



Risk and Audit Committee Agenda Item 5a

September 19, 2017

Item Name: Third Party Parallel Valuation and Certification of the Judges' Retirement System, Judges' Retirement System II, Legislators' Retirement System, 1959 Survivor Benefit Program as of June 30, 2016.

Program: Audits

Item Type: Information

Executive Summary

The third-party actuarial firm, Conduent HR Consulting, LLC (Conduent), 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 (SBP) as of June 30, 2016. Overall, Conduent's review indicated that the actuarial process followed by CalPERS staff is thorough, complete, and complies with applicable Actuarial Standards of Practice (ASOP). The actuarial firm noted some non-material issues with a portion of the liability calculation, which are detailed under the Analysis section. The full reports are attached as Attachments 1 through 4 of this agenda item.

Strategic Plan

This agenda item supports Strategic Plan Goal Fund Sustainability – Strengthen the long-term sustainability of the pension fund.

Background

Under the California Constitution, the CalPERS Board of Administration (Board) has plenary authority and fiduciary responsibility to provide for actuarial services. The CalPERS Chief Actuary advises the Board and directs the activities of the CalPERS actuarial staff. The Board also retains the services of an outside actuarial firm to review the work of the CalPERS actuarial staff and to certify that such work complies with actuarial professional standards. The Board's Delegation Resolution RA-17-01 includes the delegation to the Risk and Audit Committee to oversee key internal auditor activities including actuarial parallel valuations.

In November 2015, the Board selected a third-party actuarial firm, Buck Consultants, LLC, which changed its name to Conduent HR Consulting, LLC in 2017, to provide the parallel valuation and certification services to the Board. Conduent has completed the parallel valuations and certification services for JRS, JRS II, LRS and the 1959 SBP Plans as of June 30, 2016. These activities represent the completion of Task 3 of Contract 2015-8123.

The JRS provides benefits to California Supreme and Appellate Court Justices and Superior Court Judges appointed or elected prior to November 9, 1994 while the JRS II provides benefits to the same officials elected or appointed on or after November 9, 1994.

The LRS provides benefits to California Legislators elected to office prior to November 7, 1990, and to constitutional, legislative, and statutory officers elected or appointed prior to January 1, 2013.

The 1959 SBP provides benefits to eligible survivors of CalPERS members who are not covered by Social Security and die prior to retirement.

Analysis

Conduent reviewed the actuarial assumptions and methods used in the JRS, JRS II, LRS, and the 1959 SBP valuations and concluded that the assumptions used are reasonable and the methodology used to select these assumptions is appropriate and consistent with the guidance provided in ASOP 27 and 35. ASOP 27 discusses the selection of economic assumptions for the measurement of pension or retiree group benefits liabilities, and ASOP 35 discusses the selection of demographic assumptions for the measurement of pension or retiree group benefits liabilities.

Conduent also completed parallel actuarial valuations for the JRS, JRS II, LRS, and the 1959 SBP and compared their key results to the key results produced by CalPERS actuarial staff on an aggregate basis. The discrepancies fall within the 5 percent tolerance level specified by CalPERS. Conduent stated that the actuarial process followed by CalPERS staff is thorough, complete, and complies with applicable ASOP.

Although not required by Contract, Conduent also compared the key valuation results on an individual participant level for JRS, JRS II, and LRS. Conduent's additional observations and recommendations are listed below.

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

Conduent found two issues that have non-material impact on the liabilities for CalPERS to address. First, liabilities were not determined correctly for 12 out of 2,125 members due to a problem with the underlying data for the 12 individuals. Second, for separated employees, no mortality assumption (decrement) is being applied in the period prior to retirement for participants who have separated from employment and are entitled to benefits at a future retirement age.

Conduent provided two recommendations for the JRS:

- Add information to the report to meet new ASOP 4 requirements.
- Consider reflecting pre-retirement mortality for all separated participants.

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

Conduent provided three recommendations for CalPERS to include in the JRS II valuation reports to more completely fulfill the new ASOP 4 requirements:

- Add enhanced description of the contribution allocation procedure, including a more detailed description of what the five-year ramp-up and ramp-down in amortizations entail.

- Add a statement regarding the impact of funding policy on future contributions.
- Include more detail information on the rationale for changes in assumptions.

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

Conduent provided one recommendation for inclusion in the LRS valuation report in order to more completely fulfill the new ASOP 4 requirements:

- Add a statement regarding the impact of the funding policy on future contributions.

Independent Review of the Actuarial Valuation for the 1959 SBP

Conduent provided four recommendations for inclusion in the 1959 SBP valuation report in order to more completely fulfill the new ASOP 6 requirements:

- Add an enhanced description of the contribution allocation procedure, including a more detailed description of what the five-year ramp-up and ramp-down in amortizations entail.
- Add a statement regarding the impact of the funding policy on future contributions.
- Add additional comments about the appropriateness of reported measures of the funded status of the plan.
- Add a statement regarding the potential effects of differing returns from assumptions.

Budget and Fiscal Impacts

The fee for the parallel valuation and certification of the 2016 annual valuations for the JRS, JRS II, LRS, and 1959 SBP plans is \$73,000. Funding is identified within existing budgetary resources.

Benefits and 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 (Judges Retirement System, Judges Retirement System II, Legislators' Retirement System, and the 1959 SBP). The Board's current independent actuarial firm, Conduent, 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 – Parallel Valuation and Certification Report Judges' Retirement System Valuation as of June 30, 2016

Attachment 2 – Parallel Valuation and Certification Report Judges' Retirement System II Valuation as of June 30, 2016

Attachment 3 – Parallel Valuation and Certification Report Legislators' Retirement System Valuation as of June 30, 2016

Attachment 4 – Parallel Valuation and Certification Report 1959 Survivor Benefit Program Valuation as of June 30, 2016

BELIZ CHAPPUIE
Chief Auditor
Office of Audit Services

MATTHEW G. JACOBS
General Counsel

SCOTT TERANDO
Chief Actuary