Retirement Programs for University Employees

Presentation to the Board of Trustees
April 18, 2014
State University Retirement Systems (SURS)
Three Pension Programs

Tier 1
Joined prior to 2011
Defined Benefit

Tier 2
Joined after Jan 1, 2011
Defined Benefit

Prior to 2005

2005 - 2010

Money Purchase Option

Money Purchase is an alternative formula for calculating benefits
Money Purchase Option

During Employment Contributions Accumulate with Interest

During Retirement Monthly Annuity

Total accumulation converted to monthly annuity
Annuity based on interest rate

PA98-0599 fixed interest rate for calculating annuity (effective 7.1.2014)

Interest Rate 6.30.14  7.75%
Interest Rate 7.1.14  4.27% (approx)
### Impact of Rate Reduction

<table>
<thead>
<tr>
<th>Date</th>
<th>Annuity Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.30.14 (old rate)</td>
<td>$2,540</td>
</tr>
<tr>
<td>7.1.2014 (new rate)</td>
<td>$1,640</td>
</tr>
<tr>
<td>6.1.2013</td>
<td>$1,810</td>
</tr>
</tbody>
</table>

**Penalty for not retiring**

29% loss in lifetime income
Additional Changes Imposed by PA98-0599

- Reduce COLA
- Temporarily suspend COLA for future retirees
- Cap pensionable earnings
- Delay retirement age for those under 45
- Change effective rate of interest
- Reduce employee contribution by 1%
Level of Benefit Reduction Depends on Salary Level

Consider individuals who joined 10 years ago and expect to work for another 25 years. The table below shows benefit reduction for this group of employees (for different starting salary levels).

<table>
<thead>
<tr>
<th>Benefit Reduction</th>
<th>Starting Salary Level</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$40,000</td>
</tr>
<tr>
<td>At Retirement</td>
<td>0%</td>
</tr>
<tr>
<td>20th Year of Retirement</td>
<td>8%</td>
</tr>
<tr>
<td>Present value Of Lifetime Loss</td>
<td>5%</td>
</tr>
</tbody>
</table>

Assumptions: (1) Average annual salary growth 3%, (2) Inflation rate 2.5% (3) Present value discounted at 5%, assuming life expectancy of 25 years after retirement
<table>
<thead>
<tr>
<th>Institution</th>
<th>Social Security</th>
<th>University Retirement Plan</th>
<th>Total</th>
<th>GRAND TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee</td>
<td>Employer</td>
<td></td>
<td></td>
</tr>
<tr>
<td>University of Minnesota</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.50%</td>
<td>11.70%</td>
</tr>
<tr>
<td>University of Iowa</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.00%</td>
<td>11.20%</td>
</tr>
<tr>
<td>University of Michigan</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.00%</td>
<td>11.20%</td>
</tr>
<tr>
<td>Michigan State</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.00%</td>
<td>11.20%</td>
</tr>
<tr>
<td>Northwestern University</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.00%</td>
<td>11.20%</td>
</tr>
<tr>
<td>Penn State</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.00%</td>
<td>11.20%</td>
</tr>
<tr>
<td>Purdue University</td>
<td>6.20%</td>
<td>6.20%</td>
<td>4.00%</td>
<td>10.20%</td>
</tr>
<tr>
<td>University of Wisconsin</td>
<td>6.20%</td>
<td>6.20%</td>
<td>7.00%</td>
<td>13.20%</td>
</tr>
<tr>
<td>University of Nebraska</td>
<td>6.20%</td>
<td>6.20%</td>
<td>5.50%</td>
<td>11.70%</td>
</tr>
<tr>
<td>Ohio State University</td>
<td>0.00%</td>
<td>0.00%</td>
<td>11.00%</td>
<td>14.00%</td>
</tr>
<tr>
<td>Indiana University</td>
<td>6.20%</td>
<td>6.20%</td>
<td>0.00%</td>
<td>6.20%</td>
</tr>
<tr>
<td><strong>Average Big Ten</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>University of Illinois Tier I</td>
<td>0.00%</td>
<td>0.00%</td>
<td>8.00%</td>
<td>7.00%</td>
</tr>
<tr>
<td>University of Illinois Tier II</td>
<td>0.00%</td>
<td>0.00%</td>
<td>7.00%</td>
<td>8.00%</td>
</tr>
<tr>
<td>University of Illinois SMP</td>
<td>0.00%</td>
<td>0.00%</td>
<td>8.00%</td>
<td>8.00%</td>
</tr>
</tbody>
</table>

Illinois employer costs are estimates post 7.1.2014. Source: 2010 Buck Consulting study updated by UI HR
Supplementary Benefits Will Help To:

- Gain parity with peer institutions
- Improve ability to recruit and retain talent
- Enhance individual retirement savings
- Facilitate appropriate workforce transitions
How: Expand 403(b) Plan

- Supplementary 403(b) Retirement Plan established in 1964
- 403(b) allows employee and employer contributions
- Amend existing plan to make University contribution
- All current and future employees who are “SURS” eligible should receive contribution (Tier I, Tier II and SMP)
- Pensionable salary limited to IRS limit (currently $255,000)
Principles for Plan Design

• Provide retirement benefits comparable to peers

• Increase combined contribution level to accumulate adequate retirement savings

• Utilize mix of core and matching university contributions

• Encourage all participants to utilize matching program

• Follow industry best practice in plan design
Three Part Framework

A. A level of university contribution for all SURS eligible employees

B. University matching of employee contribution up to specified limit.

C. Additional contribution for Tier I members with salary caps based on portion of the individual’s salary that is above the cap

All pensionable salaries will be subject to IRS limit
A. University contributes 2% of all pensionable salary of all eligible employees

B. University provides 50% match for contributions made by employees to 403(b) accounts up to maximum of 2% of salary

C. In addition, University provides 100% match for Tier I members with salary caps based on portion of the individual’s salary that is above the cap up to a maximum of 5% of that amount

All pensionable salaries will be subject to IRS limit
Augmenting Retirement Savings

Individual works for 25 years and receives 2.5% annual salary increase. Fund earns 5% per annum. At retirement converts to 25 year annuity earning 5% return.

<table>
<thead>
<tr>
<th>Starting Salary</th>
<th>$40,000</th>
<th>$80,000</th>
<th>$120,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Accumulation</td>
<td>$217,186</td>
<td>$434,273</td>
<td>$651,558</td>
</tr>
<tr>
<td>Monthly Annuity at Retirement</td>
<td>$1,264</td>
<td>$2,539</td>
<td>$3,793</td>
</tr>
</tbody>
</table>

Annuity approximately equals 20 percent of final income
Discretionary University Contributions

- University contributions not guaranteed on an ongoing basis
- It will be set annually and can be changed or suspended in the future
- University retains right to prospectively terminate all employer contributions to the 403(b) plan
Necessary Steps After Board Approval

- Amend current 403(b) plan
- Legal review and approval of plan amendments
- Communicate program features to eligible employees
- Communicate new program guidelines to vendors
- Enrollment to program—communicate repeatedly
- Reprogram payroll, salary deferral and other systems
- Arrange transfer of contributions to vendors.