VIDEOCONFERENCE MEETING

STATE OF CALIFORNIA

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

BOARD OF ADMINISTRATION

FINANCE & ADMINISTRATION COMMITTEE

ZOOM PLATFORM

TUESDAY, SEPTEMBER 14, 2021

3:15 P.M.

JAMES F. PETERS, CSR
CERTIFIED SHORTHAND REPORTER
LICENSE NUMBER 10063

APPEARANCES

COMMITTEE MEMBERS:

David Miller, Chairperson

Theresa Taylor, Vice Chairperson

Henry Jones

Fiona Ma, represented by Frank Ruffino

Lisa Middleton

Ramon Rubalcava

BOARD MEMBERS:

Margaret Brown

Rob Feckner

Eraina Ortega

Shawnda Westly

Betty Yee, represented by Lynn Paquin

STAFF:

Marcie Frost, Chief Executive Officer

Dan Bienvenue, Interim Chief Investment Officer

Michael Cohen, Chief Financial Officer

Matthew Jacobs, General Counsel

Anthony Suine, Deputy Executive Officer

Scott Terando, Chief Actuary

Fritzie Archuleta, Deputy Chief Actuary

Randy Dziubek, Deputy Chief Actuary

APPEARANCES CONTINUED

STAFF:

Kelly Fox, Chief, Stakeholder Relations

Allen Han, Associate Pension Actuary

Pam Hopper, Committee Secretary

Arnita Paige, Chief, Pension Contract and Prefunding Programs

Nina Ramsey, Associate Pension Actuary

Michele Nix, Controller

Julian Robinson, Senior Pension Actuary

Dallas Stone, Chief, Operations Support Services Division

ALSO PRESENT:

Tim Behrens, California State Retirees

Larry Woodson, California State Retirees

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PROCEEDINGS

CHAIRPERSON MILLER: Okay. We'll convene the Finance and Administration Committee open session and call to order. And the first order of business is the roll call. Ms. Hopper, please.

COMMITTEE SECRETARY HOPPER: David Miller?

CHAIRPERSON MILLER: Here.

COMMITTEE SECRETARY HOPPER: Henry Jones?

COMMITTEE MEMBER JONES: Here.

COMMITTEE SECRETARY HOPPER: Frank Ruffino for Fiona Ma?

ACTING COMMITTEE MEMBER RUFFINO: Present.

COMMITTEE SECRETARY HOPPER: Lisa Middleton?

COMMITTEE MEMBER MIDDLETON: Present.

COMMITTEE SECRETARY HOPPER: Stacie Olivares?

CHAIRPERSON MILLER: Excused.

COMMITTEE SECRETARY HOPPER: Ramon Rubalcava?

COMMITTEE MEMBER RUBALCAVA: Here.

COMMITTEE SECRETARY HOPPER: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Here.

COMMITTEE SECRETARY HOPPER: Mr. Chair, all is in attendance with Stacie Olivares being excused.

CHAIRPERSON MILLER: Excellent. Thank you.

So Item 2, approval of the September 14th, 2021 Finance and Administration Committee timed agenda. What's the pleasure of the Committee?

VICE CHAIRPERSON TAYLOR: Move approval.

COMMITTEE MEMBER JONES: Move approval.

ACTING COMMITTEE MEMBER RUFFINO: Second.

CHAIRPERSON MILLER: Got it. Moved by Taylor, seconded by Ruffino?

CHAIRPERSON MILLER: And we'll -- any discussion?

Hearing none.

Call for the question. Ms. Hopper.

COMMITTEE SECRETARY HOPPER: Henry Jones?

COMMITTEE MEMBER JONES: Aye.

COMMITTEE SECRETARY HOPPER: Frank Ruffino for Fiona Ma?

ACTING COMMITTEE MEMBER RUFFINO: Aye.

COMMITTEE SECRETARY HOPPER: Lisa Middleton?

COMMITTEE MEMBER MIDDLETON: Aye.

COMMITTEE SECRETARY HOPPER: Stacie Olivares?

CHAIRPERSON MILLER: Excused.

COMMITTEE SECRETARY HOPPER: Ramon Rubalcava?

COMMITTEE MEMBER RUBALCAVA: Here.

COMMITTEE SECRETARY HOPPER: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Aye.

COMMITTEE SECRETARY HOPPER: Ramon, that was an aye for this, please?

COMMITTEE MEMBER RUBALCAVA: That was an aye. I apologize. Aye.

COMMITTEE SECRETARY HOPPER: Thank you.

Mr. Chair, I have all ayes, motion being made by Theresa Taylor, seconded by Frank Ruffino for Fiona Ma.

CHAIRPERSON MILLER: Thank you.

Okay. On to Item 3, the executive report. Welcome, Mr. Cohen.

CHIEF FINANCIAL OFFICER COHEN: Thank you, Mr. Chair and Board members. I'm Michael Cohen with the Financial Office. Just a couple of things to highlight before we get into the Agenda. First, as you know, we'll be continuing our asset liability management discussion later in this Committee with the experience study. But I didn't want to just appreciate our comments we received yesterday from the public, particularly our employers, regarding the stakeholder outreach that we've been doing. Just to highlight that we have, since the last time we met, held two more ALM webinars in July and August. And those are all on our ALM homepage on the CalPERS website.

And we'll be doing an additional one in November, as well as our Ed Forum conference we'll have an ALM-specific conversation in October. In addition to that, we are going out to as many of the various stakeholders meetings in the coming months to continue to discuss the portfolios and the experience study we'll discuss shortly.

And then second, many of you know that we offer our employees -- the employers the opportunity to prepay their unfunded liability at the start of each year for an interest rate discount. It gives the Investment Office some extra months to invest the funds. And that is passed along to our employers. I'm happy to report that this year, 74 percent of our employers took advantage of that opportunity paying roughly 80 percent of the unfunded liabilities that were owed. So we certainly appreciate that opportunity that we're able to have that working relationship with our employer community.

With that, let me turn it back to you, Mr. Chair.

CHAIRPERSON MILLER: Okay. Thank you. And that's very encouraging.

So our next item is Item 4, action consent items, the approval of the April 19th, 2021 Finance and Administration Committee meeting minutes. So do I have a motion?

VICE CHAIRPERSON TAYLOR: Move approval.

CHAIRPERSON MILLER: Moved by Taylor, seconded by?

Someone?

COMMITTEE MEMBER MIDDLETON: Second.

CHAIRPERSON MILLER: Seconded by Ms. Middleton.

And so any discussion?

Hearing none.

I'll call for the question.

Ms. Hopper.

COMMITTEE SECRETARY HOPPER: Henry Jones?

COMMITTEE MEMBER JONES: Aye.

COMMITTEE SECRETARY HOPPER: Frank Ruffino for Fiona Ma?

ACTING COMMITTEE MEMBER RUFFINO: Aye.

COMMITTEE SECRETARY HOPPER: Lisa Middleton?

COMMITTEE MEMBER MIDDLETON: Aye.

COMMITTEE SECRETARY HOPPER: Stacie Olivares?

Excused.

CHAIRPERSON MILLER: Excused.

COMMITTEE SECRETARY HOPPER: Ramon Rubalcava?

COMMITTEE MEMBER RUBALCAVA: Aye.

COMMITTEE SECRETARY HOPPER: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Aye.

COMMITTEE SECRETARY HOPPER: Mr. Chair, on Agenda Item 4a, approval of the April 19, 2021 Finance and Administration Committee meeting minutes, all ayes, motion made by Theresa Taylor, seconded by Lisa Middleton.

CHAIRPERSON MILLER: Thank you, Ms. Hopper. Very good.

We move now to the information consent items.

And I do have requests to pull a couple of items. I believe it's 5d and 5f. So we'll go to 5d, annual discharge of accountability for uncollectible debt. And I guess I'll come back to Mr. Cohen or whoever -- what staff will be addressing it.

CHIEF FINANCIAL OFFICER COHEN: Sure. Yeah, if we can go ahead and pull Controller Nix forward, but we're happy to take any questions, unless the Board is interested in a presentation on this item.

CHAIRPERSON MILLER: Ms. Brown, what would your preference be, since you asked for this one.

BOARD MEMBER BROWN: Okay. Yeah. I can just ask my -- a couple questions.

CHAIRPERSON MILLER: Okay.

BOARD MEMBER BROWN: So I think I ask every year about the uncollectible debt. I do appreciate getting the detailed spreadsheet, because on this report is a summary of the debt. And I'm just wondering if you can't tell me about some of the larger items that appear when we -- we look at it, there's some -- I think some of the larger items are statute of limitations. I sorted that data table, of course, by dollar amount like all good accounting people do.

And, you know, the highest one an individual, it says miscellaneous, $412,000 for one individual. That's a -- that's a -- I mean, it's a tiny house in Sacramento, but I'm wondering -- it used to be a large house in Sacramento. Let's be clear. It's a tiny house in Sacramento. But can you tell me what that was? I think that's the broken finger --

CHIEF FINANCIAL OFFICER COHEN: Sure. Why don't --

BOARD MEMBER BROWN: -- that's the broken finger police officer or something like that.

CHIEF FINANCIAL OFFICER COHEN: Yeah. Let me have -- also bring forward Anthony Suine, who -- typically these cases start in our Customer Service Unit and then eventually make it -- their way over to Controller Nix for the final dissolution and when they show up on the report. But Anthony is going to have much more detail on the individual cases.

BOARD MEMBER BROWN: Yeah.

CHIEF FINANCIAL OFFICER COHEN: So Anthony, the $400,000 one, do you want to provide a quick summary of that?

BOARD MEMBER BROWN: So before we -- before we do the summary on that case, can you just explain for me and other members of the Board -- or the public sort of how the debt gets given to -- I would assume it comes to the Finance Office to try to collect once benefits can't do it or it tells you about the problem. But maybe not. Maybe it's under Mr. Suine's department that they try to collect these amounts. I'm just -- I'm curious as to the process. And then we'll go -- I want to go over the two big ones. There's three hundred -- 412,000 and then there's another one for 314. Those are pretty big dollar amounts. And you think --

CHIEF FINANCIAL OFFICER COHEN: They are, yeah.

BOARD MEMBER BROWN: You think we'd assign some staff to collect that, not that $12.86.

CHIEF FINANCIAL OFFICER COHEN: Let's have Michele give an overview from the Financial Office perspective, and then we can turn it over to Anthony to add anything and then go into the individual cases.

CONTROLLER NIX: Sure. Happy to do so. Michele Nix, Controller, CalPERS team member.

The process starts with the -- Anthony's team, but then as it -- as it's noticed to become uncollectible for whatever reason, then it comes to the Finance area, where we do the process of dunning it. The law requires us that we send out letters and we also make phone calls to the members and to anyone that could be associated with a member to try to collect the debt.

We do this every month until it's seen that it can't -- probably three times we send three separate different letters and we make several phone calls. And at that point in time, we keep track of it. And if it happens to go into the statue of limitations, that's when it gets written off. So all the items on our list today have met the statute of limitations, either the three years or the 10 years, depending on what it was.

BOARD MEMBER BROWN: Great. So the question is though, at what point does Mr. Suine's group kick it over to the business office as uncollectible? Because if Mr. Suine's department is kicking over -- kicking it over to you at, you know, 33 months -- I assume the statue of limitations is three years, but maybe we can talk about that. But if they're kicking it over to you last minute, then that's not enough time for your department to collect.

And I would certainly hope that trying to collect a debt, especially one of $412,000 that we'd make an effort better than writing three letters. I mean, I would think that we would file a claim, you know.

DEPUTY EXECUTIVE OFFICER SUINE: I can assist

BOARD MEMBER BROWN: Thank you, Mr. Suine.

DEPUTY EXECUTIVE OFFICER SUINE: I can assist. I think once I explain these two cases, you would get the feel for, at least on these, how they're handled.

So the first one was the individual who came to us via ethics complaint that he was not -- no longer disabled. And so we reviewed that case, worked with the employer to reevaluate the individual. It was ultimately determined that he was not disabled. We went back to his original disability retirement date and terminated the disability retirement, and the member appealed.

So the case went to the administrative law judge. And the administrative law judge ruled in our favor that he should be removed from the roll. However, the administrative law judge also gave us some direction about what to allow the member to do as a result of the no longer being disabled. So he instructed us to go back to the member's eligibility for service retirement date and allow him to service retire. And he also limited our ability to collect to three years. So we were making the case that it could have been fraud, that the employer and the member, you know, were not truthful in this situation. But ultimately, we agreed with the administrative law judge's decision, came to the Board, and that decision was approved.

So when you took it all the way back to the original date of the disability retirement, it created a $611,000 overpayment. But then when extended to only three years, we had to write off everything beyond that, which created the $412,000 write-off. So there was no ability to dunn the individual and try to collect the extra $412,000 The judge really made that decision to write-off that amount.

BOARD MEMBER BROWN: Thank you.

And then what are we doing to collect the balance that -- isn't --

DEPUTY EXECUTIVE OFFICER SUINE: Yeah. So we've already -- we give the member two options. They can write us a check or they can choose an actuarial equivalent reduction, which basically takes the present value of the overpayment and then they can take a lifetime reduction to their allowance. So we collect immediately on those -- on either one of those options within 30 days from the member.

BOARD MEMBER BROWN: Okay. Great. Thank you for that. And then the other one --

DEPUTY EXECUTIVE OFFICER SUINE: Yep.

BOARD MEMBER BROWN: -- the 314, the calculation adjustment.

DEPUTY EXECUTIVE OFFICER SUINE: Yep. So the 314,000 is the second highest one. This was a working-after-retirement case. We looked at all the facts that occurred. There was like 16 years of, you know, I would say, you know, non-egregious. It wasn't a -- it wasn't a knowingly and willingly type of situation. But we look at all the facts of the case, we applied the $400,000 overpayment, taking his retirement -- reinstating him back to the working-after-retirement violation. The member appealed and that case went up to our Legal Office and our Legal Office works with the member and any attorneys that are involved. And ultimately in looking at the facts of the case, we were -- we ended up settling with the member for an overpayment of less than the 314,000. I believe it ended up being approximately a hundred thousand dollars that we collected from the member and wrote-off the remaining $314,000.

So again, a situation where we didn't dunn the individual or have money to collect there.

BOARD MEMBER BROWN: Great. And then -- and then how big is your team that works on collecting these overpayments? It's going to come up in Risk and Audit later, but I'm just curious how big and what poor souls that work for you, Anthony, have to do this work for you?

DEPUTY EXECUTIVE OFFICER SUINE: So depending on where the -- where the overpayment lies, right? Sometimes it's part of the retirement calculation. You know, typically it ends up in the retirement, but -- so they just handle this as part of their normal duties, right, the retirement processing team. We have an escalation unit that works on these more complex cases and the appeals. And so it's -- you know, all the team members, which there might be 50 plus processing retirements, but a team about five or six individuals who handle escalated type of cases and deal with the overpayments. And they're the ones who are able to handle this. And then we hand it off like Michelle said to her team in cases where we do try and collect from an individual. And only when there's -- ultimately determine there's no source to collect from, we write it off as a no source to collect from.

BOARD MEMBER BROWN: And then one more --

CONTROLLER NIX: And I have a team about --

BOARD MEMBER BROWN: Go ahead.

CONTROLLER NIX: -- about four to five people. Oh, sorry. I have a team of four to five people that actually spend all of their time doing collections.

BOARD MEMBER BROWN: Well, thanks for that. That's -- it's not a fun job. I did collections when I first got into accounting and it was -- it was one tough job.

And then, Mr. Suine, I do appreciate all this -- all the detail. You know, I'm looking also at a large number of these are payments issued after payee's death. A lot of them are very pennies, dollars, and then -- and then some of them are larger, 10,000, 9,700, 8,600. And so, I mean, I understand that -- does this have to do with the fact that we're not getting the death notices on time from Social Security or -- I mean, is this generally what this is or is it just like the one month that's lagging, and then they do an appeal, because they say they needed the money. I mean, I'm trying to just figure out what that is.

DEPUTY EXECUTIVE OFFICER SUINE: So the majority of those -- you know, the mid-thousand -- the ones that you identified that are death benefit related, those are the ones that typically -- and you'll hear a little bit more in the audit presentation about they exceeded a 10-year statute of limitations where we just can't collect --

BOARD MEMBER BROWN: Um-hmm.

DEPUTY EXECUTIVE OFFICER SUINE: -- and it's not worth pursuing it anymore. There's no source to collect from. So those are overpayments that are typically smaller in nature. The other are internal errors that come up due to audits, adjustments that are made to member accounts. And we uncover mistakes that were made say 10 to 15 years ago.

And, you know, they can vary of -- the money got put into an incorrect formula or the community -- the ex-spouse came forward and said, hey, where is my money, and we -- we set up a complex community property situation where we were supposed to at a certain time take that money from the member and give it to the ex-spouse. And so those are cases where we have to go back and we have to make those adjustments to correct the member's allowance going forward.

But when we make the error, they're only subject to the three-year statute. So again, there's no collection there. We must write-off everything that exceeds the three-year statue of limitations and we charge the member for the three years worth of overpayments, in that same fashion of collecting via AER or having them pay in full.

BOARD MEMBER BROWN: Well. Thank you. This information is very helpful. I will tell you when my mother passed, she was -- she's a retired teacher. She was receiving a small CalSTRS payment, and of course -- a pension. And she passed on December 28th, and so they wanted to take back the December payment. And we filed an appeal and we were allowed to keep that. And I would assume that CalPERS has ways to do that as well, I would hope. But it is -- it is tough when it's just a -- you know, one month overpayment.

But I appreciate all this information and I appreciate the efforts that both you and the business office makes in trying to collect this debt, because it's every -- every dollar can go back into the pension fund. So I appreciate the help.

Thank you, Mr. Cohen.

CHAIRPERSON MILLER: Okay. And 5f, did you want the item presented or do you just have questions, Ms. Brown?

CHIEF FINANCIAL OFFICER COHEN: You've got to unmute

CHAIRPERSON MILLER: Oh, you're muted.

BOARD MEMBER BROWN: I need to go back to my notes, so hold on.

CHAIRPERSON MILLER: Okay. It's --

BOARD MEMBER BROWN: I'm going to go into Diligent. Hold on.

CHAIRPERSON MILLER: -- pension contracts management program annual report.

BOARD MEMBER BROWN: It's -- is it the same people, Mr. Cohen?

CHIEF FINANCIAL OFFICER COHEN: No. It will be Arnita Paige, but I think she'll probably be able to hear you, if you want to start asking questions.

BOARD MEMBER BROWN: Yeah, it's -- yeah, and I really appreciate the PowerPoint. I think it would have been helpful for people to actually see the presentation, but I'm very happy to see that we're working on making payment arrangements and collecting and getting payment plans. On page -- 5f, page three of six, you talk about your administrative highlights for the cross-program termination process. Especially I'm glad to hear that you've accelerated the term -- turnaround time frame, and that you actually discuss the payment terms prior to the final termination. I know I heard from some employers that said they were sort of surprised to hear after they said we want termi -- final, final terminate, right, final answer, and then they got a big number. So I wanted to thank you for being more helpful to employers and getting the information to them.

And then my -- the one concern I have on page four of six, that's the agency termination report, we've got one there that's a JPA. And as we all know, that's where we've had problems with those old agreements. And my question was is this one of those ones with -- that have the problematic agreements where the agencies that form the JPA are not obligated to pay or did the legislation that we passed solve that problem for us?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you for the question. And I want to make sure, are you on page four of the PowerPoint in referencing the termination report?

BOARD MEMBER BROWN: Yes. Yes.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Okay. So this particular JPA -- this -- they're basically -- it's not -- the law basically will assist us in this matter. This is voluntary. The employer actually, at least to us just discussing termination information. So we don't foresee any issues with this employer at this time.

CHIEF FINANCIAL OFFICER COHEN: So just to differentiate from the other JPAs that have been a problem, those are ones that did fail to make payments --

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Right.

CHIEF FINANCIAL OFFICER COHEN: -- and therefore went into involuntary termination --

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Right.

CHIEF FINANCIAL OFFICER COHEN: -- because they, you know, weren't making the payments to CalPERS. And so -- and that's what Arnita is referencing. These are ones voluntarily choosing to follow the process, and in doing so would make a lump sum payment, so that retirees payments would be secure for their entire lifetime, as everyone works through the system.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF

PAIGE: Correct.

CHIEF FINANCIAL OFFICER COHEN: You're on mute, Board Member Brown.

BOARD MEMBER BROWN: I am sorry.

No, I appreciate that information. And so just sort of overall, do we think we're doing better with managing employers who are having financial difficulty. I know, you know, we keep hearing that, you know, our rates are harming them, but I'm just wondering are we seeing more? There's no -- there's no tracking, like, you know, multi-year telling me how many employers or how many, you know, are moving in and moving out of default. So I mean, I --

CHIEF FINANCIAL OFFICER COHEN: Right. I think it was at the beginning of the pandemic certainly it was a concern of all of us that we could see, you know, a large number of employers running into problems. We immediately set up a webinar to discuss sort of what the options were and, you know, the individual jurisdictions could approach us for discussion about payment plans, if they were having trouble making their payments. We had a surprisingly low number of employers even approach us for initial conversations, which was great. And certainly, the quick bounce back of the economy has helped to mitigate that concern.

But obviously, our rates continue to be a pressure point on many jurisdictions. And I think that's -- as you heard yesterday, it will -- it's one of the main underlying discussion points that you as a Board have in this ALM process, to understand what your decisions mean for the individual employers. And, you know, Scott's actuarial team, you know, is able to provide a sampling as they've done yesterday in terms of the likelihood of what would happen with rates.

You know, with 4,000-ish plans, it's hard to, you know, summarize any -- for any, you know, one plan there's, you know, a variety of iterations, depending on a jurisdiction's circumstances. But I will say overall, as you started with, we're very pleased with the team at CalPERS that have sort of reviewed the termination process to make sure that if we need to use it, and hopefully, you know, we use it very little, it does run as smooth as possible for jurisdictions.

This annual report format we started a year ago, so it's a little bit hard, I agree, to sort of find long-term trend lines on jurisdictions. But as we go forward, we're certainly planning on sticking with this format, so it will be much easier, you know, in two or three years to get a better sense of the trend. But at this point, I would say the number of jurisdictions in the termination process are the lowest that I've seen in my time at CalPERS.

BOARD MEMBER BROWN: Well, thank you. That's what it looks like to me. I've only been really looking at these for four years, but this report didn't seem as bad or dire as the other ones. And so I wanted to congratulate you, but I wasn't sure, because I don't have any other data to base it on. But I also --

CHIEF FINANCIAL OFFICER COHEN: I think congratulations to Arnita's team is well in order.

BOARD MEMBER BROWN: Excellent. Well, I do appreciate it. And just, you know, outreaching to the employers, I think the fact that they have the tool, the pension tool as well helps the ability to, you know, payoff unfunded liabilities, you know, finance that. I mean, all these tools that are in place help employers and hopefully keep them from, you know, panicking.

And I just think with your help and guidance, we're going to make sure that employees' pensions, you know, are secure. And hopefully we'll just keep, you know, killing it when we -- with our returns and, you know, everything will be glowing. You know, we'll be at a hundred percent in no time, so -- but I do appreciate all the efforts in the report. I think it's kind of good news. Next time, we should just share it and not just put it on consent.

Thank you.

CHIEF FINANCIAL OFFICER COHEN: Thank you.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you.

CHAIRPERSON MILLER: Okay. Thank you and thank you to the team for the answers and the fine work behind the answers.

So that moves us to our first action agenda item 6a, our Actuarial team, Mr. Cohen. Revised State Employer/Employee Contribution Rates.

CHIEF FINANCIAL OFFICER COHEN: Yes, I think --

CHAIRPERSON MILLER: Mr. Terando.

CHIEF FINANCIAL OFFICER COHEN: Yeah, I think Scott is here with his team to present on this item. There he is, so I will turn it to him.

CHAIRPERSON MILLER: Excellent.

CHIEF ACTUARY TERANDO: Good afternoon, Mr. Chair, members of the Committee. Scott Terando, CalPERS Chief Actuary.

This item is an action item and looks for approval of revised rates for certain State contribution rates. Back in April, the Board adopted the contribution rates for the State for fiscal year 2021-22. However, there has to be -- there has been some adjustments that needs to be made due to a change in the member rates.

I'm going to have Nina Ramsey step through all the details and provide additional insight on to the changes needed.

(Thereupon a slide presentation.)

ASSOCIATE PENSION ACTUARY RAMSEY: Thank you, Scott.

Good afternoon, Mr. Chair, members of the Committee. Nina Ramsey, CalPERS actuarial team member. As Scott mentioned, I will be presenting to you for your approval revised State employer contribution rates for fiscal year 2021-22.

Next slide, please.

--o0o--

ASSOCIATE PENSION ACTUARY RAMSEY: The revised rates are based on data used in our June 30th, 2020 actuarial valuation. As Scott mentioned, the Board previously adopted employer contribution rates for all five State plans at the April meeting. Subsequent to that meeting, Bargaining Units 5 and 9 have negotiated member contribution rate increases effective July 1st of this year.

The increases to the member contribution rates affect the calculation of the required employer contribution rates, and as such, we will need to revise the employer contribution rates for future contributions. It is the Board's policy that when member contribution rates change, that these be reflected in the employer contribution rates at the next opportunity, which is today's meeting.

Next slide, please.

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ASSOCIATE PENSION ACTUARY RAMSEY: Bargaining Unit 5 has initiated their agreement for employees to pay half of the normal cost, Bargaining Unit 9 had a similar agreement in place for fiscal year 2019-20. That agreement ended June 30th of 2020, but they have negotiated to return to those rates for their members effective July 1st of this year and effective for one year, meaning that it would end June 30th, 2022.

Both of these agreements apply to classic and PEPRA members. So it is both groups that will be paying half of the normal cost.

Next slide, please.

--o0o--

ASSOCIATE PENSION ACTUARY RAMSEY: Here, we have the rates that the Board approved at the April meeting and the impact of the increased membership contributions to those rates, leaving us with a revised total rate for fiscal year 2021-22. The increase in member contribution rates for the State miscellaneous plan resulted in a reduction of 0.6 percent and for CHP resulted in a reduction of 0.93 percent.

Next slide, please.

--o0o--

ASSOCIATE PENSION ACTUARY RAMSEY: So here we have the revised total rate, which includes those reductions from the previous slide, also the additional statutory contributions from Government Code 20683.2, leaving us with a final revised total contribution for fiscal year 2021-22. The additional statutory contribution is just for information purposes. It is not something we are asking the Board to approve.

Next slide, please.

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ASSOCIATE PENSION ACTUARY RAMSEY: So these are the member contribution rate increases effective July 1st of this year. Patrol members in Bargaining Unit 5 will increase from 11.5 to 12.5 percent and miscellaneous members in Bargaining Unit 5 will increase from 8 to 8 and a quarter percent. I would like to note that the patrol members in Bargaining Unit 5 will have their employee contribution rate increased one percent each year, until it ultimately reaches 14.75 percent in fiscal year 2024-25, as that is the current -- currently, half of the normal cost would be the 14.75 percent.

For Bargaining Unit 9, miscellaneous members are increasing from 8 to 8 and a half percent, and safety members are increasing from 11 to 11 and a half percent. And currently, with the agreement they have in place right now, those rates will revert back July 1st next year to the lower rates on this slide.

This concludes my presentation and I would be happy to take any questions.

ASSOCIATE PENSION ACTUARY RAMSEY: Mr. Miller, you are muted.

CHAIRPERSON MILLER: There we go. I don't see any questions in the chat. And since I can't see everyone with the screen up -- okay. Now, I can see, so I don't see anybody indicating they have a question, so thank you for the presentation. It was very clear and very helpful information. And we'll move on.

CHIEF FINANCIAL OFFICER COHEN: This one is an action item.

CHAIRPERSON MILLER: Oh, no. We have to -- we have to vote. We have to vote. So --

COMMITTEE MEMBER JONES: Move approval.

CHAIRPERSON MILLER: Moved by Mr. Jones.

Seconded by?

VICE CHAIRPERSON TAYLOR: I'll second.

CHAIRPERSON MILLER: Who was that? Was that -- oh, Ms. Taylor.

VICE CHAIRPERSON TAYLOR: Yes.

CHAIRPERSON MILLER: Okay. So we'll call for the question. Ms. Hopper.

COMMITTEE SECRETARY HOPPER: Henry Jones?

COMMITTEE MEMBER JONES: Aye.

COMMITTEE SECRETARY HOPPER: Frank Ruffino for Fiona Ma?

ACTING COMMITTEE MEMBER RUFFINO: Aye.

COMMITTEE SECRETARY HOPPER: Lisa Middleton?

COMMITTEE MEMBER MIDDLETON: Aye.

COMMITTEE SECRETARY HOPPER: Stacie Olivares?

Excused.

Ramon Rubalcava?

COMMITTEE MEMBER RUBALCAVA: Yes. Aye. Aye. I'm voting yes.

(Laughter.)

COMMITTEE SECRETARY HOPPER: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Aye. Yes. Whatever.

COMMITTEE SECRETARY HOPPER: Mr. Chair, I have all ayes, motion being made by Henry Jones, seconded by Theresa Taylor, on Agenda Item 6a Revised State Employer and Employee Contribution Rates.

CHAIRPERSON MILLER: Excellent. And it is good to be here when you say "aye", so present helps as well. It's late in the day and we want to reaffirm that we're present and voting, so --

(Laughter.)

CHAIRPERSON MILLER: Okay. That brings us to our last action agenda item. 6b, the 2021 CalPERS Board of Administration special public agency member notice of election. And, Mr. Cohen, do we have Mr. Stone?

CHIEF FINANCIAL OFFICER COHEN: He is here. I will turn it to Mr. Stone.

OPERATIONS SUPPORT SERVICES DIVISION CHIEF STONE:

Good afternoon, members of the Board. Dallas Stone, CalPERS team member. This is an action item seeking the Finance and Administration Committee's approval to initiate the 2021 special public agency member election by adopting the notice of election. This election will be conducted to fill the public agency representative seat, which was vacated by Mr. Jason Perez prior to the term's expiration.

At the July 2021 offsite meeting, the Board was provided with information on the tentative election schedule. The notice of election, which is included as Attachment 1 to this item outlines the election schedule and other requirements. The proposed notice of election for this special election is consistent with the tentative election schedule previously provided to you.

If approved, we will release the notice of election on October 25th, 2021, which will also start the nomination period. Nomination petitions containing 250 valid original signatures will need to be submitted by December 16th, 2021. All forms related to the nomination requirements will be posted on the CalPERS Board election webpage. Interested candidates may also request a copy of the forms directly by contacting the Board election office.

After approval, the notice of election will be distributed electronically to members from their employers who will receive it from CalPERS via a circular letter.

I'm happy to answer any questions you have at this time. Thank you.

CHAIRPERSON MILLER: Okay. I'm not seeing any requests for questions and I'm not seeing anybody waving frantically to speak. So thank you for that. It's been --

VICE CHAIRPERSON TAYLOR: Move approval.

COMMITTEE MEMBER JONES: Second.

CHAIRPERSON MILLER: Moved by Taylor, seconded by Jones.

So, Ms. Hopper, call for the question.

COMMITTEE SECRETARY HOPPER: Henry Jones?

COMMITTEE MEMBER JONES: Aye.

COMMITTEE SECRETARY HOPPER: Frank Ruffino for Fiona Ma?

ACTING COMMITTEE MEMBER RUFFINO: Aye.

COMMITTEE SECRETARY HOPPER: Lisa Middleton?

COMMITTEE MEMBER MIDDLETON: Aye.

COMMITTEE SECRETARY HOPPER: Stacie Olivares?

Excused.

Ramon Rubalcava?

COMMITTEE MEMBER RUBALCAVA: Aye.

COMMITTEE SECRETARY HOPPER: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Aye.

COMMITTEE SECRETARY HOPPER: Mr. Chair, I have a motion being made by Theresa Taylor, seconded by Henry Jones, all ayes, for Agenda Item 6b, 2021 CalPERS Board of Administration Special Public Agency Member Notice of Election.

CHAIRPERSON MILLER: Excellent. Okay.

So move right along to 7a, information agenda item, Annual Actuarial Valuation Terminated Agency Pool. And, Mr. Cohen, do we have Julian Robinson?

CHIEF FINANCIAL OFFICER COHEN: He is here from the Actuarial Office and I will turn it to him.

CHAIRPERSON MILLER: Great.

SENIOR PENSION ACTUARY ROBINSON: Good afternoon, Mr. Chairman, members of the Committee. I'm happy to present this afternoon the Terminated Agency Risk Pool, June 30, 2020 valuation. We present this valuation every year to the Board.

Next slide, please.

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SENIOR PENSION ACTUARY ROBINSON: The TAP, the Terminated Agency Pool, has 108 -- 119 plans. There were eight agencies added in the valuation which we conducted as of June 30, 2020. The funded ratio of the pool is 176.2 percent. We'll see some further details shortly.

Next slide, please.

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SENIOR PENSION ACTUARY ROBINSON: The changes since the last valuation were the addition of these eight agencies, which you see on the screen in front of you. They added approximately $38 million of accrued liability to the fund and they also brought in assets around that amount as well.

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SENIOR PENSION ACTUARY ROBINSON: There were assumption changes in -- during the valuation. The discount rate changed down to 1.48 percent. In the prior valuation, it was 2.62 percent. The inflation rate also was decreased to 1.65 percent from 1.85 percent. The discount rate and inflation are set by Board policy. The method is using 30-year treasury bonds as the -- to set the discount rate. And as the Committee is aware, bonds -- yields on bonds moves up and down each year, so therefore the discount rate and the inflation assumption also vary from year to year.

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SENIOR PENSION ACTUARY ROBINSON: On this slide, you can see a summary of the financial condition of the plan. I'm not sure why the June 30, 2020 results are a little bit obscured. At least on my screen, I can't see them clearly. But the market value of assets, as of the most recent valuation, is $366 million. There's approximately $208 million in accrued liability. So the unfunded accrued liability is negative $158 million, which is a funded ratio of 176.2 percent.

As you'll notice, there was a decrease in the funded ratio from the previous year. This was mostly due to, number one, the addition of new plans into the -- into the pool and also as a result of a change in the discount rate. But you can also see that the unfunded accrued liability increased -- or the -- essentially, the surplus increased from 152 million, 153 million to 158 million.

So the surplus absolute number did increase over the period.

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SENIOR PENSION ACTUARY ROBINSON: The Terminated Agency Pool assets are invest -- are invested in two separate segments. The first segment is what we call the immunized segment, which represents a -- a portfolio of bonds, which the Investment Office updates every year to match the cash flows expected from the benefit payments in the fund.

Any surplus amount is invested with the rest of the PERF in the -- in the large fund. And as you can see, the split between the amount in the immunized segment and surplus segment is approximately 50/50. The return that the TAP received from the 19-20 fiscal year was 10.7 percent.

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SENIOR PENSION ACTUARY ROBINSON: The last two slides show some of the sensitivity that the plan has or the pool has for changes in mortality. This is what we do with all of our pools in the pension plans, we want to see what would happen if mortality rates are 10 percent heavier or 10 percent lighter. And here, we can see that there would be a movement of about $8 million of increase if mortality rates dropped, and a decrease of about seven percent of accrued liability if the mortality rates increased.

On the next slide --

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SENIOR PENSION ACTUARY ROBINSON: -- we show the sensitivity to change of inflation. The current inflation assumption is 1.65. If there was a lower inflation, then the accrued liability would drop by about $26.8 million. If the inflation rate was one percent above what we had assumed, it would increase the liability about $13.8 million.

That's the end of my presentation, I'd be happy to take any questions on the Terminated Agency Pool.

CHAIRPERSON MILLER: Thank you. A very comprehensive and understandable presentation. And I see no questions, and no one indicating they have -- oh, I see Henry is waiving. So Henry go ahead. You have the floor.

COMMITTEE MEMBER JONES: I don't know what's happening to my chat box. I got it in there and just like Rob said he doesn't see it -- didn't see it. And that's -- I don't know what's going on, but I show it on my end, so something is wrong.

But anyway, on this -- the page of this

attachment, page five of eight, back to that page, and I think I raised the same question a year ago when the last time this was -- and it's just a technical -- technicality of the unfunded liability with a negative 153.8. And I understand why it's negative, because you use the term unfunded, so it's somehow -- but if you're just looking at this, you would think there's a problem. But it's a positive problem, but I don't know how you deal with that, because it's --

SENIOR PENSION ACTUARY ROBINSON: Yeah, right. That's the pension convention that we have in order to report.

COMMITTEE MEMBER JONES: Say that again.

SENIOR PENSION ACTUARY ROBINSON: A convention we have throughout CalPERS is to express an unfunded liability as a positive number, if it's a -- if there's a shortfall in the assets, and as a negative number if there's a surplus in assets.

COMMITTEE MEMBER JONES: Yeah, I understand what's showing.

SENIOR PENSION ACTUARY ROBINSON: Um-hmm.

COMMITTEE MEMBER JONES: Maybe you should put an asterisk by it, because if you just look at cold, it will look like it's a problem, but I understand that it's a good problem.

(Laughter.)

SENIOR PENSION ACTUARY ROBINSON: Absolutely, yes.

CHAIRPERSON MILLER: Okay. Thank you.

Yeah and I think what's happened. When they're sharing the screen, it cuts off part of the chat box or makes it disappear. And so until we come back to the screen view, I couldn't see you waving, so...

COMMITTEE MEMBER JONES: Oh, okay. Okay.

CHAIRPERSON MILLER: Yeah. Okay.

COMMITTEE MEMBER JONES: I try to get my questions in before it goes up then okay.

CHAIRPERSON MILLER: Yeah. So do we have a motion?

COMMITTEE MEMBER JONES: Move approval.

CHIEF FINANCIAL OFFICER COHEN: This one is actually an information item.

CHAIRPERSON MILLER: Oh, these are -- were' back to information, so --

CHIEF FINANCIAL OFFICER COHEN: Thank you, Mr. Chair.

CHAIRPERSON MILLER: Okay. So thank you. Moving along to information Item B, Long-Term Care Valuation. Mr. Cohen have we got Ms. Archuleta and her team?

CHIEF FINANCIAL OFFICER COHEN: Fritzie is here.

I see her face. So take it away, Fritzie.

(Thereupon a slide presentation.)

DEPUTY CHIEF ACTUARY ARCHULETA: Good afternoon. Fritzie Archuleta, CalPERS team. I am joined today also by Clark Heitkamp who is an actuary for UHAS Health Actuaries, as well as Allen Han who is a Long-Term Care Actuary on the CalPERS team. And I'm sorry -- I apologize. God afternoon, Mr. Chair and members of the Committee. Fritzie Archuleta, CalPERS team.

So I'm here today to present the latest results -- oh, next slide, please.

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DEPUTY CHIEF ACTUARY ARCHULETA: Next slide, please.

I'm here today to present the results of the latest valuation report for the Long-Term Care Program. All information is -- in this report is as of June 30th, 2020. This item is an annual information agenda item, which highlights the key aspects of the long-term care valuation report.

Normally, this report would go to the Board in the spring time frame. However, this program this year underwent a program stabilization effort, which took most of the normal processing time. I will discuss the program -- the details of the program stabilization effort later on in this presentation.

For your convenience, a full copy of the report is available as an attachment to this agenda item and it has much more detail than I am allowed to go over today -- than I am able to go over today. On a side note, we have received many inquiries about the experience of the program beyond 6/30/2020. Since this report was as of 6/30/2020, it only reflects about three months worth of COVID data. The June 30th, 2021 valuation will be produced in the spring of next year and it will -- and it will incorporate much more of the COVID experience, as it covers the time frame where the first and second wave of the COVID pandemic took place.

Next slide, please.

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DEPUTY CHIEF ACTUARY ARCHULETA: Next slide, please.

Thank you. This is the correct slide. I see your chat. Thank you.

Okay. So the margin as of 6/30/2020 is 1.3 percent and the funded ratio for the program is 101 percent. As a reminder, the margin is defined as the excess assets in the Program divided by the present value of future premiums for the program. I like to think of the margin though as a very important measure, because it gives us a general indication of the premium adjustment needed to get the program to be fully funded.

For example, a margin of negative 10 percent would indicate that roughly a 10 percent premium increase would be needed to get the program back to whole. The funded ratio is simply the ratio of the program assets to the program liabilities.

So every year, the actuarial office performs a reconciliation of the margin from one year to the next. During the 19-20 reconciliation, the changes to the margin were categorized into three large buckets. First, there was the program stabilization effort. Second, there was the recognition of the actual fiscal year 19-20 experience. And finally, there was the incorporation of the annual experience study.

Next slide, please.

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DEPUTY CHIEF ACTUARY ARCHULETA: So this slide -- this slide reconciles the margin from one year to the next. Let me just take a step back and explain how this slide works. The first line it has the final 2019 result margin of negative 85.5 percent and the funded ratio of 69 percent. If you go down about three lines, you'll see the row that says discount rate change.

Now, I will discuss the discount rate change in detail in just a minute. But just for exercise purposes, the discount rate change improves the margin by 29.1 percent. And so you add negative 85.5 percent to the 29.1 percent and you'll wind up with a resulting margin of negative 54 -- 56.4 percent, and you'll see that the funded status improved from 69 percent to 78 percent. So that's how the table works.

So now the details. From June 30th, 20 -- the 2019 final result, the resulting margin was negative 85.5 percent, which would indicate that a substantial premium increase was needed to get the program back to a hundred percent funded. In an effort to mitigate the risk in the program, CalPERS created a cross-divisional team to help stabilize -- to help stabilize the program.

And we collaborated on a program stabilization effort. The first part of the program stabilization effort was a review and a reset of the asset allocation of the Long-Term Care Fund.

A new asset allocation was adopted earlier this year. And the move corresponded to a discount rate of 4.75 percent. This change improved the mar -- improved the discount rate from the expected four percent to a 4.75 percent, which was an increase of 75 basis points. And this move improved the margin by 29.1 percent.

The second part of the program stabilization effort was an across the board premium increase first in 2021 of 52 percent and in 2022 an increase of up to 25 percent. The premium increase for the two years improved the margin by 61.2 percent. I just want to take a step back here and say that for the purposes of calculations in this table, even though the second year increase is up to 25 percent, our calculations for this table, we assumed the 25 percent increase.

So if a 25 percent increase does not end up happening, and something less than 25 percent comes through, that rate increase, that change to the margin will not quite be 61.2 percent. It just depends on how high the second year rate increase is.

So after it was all said and done, the program stabilization effort took the margin from a negative 85.5 percent to a positive 4.8 percent and it took the funded status from 69 percent to a positive 104 percent.

Next, the Actuarial Office reviewed the program experience during the fiscal year 19-20 and compared it to what was projected by our assumption. The experience during the 19-20 fiscal year was slightly favorable for the program. First off, a refresh of the demographic data from 6/30/2019 to 6/30/2020 improved the margin by 2.1 percent. This was predominantly due to the fact that more policies lapsed than what we anticipated and to the fact that the number of actual new claims were lower than projected.

Next, we took the cash flow for the Long-Term Care Fund and broke it out into two pieces. First was the non-investment cash flow. This is the cash flow in and out of the program due to premiums as well as claims. We found that on the aggregate, the amount of claims paid out was more than what we anticipated. This is the reason for the change to the margin of negative 0.1 percent.

Finally, the investment return for the 19-20 fiscal year was 4.7 percent. As a reminder, we expected four percent, so there was a slight gain there. And it increased the margin to point -- by 0.9 percent. So over all, the experience, the actual experience for the 2019-2020 fiscal year improved the margin from 4.8 percent to 7.7 percent, and increased the funded status of the program from 104 percent to 107 percent.

I do want to note that the investment return for the 19-20 fiscal year was 4.7 percent. This is not to be confused with the 13 percent that you heard reported to you at the Board off-site. The 13 percent return corresponded to the 20-21 fiscal year and will be reflected in next year's valuation, which will be produced in the spring of next year.

Okay. So finally, as part of the annual

valuation process, the Actuarial Office reviews and revises the actuarial assumptions in the valuation, if needed. This review is necessary to continue to improve our actuarial model and ensure that the assumptions about the future are still relevant to the program.

To ensure the validity or our review, CalPERS contracts with an external consulting firm to do a parallel review. This year, UHAS Health Actuaries provided the parallel view -- review of our assumptions. After our study, we found that two major assumptions were needed to be updated this year, the claims utilization rate assumption and the morbidity improvement assumption.

The claims utilization rate assumption models the percentage of maximum benefit allowance used by claimant. The data shows that each year there was a small increase in the average utilization by claimant due to the cost of care inflation.

Also, the data suggested that this increase would be continuing in the future. Given that data, we increased the likelihood of -- we increased the utilization -- claim utilization rate. And the increase to this claims utilization rate, reduced the margin by 7.2 percent. The morbidity improvement assumption models the anticipated reductions in the claim incidence over time. In recent years, there has not been consistent industry-wide evidence or direct data to support that an improvement trend would continue.

Given this background, the morbidity improvement assumption was reduced and the reduction to this assumption corresponded to a reduction in the margin of 1.1 percent. There were a number of other actuarial assumptions that were refined this year, but on their own did not have a significant impact on the margin. So we lumped them together in other assumption updates.

Those updates altogether improve the margin by 1.9 percent. Overall, adjustments to the actuarial assumptions reduced the margin from 7.7 percent to 1.3 percent and reduced the funded ratio of the program from 107 percent to 101 percent.

I want to reiterate that the table -- this table reconciles the data from the program from June 30th, 2019 to June 30th, 2020. Any experience after the 6/30/2020 date is not reflected in the numbers that were reported.

As a reminder the June 30th, 2021 valuation will be presented to the Board next spring. This concludes my presentation and I will now open it to any questions.

COMMITTEE SECRETARY HOPPER: Mr. Chair, you're on mute.

CHAIRPERSON MILLER: I'm not seeing any questions in chat or anyone indicating they have a question, so thank you for the presentation.

CHIEF FINANCIAL OFFICER COHEN: I think President Jones.

CHAIRPERSON MILLER: Oh, there's -- there's -- oh, Henry is --

COMMITTEE MEMBER JONES: I don't know. It's showing up on mine -- showing up on mine again. So something -- I don't -- maybe it's just my system with this chat box, but it shows that I have a question. But anyway, as we go forward, hopefully we can get that fixed.

CHAIRPERSON MILLER: Yeah, go ahead.

COMMITTEE MEMBER JONES: Yeah. Okay. Thanks Ms. Archuleta. Thank you for the presentation. And while you explained part of the problem I was having at first, but I did talk to Michael and he explained to me, you know, what had happened. But this report covers the year 20 -- 19 -- 2019-2020, but the rate increases that you reflect here is for 20-21 and 21-22. So -- because when I first looked, I said how -- why do we need to raise the rates if we have a margin of error of 1.3? And that was my question. But he said but it includes the projected rate increase in these numbers.

So perhaps going forward, you could just put an asterisk by your rate increase and say this is for the coming year, because I was having a problem -- I'm trying to understand why would we be increasing it, if this is going to be 1.3 now, okay? So thank you for the presentation.

DEPUTY CHIEF ACTUARY ARCHULETA: Thank you.

Yes. Thank you. Yeah, and you're absolutely correct. The margin of 1.3 is inclusive of the fact that we have increased the premiums. And the margin would be much less. It would be a negative number if we did not include the premium increases.

CHAIRPERSON MILLER: Yeah.

DEPUTY CHIEF ACTUARY ARCHULETA: So you're correct. Thank you.

CHAIRPERSON MILLER: Okay. Well, thank you and the team for the presentation. I do have an indication that we have public comments on this item, 7b. So Mr. Fox.

STAKEHOLDER RELATIONS CHIEF FOX: Yes, Mr. Chairman. We have two callers. The first, Larry Woodson from CSR.

MR. WOODSON: Good afternoon. Larry Woodson California State Retirees. Can you hear me okay?

CHAIRPERSON MILLER: Yes, sir, we can.

MR. WOODSON: Okay. Thank you. Chairman Miller, thank you for the opportunity to comment. And I did request a little extra time, if you're so inclined to grant it. Appreciate it.

I read the 2020 actuarial valuation and have these comments. While the report is very thorough and I respect the work of the actuaries, especially projecting into 60 years off in some cases, it's based on data that is, in this case, one year and three months old, as it's being presented to you, the Board. And even a springtime presentation, it would be nine to 10 months old, which is too outdated. It can be remedied.

The contract with LTCG only requires reporting once every six months. Critical data like mortality, lapse rate, number of claims, which are available in some cases within days and certainly monthly go unreported for months. And in the case of this report, there's a good possibility that more current data would have reduced the need for such huge premiums. By the way, the lowering the discount rate from five and a quarter down to 4.75 may have improved the margin, but it also increased our premiums greatly.

On page two of the Agenda Item 7b, it reads, since the inception CalPERS Long-Term Care Program has experienced lower-than-expected investment income. And I understand returns have been historically low, but the last two years returns have both exceeded expectations. 2019 had a return of 7.1 percent, even exceeding the 525 discount rate. And the 2020 -- and I'd like to point out that in the 2020 valuation, Appendix A, page one, it predicts investment earnings for 2021 to be $231.8 million, which is more than double last year's earnings, so -- and then finally looking at total fund assets, probably a more important figure. As of June 30th, the fund increased by 137 million to 4.87 billion. And then I was able to find the current value to date is up to 5.4 billion. That's an increase of 12 percent in the last couple years. So I believe absent the lawsuit, the fund is in better shape than is being characterized.

On page two of the agenda item, there is a statement that quote, "The majority of COVID-19 impacts occurred after June 2020, therefore the impact to the program in this report is minimal". That statement is sort of inconsistent with data reported by commercial insurers. Three major insurers that I found reported up to 30 percent mortality increase in their nursing homes in the second quarter of 2020, and it reduced their costs significantly.

Due to the data delay, CalPERS didn't incorporate that kind of information, and which probably contributed to a higher-than-necessary premium increase. Most carriers report quarterly. And the State of California requires nursing homes deaths re -- be reported within a day. Department of Health has to make that data available within weeks. CalPERS needs to amend their contract to require at least quarterly reporting, if not more frequently.

And then in report -- in the report, I see no distinction of plan costs between skilled nursing and in-home care, which is about half the cost. The trend is clearly in the direction of more in-home care, why is that not addressed? In conclusion, there's ample evidence that a 25 percent increase for 2022 is not needed. And any increase should be delayed until the final settlement of the lawsuit.

Thank you for hearing me.

CHAIRPERSON MILLER: Okay. Thank you, Mr. Woodson.

Mr. Fox, our next caller.

STAKEHOLDER RELATIONS CHIEF FOX: Yes, Mr. Chair. The next caller is Mr. Tim Behrens, California State Retirees.

MR. BEHRENS: Kelly, can you hear me?

Hello.

CHAIRPERSON MILLER: Yes, sir, we can. Go ahead.

MR. BEHRENS: Okay. Good afternoon. I'm Tim Behrens, the President of the California State Retirees. Thank you, Chairman Miller, for the opportunity to comment.

CSR believes the 2020 valuation report, as Larry indicated, is very thorough. It is still lacking due to data lag and reporting from the LTCG. We are informed by staff that they are only required to report every six months. We, of course, would like to see this done every quarter, so the Board could make a better informed decision before raising the cost of the plan.

We also believe there is ample evidence, or at least significant uncertainty about the status of the LTC fund, that there should be no premium increases for 2022 or at a minimum delayed until more recent data can be incorporated into actuarial projections and a final decision on the preliminary settlement on the class action lawsuit being made.

Thank you. Stay safe.

CHAIRPERSON MILLER: Thank you.

Does that conclude our public commenters, Mr. Fox?

STAKEHOLDER RELATIONS CHIEF FOX: Mr. Chairman, yes, that concludes public comment.

CHAIRPERSON MILLER: Okay. On to 7C, Review of PERF Actuarial Assumptions. Mr. Cohen, do we have Mr. Terando and his team?

CHIEF FINANCIAL OFFICER COHEN: Correct.

COMMITTEE MEMBER JONES: I think Ms. Brown has a comment, Mr. Chair.

CHAIRPERSON MILLER: Oh. Oh, I see that. Okay. Let's go back. Ms. Brown, comment.

We can't hear you. It looks like you're unmuted, but --

BOARD MEMBER BROWN: One more second.

CHAIRPERSON MILLER: There we go. We can hear you now.

BOARD MEMBER BROWN: Thank you. I apologize. I was switching ear pieces, because my other one has died.

Thank you for the ability to comment. I want to thank Mr. Woodson and Mr. Behrens for their comment. And I would like to ask the Committee to consider doing quarterly updates for long-term care. I'm sure, Mr. Miller, you have received a lot of comments and concerns about what's going on with the Long-Term Care Program and just the amount of pressure and distress we've put a lot of our policyholders under.

And I'm hoping that CalPERS can take this extraordinary step to not just do these annual updates on the Long-Term Care Program. And, in fact, we could in fact make an exception to help out our long-term care members and get current data and do the report again. I know it's a lot of work, but, you know, these long-term care policyholders, over a hundred thousand of them, are in trouble. And I'd like us to see if this Committee wouldn't ask staff to come back and tell us, you know, what it would take to do updates more than once a year, potential quarterly to help out our policyholders.

Thank you.

CHAIRPERSON MILLER: Thank you, Ms. Brown.

I don't see any other comments on this, so we will go to 7c, Review of PERF Actuarial Assumptions. And I believe it's Mr. Terando. You have the floor.

(Thereupon a slide presentation.)

CHIEF ACTUARY TERANDO: Thank you, Mr. Chair. Scott Terando, CalPERS Chief Actuary.

This item is part of the ALM process. And it is a continuation of the presentation yesterday. During the Investment Committee yesterday, we talked about the capital market assumptions, the asset allocations, and pretty much covered a lot of information on the asset side. Today, we're going to be moving to the liability side and we're going to be going over the experience study results that the actuarial office performed. We're going to go over -- we're going to cover -- sure. We're going to cover the -- both the economic and the demographic assumption changes that we're proposing and kind of measure and -- and let -- kind of gauge how much impact it would have on the various plans.

At this time, I'll pass it along to Randy Dziubek who will step through our presentation and fill you in on the details.

DEPUTY CHIEF ACTUARY DZIUBEK: Thank you, Scott.

Good afternoon, Mr. Chair, Committee members. Ran Dziubek, CalPERS Actuarial team.

Next slide, please.

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DEPUTY CHIEF ACTUARY DZIUBEK: As Scott said, I will be discussing the results of our actuarial experience study and evaluation of all the actuarial assumptions that CalPERS uses to perform actuarial valuations.

The purpose of the study is to collect the data over the period of time since the previous study and use that information to inform us as to whether any of the actuarial assumptions should be modified for future valuations.

As Scott said, normally, as part of an experience study, you would hear discussion about the investment return, which is for our purposes also the discount rate assumption. We have chosen, as an organization, to have that discussion separately as part of the ALM process, and with the Investment Committee. The Committee heard some good presentations yesterday with regard to the investment return, potential candidate portfolios, and discount rates. And that will not be part of today's discussion.

However, the outcomes of both processes, the discount rate, as well as other actuarial assumptions, will be implemented simultaneously with the June 30, 2021 actuarial valuations and will therefore impact contribution requirements for fiscal year 2023-24 for our public agencies.

Both of these processes are important for the long-term sustainability of the system. They also allow us to satisfy certain requirements within the State Constitution, State retirement law, as well as actuarial standards of practice.

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DEPUTY CHIEF ACTUARY DZIUBEK: So the assumptions that we're talking about today can be broken down into a couple different categories, and that would be economic assumptions, as well as demographic assumptions.

I understand the slides are moving a little bit slowly. I don't see slide three on my screen, which is what I'm speaking to. I don't know if it will eventually appear, but I will keep talking.

The economic assumptions -- there we go. The economic assumptions that we will be discussing today are price inflation, wage inflation, payroll growth, and investment return, although very little commentary on investment return. The demographic assumptions have to do more with how our members behave in terms of when they retire, whether they'll become disabled, rates of termination, rates of mortality and so on. We use the experience of the membership to a great degree for setting demographic assumptions, particularly experienced within the last four years. That's a very good indicator for us as to how to set assumptions going forward.

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DEPUTY CHIEF ACTUARY DZIUBEK: So just some general commentary with regard to COVID-19. Of course, the pandemic has had significant implications to our agencies, our state, and on certain CalPERS items of experience. We have seen a slightly higher level of debts during the pandemic. We've seen some changes to patterns of retirement. Anthony Suine has talked about those in some of his presentations to the Board. But for purposes of this study, it's important to note that the data that we used for the experience study only runs through June 30, 2019. So the data does not really reflect any impact from the pandemic, but that isn't necessarily a bad thing, because if you think of what we're trying to do here.

We're tying to set long-term assumptions to be used in future actuarial valuations.

And at this time, we have no evidence that would suggest that the pandemic will have a lasting impact on the experience of our system. And so for that reason, the data that we've used excludes impacts of COVID and the assumptions that we will be recommending as a result of the study have not been adjusted in any way, you know, due to the impacts of COVID-19.

Now, perhaps as we move forward year by year, we will see that certain behaviors have been impacted, at which point, once that evidence presents itself, we will take that into account.

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DEPUTY CHIEF ACTUARY DZIUBEK: So moving ahead into the economic assumptions. The only change that we are recommending with regard to economic assumptions is a decrease in the price inflation assumption from 2.5 percent to 2.25 percent. The other two assumptions noted on the slide are wage inflation and payroll growth. We are not recommending changes to those assumptions at this time. The basis for the recommendation to reduce price inflation is really coming from significant information that we've accumulated from economists, from investment professionals, the Social Security trustees report. Much of this is discussed, by the way, within the draft report, which is an attachment to this item. If you're looking for more information on any of these assumptions, I encourage you to read through the report.

So after collecting this information and understanding as actuaries how this assumption affects our valuations -- and by the way, one of the impacts of this assumption would be to project future cost of living increases. So based on the information available to us, we are recommending a decrease from 2.5 to 2.25. And this is also consistent with the assumption that the Investment Office arrived at for purposes of their portfolio analysis, which was communicated yesterday in the Investment Committee at 2.3.

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DEPUTY CHIEF ACTUARY DZIUBEK: Long term expected return on assets, again, that's not part of this study. I'll just make a couple of quick comments here that the first step in selecting that assumption will be for the Board to select the asset allocation, at which time, the discount rate is generally pre-determined based on that allocation, and on the capital market assumptions already adopted by the Board.

But I will mention that that assumption is not completely independent of the economic assumptions that we are talking about in this presentation. For example, you know, our assumption for price inflation needs to be consistent with the built-in price inflation assumption in the analysis of the portfolios. And again, as we discussed, our assumption of 2.25 is consistent with the 2.3 assumption used by the Investment Office.

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DEPUTY CHIEF ACTUARY DZIUBEK: So moving on into the demographic assumptions. I'll make a general statement at the beginning here that when we performed this analysis and this is a lot of data that we're combing through for this study, as you can imagine, four years worth of data from our very large population. What we saw for many of the groups and with regard to many of the assumptions, was that the experience was fairly consistent with our assumptions, meaning that even in cases where we're recommending minor changes to these assumptions, they are not changes that will translate into significant employer or member contribution changes.

And so the idea with this presentation was to point out areas where the experience did deviate a little bit more so from the assumptions and where the recommended assumptions will have somewhat of a material impact on required contributions going forward.

So starting with service retirement, and this is the assumption that projects when people will retire, at what age. What we saw in this regard was some groups had more retirements than expected, some had fewer. The areas where we saw the greatest deviation was for some groups that had more retirements than expected, in particular the California Highway Patrol group, and some of the public agency safety groups. And for those we are recommending higher rates of retirement, which generally translates into higher employer costs. And in this case, we are expecting these changes to translate to about a one percent of pay increase for the California Highway Patrol plan.

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DEPUTY CHIEF ACTUARY DZIUBEK: The next assumption we want to talk about is the merit and seniority pay increase assumption. Now, we mentioned wage inflation on a previous slide. Wage inflation is a portion of the total pay increase that a member receives in a given year, and the remaining portion of that pay increase, we refer to as the merit and seniority increase. And so we make a separate assumption for that piece of the pay increase. And consistent with the retirement assumption, we saw a few groups that received higher increases over the last four years than our actuarial assumptions predicted.

Again, the CHP was one of those groups. Many of the safety groups and also the State miscellaneous group all experienced slightly higher pay increases than our assumptions would have predicted. And so for that reason, we are recommending slightly higher assumptions going forward. The CHP will experience the largest change in their required contribution, as a result of this, roughly between two and three percent of payroll. Some of the other safety groups and State miscellaneous should be closer to one percent of pay.

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DEPUTY CHIEF ACTUARY DZIUBEK: So I know it's late in the day, and in the interests of time, with regard to the next two assumptions, which are termination of employment and disability retirement, I would like to suggest that we not spend a lot of time talking about those. In both cases, the actual experience lined up fairly well with our actuarial assumptions. We are making minor recommended changes to the assumptions, which will not have a significant impact on employer or employee rates.

Again, for much more information on either of those, feel free to look at the attached report or at the end of this presentation, I'd be happy to take questions on either of these as well.

But with that, I'd like to just move to the mortality assumptions slide.

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DEPUTY CHIEF ACTUARY DZIUBEK: Mortality, other than the discount rate, always seems to be the assumption that gets the most attention. I think the reason for that goes back, you know, a decade or so ago when whenever an actuary would relook at mortality experience, they would measure improvements since the last study, and the proposed new mortality rates would sometimes have a large impact on employer contribution rates.

Luckily, about 10 years or so go ago, actuaries realized that we're seeing improvements to these rates every time we do a study. Why don't we assume that mortality will continue to improve going forward and just build that into our rates.

And so CalPERS did that in 2013. Most systems now will use some type of expected improvement in their mortality assumption. So the result of that is that we don't expect to see the same level of impact on new mortality rates from study to study.

Now, we are though recommending a couple structural changes to our mortality assumptions. The first is how we are proposing to recognize these expected improvements. Our current assumption is estimating 15 years worth of improvement from where we are today and putting that all into the current mortality rates, as if we were 15 years in the future and mortality was that much better, because of those improvements.

Our recommended approach going forward is to recognize those expected improvements one year at a time, which is much more in line with how that will actually occur in the future. We needed a software enhancement to be able to handle that type of process. We have that now and we're able to use this method, which we refer to as generational mortality. And so that's one of our recommendations.

The second recommendation has to do with the fact that it's a fairly recognized fact that more affluent folks in society have lower rates of mortality than those who are less affluent.

And so if our mortality rates are predicting the right number of deaths in a particular year, they may not be predicting the right number of deaths, the right people that might die during the year.

In other words, you know, what the data shows is that we're getting higher rates of death among those that are less affluent than the more affluent folks. Now we don't have a lot of information about individual wealth of our -- of our retires, but we do know their pay and their retirement benefit. And so we believe that looking at the retirement benefit is a good indication of wealth and a good predictor of the fact that they are likely to have lower mortality than those with smaller benefits.

And so we are recommending a process known as benefited-weighted mortality, where we recognize that phenomenon and we think we will get better results going forward with that approach. Now, all of these changes to the mortality assumption combined are resulting in contribution increases that we expect to be under one percent for the most part, maybe approaching one percent in some cases.

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DEPUTY CHIEF ACTUARY DZIUBEK: So just to drill down on the mortality assumption a little bit more. This particular chart is showing us life expectancy for males and females at every point in time where a new mortality study was conducted at CalPERS, so going back to 1994 and through the current study, which we're presenting today.

And you can see general improvements for both males and females, but I think you can also see that the largest improvements tended to happen in the earlier years when we were not reflecting expected improvements in mortality rates.

If you look at the last three sets of results, since we implemented mortality improvement, we're not seeing the same level of changes from study to study, which is the goal obviously. I think the one exception might be for males we seeing an increase from 29.3 years life expectancy to 30 years. And this is for a 55-year old, by the way, if I didn't mention that. So that's a 0.7 year increase. But that is probably more due to using the benefit-weighted mortality rates than any real improvement in mortality for those 55-year olds.

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DEPUTY CHIEF ACTUARY DZIUBEK: So this chart just gives us a little bit more information about the impact of the proposed mortality rates. What we're showing here again is life expectancy, but now we're including members at different ages. We're just looking at the current rates -- mortality rates versus the proposed rates. And what you can see for both males and females, particularly at younger ages, you're seeing a little bit of an increase from the current rates to the proposed rates. Where you do see a little bit of a decrease is with the older members, particularly at age 70. And that is really a function of the expectation that 70-year olds are not living as long as we thought in the previous study. That has more to do with how we will be reflecting future mortality improvements in our mortality assumption.

In the past, as we discussed, we would take 15 years worth of improvement and build that right into the current rates for those 70-year olds. And in reality, a 70-year old has less of a chance, I guess, of seeing 15 years worth of mortality improvements than the younger folks. And so that change in how we're reflecting future mortality improvements is what's causing that small decrease in life expectancy at those ages.

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DEPUTY CHIEF ACTUARY DZIUBEK: So on the previous slides, we tended to focus on the impact of these proposed assumptions on employer contributions. Of course, as we all know, there's a large portion of our population that we refer to normally as PEPRA members, those hired after January 1st, 2013 that are required to share the normal cost of the plan 50 percent with the employer. And so changes that we are proposing for these assumptions will likely have impacts on the normal cost for these plans, and therefore have the potential of resulting in increased member contributions.

Now, the range that we show on this slide for our PEPRA membership is an impact of 0.1 to 1.3 percent increases to plan normal costs for these PEPRA groups. The PEPRA rules require that the normal cost changes by at least one percent before any changes made to the member contributions.

So because some of these groups on the high side will experience a one percent or slightly more change, we do expect these assumption changes to result in some increases to member contributions. Now, it's important to note, first, that what we're talking about here are the impacts of the assumption changes excluding the discount rate. Remember, the discount rate is a separate topic. We don't know what the discount rate will be, so the 0.1 to 1.3 percent that you see here is based on the seven percent discount rate that was used in the last valuation.

If there is a discount rate change to perhaps 6.75, maybe 6.50, I understand was a portfolio that was asked for by the Investment Committee, that would increase the range of impact of all of the assumptions together. And with a 6.75 quarter percent discount rate, the range, instead of 0.1 to 1.3 is more like one percent to 2.9

percent.

And so these changes we're talking about combined, with the potential discount rate change to 6.75 is likely to result in increases to member rates in most of our groups, and in some cases perhaps a percent or a percent and a half even.

It's very difficult to estimate group by group who will get these increases. There's a lot of factors that go into this. This calculation will be done on a plan-by-plan basis with the June 30, 2021 valuations. Even just changes in the membership of a population will change the normal cost that we determine in the next valuation. Those are completely unpredictable, but I think there's enough evidence that we see here to suggest that even without a discount rate change, we are -- we're likely to see some member groups with contribution increases and with the discount rate change of 6.75, certainly if we moved on to 6.50, it appears that most of our PEPRA members would receive increases to the member rates.

The other -- the last comment I want to make is that the plans on the higher side of this range tend to be the safety plans, whose normal costs are higher than miscellaneous plans in general. And so they are -- they are the groups likely to see the biggest increases in member rates.

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DEPUTY CHIEF ACTUARY DZIUBEK: So as far as next steps, this is an information item. The report that's attached is a draft report. We are asking you to take a look at these assumption changes, consider them. We will bring them back in November for a final reading and a vote of approval, at which time we will also presumably be getting a decision on the discount rate through the ALM process. And then as I said earlier, all of these changes, if adopted, will affect the June 30, 2021 valuations.

And with that, I'm happy to take any questions.

CHAIRPERSON MILLER: Okay. Thank you for the presentation. And we do have a first question from Ms. Taylor about page 14. Ms. Taylor, you have the floor.

VICE CHAIRPERSON TAYLOR: Thank you very much. So you said that the PEPRA rate for the employees will go up most likely if the 6.5 percent increase -- or decrease in the discount rate is adopted. Does that also include an increase for employers?

DEPUTY CHIEF ACTUARY DZIUBEK: Yes, absolutely. And, you know, my understanding from listening in on the committees yesterday was that they were interested in seeing 6.75 and 6.50. So it appears that those will be the discount rates being decided between.

VICE CHAIRPERSON TAYLOR: 6.8 and 6.50. I think it's 6.75 was one of them that ends up with a discount rate of 6.8, but, yeah.

DEPUTY CHIEF ACTUARY DZIUBEK: Yes. It's confusing. The Investment Office has their own expectation of return and then -- or he comes in and says but this is the discount rate we'll use. Usually, they're very close, but it gets a little -- it gets a little muddled.

Yeah, a decrease in the discount rate to either 6.8 or 6.75, 6.5 definitely comes along with additional costs to the employers. That is not captured anywhere in my presentation today. I was part of Scott's discussion yesterday. He had a couple slides of projected contribution rates under different discount rates. Now, 6.50 was not a candidate portfolio that we modeled for yesterday's meeting. But there were slides in that presentation that indicated projected contribution rates employer rates under the different discount rates that are on the table.

VICE CHAIRPERSON TAYLOR: And the 6 -- I thought because -- we bought down the rate to 6.8, so that -- that's not going to cost the employers any more.

DEPUTY CHIEF ACTUARY DZIUBEK: Well, right, and that's also confusing. Unfortunately, that the Risk Mitigation Policy necessitated a decrease in the seven percent discount rate to 6.8. Now, the meaning of that though is it's really just a discount rate on paper, right? It's not been used for any actuarial valuation. It's not been used to determine any option factors or service purchase factors. It will never be used as a discount rate if the Board adopts something different than 6.8 as a result of this ALM process.

So really the last discount rate that was used to determine employer contributions was seven percent. If we end at 6.8, 6.75, or 6.5, we are expecting cost increases from what I would say are the most recent projections of employer costs that are basically done at seven percent, which is the discount rate that was used in the 2020 valuations.

I know that's confusing. And some of the webinars that we had for risk mitigation did speak to the cost impacts of the 6.8 discount rate. But again, those are -- those are sort of hypothetical, in that it's likely that we won't end up at 6.8. It will be 6.75 or maybe 6.5. I hope that somewhat answered your question.

VICE CHAIRPERSON TAYLOR: So I don't think anybody is going to want to go down to 6.5, if you're saying that 6.8 will also cost everyone a little more money. And you're of the 6.8, this is what is the PEPRA costs. And so we probably won't have that many employees impacted. However, we probably will have employers impacted.

DEPUTY CHIEF ACTUARY DZIUBEK: Well, so the numbers on this slide in the higher row that shows 0.1 to 1.3, those represent the impacts of all assumptions, except the discount rate. And that actually still reflects the seven percent discount rate, not the 6.8.

And so those assumptions alone have the potential of increasing member rates for some of the groups on the high end of that range. If we -- if we then decrease the discount rate to either 6.8, 6.75, 6.5, that range grows to something larger. And I would expect in November, because we have fewer portfolios to work with, we can have more information on the combined effect of discount rate versus other assumptions on these PEPRA member rates.

But again, going back to something I said earlier, at a 6.75 discount rate, which is very close to 6.8, so not much of a difference there, that range goes to more like one percent to just under three percent. So that's a more likely range of impact on the normal costs. And, of course, the member then would pick up half of that through 50 percent cost sharing. So for those at the higher end where the impact is three percent, that could mean a 1.50 percent change to the member rate, in that case, for those probably safety plans toward the higher end of this range.

VICE CHAIRPERSON TAYLOR: Okay. Thank you.

CHAIRPERSON MILLER: Okay. Thank you.

Next, I have Mr. Rubalcava. You have the floor, sir.

COMMITTEE MEMBER RUBALCAVA: Thank you. Thank you very much for the presentation. I had a couple -- one or two comments -- a comment and then some questions.

First, I was very -- I appreciated the discussion on the -- on the mortality assumption. We need the generation mortality. I actually enjoyed the -- I've heard it defined differently, generation mortality. So I think I appreciate your -- it makes it easier to understand.

And I also appreciate how you were able to incorporate the -- the benefit-weighted data. I know I've been -- I've been following other actuarial valuations, '37 Act, and they all try to customize to their population, but I don't think they do it as well as you folks have done, because you combined to their methodology and actual data based on this benefit-weighted. And I appreciated that, because it's something that I think a lot of systems perhaps don't recognize that just because mortality is improving for it, it improves unevenly. And depending -- you used it based on the -- on what the benefit level is, which I think also corresponds to what we've always said that it matters what the classification you are and where you live, you know, so by the freeway versus some suburb. So I appreciate you doing that.

I had a couple questions. Since Ms. Taylor started on the -- on the normal costs, I'll start with that one. On Attachment 2, you have the chart under -- looking at the public agencies, page one of two, Attachment 2, I just want to make sure I'm reading it right. When you talk about total normal cost, it's total. So for the -- for determining the PEPRA rates for employer and/or the member, it will be half of that increase, correct, that's how we read it?

DEPUTY CHIEF ACTUARY DZIUBEK: Yeah. So you're on page two of Attachment 2?

COMMITTEE MEMBER RUBALCAVA: Correct.

DEPUTY CHIEF ACTUARY DZIUBEK: We are providing the estimated change in the total normal cost for these different PEPRA groups. And you are correct then, the member in theory shares half of that. Although, there's a lot of specific rules about when the rate actually changes or not that have to be met. Bet, yes, in general, the member would be subject to paying half of this increase for these groups. That's correct.

COMMITTEE MEMBER RUBALCAVA: Okay. And then the other question, just in general based on the report and the presentation, the reason the normal cost -- can you explain why the normal costs increase? Is it -- I'm assuming it's -- because it's mostly demographic as opposed to economic changes here, is that correct? Why did it increase?

DEPUTY CHIEF ACTUARY DZIUBEK: Yeah, so, you know, the increases are based on the specific recommendations for assumption changes that we're making for all of the assumptions that we've talked about. And there's too many groups and too many assumptions for us to have talked about all of them. As I said, the report that's attached to this item has a lot of information for all the groups and all the different decrements.

But what we -- what we typically saw with our experience is that it was slightly less favorable than the current actuarial assumptions would have predicted. And so in order to bring our assumptions in line with that recent experience, which is a good predictor of future experience, we are proposing changes that will -- that will increase costs to this extent for these groups. Does that make sense?

COMMITTEE MEMBER RUBALCAVA: Yes, it does. And I guess where I'm going will be explain the next question. And let me make a comment first. I'm used to seeing like a sheet of, I don't know if decrements is the right term, for example, for every assumed -- every change in assumed -- assump -- every proposed change in a current assumption, there's always like a plus or negative increment -- decrement or increment on the current assumption rate.

But in your opening remarks and I think I'm still learning, because this is the first asset allocation -- I guess you do it every four years that I've been involved in. It's a little bit divorced. I'm used to it the other way around, where the assumed rate of return comes out of the experience study and then they do the asset allocation. But here it's separated. So can you explain why in CalPERS they do it this -- it's a little bit different, the approach is different? Can that be explained?

DEPUTY CHIEF ACTUARY DZIUBEK: I'll certainly try. I'll do my best and if Scott or someone else wants to chime in. I think what we do at CalPERS with our ALM process, in my experience - and I used to be a consulting actuary that worked with State retirement systems around the country - I think we have a much more comprehensive approach for analyzing candidate portfolios, capital market assumptions, and then corresponding discount rates.

You know, a typical experience study from an actuary is going to have some discussion of the discount rate and make a recommendation. From what I see being done around the country is our ALM process is really expanding that analysis greatly from what you would typically see in an experience study and providing, as you saw yesterday, stochastic analysis where we're running 5,000 simulations of possibilities.

So I think we couldn't do the same justice to that assumption as part of the experience study. It needed its own full process, the ALM process, to do it in the way that we think is most appropriate, and that gives us the best result. But you're right, it is -- it is a little different. Normally, an experience study is going to talk about the investment return. But as I said, I think we have a much more comprehensive process with the ALM process, and -- but it still is an actuarial assumption. It still will be folded into our valuations at the same time as these assumption changes and become part of our full assumption set. I do think there are advantages to this approach though in that it allows us more time, more effort on focusing us on the most important assumption, the most important decisions that the Board makes. That's my opinion. I don't know if anybody else wants to chime in with additional information.

CHIEF ACTUARY TERANDO: I'll just --

COMMITTEE MEMBER RUBALCAVA: Yeah, go ahead.

CHIEF ACTUARY TERANDO: -- add a few words and say that, you know, I agree with what Randy said. Part of the issue you see with other retirement systems is they have one investment firm investing their money and they have an outside actuarial firm doing their actuarial valuations. And so when the actuarial firm does the valuation, they have to kind of coordinate and call the investment firm behind the scenes and make sure that the CMAs lineup and the asset allocation lines up before they make that recommendation on the discount rate. And that's kind of what happens behind the scenes.

You know, as Randy mentioned, our process is a lot more open and a lot more involved and thorough, where we -- where we sit down and the Investment Office goes through various candidate portfolios and risk assessment. And we work in conjunction with them throughout this whole process. And I think that's one advantage of having both the investment team and the actuarial team, you know, as employees of the retirement system is we can spend a lot of time working together and coordinating the outputs so everything is linked together.

You -- that coordination does happen in other retirement systems. It kind of happens behind the scenes, because actuaries do need to make sure the discount rate is consistent with the asset allocations being used in the CMAs. It's just not as I think a thorough a process that we have at CalPERS.

COMMITTEE MEMBER RUBALCAVA: No. I appreciate -- I appreciate that it is more comprehensive perhaps, but I would disagree that it's -- and I like it that the Actuarial Office is internal, but I was speaking more to -- my experience has been in '37 Act and I don't think they do that where they -- the actuarial -- outside actuary check with the Investment Office on their asset allocation, because my experience has been the actuary thus has worked the Board based on whatever experience and their deliberation makes a decision on the assumed rate of return. And then they have to adopt a new asset allocation to try to hit that bogey so to speak that will match it with the interact. So it's not exactly like that Scott, like you said, that happens in other places.

But I do appreciate -- so I'm trying to understand why it's different. And I think I understand it's a more cumbersome approach. I just need to -- and there's some advantages. So I want to understand that.

And maybe I'll just have some more offline discussion later, but I think for my purposes this is good.

So thank you, Mr. Chair, and thank you, folks. Appreciate it.

DEPUTY CHIEF ACTUARY DZIUBEK: Yeah, I will chime in with one additional point, based on what you just said, that we believe the appropriate way to select a discount rate is first to select asset allocation based on information on risk to the system and that's exactly what our process does. It's showing you multiple portfolios and asking you to decide what level of risk am I comfortable with. Of course, we're going to look at the impacts to contributions that's part of the picture and has to be communicated as well, but it's more of -- the first decision is more of -- an excepted level of risk. And once you have that, then you proceed with setting the discount rate.

But that that's, in our opinions, how it should work as opposed to saying, well, we just want to keep a seven percent discount rate, because we like the contributions that come out of that and then asking investment folks to come up with a portfolio that, at the end of the day, might produce levels of risk that are actually worse for the system if they had been evaluated up front properly. So I like that part of our -- of our process as well.

COMMITTEE MEMBER RUBALCAVA: And I like that answer better.

(Laughter.)

COMMITTEE MEMBER RUBALCAVA: Thank you very much.

CHAIRPERSON MILLER: Thank you.

And next we have Director Middleton.

COMMITTEE MEMBER MIDDLETON: Thank you, Mr. Chair.

This goes back probably a year and a half ago. I asked the question if we were to reduce the discount rate by a quarter point, what would that equate to in terms of increased employer costs?

And obviously there are factors that impact what that's going to be, but the number I was given was approximately 10 percent. Is that, in your estimation, still an accurate number?

DEPUTY CHIEF ACTUARY DZIUBEK: I might bring in our Chief Actuary to help me with this question. I know we've done a lot of modeling recently with these new assumptions under multiple different discount rates. That hasn't been my focus as part of this presentation, since the discount rate was not part of this discussion as much. I know Scott has been reviewing some of those numbers. Scott do you have a feel for the -- you're asking for the change in employer contributions for a 25 basis point drop in the discount rate. Scott, any rule of thumb that you're comfortable giving?

CHIEF ACTUARY TERANDO: I think the 10 percent is a possibly reasonable number. It depends on the situation. I think there's a wide range of impacts. And you could say there's any -- they range anywhere from say -- we would say anywhere from say four percent up to, you know, 10, 12 percent I think a key aspect to consider on employers is the 20 per -- the 21 percent return that we got just recently is going to be bringing a lot of those costs down. You know, we had some earlier talk about, you know, the risk mitigation policy and does it buy it down.

And, you know, dropping the discount rate to 6.8, 6.75, the investment return of 20 percent covers or -- on the employer's side that increase in liabilities dropping that discount rate. So, you know, if we were assuming the seven percent return before and we dropped it to 6.75 percent, and we didn't have a high return on investments, yeah, the 10 percent increase in employer costs might be reasonable. You have to reduce it now, given that we have a large return on the investment side. You cut that -- you know, you could basically eliminate that and cut it in half, and you're looking around possibly half that amount for a quarter percent.

I think Randy talked about -- you know, we talked about the increases for the demographic side. I think normal cost side with a quarter percent and the increases, I think we'd be talking anywhere from, you know, up to two, three percent increase on the employers and a low of maybe one percent. So one to three percent increase on the normal cost side.

The accrued liability with the risk mitigation is pretty much neutral for most plans and then -- and then you would still have a little bit left over of the gain bringing costs down somewhat. If you remember the -- kind of remember those cost projects from yesterday, we talked about the State plan. Remember how costs trended down over five years for the -- dropping the discount rate a quarter percent. And that's kind of what's happening is the cost will slowly work its way down on the employer side. The -- remember, the risk mitigation doesn't offset the normal cost piece. It offsets the unfunded liability. So the employer with the risk mitigation sees a increase on the normal cost side. PEPRA employees would see and increase due to the increase on the normal cost, but the UAL would stay flat or come down, given the 20 percent return that -- 21 percent return we had last year.

COMMITTEE MEMBER MIDDLETON: So I appreciate that there's considerable complexity to this, but as we start talking about reducing the discount rate to 6.75 or even 6.50 percent, the costs that are being passed on are astronomical. And we're going to have to have, moving into November clarity as to exactly what the impact is going to be and be able to define for the employer community what the variables, so that they can make assessments for their individual responsibilities.

But these numbers are -- I can't -- I can't emphasize enough how important of a potential change we are making and we have got to be extremely clear with individuals what those numbers could mean. And I'm asking it now, so that we've got it when we get to November.

CHIEF ACTUARY TERANDO: Yeah, the plan will be to try and present.

COMMITTEE MEMBER MIDDLETON: Right.

CHIEF ACTUARY TERANDO: If you look at what we presented on the demographic side, in terms of breaking down ranges based on the benefit formula, we'll be bringing that back with the dis -- the various discount rates so you can see the particular ranges on -- by plan -- or not by plan, but by, you know, summarized by benefit formula, so people can get a sense of where the impacts are.

And we can -- you know, we had a min and a max, we can probably provide a little bit more detail on the distribution of those costs as well, so you get a better sense, you know of -- you have a min and a max, but, you know, we can provide information on, you know, quartile percentages and median, so you could -- you get a better sense of where the distribution of those increase are.

COMMITTEE MEMBER MIDDLETON: So my last question -- and I certainly understand you want to have solid date and that we're looking at data that effectively, as I understand it, ends June 30 of 2020. But the last year in every other respect, because of COVID, has had enormous impacts. And I think it does beg the question as to what decisions should we be making in the absence of a full -- a full picture of what COVID has done to everything from mortality rates to retirement rates.

DEPUTY CHIEF ACTUARY DZIUBEK: Yeah, that's a -- that's a great point. As we talked about in the presentation, there certainly have been impacts on our system experience during the pandemic. Those will be quantified within our actuarial valuations over the next couple years. We will calculate those as what we call actuarial gains or losses. For example, a higher number of deaths in that period would translate to an actuarial gain for the system, which would slightly lower required contributions going forward.

Retirements, that's harder to predict. They went both ways. You know, some people didn't want to work from home, so they retired. Some people didn't want to come back to work, so they retired. It -- we don't know exactly what we'll see over the next couple years. At this point, I can say the experience that we're seeing isn't indicating -- first of all, we already mentioned, it's not indicating any expected long-term impacts on experience. It's also not really indicating any material change on our valuation results over the next couple years.

I don't have all the facts, but the extra deaths, and also the ages of these extra deaths being as high as they typically are, we really don't expect there to be a significant impact on the valuation results. That's our help any way. But we agree, it's something we need to keep collecting data on and keep getting a better idea of the full picture.

COMMITTEE MEMBER MIDDLETON: I -- we all want to see the data. We've all experienced a million anecdotes over the course of the last year, but it's -- we need to be driven by the data.

Thank you. That's -- that was the end of my questions.

CHAIRPERSON MILLER: Okay. And I'm not seeing anymore questions, and so thank you for the presentation, the work of the team, thoughtful questions, helpful answers.

And that brings us to summary of Committee direction. Mr. Cohen.

CHIEF FINANCIAL OFFICER COHEN: Thank you, Mr. Chair. I did not record any Committee direction, other than obviously bringing back the best information we have on the second reading of the experience study in November.

CHAIRPERSON MILLER: Okay. And I don't see any requests to speak from the public, but I'll just double check with Mr. Fox.

STAKEHOLDER RELATIONS CHIEF FOX: That is correct, Mr. Chair. There are no public comments.

CHAIRPERSON MILLER: Okay. And so with no objections, we are adjourned. And we'll see everyone tomorrow.

VICE CHAIRPERSON TAYLOR: Risk and Audit.

CHAIRPERSON MILLER: Risk and Audit, yep. Is it 9 a.m.?

VICE CHAIRPERSON TAYLOR: No, I think it's tonight.

BOARD MEMBER BROWN: It's today. It's today.

CHAIRPERSON MILLER: Oh, it's today. Oh, my. Sorry, I --

BOARD MEMBER BROWN: It's next.

CHAIRPERSON MILLER: -- didn't notice.

Okay. Well, Risk and --

COMMITTEE MEMBER JONES: Where's the Chair? Where's the Chair?

CHAIRPERSON MILLER: What -- okay. What time Chair Middleton?

COMMITTEE MEMBER MIDDLETON: According to my watch, it's 5:14. Let's take a 10-minute break and let's be really strict about 10 minutes and we will gather together at 5:25.

CHAIRPERSON MILLER: Okay. We'll see you then.

(Thereupon the California Public Employees' Retirement System, Board of Administration, Finance & Administration Committee meeting adjourned at 5:14 p.m.)

CERTIFICATE OF REPORTER

I, JAMES F. PETERS, a Certified Shorthand Reporter of the State of California, do hereby certify:

That I am a disinterested person herein; that the foregoing California Public Employees' Retirement System, Board of Administration, Finance & Administration Committee meeting was reported in shorthand by me, James F. Peters, a Certified Shorthand Reporter of the State of California;

That the said proceedings was taken before me, in shorthand writing, and was thereafter transcribed, under my direction, by computer-assisted transcription.

I further certify that I am not of counsel or attorney for any of the parties to said meeting nor in any way interested in the outcome of said meeting.

IN WITNESS WHEREOF, I have hereunto set my hand this 21st day of September, 2021.

JAMES F. PETERS, CSR
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