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# UCRS Advisory Board

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Meeting of April 28, 2006

## AGENDA ITEM C

### Item – New Business

#### UCRS – Cost-of-Living Adjustment for July 2006 and Measurement of Annuitant Purchasing Power

#### **July 1, 2006 COLA**

The July 1, 2006 Cost-of-Living Adjustment (COLA) is based on the average increase in the Consumer Price Index (CPI) for urban consumers in the metropolitan areas of San Francisco and Los Angeles from February 2005 to February 2006. This average CPI increase was 4.01%; therefore, the July 1, 2006 COLA will be:

<b>Retirement Date</b>	<b>COLA</b>
On or before July 1, 2002	2.01%
July 2, 2002 to July 1, 2003	2.29%
July 2, 2003 to July 1, 2005	2.01%

#### **COLA Methodology**

The University of California Retirement Plan (“UCRP” or “Plan”) provides an annual COLA that generally matches the increase in the CPI up to 2%, plus 75% of the CPI increase in excess of 4%, to a maximum COLA of 6%. The COLA percentage for a specific year depends not only on the CPI increase that year, but also on the cumulative increase in CPI since the Member retired. For this purpose, two banks are maintained, an “inflation bank” and a “COLA bank”, which are then used to determine the total COLA amount that an annuitant is entitled to in a given year.

The inflation bank accumulates in years in which the CPI increase is greater than 2%. The inflation bank represents the portion of the cumulative increase in the CPI since the

Member's Retirement Date for which the annuitant has not received a COLA. For example, the annual CPI increase as measured in February 2003 was 3.45%, but based on Plan provisions the July 2003 COLA was only 2%. The remaining 1.45% is adjusted for compounding, resulting in an inflation bank of 1.42% for annuitants who were first eligible in July 2003. The inflation bank can be used to increase the COLA that would be payable in years in which inflation is less than 2%. For example, the inflation bank was used to provide Members who retired on or before July 1, 2002, a 2% COLA on July 1, 2004, even though the increase in the CPI average was less than 2%.

The second bank is the COLA bank. In years in which inflation is less than 2%, the difference between 2% and the CPI increase is accumulated in the COLA bank. The COLA bank represents that portion of the potential COLA which has not been paid to the annuitant due to low inflation. For example, the annual CPI increase as measured in February 2004 was 1.04%. Annuitants who received a 1.04% COLA in July 2004 accumulated 0.96% in their COLA bank. The CPI increase measured in February 2006 was 4.01%. Those annuitants with nothing accumulated in their COLA bank are entitled to receive a 2.01% COLA on July 1, 2006, based on the formula. However, those annuitants who had 0.96% in their COLA bank after the July 1, 2004 effective date, still have 0.28% left to use on July 1, 2006. This COLA bank is used to give these annuitants a 2.29% COLA on July 1, 2006 (2.01% + 0.28%).

Both banks accumulate from the Member's initial eligibility for a COLA. Therefore, when economic conditions warrant using either of the banks, it is possible for the Plan to pay different annual COLA amounts in the same year to different Retired Member groups depending on the year in which the Members retired and the resulting amounts in the inflation bank and COLA bank. Attachment 1 shows the current level of the inflation and COLA banks as they apply to each group of Retired Members, just after the July 1, 2006 COLA is credited.

### **Measurement of Annuitant Purchasing Power – UCRP Annuitants**

Once the annual COLA is determined, annuitants' purchasing power may then be measured. Since the 2006 COLA is less than the actual increase in the CPI, purchasing power has decreased slightly. Attachment 1 demonstrates that purchasing power remains above 80% for all annuitants as of July 1, 2006.

Historically, The Regents have striven to protect annuitants' benefits from being significantly eroded by inflation. However, this is not a guaranteed contractual benefit. Rather, in February 1988, the UCRS Advisory Board passed a resolution indicating its intent to recommend, from time to time and, subject to the availability of funds, adjustments to approximate a 75% level of purchasing power. "Ad hoc" COLAs were

given in January 1986 and July 1988 to restore annuitants' purchasing power to a 75% level. In January 1991, a one-time ad hoc COLA was given to restore retirement benefits to a floor of 80% of purchasing power and in January 2001 a one-time ad hoc COLA was given to restore retirement benefits to a floor of 85% of purchasing power. The 85% level was recommended so that it would not be necessary to provide additional ad hoc COLAs as frequently to restore the 75% purchasing power level.

The advantage to UCRP of a periodic ad hoc COLA over a guaranteed COLA is that the funding requirements are lower. A guaranteed COLA, expressed in terms of inflation, produces significant costs and requires the creation of additional financial resources within the Plan that may or may not be needed depending on actual inflation. Alternatively, a periodic ad hoc COLA requires no advance funding and does not increase actuarial liability until the COLA is granted.

### **Measurement of Annuitant Purchasing Power – UC-PERS VERIP (PERS Plus 5 Plan) Annuitants**

The UC-PERS Plus 5 Plan is the University of California Voluntary Early Retirement Incentive Program (VERIP) for former eligible UC employees for whose benefit UC contributed to the California Public Employees' Retirement System (i.e., UC-PERS members). It is a frozen plan that was created as a means of providing a retirement incentive supplement for a closed group of eligible UC-PERS members that retired concurrently under PERS and the UC-PERS PLUS 5 Plan on October 1, 1991.

There is no automatic annual COLA paid to PERS Plus 5 Plan retirees and beneficiaries. However, in May 2002, The Regents approved a proposal to award these annuitants with a 25% ad hoc COLA, which restored their purchasing power to 96%, effective July 1, 2002.

Since that time, the CPI has increased by about 10%. Therefore, as of July 1, 2006, the retained purchasing power for PERS Plus 5 Plan annuitants is approximately 86%, whereas their UCRP counterparts have retained purchasing power of approximately 92%.

Attachment

**UNIVERSITY OF CALIFORNIA RETIREMENT PLAN**  
Increase in Benefits vs Increase in Cost-of-Living

For Annuitants Whose Benefit Commenced***	Number of Annuitants	Increase in Benefits			CPI *			Increase in CPI **	Cumulative Increase in CPI	Retained Purchasing Power	Inflation Bank	COLA Bank
		Auto- matic	Ad Hoc	Total	(preceding February)							
					Old Basis	New Basis	New Basis-2					
On or before 01-Jul-61	2	117.65%	159.11%	463.95%	89.30	--	--	0.90%	600.85%	80.47%	24.28%	0.00%
02-Jul-61 to 01-Jul-62	2	117.65%	156.80%	458.93%	90.10	--	--	1.22%	594.63%	80.46%	24.28%	0.00%
02-Jul-62 to 01-Jul-63	3	117.65%	153.70%	452.19%	91.20	--	--	1.43%	586.25%	80.46%	24.28%	0.00%
02-Jul-64 to 01-Jul-65	1	117.65%	143.82%	430.68%	94.90	--	--	1.90%	559.50%	80.47%	24.27%	0.00%
02-Jul-65 to 01-Jul-66	2	117.65%	139.27%	420.78%	96.70	--	--	1.86%	547.22%	80.46%	24.28%	0.00%
02-Jul-66 to 01-Jul-67	3	117.65%	134.89%	411.25%	98.50	--	--	4.67%	535.39%	80.46%	24.28%	0.00%
02-Jul-67 to 01-Jul-68	7	117.65%	124.42%	388.46%	103.10	--	--	4.75%	507.04%	80.46%	24.28%	0.00%
02-Jul-68 to 01-Jul-69	11	113.39%	118.52%	366.30%	108.00	--	--	5.00%	479.50%	80.47%	24.28%	0.00%
02-Jul-69 to 01-Jul-70	11	109.20%	112.28%	344.08%	113.40	--	--	4.06%	451.91%	80.46%	24.28%	0.00%
02-Jul-70 to 01-Jul-71	26	105.10%	108.09%	326.79%	118.00	--	--	3.47%	430.39%	80.47%	24.28%	0.00%
02-Jul-71 to 01-Jul-72	41	101.08%	105.10%	312.42%	122.10	--	--	4.50%	412.58%	80.46%	24.29%	0.00%
02-Jul-72 to 01-Jul-73	62	97.14%	100.21%	294.68%	127.60	--	--	8.46%	390.49%	80.47%	24.28%	0.00%
02-Jul-73 to 01-Jul-74	89	93.27%	88.28%	263.88%	138.40	--	--	12.07%	352.21%	80.47%	24.27%	0.00%
02-Jul-74 to 01-Jul-75	91	89.48%	71.36%	224.68%	155.10	--	--	6.19%	303.52%	80.46%	24.28%	0.00%
02-Jul-75 to 01-Jul-76	125	85.76%	64.59%	205.75%	164.70	--	--	7.16%	280.00%	80.46%	24.29%	0.00%
02-Jul-76 to 01-Jul-77	208	82.12%	56.66%	185.32%	176.50	--	--	6.43%	254.60%	80.46%	24.28%	0.00%
02-Jul-77 to 01-Jul-78	242	78.55%	50.15%	168.09%	187.85	--	--	8.01%	233.17%	80.47%	24.28%	0.00%
02-Jul-78 to 01-Jul-79	329	75.05%	41.79%	148.20%	202.90	--	--	17.87%	208.46%	80.47%	24.28%	0.00%
02-Jul-79 to 01-Jul-80	336	71.62%	22.69%	110.56%	239.15	--	--	9.16%	161.70%	80.46%	24.29%	0.00%
02-Jul-80 to 01-Jul-81	362	68.25%	14.66%	92.92%	261.05	--	--	11.32%	139.75%	80.47%	24.27%	0.00%
02-Jul-81 to 01-Jul-82	467	64.91%	5.08%	73.29%	290.60	--	--	0.50%	115.37%	80.46%	24.28%	0.00%
02-Jul-82 to 01-Jul-83	536	61.72%	6.63%	72.44%	292.05	--	--	4.76%	114.30%	80.47%	24.27%	0.00%
02-Jul-83 to 01-Jul-84	582	58.19%	4.05%	64.60%	305.95	--	--	5.05%	104.56%	80.46%	24.28%	0.00%
02-Jul-84 to 01-Jul-85	612	54.56%	1.38%	56.69%	321.40	--	--	3.87%	94.73%	80.47%	24.28%	0.00%
02-Jul-85 to 01-Jul-86	723	51.53%	0.00%	51.53%	333.85	--	--	2.98%	87.47%	80.83%	23.72%	0.00%
02-Jul-86 to 01-Jul-87	863	48.56%	0.00%	48.56%	343.80	114.05	--	4.16%	82.04%	81.61%	22.54%	0.00%
02-Jul-87 to 01-Jul-88	1,025	45.57%	0.00%	45.57%	--	118.80	--	5.01%	74.76%	83.30%	20.05%	0.00%
02-Jul-88 to 01-Jul-89	962	42.25%	0.00%	42.25%	--	124.75	--	5.33%	66.43%	85.47%	17.00%	0.00%
02-Jul-89 to 01-Jul-90	1,361	38.86%	0.00%	38.86%	--	131.40	--	5.02%	58.01%	87.88%	13.79%	0.00%
02-Jul-90 to 01-Jul-91	3,901	35.68%	0.00%	35.68%	--	138.00	--	3.59%	50.45%	90.18%	10.88%	0.00%
02-Jul-91 to 01-Jul-92	619	33.02%	0.00%	33.02%	--	142.95	--	3.36%	45.24%	91.59%	9.18%	0.00%
02-Jul-92 to 01-Jul-93	2,514	30.40%	0.00%	30.40%	--	147.75	--	1.39%	40.52%	92.80%	7.76%	0.00%
02-Jul-93 to 01-Jul-94	5,736	27.85%	0.00%	27.85%	--	149.80	--	1.80%	38.60%	92.25%	8.40%	0.00%
02-Jul-94 to 01-Jul-95	538	25.35%	0.00%	25.35%	--	152.50	--	1.44%	36.14%	92.07%	8.61%	0.00%
02-Jul-95 to 01-Jul-96	722	22.89%	0.00%	22.89%	--	154.70	--	2.52%	34.21%	91.57%	9.21%	0.00%
02-Jul-96 to 01-Jul-97	1,002	20.48%	0.00%	20.48%	--	158.60	--	2.40%	30.91%	92.04%	8.65%	0.00%
02-Jul-97 to 01-Jul-98	1,145	18.12%	0.00%	18.12%	--	162.40	162.15	2.99%	27.84%	92.39%	8.23%	0.00%
02-Jul-98 to 01-Jul-99	1,321	15.80%	0.00%	15.80%	--	--	167.00	3.50%	24.13%	93.29%	7.19%	0.00%
02-Jul-99 to 01-Jul-00	1,440	13.53%	0.00%	13.53%	--	--	172.85	5.09%	19.93%	94.67%	5.64%	0.00%
02-Jul-00 to 01-Jul-01	3,869	10.42%	0.00%	10.42%	--	--	181.65	2.23%	14.12%	96.76%	3.35%	0.00%
02-Jul-01 to 01-Jul-02	2,032	8.25%	0.00%	8.25%	--	--	185.70	3.45%	11.63%	96.97%	3.12%	0.00%
02-Jul-02 to 01-Jul-03	2,301	6.12%	0.00%	6.12%	--	--	192.10	1.04%	7.91%	98.34%	1.69%	0.00%
02-Jul-03 to 01-Jul-04	2,853	4.05%	0.00%	4.05%	--	--	194.10	2.68%	6.80%	97.42%	2.64%	0.00%
02-Jul-04 to 01-Jul-05	2,400	2.01%	0.00%	2.01%	--	--	199.30	4.01%	4.01%	98.07%	1.96%	0.00%
02-Jul-05 to 01-Jul-06	#N/A	0.00%	0.00%	0.00%	--	--	207.30	--	--	--	--	--

\* Beginning in 1988, the CPI index shifted to a 1982-84 reference base year (New Basis). Previously, the index used a 1967 base year (Old Basis). For comparison purposes, the prior year has been rebased to 1982-84. Beginning in 1998, the CPI index reflects a different market basket of goods. This CPI change first takes effect for the 1999 COLA.

\*\* CPI increase shown is for the year following retirement.

\*\*\* For Benefit Commencement Periods containing no surviving annuitants, information has been suppressed.

