



Agenda Item 7b

March 17, 2015

ITEM NAME: Third-Party Parallel Valuation and Certification of the Judges' Retirement System, Judges' Retirement System II, Legislators' Retirement System and 1959 Survivor Benefit Program

PROGRAM: Audits

ITEM TYPE: Action

RECOMMENDATION

Accept the third-party valuations and certifications of the Judges' Retirement System, Judges' Retirement System II, Legislators' Retirement System, and the 1959 Survivor Benefit Program as of June 30, 2013.

EXECUTIVE SUMMARY

The third-party actuarial firm completed its independent reviews of the actuarial valuations for the Judges' Retirement System (JRS), Judges' Retirement System II (JRSII), Legislators' Retirement System (LRS), and the 1959 Survivor Benefit Program. Overall, the reviews found the valuations were computed in accordance with generally accepted actuarial principles, although the actuarial firm noted some non-material issues with a portion of the liability calculation, as detailed below. A representative from the actuarial firm, Cheiron, will be presenting the results of its review. The reports are attached as Attachments 1 through 4 of this agenda item.

STRATEGIC PLAN

This item is not a specific product of the Strategic or Annual Plans but is part of the regular and ongoing workload of the Actuarial Office and the Office of Audit Services.

BACKGROUND

Under Board Resolution ACT-95-05A (Actuarial Policies – General), the Board retains the services of an outside actuarial firm to review the work of the Board's actuarial staff and to certify that such work satisfies actuarial professional standards. The Risk and Audit Committee's Delegation Resolution includes the delegation to approve and oversee actuarial audits and reassurance activities.

The Board selected a third-party actuarial firm (EFI, which later merged with the current firm Cheiron) to perform a series of parallel actuarial valuations and certify the results of the actuarial valuations produced by the Actuarial Office. In the current

segment of the contract, Cheiron performed parallel valuations and certified the JRS, JRS II, LRS and the 1959 Survivor Benefit Program Plans as of June 30, 2013 with results in the attached reports. These activities represent Task 6 of Contract 2009-5377.

ANALYSIS

In summary, Cheiron certified the results as “accurate” and “computed in accordance with generally accepted actuarial principles” for the 1959 Survivor Benefit Program and “reasonable” and “computed in accordance with generally accepted actuarial principles” for JRS, JRS II and LRS. Overall, the costs independently computed by Cheiron are all within 5 percent of the costs calculated by CalPERS actuarial staff. However, in the case of JRS, JRS II and LRS, Cheiron identified non-material problems with a portion of the liability calculation. The findings for each valuation are discussed in further details below.

Independent Review of the Actuarial Valuation for the Judges’ Retirement System

Cheiron’s independent parallel valuation of JRS matched the total actuarial accrued liability calculated by CalPERS’ actuarial staff within 3.76 percent. Cheiron certified that the liabilities and costs computed by CalPERS’ actuarial staff are “reasonable” and “computed in accordance with generally accepted actuarial principles and practices.”

Cheiron found that the valuation results for the present value of benefits and actuarial accrued liability for active members, the present value of benefits for inactive members with a deferred benefit, the employer normal cost, and the actuarial required contribution fell outside the expected tolerance levels. When results fall outside predefined tolerances, further examination is required. Under further analysis, Cheiron found discrepancies relating to usage of benefit multiplier for members that retire after age 60 with at least 20 years of service, calculation of benefit amount for terminated vested members eligible for retirement as of the valuation date, and benefit accrual rates and eligibility criteria for members entitled to DRO benefits. After discussing with CalPERS staff, the programming errors have been fixed and are not expected to impact future valuations.

Two other minor discrepancies were found but have minimal effect on liabilities. First, disability rates are currently set to zero when a member is eligible to retire, but instead should extend past the point that a member becomes eligible to retire. Second, where a retiree has elected a form of payment that allows the balance of their accumulated contributions to be paid to a beneficiary at the time of their death, their liabilities should reflect this possible contingency. These retirees are currently valued as having a single life annuity with no possibility of a contribution refund at death. CalPERS staff intends on making these changes in next year’s annual valuations.

A copy of the parallel valuation report for JRS can be found in Attachment 1.

Independent Review of the Actuarial Valuation for the Judges' Retirement System II

Cheiron's independent parallel valuation of JRS II matched the total actuarial accrued liability calculated by CalPERS' actuarial staff within 0.3 percent. Cheiron certified that the liabilities and costs computed by CalPERS' actuarial staff are "reasonable" and "computed in accordance with generally accepted actuarial principles and practices."

Cheiron pointed out that there were some minor and immaterial differences in member data. The differences were within the scope of normal actuarial practice.

A copy of the parallel valuation report for JRS II can be found in Attachment 2.

Independent Review of the Actuarial Valuation for the Legislators' Retirement System

Cheiron's independent parallel valuation of LRS matched the total actuarial accrued liability calculated by CalPERS' actuarial staff within 0.30 percent. Cheiron certified that the liabilities and costs computed by CalPERS' actuarial staff are "reasonable" and "computed in accordance with generally accepted actuarial principles."

However, Cheiron discovered one area in which the valuation results were not within the acceptable tolerance levels: the Required Employer Contribution. CalPERS and Cheiron's calculations of the unfunded accrued actuarial liability amortization and employer normal cost are in close agreement. However, when added together to calculate the Required Employer Contribution, the small differences caused a material difference. Because the Legislators' Retirement System is well funded, the net employer contribution is relatively small. Accordingly, small differences in the actuarial liability and the normal cost are magnified into large relative changes in the net employer cost.

A copy of the parallel valuation report for LRS can be found in Attachment 3.

Independent Review of the Actuarial Valuation for the 1959 Survivor Benefit Program

Cheiron's independent parallel valuation of the 1959 Survivor Benefit Program matched the total liabilities calculated by CalPERS' staff actuaries within 5 percent and has certified our results as "accurate and complete, and fully compliant with generally accepted actuarial principles and with all standards of practice".

A copy of the parallel valuation report for the 1959 Survivor Program can be found in Attachment 4.

BUDGET AND FISCAL IMPACTS

The fee for this audit was \$28,025. Funding was already identified within existing budgetary resources.

BENEFITS/RISKS

It is essential to periodically review contribution requirements and funding levels to ensure the ongoing financial soundness of a pension system. The actuarial office has divided the retirement plans at CalPERS into three categories: Public agencies, State and Schools, and Affiliates (LRS, JRS, JRS II, and the 1959 Survivor Benefit Program). The Board's current independent actuarial firm, Cheiron, performs one parallel valuation for each of the three categories on a rotating three year cycle. These parallel valuations provide an additional "check and balance" that increases the financial security of the retirement system for its participating members by reducing the risk of undetected errors in actuarial calculations.

ATTACHMENTS

Attachment 1 – Judges' Retirement System Independent Review of the Actuarial Valuation as of June 30, 2013

Attachment 2 – Judges' Retirement System II Independent Review of the Actuarial Valuation as of June 30, 2013

Attachment 3 – Legislators' Retirement System Independent Review of the Actuarial Valuation as of June 30, 2013

Attachment 4 – 1959 Survivor Benefit Program Independent Review of the Actuarial Valuation as of June 30, 2013

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