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Circular Letter

May 23, 2012

TO: **ALL PUBLIC AGENCY EMPLOYERS**

SUBJECT: **PHASE-IN OF IMPACT OF THE CHANGES IN ECONOMIC ASSUMPTIONS (INCLUDING DISCOUNT RATE)**

The purpose of this Circular Letter is to inform you of recent changes to the CalPERS economic assumptions and the impact this will have on employer contribution rates.

At the March 14, 2012 meeting, the CalPERS Board of Administration (Board) approved a recommendation to lower the CalPERS discount rate assumption, or the rate of investment return the pension fund assumes, from 7.75 to 7.50 percent. This will increase public agency employer rates for the 2013-14 fiscal year.

At the April 18, 2012 meeting, the Board approved a recommendation to phase-in the employer contribution rate increases over a period of two years.

Agencies with non-pooled plans will have the opportunity to elect not to phase-in the higher rates for 2013-14 by notifying their plan actuary prior to May 1, 2013.

Background

At its March meeting, the Board directed staff to develop a phase-in of the impact of the change in the price inflation assumption and discount rate over the next two years. Staff recommended that the phase-in be accomplished by requiring public agency employers to pay in 2013-14 one-third of the amortization payment that would otherwise be required for the increase in actuarial liabilities resulting from the change in assumptions. The remaining two-thirds will be paid by public agency employers over the remaining 19 years so that at the end of 20 years, the full increase in actuarial liabilities will have been paid.

For most plans, the proposed method will allow for a phase-in of roughly 50 to 55 percent of the required increase in employer rates resulting from the change in actuarial assumptions adopted by the Board on March 14, 2012.

Results

The Board's decision to phase-in the lower discount rate assumption will have the following estimated impacts on sample public agency employers:

Estimated Increase in Employer Contribution Rates in Fiscal Year 2013-14 (% of Payroll)

Group	Without Phase-in	Phase-in Rate	Phase-in Percentage
Public Agency Miscellaneous			
Sample Agency A	1.24%	0.65%	52.4%
Sample Agency B	1.15%	0.63%	54.8%
Public Agency Safety			
Sample Agency A	1.94%	1.00%	51.5%
Sample Agency B	1.62%	0.90%	55.6%

Phasing-in the impact of the change in assumptions by reducing the amortization payment in the first year is expected to result in higher contribution rates in the 19 years following the phase-in. Staff determined that employer rates in the 2nd through 20th year would be approximately 0.04 to 0.05 percent of payroll higher than the rates without the phase-in for miscellaneous plans and approximately 0.05 to 0.08 percent of payroll higher for safety plans.

To help illustrate the impact of the phase-in, below is a table showing the expected increase in employer rates resulting from the change in assumptions for a sample miscellaneous plan with and without the phase-in.

Estimated Increase in Employer Contribution Rates (% of Payroll)

	Without Phase-in	With Phase-in	Difference
Sample Public Agency Miscellaneous			
Year 1	1.24%	0.65%	(0.59%)
Years 2 - 20	1.24%	1.29%	0.05%

The measured impact of the change in the discount rate assumption for each agency will be known when the Actuarial Office completes the June 30, 2011 actuarial valuations in fall 2012. The June 30, 2011 valuations will set the employer rates that take effect on July 1, 2013.

The valuations for non-pooled plans will reflect the employer rates with the phase-in and will also disclose what the rates would be without the phase-in. Employers will be assumed to be using the phased-in rates. However, public agencies with non-pooled plans will have until May 1, 2013 to notify their CalPERS actuary if they decide they would prefer not to phase-in the increased rates.

Potential Accounting Impact

It is possible that the funding contribution determined in the annual valuation may be less than the Annual Required Contribution (ARC) under the current Governmental Accounting Standards Board (GASB) rules. This could create an accounting event and require special accounting treatment for the difference. It is advised that you speak with your auditor concerning this issue.

If you have any questions, please call our CalPERS Customer Contact Center at **888 CalPERS** (or **888**-225-7377).

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