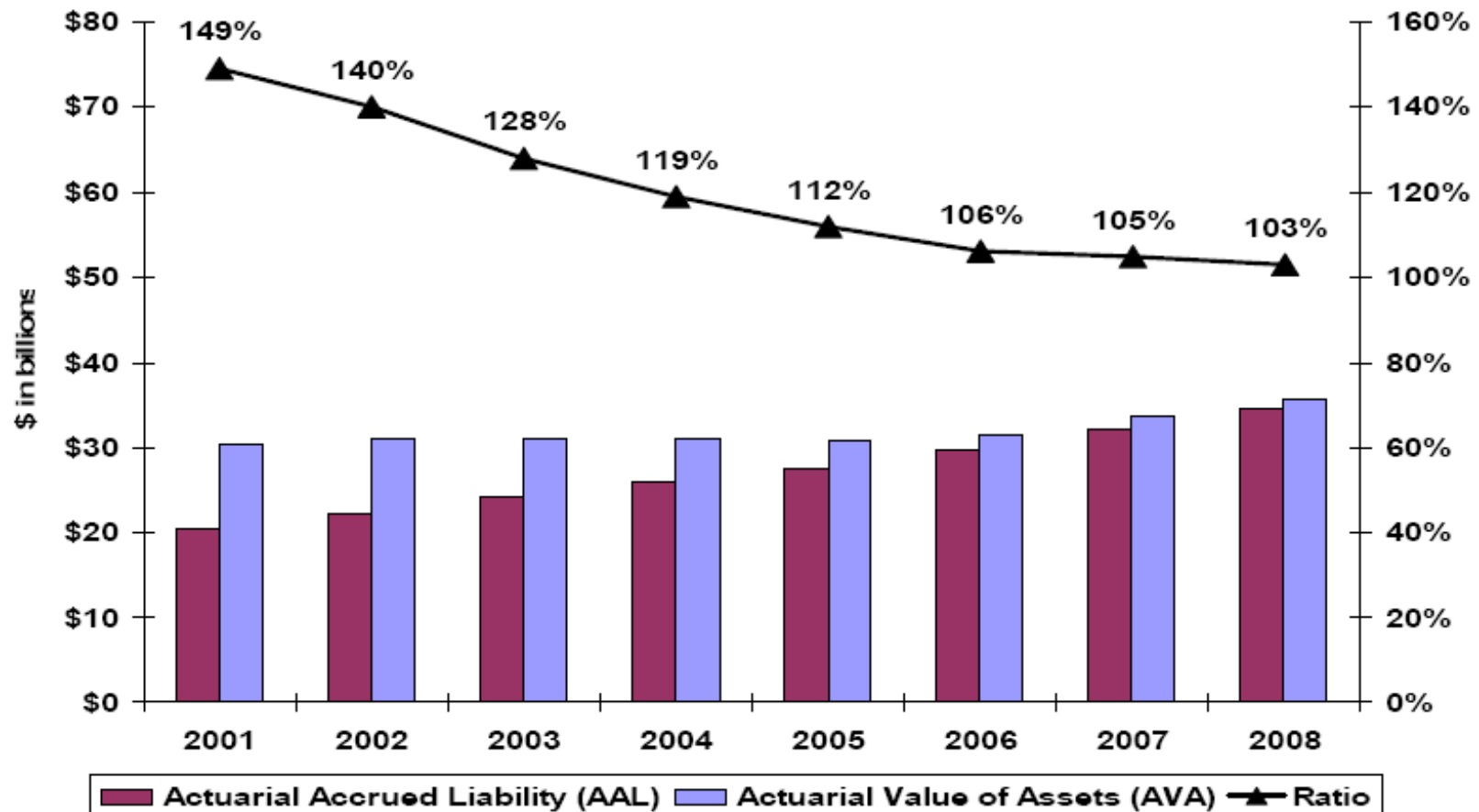
# UCRP Investment Rates of Return



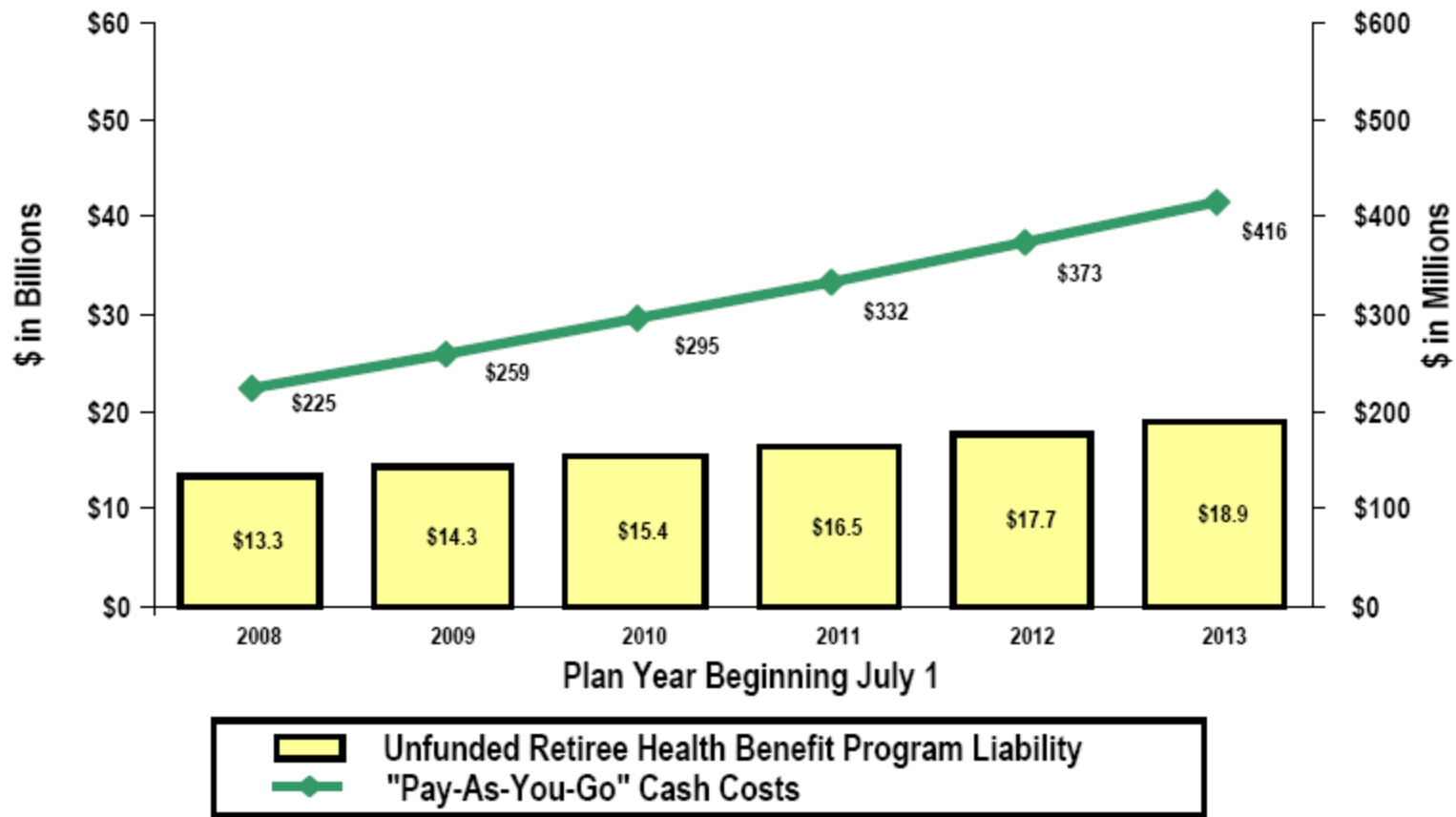
**AVA recognizes each MVA return above or below the assumed rate (7.5%) over five years; the loss in 2008-09 will continue to reduce AVA each year until 2013**



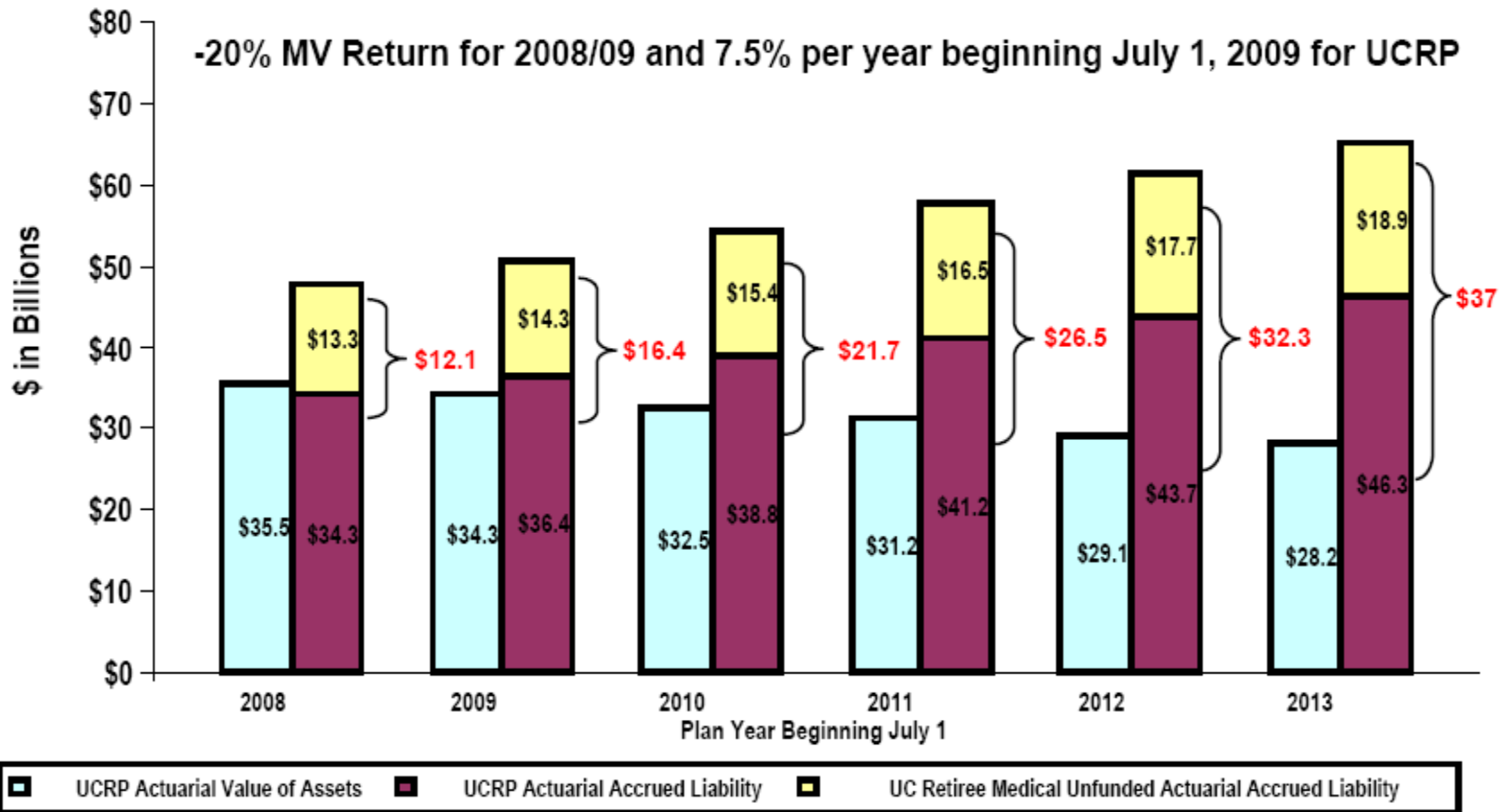
# UCRP Historical Funded Status



# Retiree Health Benefit Program Unfunded Liability and Cash Costs



# Overview of Employee PEB Assets / Liabilities / Shortfall



## Normal Cost

- **Every year, people earn an additional year of service credit; value is “Normal Cost”**
  - **about 17% of covered compensation**
- **Pension plan needs contributions equal to Normal Cost, plus amounts to amortize past deficit, less amounts to amortize past surplus.**
- **Similarly, there is a Normal Cost of retiree health, which we should be setting aside, plus funds to amortize the current unfunded liability.**

# **Regents' UCRP Funding Policy**

## **September 2008**

- **Five year smoothing of returns: take difference between actual return and 7.5%, and incorporate one-fifth of that into Actuarial Value of Assets each year for five years.**
- **15 year amortization of unfunded Actuarial Accrued Liability**
- **30 year amortization of Actuarial surplus; means UC would never completely stop contributions unless you got to about 200% funding.**
- **Applying this to situation as of June 30, 2008, needed 11.5% (employer 9.5%, employee 2%/4%) as of July 1, 2009.**
- **Would have required contribution in excess of 20% as of July 1, 2010.**

# Slow Ramp-Up

- Concerns about availability of state funding led to **Slow Ramp-Up**, planned but not formally adopted:
  - contributions deferred to April 15, 2010
  - Employee contribution starts at 2%, rises 1% per year to 5%
  - Employer contribution starts at 4%, rises 2% per year until it meets the **Regents' UCRP Funding Plan**.

# Slow Ramp-Up is Inadequate

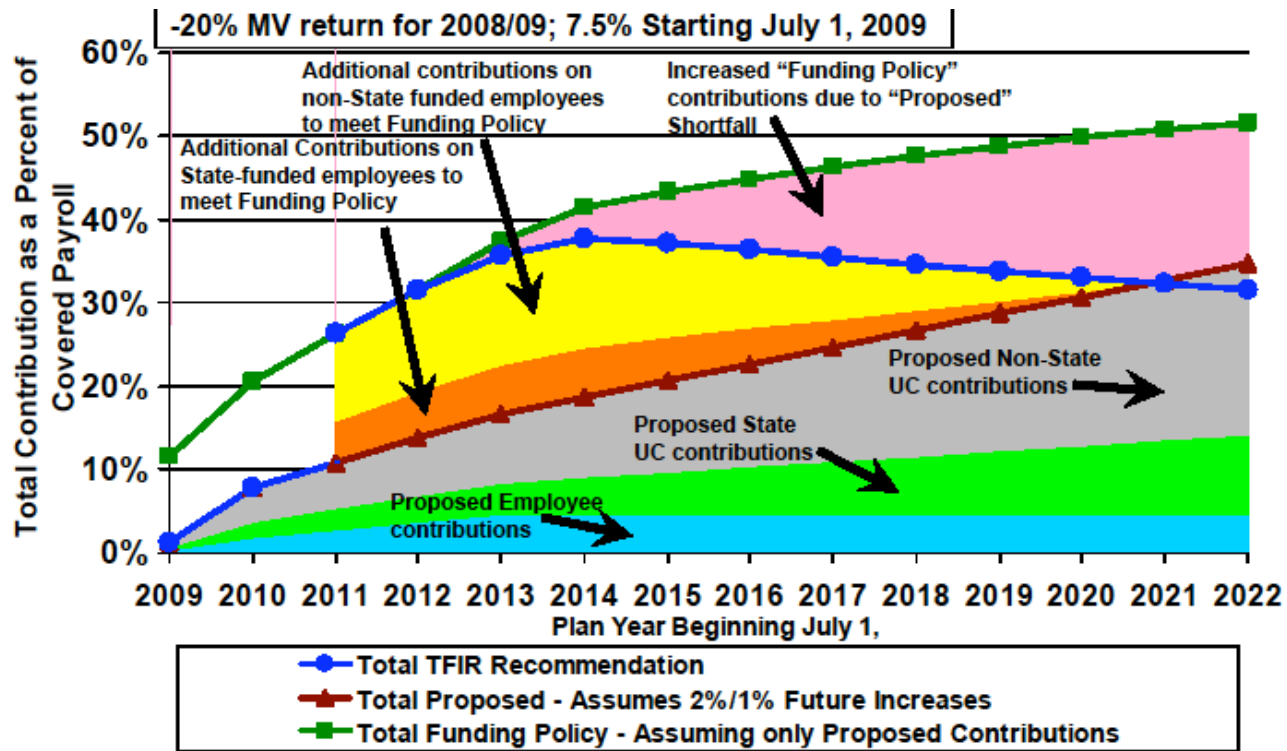
- **Slow Ramp-Up** would have been adequate if the markets had not fallen dramatically in 2008-09.
- Given current market values, **Slow Ramp-Up** probably won't get contributions up to the **Funding Plan** requirement for about 20 years, at which point contributions in excess of 50% of covered compensation will be needed.
- UCRP has been well managed; problem is in markets.
- **Slow Ramp-Up** keeps digging us into a deeper hole.

## Digging the Hole Deeper

- **Deferring contributions means we forego the 7.5% earnings on those contributions.**
- **Deferring \$1 contribution now requires over \$4 contribution 20 years from now.**
- **Deferring \$1 in contributions on state-funded employees results in loss of \$2 contributions from other fund sources (federal grants and contracts, hospitals, etc.)**
- **Required **Funding Policy** contributions projected to exceed 50% of covered compensation.**



# Proposed and Funding Policy Total Contributions for Campus and Medical Centers Only



# **Deferred Contributions From Other Fund Sources May Never Be Recouped**

- **No way for federal grants and contracts to commit to amortizing deficit years from now (except for DoE Labs).**
- **Future UCRP contributions in excess of 50% of covered compensation may make UC uncompetitive for these funding sources**
  - **Pension contributions are a direct cost; would make funding UC research expensive from point of view of federal agencies.**
  - **Hospitals may be unable to compete for insurance contracts with this cost structure.**
- **Same problem with retiree health.**

# Cutting Pension Benefits Won't Fix Problem

- UC can't renege on **pension** benefits already accrued. Employees/retirees have a right to the years of service credit already earned, and to apply the current age factors to those years when you retire.
- Gray area as to whether UC could reduce future **pension** accrual for current employees; would certainly be litigated.

## **Cutting Pension Benefits Won't Fix Problem (continued...)**

- **Even if UCRP stopped accrual of additional benefits, UC would still have to amortize the unfunded liability.**
- **Freezing would make it difficult or impossible to collect employer contributions from hospitals or federal grants and contracts if the employees were no longer accruing benefits; Disaster for state-funded budget.**
- **Freezing would make it difficult or impossible to collect employee contribution to UCRP, since employees are no longer accruing benefits.**

## **Cutting Pension Benefits Won't Fix Problem (continued...)**

- **UC still needs a competitive pay/benefits package.**
  - **UCRP with a 5% employee contribution is *uncompetitive* with faculty retirement plans at the Comparison 8, in part because faculty retire relatively late.**
  - **UCRP with a 5% employee contribution is more than competitive for some employee groups, in part because staff retire right around age 60.**
  - **A DC plan still requires employer contributions.**

## **Cutting Pension Benefits Won't Fix Problem (continued...)**

- **UCRP has important institutional benefits in retaining mid-career faculty and staff, compared to DC plans.**
- **UCRP has important benefits in encouraging faculty retirement, compared to DC plans; Yale and Stanford have expensive formal programs to encourage retirement by age 70. Other institutions do negotiated buy-outs.**

## **Moving Retirement Later Would Help**

- **Significant savings in UCRP since pension drawn over fewer years.**
- **Significant savings in retiree health since benefit drawn over fewer years, especially the expensive years before Medicare kicks in at age 65.**
- **New employees could be given a choice of retiring later (perhaps 65) on a full benefit, or continue to retire relatively early (around 60) on a smaller benefit.**
- **Current employees might be incentivized to retire later.**

# **Large Contributions are Urgently Needed Now**

- **Whatever may be done to reduce costs, we have a serious funding shortfall.**
- **Action is urgently needed to address it with substantial contributions.**



# TFIR Recommendation

- “...the least bad option is to raise UCRP contributions as soon as possible to the full recommended contribution under the **Funding Policy**. Doing so avoids far higher contributions in the future, and also ensures that nonstate sources pay their fair share of the unfunded liability and the additional pension benefits that are earned each year. Every dollar of contributions made on behalf of employees whose salaries are paid from state funds is matched, on a two-for-one basis, by the contributions that will be made from other fund sources, on behalf of employees who are not paid from state fund sources. TFIR therefore recommends that The Regents commit to allocate funds sufficient to follow the **Funding Policy**, starting no later than July 1, 2011;...”

# UCFW and Academic Council

- **UCFW and Academic Council endorsed the TFIR Recommendation and transmitted it to President Yudof.**
- **President Yudof has forwarded the TFIR/UCFW/ Academic Council Recommendation to the Presidential Task Force on Post-Employment Benefits.**
- **Recommendation simply calls on The Regents to follow their own **Funding Policy**, which requires a faster ramp-up.**