Consent

Agenda Item 5f

February 19, 2014

ITEM NAME: Results of Actuarial Valuations for Public Agencies

PROGRAM: Actuarial Office

ITEM TYPE: Information Consent

EXECUTIVE SUMMARY
The Actuarial Office completed the June 30, 2012, Public Agency actuarial valuations in November 2013. These valuations set the employer contribution rates for Fiscal Year 2014-15. Overall, average employer rates increased by about 0.6 percent of payroll for miscellaneous plans and decreased by 0.1 percent of payroll for safety plans. Note that these average rate changes include all public agency plans, including plans which adopted new tiers with lower benefit formulas. Had there been no new tiers with lower benefits adopted by employers, the increase in average employer contribution rates for miscellaneous plans would have been 0.9 percent of payroll while the increase in average employer contribution rates for safety plans would have been 0.8 percent of payroll. The average funded ratio decreased from 74.8 percent to 70.4 percent for miscellaneous plans and from 73.1 percent to 68.7 percent for safety plans.

STRATEGIC PLAN
This item is not a specific product of the Strategic Plan but is part of the regular and ongoing workload of the Actuarial Office.

BACKGROUND
The 2012 valuations were performed to establish the employer contribution rate for 2014-15. Note that these rates do not reflect any cost sharing agreements which employers may have with their employee groups which would serve to lower these reported employer contribution rates. The employer contribution rates for 2014-15 do reflect the impact of the second year of the two-year phase-in (for most plans) of the change in the discount rate assumption in the 2011 valuations and the 0 percent investment return for 2011-12.

The 2012 valuations also include projected employer contribution rates for 2015-16. However these projected rates for FY 2015-16 do not include the potential impact of changes to the actuarial assumptions that the Board is considering.

On January 1, 2013, the Public Employees' Pension Reform Act of 2013 (PEPRA) took effect. The impact of most of the PEPRA changes will first show up in the rates and the benefit provision listings of the June 30, 2013, valuation, which sets the 2015-16 contribution rates. The anticipated reduction in employer contribution rates due to PEPRA is expected to take several years to materialize.

ANALYSIS

The Actuarial Office completed the June 30, 2012, Public Agency actuarial valuations in November 2013. These valuations set the employer contribution rates for Fiscal Year 2014-15. On April 17, 2013, the CalPERS Board of Administration approved a recommendation to change the CalPERS amortization and smoothing policies. Prior to this change, CalPERS employed an amortization and smoothing policy, which spread investment returns over a 15-year period while experience gains and losses were amortized over a rolling 30-year period. Effective with the June 30, 2013, valuations, CalPERS will no longer use an actuarial value of assets and will employ an amortization and smoothing policy that will spread rate increases or decreases over a 5-year period, and will amortize all experience gains and losses over a fixed 30-year period.

The new amortization policy will be used for the first time in the June 30, 2013, actuarial valuations. These valuations will be performed in the fall of 2014 and will set employer contribution rates for Fiscal Year 2015-16.

What follows are highlights of the changes in employer rates between fiscal years 2013-14 and 2014-15.

- 13 percent of the plans (268 plans) experienced a decrease in their rate
- 87 percent of the plans (1,782 plans) experienced an increase in their rate
- Less than 1 percent of the plans (2 plans) experienced no change in rate
- 121 plans must pay the plan Normal Cost as a minimum contribution as required by PEPRA. Of these, 27 plans would have had an employer contribution rate of zero percent if not for the PEPRA required minimum.

An additional 362 actuarial valuation reports were distributed for pooled plans with new different level of benefits, new agencies, and inactive plans. These are not included in the metrics that follow.

No plans have a zero rate as a result of the PEPRA requirement that plans contribute at a minimum the plan's normal cost. The PEPRA requirement that a plan must pay at a minimum the plan normal cost also means members must pay the member contribution rate.

PEPRA plans created January 1, 2013, were provided with a rate letter on December 19, 2012, providing the Normal Cost rate and matching Employee rate and are not part of the following analysis.

The distribution of the changes in employer rates is shown in the following table.

Distribution of Changes in Employer Rates Between 2013-14 & 2014-15

Change in Employer Rate as a Percentage of Payroll	Number of Plans	Percent of All Plans
Decrease more than 4%	54	3%
Decrease between 2% and 4%	32	1%
Decrease 0% to 2%	182	9%
No change	2	0%
Increase 0% to 2%	1356	66%
Increase between 2% to 4%	291	14%
Increase more than 4%	135	7%
Total	2,052	100%

As stated above, most plans are experiencing an increase in rate as a result of the impact of the 0 percent return in 2011-12 and the economic assumption change.

The following tables show the distribution of the 2013-14 and the 2014-15 contribution rates for Miscellaneous and Safety plans.

2013-14 Employer Rates

	Miscellaneous Plans		Safety Plans	
	Number of Plans	**Percent of Plans**	**Number of Plans**	**Percent of Plans***
0%	22	2%	0	0%
0-10%	226	16%	2	0%
10-20%	882	61%	54	9%
20-30%	280	19%	280	44%
30-40%	28	2%	214	34%
40+%	4	0%	80	13%
	1,442	100%	630	100%

2014-15 Employer Rates

	Miscellaneous Plans		Safety Plans	
	Number of Plans	**Percent of Plans**	**Number of Plans**	**Percent of Plans***
0%	0	0%	0	0%
0-10%	286	19%	0	0%
10-20%	889	59%	41	6%
20-30%	292	19%	334	49%
30-40%	46	3%	198	29%
40+%	5	0%	109	16%
	1,518	100%	682	100%

* Percentages may not add up to 100% due to rounding

In addition, see Attachment 1 for a breakdown of employer contribution rates for Fiscal Year 2014-15 by benefit formula.

Estimate of 2015-16 Employer Contribution Rates
As in prior years, the actuarial valuation reports include an estimate of the employer contribution rates for the next fiscal year, in this case 2015-16. The estimated rates were calculated based on an estimated 12 percent investment return for Fiscal Year 2012-13.

The estimate for 2015-16 assumes unfunded liability payments will continue to be allocated on and amortized over payroll increasing 3% per year. However, for pooled plans effective January 1, 2013, PEPRA will result in a shift of new members away from existing pools. This is expected to reduce the payroll increases for these pools. As a result, effective with the June 30, 2013, valuation, CalPERS may change its method of allocating pooled plan unfunded liability. As outlined in an agenda item to this committee last December, these potential changes in allocating pooled plan unfunded liability could impact 2015-16 and later rates.

Beginning with the June 30, 2013, valuations that will set the 2015-16 rates, CalPERS will no longer use an actuarial value of assets and will employ an amortization and smoothing policy that will spread rate increases or decreases over a 5-year period, and will employ an amortization and rate smoothing policy that will pay for all gains and losses over a fixed 30-year period with the increases or decreases in the rate spread directly over a 5-year period.

The following tables show the distribution of the estimated 2015-16 contribution rates for Miscellaneous and Safety plans based on the new amortization and smoothing policy.

Estimated 2015-16 Employer Rates

	Miscellaneous		Safety	
	Number of Plans	**Percent Of Plans***	**Number of Plans**	**Percent Of Plans**
0-10%	278	18%	2	0%
10-20%	843	56%	34	5%
20-30%	339	22%	276	40%
30-40%	53	3%	230	34%
40+%	5	0%	140	21%
	1,518	100%	682	100%

* Percentages may not add up to 100% due to rounding

As always, member contributions (whether paid by the employer or the employee) are in addition to the above rates**.**

Below is a table showing the average employer contribution rates for Miscellaneous plans and Safety plans for fiscal years 2013-14, 2014-15 and 2015-16. In addition, see Attachment 2 for a breakdown of the average employer contribution rates for fiscal year 2014-15 by benefit formula.

Average Employer Contribution Rates

	Public Agency Miscellaneous Plans	**Public Agency Safety Plans**
Fiscal Year 2013-14	15.3%	32.0%
Fiscal Year 2014-15	15.9%[1]	31.9%[2]
Fiscal Year 2015-16	16.5%*	33.2%*

[1] The increase in average employer contribution rates for continuing Miscellaneous plans with the same formula was 0.9%.

[2] The increase in average employer contribution rates for continuing Safety plans with the same formula was 0.8%.

* The average projected rates for fiscal year 2015-16 were based on the estimated 12% return used for the valuations and the new amortization policy.

Funded Status
As a result of the 0 percent return for 2011-12, Public Agency plans are less funded as of the June 30, 2012, valuation date than they were on June 30, 2011. In addition**,** Miscellaneous plans tend to be better funded than Safety plans.

We are monitoring the funded status of Public Agency plans using the market value of assets. The funded ratio is equal to the market value of assets divided by the actuarial accrued liability, expressed as a percentage. The funded status on an actuarial value of assets basis is used for rate setting only and is not a true measure of the plan's ability to pay benefits.

The following table shows the average funded ratios on a market value of assets basis for all Miscellaneous and Safety plans.

Funded Ratios on a Market Value Basis

	Miscellaneous Plans	Safety Plans	All Plans
Average Funded Ratio on June 30, 2010	66.3%	64.9%	65.8%
Average Funded Ratio on June 30, 2011	74.8%	73.1%	74.1%
Average Funded Ratio on June 30, 2012	70.4%	68.7%	69.7%

In addition, see Attachment 2 for a breakdown of the average funded status as of June 30, 2012, by benefit formula.

As a result of the approximately 12 percent investment return for Fiscal Year 2012-13, the average funded ratio on June 30, 2013, is estimated to increase by about 3.5 percent for both the Miscellaneous and the Safety plans.

Hypothetical termination liabilities were also included in the valuation reports. The funded ratios on a termination basis generally ranged from approximately 35 percent to 45 percent for Miscellaneous plans and from approximately 30 percent to 40 percent for Safety plans. These were based on the termination discount rate of 2.98 percent which is the yield on the 30-year US Treasury Separate Trading of Registered Interest and Principal of Securities (STRIPS) as of June 30, 2012. As of June 30, 2013, the 30-year STRIPS yield was 3.72 percent.

Risk Analysis

With the goal of being more transparent and providing additional information to all employers to better help them budget for future years, the Actuarial Office includes a risk section in each valuation report that includes an investment return scenario analysis and a discount rate sensitivity analysis.

Investment return scenario analysis can show potential risk to contribution rates by projecting employer rates for 2014-15 using the investment return from the 2012-13 fiscal year and an investment return scenario analysis for the three years following. A scenario analysis was performed to determine the effects of various investment returns during fiscal years 2013-14, 2014-15 and 2015-16 on the 2016-17, 2017-18 and 2018-19 employer rates.

In addition, the Actuarial Office includes a discount rate sensitivity analysis in the annual actuarial valuation reports that look at the 2014-15 employer rates using discount rate scenarios if the Public Employees' Retirement Fund were to realize long-term investment returns of 1 percent lower and 1 percent higher than the current valuation discount rate of 7.50 percent.

BUDGET AND FISCAL IMPACTS

Work to prepare the Public Agency Valuations is part of the core workload and did not impact the budget.

ATTACHMENTS

Attachment 1 – Distribution of Employer Contribution Rates for Fiscal year 2014-15 Broken Down by Benefit Formula

Attachment 2 – Average Employer Contribution Rate by Benefit Formula and Average Funded Status by Benefit Formula

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