MEETING

STATE OF CALIFORNIA

PUBLIC EMPLOYEES' RETIREMENT SYSTEM

BOARD OF ADMINISTRATION

FINANCE & ADMINISTRATION COMMITTEE

ROBERT F. CARLSON AUDITORIUM

LINCOLN PLAZA NORTH

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SACRAMENTO, CALIFORNIA

TUESDAY, DECEMBER 19, 2017

11:45 A.M.

JAMES F. PETERS, CSR
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APPEARANCES

COMMITTEE MEMBERS:

Mr. Richard Costigan, Chairperson

Ms. Theresa Taylor, Vice Chairperson

Mr. John Chiang, represented by Mr. Matthew Saha

Mr. J.J. Jelincic

Mr. Henry Jones

Mr. Bill Slaton

Ms. Betty Yee, represented by Ms. Lynn Paquin

BOARD MEMBERS:

Mr. Rob Feckner, President

Mr. Michael Bilbrey

Mr. Richard Gillihan, represented by Mr. Danny Brown

Ms. Dana Hollinger

Mr. Ron Lind

Ms. Priya Mathur

STAFF:

Ms. Marcie Frost, Chief Executive Officer

Mr. Charles Asubonten, Chief Financial Officer

Mr. Matthew Jacobs, General Counsel

Ms. Donna Lum, Deputy Executive Officer

Mr. Brad Pacheco, Deputy Executive Officer

Mr. Scott Terando, Chief Actuary

A P P E A R A N C E S   C O N T I N U E D

STAFF:

Mr. Mary Anne Ashley, Chief, Legislative Affairs Division

Ms. Tanya Black, Committee Secretary

Mr. Randy Dziubek, Deputy Chief Actuary

Ms. Jan Falzarano, Chief, Retirement Research and Planning Division

Mr. Matt Flynn, Chief, Chief, Operations, Performance & Technology Division

Mr. Rob Jarzombek, Chief, Health Account Management Division

Mr. Don Martinez

Ms. Arnita Paige, Chief, Pension Contract & Prefunding Program

Mr. Anthony Suine, Chief, Benefit Services Division

ALSO PRESENT:

Ms. Dorothy Johnson, California State Association of Counties

Mr. Derick Lennox, School Employers Association of California

Mr. Jai Sookprasert, California School Employees Association

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I N D E X   C O N T I N U E D

P R O C E E D I N G S

CHAIRPERSON COSTIGAN: All right. Good afternoon. It's 11:45. We're going to call to order the December meeting of the Finance and Administration Committee.

Madam Secretary, please call the roll.

COMMITTEE SECRETARY BLACK: Richard Costigan?

CHAIRPERSON COSTIGAN: Here.

COMMITTEE SECRETARY BLACK: Theresa Taylor?

VICE CHAIRPERSON TAYLOR: Here.

COMMITTEE SECRETARY BLACK: Matthew Saha for John Chiang?

ACTING COMMITTEE MEMBER SAHA: Here.

COMMITTEE SECRETARY BLACK: J.J. Jelincic?

COMMITTEE MEMBER JELINCIC: Here.

COMMITTEE SECRETARY BLACK: Henry Jones?

COMMITTEE MEMBER JONES: Here.

COMMITTEE SECRETARY BLACK: Bill Slaton?

COMMITTEE MEMBER SLATON: Here.

COMMITTEE SECRETARY BLACK: Lynn Paquin for Betty Yee?

ACTING COMMITTEE MEMBER PAQUIN: Here.

CHAIRPERSON COSTIGAN: Great. All Committee members are present.

All right. We're going to start off first with the Executive Report. Charles, please, sir.

CHIEF FINANCIAL OFFICER ASUBONTEN: Good morning, Mr. Chairman and Committee members. Charles Asubonten CalPERS CFO.

Mr. Chairman, before we get started, I want to recognize a member, J.J. Jelincic, on my behalf and behalf of the Financial organization, for all his contributions to this Committee.

On a personal note, as some of you probably know, my first interaction here at CalPERS was at a diversity forum. And the last card I had, business card, I was about to hand it over to Mr. Jelincic. And I mentioned it to him, and he said I think you want to give to the CEO Marcie Frost. That's something that I shall not forget for a very long time.

I want to assure you, Mr. Jelincic, as you leave the Board, that as a fellow CFO -- CFA charter holder, we will uphold the tenets of the professional standards that you've worked very hard to maintain. Thank you.

COMMITTEE MEMBER JELINCIC: Thank you.

CHIEF FINANCIAL OFFICER ASUBONTEN: I'd like to start with an item from the September Committee meeting. The direction from the Committee was to have preliminary discussion with CalHR and consolidation of the Supplemental Income Plans. Team members met with CalHR and we decided to continue discussions outside of consolidations. We will find opportunities to work together to find efficiencies for our members without merging at this time.

Now I move on to the November Committee meeting. There was a request to provide a list of direct authorization vendors and the types of deductions currently made through retiree warrants. And I'm here to report that through Customer Service and the Stakeholder Relations this has already been completed.

The first action item today represents the second reading of the 2017 mid-year budget, and there's no change from the first reading. The proposed budget has a total of approximately 1.7 billion for 2,875 positions, which shows about a 0.6 million or 0.03 percent decrease compared with a 2017/18 annual budget.

At this point, Mr. Chairman, let me report also that the permanent blanket positions staying at 27. This is a substantial improvement, bearing in mind that when we commenced the exercise to work on blanket, it was 335 in 2013. As directed at the last Committee meeting, I will update you on the State Controller's contract, which was brought up during the first budget reading.

This second and third action items today, both legislative proposals one covers the service credit purchase and the other replacement benefit plan updates to the PERL.

Agenda Item 7a will review the review -- will be the review of the actuarial assumptions and a selection of discount rate based on the work completed by Karen. This will require approval of the discount rate based on the candidate portfolio selected yesterday by the Investment Committee to be ratified by the plenary Board.

As part of our quarterly reporting information, we also provide you Agenda Item 8a, status of participating employers. We will provide the benefits reduction information for Niland Sanitary District and Trinity Waterworks District as requested by the Committee in the November meeting.

The last item today will cover the health care administrative expenses providing the Committee an update on recent statutory changes to the Health Care Fund.

The Next Finance and Administration Committee meeting is scheduled for February 13, and would include updates for the employer and employee contribution rates for Judges and Legislators, notice of election for the 2018 State school and public agency member notice of election, review of the Committee Delegation, and a second reading of the amortization policy.

Also, we will be reporting updates on the participating employers annual diversity and the election results for the 2017 CalPERS member-at-large.

Mr. Chair, this concludes my report. And I'll be pleased to take any questions at this time.

CHAIRPERSON COSTIGAN: All right. Thank you.

There are no questions on your report.

Action -- or Item 3 contains 3 action consent items. However, we are going to pull 3b in and 3c, but we're going to immediately move to them.

So, Mr. Jelincic has a concern on item 3b.

COMMITTEE MEMBER JELINCIC: Are we going to do 3a first?

CHAIRPERSON COSTIGAN: Well, I was just going to see if we could end up ultimately with one motion.

Hang on. Push your microphone, please.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: 3b is the semi-annual contracting prospective report. There are contracts in there that I believe State workers are perfectly capable of doing. I believe we are increasing costs needlessly by contracting it out, rather than hiring staff to do it.

Therefore, for the 16th time in my term on the Board, I'm going to be voting no on the semi-annual report.

CHAIRPERSON COSTIGAN: Mr. Jelincic, I appreciate your comments. Actually, as someone who spends lots of time looking at 19130, as you know, unless a contract is challenged by one of the impacted parties, the position that you continued to take I understand, but I don't believe any of these contracts have actually been challenged.

COMMITTEE MEMBER JELINCIC: I don't believe any of them have. That's -- shame on the unions. But I also will point out that we are fiduciaries, and we are spending Trust money that we should not be spending.

CHAIRPERSON COSTIGAN: All right. Thank you, Mr. Jelincic.

All right. So then we will be separating out -- based upon Mr. Jelincic. Before I go to 3c, Ms. Malm. Can I get just a motion on 3a. Any concerns with the November minutes?

COMMITTEE MEMBER SLATON: Move.

COMMITTEE MEMBER JONES: Second.

CHAIRPERSON COSTIGAN: Moved by Slaton, seconded by Jones.

All those in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Motion carries.

All right. On Item 3b, can I get a motion?

COMMITTEE MEMBER SLATON: Move.

CHAIRPERSON COSTIGAN: Moved by Slaton.

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: Seconded by Taylor.

All those in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed

COMMITTEE MEMBER JELINCIC: No. Record me.

CHAIRPERSON COSTIGAN: Record Mr. Jelincic as a no.

All right. And then on Item 3c. Ms. Malm or INVO, Matt.

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: Good morning. Matt Flynn, CalPERS team member.

There was an administrative oversight on Item 3c in one of our investment manager contracts with the vendor First Quadrant was inadvertently left off. You will have a revised attachment for 3c that contains the correct population of managers, including --

COMMITTEE MEMBER JELINCIC: Is that this one?

CHAIRPERSON COSTIGAN: The document should be in front of each of you.

OPERATIONS, PERFORMANCE & TECHNOLOGY DIVISION CHIEF FLYNN: The very last manager, First Quadrant.

CHAIRPERSON COSTIGAN: All right. Any questions or concerns?

Okay. Can I get a motion on 3c?

COMMITTEE MEMBER JONES: Move it.

CHAIRPERSON COSTIGAN: Moved by Jones.

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: Seconded by Taylor.

All those in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed?

Motion carries. Thank you

All right. Item 4 is just consent items, information consent.

Any questions, concerns?

Mr. Jelincic, your mic is, but -- okay. Thank you, sir.

All right. Seeing none on Item 4, those were just informational. Let's go to our first action item, which is Item 5a, the 2017-18 mid-year budget revision, second reading.

(Thereupon an overhead presentation was presented as follows.)

CHIEF FINANCIAL OFFICER ASUBONTEN: Mr. Chairman, through you. This is the action item, the 17-18 mid-year budget. There are not changes from the first reading. The proposed total budget for the $1,676,851,000 for 2,875 position represent 0.6 million, or 0.3 percent, decrease compared with 2017-18 annual budget.

I will not belabor the point at this point. As I mentioned, there is no change from the first reading. But I wanted to bring up an issue that came up on the SCO contract. When we reported it, and as you have in your materials, there was an increase of 1.9 million shown as an increase in the third-party administrative fees. I want to point out that actually it's a decrease of 5 million. The previous year's -- the previous year amount was 6.9. And this is the first time that we will -- we are classifying it as a budget item, and that's why it showed up as a decrease -- as an increase during the first reading.

Also, in the budget I believe that --

CHAIRPERSON COSTIGAN: Hang on one second.

Ms. Paquin, is your comment on this item? I mean, on this portion of the report?

ACTING COMMITTEE MEMBER PAQUIN: (Nods head.)

CHAIRPERSON COSTIGAN: Let me turn your mic on.

Yes, ma'am.

ACTING COMMITTEE MEMBER PAQUIN: Yes. Thank you, Mr. Chair. I want to thank you, Mr. Asubonten, and your staff clarifying that and doing the research and adding the footnote to the presentation. And didn't want to cut your presentation off, but I would also like to move approval of the agenda item.

CHAIRPERSON COSTIGAN: Okay. All right.

CHIEF FINANCIAL OFFICER ASUBONTEN Thank you.

CHAIRPERSON COSTIGAN: I'm sorry keep going. I just knew that her reference was what you just covered, sir.

CHIEF FINANCIAL OFFICER ASUBONTEN: I just wanted to also mention that during the present, there was a direction for us to work with the Department of Finance. And there will be an item today on the Health Care Fund and Contingency Reserve Fund as well. So I just wanted to point that out.

CHAIRPERSON COSTIGAN: Okay.

Mr. Jelincic, did you want to speak still?

COMMITTEE MEMBER JELINCIC: (Nods head.)

CHAIRPERSON COSTIGAN: There you go, sir.

COMMITTEE MEMBER JELINCIC: I actually had a question about that, but I'll hold it till that item.

CHAIRPERSON COSTIGAN: Okay. All right. Anything else?

CHIEF FINANCIAL OFFICER ASUBONTEN: No.

CHAIRPERSON COSTIGAN: It has been moved by Paquin. Seconded by?

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: By Taylor.

Any further discussion?

All those in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed?

Motion carries. Thank you, sir.

CHIEF FINANCIAL OFFICER ASUBONTEN: Thank you.

CHAIRPERSON COSTIGAN: All right. Next item is going to be 6a, which is going to be the legislative proposal for service credit purchase, tier conversion, and redeposits.

Mr. Pacheco.

DEPUTY EXECUTIVE OFFICER PACHECO: Good morning, Mr. Chair and members of the Committee. Brad Pacheco, CalPERS team.

Item 6a and 6b are two legislative proposals that we're bringing back to the Committee following our discussions last month. Before I turn it over to Donna Lum, I did want to address a topic that we raised last month as it relates to joint powers of authority, or JPAs.

Our FINO -- our Finance Office, as you recall, has brought information to this Committee about JPAs in our system, and more specifically those that have joint and several liability in their contracts for continued pension contributions. And as you may recall, the majority of the JPAs in our system do not have this language within their contracts, which does raise risk for both our members and retirees. And an example of that would be the East San Gabriel Valley Consortium that the Board had to make a difficult decision on.

So this was an issue that we wanted to address with a legislative fix. We have talked to our member and employer associations, and we've determined, and all agreed, that our member associations will carry this legislation, and we will serve as a technical expert. And we look forward to working with them and bringing a bill back to the legislature to correct this.

So with that, I'll turn to Donna Lum on the discussion -- oh, I'm sorry there's a question.

CHAIRPERSON COSTIGAN: Okay. Hang on a second, Mr. Pacheco.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Brad, on the JPAs, the member associations are going to carry language that will insist on joint and several, is that what I heard?

DEPUTY EXECUTIVE OFFICER PACHECO: Correct. Yes.

COMMITTEE MEMBER JELINCIC: And we obviously will be supporting that?

DEPUTY EXECUTIVE OFFICER PACHECO: We've already shared some language with them. They may take it a little bit further, and we will have to look at what they're recommending, but for sure around joint and several liability.

COMMITTEE MEMBER JELINCIC: And it will come back to this Committee at some point?

DEPUTY EXECUTIVE OFFICER PACHECO: Correct.

COMMITTEE MEMBER JELINCIC: Thank you.

CHAIRPERSON COSTIGAN: All right. Mr. Pacheco, we're going to have folks have who have requested to speak on both Item 6a and 6b, so let's do them separately. So 6a first and then I'll call up the folks that want to comment and then we'll do 6b

DEPUTY EXECUTIVE OFFICER PACHECO: Sure. And I'll turn to Donna Lum on 6a.

CHAIRPERSON COSTIGAN: Thank you, Ms. Lum.

DEPUTY EXECUTIVE OFFICER LUM: Good morning, Mr. Chair, members of the Committee. Donna Lum, CalPERS team member.

Agenda Item 6a is an action item. And if you recall from the Finance and Administration Committee last month, we were requested to bring this item back, and to look at potential other options, in addition to what we were proposing.

The team is recommending that the Committee sponsor legislation to require members who elect to purchase service to purchase or convert service credit on or after January 1st, 2019, to pay any remaining balances on the member's retirement date or to elect an Actuarial Equivalent Reduction, also known as an AER, in lieu of making installment payments into retirement.

These same payment options will also be provided to the survivor or beneficiary upon notification from CalPERS following the member's pre-retirement death.

You'll note in the agenda item that the team did look at a couple of different options, and the option that we're bringing forward to you we feel is a very viable option is the AER.

Joining me today is Don Martinez from Customer Support who will be presenting this item, along with Fritzie Archuleta from our Actuarial Office who will be available to answer questions as well.

So at this time, I'd like to turn the presentation over to Don Martinez.

MR. MARTINEZ: Good afternoon. Don Martinez, CalPERS team members. So Agenda Item 6a is an action item, as Donna had mentioned. And again, the recommendation is to sponsor legislation that would require members who elect to purchase or convert service credit on or after January 1st, 2019 to pay any remaining balance on the member's retirement date, or to elect a

Actuarial Equivalent Reduction, also known as an AER, in lieu of making installment payments into retirement.

So as Donna had mentioned, this proposal -- we did present the proposal last month. The Committee directed us to research other options. So over the course of the past month, the team is researching -- has been researching the options that are listed on page 3 on the agenda item.

If you're viewing the agenda on your iPad, that would -- the options are listed on page 62.

So our research concluded that each one of the options that's outlined in the agenda item would create additional risk, would significantly increase workload and complexity. However, our research did determine that offering an AER is a viable alternative for our members.

At the time of retirement, if a member is unable to pay the balance in full, they can elect an AER. An AER is a permanent reduction in their retirement allowance, and it ensures that the remaining service credit purchase balance, and the lifetime monthly payments are equivalent in value.

In addition, this proposal would allow members who retire on or after January 1st, 2019 and elected to purchase or convert service credit prior to January 1st, 2019, the additional option of being able to elect and AER at the time of retirement.

So this group of members would have the same options that are available to them today, which is a lump sum payment or install payments into retirement, but they would have the additional option of being able to elect an AER.

So we believe the AER option is a viable alternative for members who do not have the resources to pay a lump sum balance at the time of retirement. This option would allow members to maintain their service credit balance -- I'm sorry, their service credit purchase and receive a benefit increase in their retirement allowance. In addition, this proposal would allow us to reduce complexity, which, of course, is a goal in our strategic plan. This concludes my presentation, and we'd be happy to answer any questions.

CHAIRPERSON COSTIGAN: Thank you very much. We're going to first go to Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: I really believe that we should allow the retirees to pay this into their retirement. If we capture all of the benefits and use that to reduce their obligation, then we really haven't created a unfunded liability, because they haven't gained that benefit. And therefore, you know, if they do die and don't pay it, they haven't gained so it's not an issue there.

And so I -- I really think that we ought to let them continue. And the other question I have is how much are we talking about? Is this statistical noise or is it something really of significance?

MR. MARTINEZ: Yes. Excuse me.

So currently there are a little under 40,000 members who have elected to purchase service credit. So these members are in some stage of an installment payment plan. So of the little under 40,000, 20 -- 50 -- I'm sorry, 58 percent are retirees. And the outstanding liability for the retirees is 383 million.

COMMITTEE MEMBER JELINCIC: And do we have any idea how many people die on us?

MR. MARTINEZ: I'm sorry?

COMMITTEE MEMBER JELINCIC: How many of the -- do we have any statistics on how many of these people have -- are paying into retirement have died on us, the total liability is 330 million, but we're only concerned about people who die and don't pay us back. So do we have any data on how many people actually die?

DEPUTY EXECUTIVE OFFICER LUM: Mr. Jelincic, we did do some research over the period of 3 years. And what we did identify is approximately 286 retirees who died before the benefit was paid resulting in about a $4.6

million uncollectible debt to the system, of which the system had to absorb. These are members that did not have an ongoing allowance to share that we would be able to collect that debt from.

COMMITTEE MEMBER JELINCIC: Okay. So over 3 years, it's $4.6 million and we're paying out $16 billion a year.

DEPUTY EXECUTIVE OFFICER LUM: (Nods head.)

COMMITTEE MEMBER JELINCIC: I would argue it's statistical noise. Thank you.

CHAIRPERSON COSTIGAN: However, I just want to be clear, what you're talking about is this -- above that 4.6 million, the rest of the membership in the system absorb that?

DEPUTY EXECUTIVE OFFICER LUM: That's correct.

CHAIRPERSON COSTIGAN: Okay. And then of the -- that's a different issue. Of the 52 percent, do you have a breakdown between local and State?

MR. MARTINEZ: So we sure do. So currently, we'll just look at the 39,000. So of the 39,000, a little under 40,000, percent are -- have a school employer, 44 percent are State, and 31 percent are public agencies.

CHAIRPERSON COSTIGAN: Okay. See if you can answer the next one too. We'll keep peppering you with questions. How about the average benefit among that 52 percent, what't their average monthly benefit?

MR. MARTINEZ: All right. So we've looked at this from an employee standpoint. So what we did is we looked at the number of employees. We looked at their serve credit and did kind of an average. The average service credit balance per employee is right at 19,000

CHAIRPERSON COSTIGAN: Okay. An so on average -- so are we -- sort of to Mr. Jelincic's question, which is sort of kidding aside, I'm trying to figure out the population. The 4.6 million is significant, because that is -- that's a cost that members end up absorbing. But are we talking that -- with folks that are on the sort of the average benefit that we talk about around 3000 a month or are these statistically folks who have a significant -- I'm just trying to figure out how you get to the 300 -- over $300 million liability, what's the average monthly benefit?

MR. MARTINEZ: Yeah, I don't have that --

CHAIRPERSON COSTIGAN: Okay.

MR. MARTINEZ: We'd have to provide that.

CHAIRPERSON COSTIGAN: Because I was just trying to figure out what this population looks like. We're going to -- Mr. Feckner, I know you had some issues last time this issue was up, sir.

PRESIDENT FECKNER: Thank you, Mr. Chair. In the last month, I raised a lot of questions on this topic, and have done a lot of thinking about it in the meantime. And I appreciate the work that you've all done.

My biggest problem with this going forward again is, like I said last month, there's no leverage on the employer to report the time that the employees could have had in previous service. So I'm not talking about the re-deposit. Those are choices that the members made.

I'm talking about employees that came into the State work system, whether it be schools, et cetera, mainly schools, and we have some unscrupulous employers out there that are hiring at 3 hours and 55 minutes a day to stay below that 4-hour minimum for PERS membership. They're doing it on a budget basis. I understand that.

But that then creates this problem later on when the member makes that 4-hour threshold, and wants to get that time back, and the employer doesn't go on and cooperate and give us the time et cetera.

So for me, and I look at it as an easy fix. It's not going to be for you other others. But I would like to recommend through the Chair that our CEO be asked to meet with the Chairs of the Committees of both the Assembly and Senate Percent Committees, and ask to seek legislation that whenever a school employee is hired, they start in the PERS system on day one regardless of the number of hours, that we don't have that 4-hour threshold anymore. They don't have it at STRS. This STRS employees when they're hired in they're put into the system.

It would put -- A, put more members into our system. Yes, less hour members, but it would take away this problem of that service credit purchase in the past, and also give our members -- our school employees chance to actually gain some retirement incentive.

Thank you, Mr. Chair.

CHAIRPERSON COSTIGAN: Okay. Mr. Feckner, hang on leave your mic on, sir. And just a question. As to the proposal before us, are you supportive or are you offering this as companion legislation?

PRESIDENT FECKNER: Companion. I would like to see -- I I'm not as -- I don't have as much heartburn on it planned as we have right now, that they're serving it to us. But again, I think that my biggest part is the back end, that the employer not being responsible and not giving back the information from a prior dated employee that may have started like in 1990, and had a bunch of years, and the employer doesn't have that information any more.

So then the employee, the member, is then disenfranchised. So I think if we can move this forward --

CHAIRPERSON COSTIGAN: All right. So we're going to start.

PRESIDENT FECKNER: -- and everybody starts on the same page day 1 that we don't have this problem anymore.

CHAIRPERSON COSTIGAN: All right. We're going to give Committee direction to both Ms. Frost and Mr. Pacheco, and Ms. Lum. I know we don't have a meeting in January. But what I would like to try and do is if we could have some information or some -- as part of the executive report in January, because the calendar is starting to get late, for when we would be introducing legislation, and we would have to take up, if the Board was going to look at proposing something, Mr. Feckner, to take it up at the February meeting for introduction in late February. So thank you, Mr. Feckner.

PRESIDENT FECKNER: Thank you.

CHAIRPERSON COSTIGAN: Jai, you want to come on down. Sorry. I should have called you a moment ago.

Any other questions from Board members while we're waiting for -- Okay. Donna you don't have to get up. He can sit right next to you.

Good afternoon, sir.

MR. SOOKPRASERT: Good morning, Mr. Chairman -- or afternoon, Mr. Chairman and members. Jai Sookprasert with the California School Employees Association. The Committee is raising all the questions that we're raising, and so we appreciated -- but first of all, I just want to acknowledge, we have been working with the CalPERS staff. I appreciate some of the data they provided us.

Our concern not only to Mr. Feckner's point -- or Mr. Jelincic is it statistical noise? Now, we have a certain policy that allows people to get the benefit, and be able to make that installment into their retirement. But we're changing that now. And we're looking at the AER and say sure, it makes sense on an actuarial basis, that you're covering to make sure that people who die off, you know, are covered somehow. So we're looking at that, and we do feel that that is a fair actuarial view of that, but still, it gets back to our issue.

And so I'm here. I don't have a formal position. We have a neutral position at this point. We want to knowledge the work that we're doing with the staff, but we want to continue to look at this into the legislative process to try and protect, particularly for my members, who make very little money, you know, low wage workers who come into the system, denied this all through the process for decades even.

We have real stories of people who dedicated their lives to help children, and did not get these benefits until later in life in their career, now, they have less time to payoff. They AER is reducing their benefit. It just feels a little bit wrong, and we want to find a fair way what to address the liabilities at hand, but we want to also to acknowledge that these folks are not high-wage workers.

And now, whether it's 2000 for their buy -- buyback or the re-deposit at 20,000, those are significant figures for somebody at the end of their career to try to make up. And what's fair for 24 percent of this group of retirees to try to be able to recoup that. So we're looking at all the different aspects, and we'll continue to work with CalPERS, you know, the legislative process unfold over several months period. We want to bring back some reasonable proposal, and maybe no changes at all ultimately to what you're trying to do.

And so we want to at least acknowledge the work, and that be on record as saying we're still reviewing this. This is relatively new for us. So thank you for all the different questions.

CHAIRPERSON COSTIGAN: All right. Thank you. As you know, if the Committee sides to move forward with it, it will just be introduced. We'll continue to have both the legislative discussions and then this Committee would still, over the course of the next 10 months, continue to have these discussions on amendments.

So any other questions on 6a?

Okay. What's the pleasure of the Committee?

Did I hear a motion?

Oh, now you -- there was no on here before. Now, Mr. Jones.

COMMITTEE MEMBER JONES: Yeah. Thank you, Mr. Chair. The question is is this proposed legislation is effective January 1st, 2019. So does that mean that everyone in the system now is grandfathered in? They would not be subjected to this?

MR. MARTINEZ: So, yes. So this proposal is being -- would go on a prospective basis. So it would only impact those individuals who elect to purchase service credit or convert service credit on or after January 1st, 2019.

COMMITTEE MEMBER JONES: So all the retirees in the system, if they elect to purchase that time before the 19th -- january 2019, they would not be affected by this policy?

MR. MARTINEZ: That is correct.

COMMITTEE MEMBER JONES: So there is a window of opportunity here to fix it for those that are already in?

MR. MARTINEZ: That is correct.

COMMITTEE MEMBER JONES: Okay.

CHAIRPERSON COSTIGAN: Mr. Slaton.

COMMITTEE MEMBER SLATON: Thank you, Mr. Chair. It just seems to me that it's a -- if we add in what Mr. Feckner has advocated for on the school employees, I think it creates a reasonable balance to have the -- and I would take issue that $4 million, yes, when you compare it to what we pay out it's noise, but it's still $4 million.

And so I think from a fiduciary standpoint, we need to have a system that is fair to everybody else, as well as fair to those who are making these purchases. So I think it's a good balance, especially with what Mr. Feckner is advocating. So do you -- are you looking for a motion?

CHAIRPERSON COSTIGAN: Well, let me call on the Vice Chair, and then we'll come back for a motion.

COMMITTEE MEMBER SLATON: Okay.

CHAIRPERSON COSTIGAN: Ms. Taylor.

VICE CHAIRPERSON TAYLOR: So I was just going to say I also support the legislation. I think that we need to realize that it is our members' money paying for those members that are passing away, still owing money. So I would be in support of the legislation.

I am also in support of Mr. Feckner's proposed companion legislation at a later date to accommodate those employees that you're talking about. I didn't know you had employees like that. So I'm going to let Mr. Slaton make the motion.

COMMITTEE MEMBER SLATON: So I move that we adopt the -- we advocate for legislation for the actuarial approach as presented by staff, along with the recommendation of Mr. Feckner regarding school employees.

CHAIRPERSON COSTIGAN: Let me just get clarification on that. I think what --

COMMITTEE MEMBER SLATON: Would it be a separate --

CHAIRPERSON COSTIGAN: It would be a separate, because what we're just going to move right now would be Item 6a, and then we have Committee direction to come back --

COMMITTEE MEMBER SLATON: Gotcha.

CHAIRPERSON COSTIGAN: -- hopefully in January, at least no later than February for this Board to consider the legislation that Mr. Feckner is talking about. Is that correct acceptable, Mr. Feckner?

PRESIDENT FECKNER: It is.

COMMITTEE MEMBER SLATON: So move 6a.

CHAIRPERSON COSTIGAN: 6a. Is there a second?

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: And seconded by Taylor. Any further discussion?

All right. Hearing none.
All in favor?
(Ayes.)
CHAIRPERSON COSTIGAN: Opposed?
(Noes.)
CHAIRPERSON COSTIGAN: Please note Mr. Jones and Mr. Jelincic as no votes.
Motion carries.
COMMITTEE MEMBER JONES: And I just want to --
CHAIRPERSON COSTIGAN: Oh, hang on a second, Mr. Jones.
COMMITTEE MEMBER JONES: Yeah, I want to be clear. I, too -- the $4 million is real money. And I don't think we should be having policies where one member is getting a benefit that's costing another member funds.
But I want to look at the process that Mr. Feckner recommended, so that if that could take effect, and we still have this by the time, we could fix this problem if all those members are notified that if they want to make that purchase, they can make it before that time, then the harm on those employees would be mitigated
CHAIRPERSON COSTIGAN: No. And I think as you know, Mr. Jones, the reason we're doing this, as Mr. Pacheco can attest to you, you've got to get the language into leg counsel. We need to get the draft back. We've

got to find an author. We're working, I think, it's February 26th this year that we've got to have it introduced.

And so, we're at the very beginning, as you know, of the legislative process. So I'm sure we're going to see matter at least three or four more times. And given how good Jay is, I'm sure we're going to hear it at every Committee. And I just want to get it out of the first house, so anyway.

Anything else on this item?

All right. So 6b, sir, Mr. Pacheco.

DEPUTY EXECUTIVE OFFICER PACHECO: So 6b is being brought back at the request of one of the Committee members, Mr. Jelincic, related to options with our Retirement Benefit Replacement Program.

I'll turn to Donna Lum to tee this item up.

DEPUTY EXECUTIVE OFFICER LUM: Thank you, Brad. Donna Lum, CalPERS team member.

So as Mr. Pacheco said in his opening, we're bringing this matter back to you at the request of Mr. Jelincic from the last meeting. We are seeking the Committee's direction to either continue to process the RBP as we do today, or to propose legislation which would eliminate the custodial fund and our interaction -- our intermediate responsibility.

So at this time, I'm going to go ahead and turn it over to Jan Falzarano, who has done a lot of research in this area, who will then turn it over to Anthony Suine who will give you some information on the program operation as well.

RETIREMENT RESEARCH AND PLANNING DIVISION CHIEF FALZARANO: Thank you, Donna.

So, good afternoon Mr. Chair, and members of the Committee. Jan Falzarano, CalPERS team member.

Agenda Item 6b is an action item requesting direction on whether CalPERS should amend its Replacement Benefit Plan by eliminating the Replacement Benefit Custodial Fund, otherwise known as the RBF. If the Board's direction is to amend the Replacement Benefit Plan, CalPERS team member would make the necessary legislative changes to amend the provisions that govern this plan.

Amending the Replacement Benefit Plan does support the CalPERS 2017 though '22 strategic plan to reduce complexity, and to also simplify the program.

To provide some background, the Internal Revenue Code, section 415 B, limits the amount of benefits that a tax qualified plan can provide to participants. Currently, the limit for participants that retire at the age of 62 is to $215,000. That number will increase line

$220,000 starting with January 1, 2018.

For participants that retire prior to the age of 62, that limit is actuarially reduced. The IRC 415(m) section allows governmental pension plans to provide benefits that exceed this limit, but the benefit can only be paid from a qualified governmental excess benefit arrangement and not from the retirement fund.

Now, providing this excess benefit from the qualified governmental excess benefit arrangement is an optional option, and CalPERS chose to exercise this option and establish the Replacement Benefit Plan and corresponding RBF in 1989 and 1990.

The purpose of the Replacement Benefit Plan is to ensure that the members impacted by IRC 415(b) limit are provided to the extent reasonable with commensurate replacement benefits. Right now there are close to a thousand CalPERS benefit recipients that have retirement benefits that exceed the IRC 415(b) limit, and have received an excess benefit payment through the RBF.

Team members anticipate that the number of RBP participants will continue to increase as more of our classic members retire. But eventually, it will decrease as PEPRA retirements increase. In 2013, the Public Employees's Pension Reform Act prohibited any California employers from offering a replacement benefit plan for employees that are hired on or after January 1 of 2013.

So at this time, I'm going to turn the presentation over to Anthony Suine and he will discuss the program considerations.

BENEFIT SERVICES DIVISION CHIEF SUINE: Thanks, Jan.

Good afternoon, Mr. Chair, members of the Committee. Anthony Suine, CalPERS team member.

So as Donna and Jan both mentioned, the two options before you for consideration are modify the Replacement Benefit Plan by eliminating the Replacement Benefit Fund or keep the current Replacement Benefit Plan as is.

If you desire to modify the Replacement Benefit Plan by eliminating the RBF, it would remove CalPERS and their intermediary role between the benefit recipient and the employer.

So currently, how it works is CalPERS annually tests benefit allowances against the limit. We invoice employers for the amounts over the limit to all former employers of the participant. We manage the fund. And we pay the participants of the plan on a monthly basis once the employers fund the benefits.

We then handle inquiries from the members and employers, and we issue annual W-2s to the participants of the plan.

If the Board direction was to eliminate our administration of the RBF, we would continue to annually test the benefit allowances against the 415 limits, notify the employers of their limited amount and the members of their amount in excess of the benefits proportionate to each employer, and we would respond to general inquiries.

We would no longer collect employer payments. We would no longer invoice the employer. We would no longer manage the Replacement Benefit Fund itself. We would no longer issue tax forms, and we would no longer be responsible for the payments to each of the RBP participants.

So although this does transfer responsibility for administration to the employer and the participants to collect from their employers, this proposal does align with our strategic plan goal of reducing complexity, and allow us to focus more on our core processes.

That concludes our presentation, and we're happy to take any questions.

CHAIRPERSON COSTIGAN: All right. Thank you, Mr. Suine.

Vice Chair Taylor.

VICE CHAIRPERSON TAYLOR: Hi. Thank you, Mr. Chair.

Mr. Suine, you and I talked about this a little bit earl -- at little bit last week. And I was a little concerned because I think you -- I don't know that you covered it right now, but before you told me that we have automated some systems already to take care of mitigating some of the, you know, longhand issues that we ran into.

So we do already have a system in place to take care of this, an actual automated system, is that correct?

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct, many of the functions are automated.

VICE CHAIRPERSON TAYLOR: Okay. And then we've been doing it for how long?

BENEFIT SERVICES DIVISION CHIEF SUINE: About 25 years.

VICE CHAIRPERSON TAYLOR: About 25 years?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes.

VICE CHAIRPERSON TAYLOR: Okay. And so now you're asking for employers who have absolutely no experience with this to suddenly us to back away and say, hey, sorry, you guys have to do this now. We'll give you the estimate and everything, but you guys have to process all of this.

And my fear is that our retirees will then have a hard time obtaining those payments. And I get that we -- you know, they don't -- they don't get those payments right away now. They don't get them with their normal retire payment, and then we get kind of the blame for that. But I think it's important to understand that we can -- we're big. And I can't see a tiny little city or a county or whatever being able to handle this. And maybe they only have one employee. Maybe it's not a big deal.

But I think that taking this option away hurts our retirees. And I just don't think it's necessary, since we've been doing it for so long, and we have an eventuality that it sort of peters out on its own anyway. So that's my feeling on this.

Thank you.

BENEFIT SERVICES DIVISION CHIEF SUINE: Thanks, Ms. Taylor. We're bringing the information back based on the Board direction, so I'm not asking necessarily.

(Laughter.)

CHAIRPERSON COSTIGAN: All right, Mr. Suine.

Mr. Saha. Matthew.

ACTING COMMITTEE MEMBER SAHA: Thank you, Mr. Chair. Kind of piggyback off of Ms. Taylor's question a little bit, that the -- I guess my understanding is it accurate that the employers are expected to pick up any excess benefit or what happens to that excess benefit for members?

BENEFIT SERVICES DIVISION CHIEF SUINE: So the employers already pick up the excess benefit.

ACTING COMMITTEE MEMBER SAHA: Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: It's just we play this intermediary role where we invoice them for the money, they send it to us --

ACTING COMMITTEE MEMBER SAHA: Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: -- then we administer the payment of those funds. So under this proposal, we would just let them know how much the participant was limited, and then they would make that payment directly to the member.

ACTING COMMITTEE MEMBER SAHA: Okay. Thank you, Mr. Chair.

CHAIRPERSON COSTIGAN: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: One of the complaints that we've gotten is that, well, I've got three different employers in my career. And I would have to contact all three of the employers. What happens now when we invoice those three employers, and one pays and two don't, or two do and one doesn't?

BENEFIT SERVICES DIVISION CHIEF SUINE: Sure. So we make those payments proportionately. Whoever pays, then it triggers us to make that monthly payment based on what has been paid. And then we continue to communicate with the other employer to fund their invoice.

COMMITTEE MEMBER JELINCIC: And I recognize that this is a dying program. I also recognize it's an employer promise that was made. One of the issues that first raised this is I get tired of hearing of the people who are getting, you know, $300,000 pensions. And I know part of that is, you know, this excess pension.

I'm just wondering from an administrative viewpoint, can we report them separately, so that when we get a public records request, we don't say this guy is getting a $300,000 pension. We say he's getting 220, plus another 80 directly from the employer?

BENEFIT SERVICES DIVISION CHIEF SUINE: We surely could. And we do list our RBF participants. I believe they're identified on the Transparent California on our data extract.

RETIREMENT RESEARCH AND PLANNING DIVISION CHIEF FALZARANO: I think we pulled the entire dollar amount, but I think we are able to pull those -- the portion of the RBF separately, but I would have to go back to my team and take a look at that data specifically.

COMMITTEE MEMBER JELINCIC: I would strongly urge that we do that. Now Transparent California is probably going to combine the two, but -- because they've got their own agenda. But we ought to be pushing our agenda, which is to expose what real pensions are to real employees.

The -- and I'm the one who asked that this go forward. You know, I would ask you to look at the reporting, but I will not make a motion to terminate it.

CHAIRPERSON COSTIGAN: Okay. I'm sorry, Mr. Jelincic. This is in response to a request that you made.

COMMITTEE MEMBER JELINCIC: Yes.

CHAIRPERSON COSTIGAN: So at some point - I'm not asking now - will you be making a motion to support Option 1, or did I just understand that you're not -- I'm sorry, Option 2.

COMMITTEE MEMBER JELINCIC: I'm not going to make a motion at all. And it -- you know, the current practice can continue in the absence of any motion to change it.

CHAIRPERSON COSTIGAN: Okay. All right. That's what I needed to understand. Thank you.

Mr. Slaton.

COMMITTEE MEMBER SLATON: Thank you, Mr. Chair. Let me make sure I understand. Out of those thousand CalPERS members, are there -- just so I understand the rules, prior to -- if they started employment prior to 1990, they're not subject to these limits, is that accurate or not?

BENEFIT SERVICES DIVISION CHIEF SUINE: That's not true.

COMMITTEE MEMBER SLATON: Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: They still are subject to the limits. There's various rules about a portion of the benefit being grandfathered, if there was no benefit increases since 1990.

COMMITTEE MEMBER SLATON: I see.

BENEFIT SERVICES DIVISION CHIEF SUINE: And it gets real complex in that area. But even if you were a member prior to 1990, you're subject?

COMMITTEE MEMBER SLATON: You're still subject to the IRS limits?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes, correct.

COMMITTEE MEMBER SLATON: Okay. And these benefits are paid -- are a pay-as-you-go benefit, the excess portion. So they're just paid out of the employer's budget -- annual budget expenditure?

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct. We invoice them twice a year, and they write us a check.

COMMITTEE MEMBER SLATON: Okay. Now, we -- how is administrative fee set? Because we capture an administrative fee from the employers, is that correct?

BENEFIT SERVICES DIVISION CHIEF SUINE: We actually capture it from the participant and we bill the participant --

COMMITTEE MEMBER SLATON: From the employee?

BENEFIT SERVICES DIVISION CHIEF SUINE: -- per the law.

COMMITTEE MEMBER SLATON: So it's a -- so we net that against the payments that are being made?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yeah. We look at all -- look at the total amount being paid out, and then we look at how much in administrative costs we have. So we look at the team members associated with it. We look at the system costs that have been generated from it, and then we look at the percentage to make up that. And so for last year, it was 2 percent. And so each participant was charged a 2 percent admin fee on their RBP payment.

COMMITTEE MEMBER SLATON: But you do the calculation holistically and then everybody is charged the same --

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct.

COMMITTEE MEMBER SLATON: -- percentage as a charge?

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct.

COMMITTEE MEMBER SLATON: And then we look at that every year or so, every five years, or --

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes. Every year we reanalyze our admin fees. And we would apply that percentage.

COMMITTEE MEMBER SLATON: Okay. So we're net neutral on the expense of doing this?

BENEFIT SERVICES DIVISION CHIEF SUINE: Correct.

COMMITTEE MEMBER SLATON: Okay. It just seems to me, particularly with the multiple employer situation to -- even though these are highly compensated people, you know, when you stop and think about it, it's the amount over 217 -- whatever the number is this year.

BENEFIT SERVICES DIVISION CHIEF SUINE: 215.

COMMITTEE MEMBER SLATON: 215. So these are pretty highly compensated retirees who are in this situation. On the other hand, it still leaves them in a lurch, if you -- especially in a multi-employer situation where they have to go work with each employer, and then who does the calculation for how much comes from employer A versus employer B?

BENEFIT SERVICES DIVISION CHIEF SUINE: We do that.

COMMITTEE MEMBER SLATON: Right. But if -- would we still do that?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes, we would.

COMMITTEE MEMBER SLATON: Okay. So we would still provide that information to the employee as data for them to try to go after their money.

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes.

COMMITTEE MEMBER SLATON: Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: And a clarification on the high wage earner. While many of them are the benefit, as Jan mentioned, is actuarially reduced at an early age of retirement. So they -- not all of them are earning 215,000, and about 20 percent are correctional officers who are not seen as safety per the rules of the IRS.

So they -- they may retire at age 50, and have a 3 percent at 50 benefit formula and be limited. So they could earn $100,000 and be limited, even though the 62 limit is 215. So I just wanted to make that clarification.

COMMITTEE MEMBER SLATON: Well, I, for one, don't see the compelling reason to drop this program. My inclination would be to continue it as it is, which is Option 2, is that --

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes, that's correct.

COMMITTEE MEMBER SLATON: Is that right Option 2? Would you -- the chair entertain a motion?

CHAIRPERSON COSTIGAN: Well, as Ms. Taylor and I were having a conversation, we have a few more speakers. I'm not actually sure a motion is required, if we're going to just maintain the current practice.

COMMITTEE MEMBER SLATON: Okay.

CHAIRPERSON COSTIGAN: But I don't know yet.

COMMITTEE MEMBER SLATON: That's fine.

CHAIRPERSON COSTIGAN: That's where we may land. We still have three more folks.

Ms. Paquin.

ACTING COMMITTEE MEMBER PAQUIN: Thank you, Mr. Chair. I noted in the staff report that since this request was recently mad, you didn't have much time to do much stakeholder outreach. Did you do any?

BENEFIT SERVICES DIVISION CHIEF SUINE: So we've had some conversations, Stakeholder Relations and our CEO has had some conversations with stakeholders about the program.

ACTING COMMITTEE MEMBER PAQUIN: Is there any sense of exactly how many employers are currently providing these payments?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yeah, there's -- we bill between 450 and 500 employers annually.

ACTING COMMITTEE MEMBER PAQUIN: Okay. You know, I guess my point of view I think that unless or until you've had a chance to really reach out to these employers and talk about what this would mean for them and other options, then we would be in favor of just keeping with the status quo.

CHAIRPERSON COSTIGAN: Anything else?

ACTING COMMITTEE MEMBER PAQUIN: No.

CHAIRPERSON COSTIGAN: Ms. Taylor.

VICE CHAIRPERSON TAYLOR: So I just had a couple more questions that I forgot to ask before.

Do we have any idea how many employees actually participate in this?

BENEFIT SERVICES DIVISION CHIEF SUINE: There's a thousand.

VICE CHAIRPERSON TAYLOR: Okay. A thousand. And do we have a dollar amount attached to that thousand?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yes. So the average dollar amount is approximately $1400 a month for each participant in the plan. There's highs of 20,000 annually that somebody receives, and lows of $20 annually that somebody receives from the program.

VICE CHAIRPERSON TAYLOR: Oh, my goodness. Just because they exceed the IRS, right?

BENEFIT SERVICES DIVISION CHIEF SUINE: If it's a dollar over, they're in the program.

VICE CHAIRPERSON TAYLOR: I got you. Okay.

So -- and then I just want to clarify. Even though it asked for an action, Option 2 is really just status quo, right?

BENEFIT SERVICES DIVISION CHIEF SUINE: All right. So this was just an information item to share -- as I mentioned before, we're just bringing back the information.

VICE CHAIRPERSON TAYLOR: It says action item.

BENEFIT SERVICES DIVISION CHIEF SUINE: Oh, it is an action item.

CHAIRPERSON COSTIGAN: No, it is an action item

BENEFIT SERVICES DIVISION CHIEF SUINE: Sorry. So we are looking for your direction for one or the other.

CHAIRPERSON COSTIGAN: So we are going to --

VICE CHAIRPERSON TAYLOR: Okay. Thank you.

CHAIRPERSON COSTIGAN: -- the Vice Chair and I have decided we will take a motion depending on which way the Committee wants to go.

Anything else, Ms. Taylor?

VICE CHAIRPERSON TAYLOR: That's it.

CHAIRPERSON COSTIGAN: Okay. I'm going to call on Mr. Jones, but Ms. Johnson and Mr. Lennox, would you come on down.

Mr. Jones.

COMMITTEE MEMBER JONES: Yeah. Thank you, Mr.

Chair. The -- I think Bill asked the question about the administrative charge. So whatever the cost is, you can recoup that cost. So it's not like an encroachment on our other funds in any way whatever, is that correct?

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct, the administration of it.

COMMITTEE MEMBER JONES: And secondly, this is a decreasing pool of members, because it -- doesn't PEPRA avoid this going forward after 2013?

BENEFIT SERVICES DIVISION CHIEF SUINE: It does. So the -- it will increase as our retirements increase, and, you know, more retirements from people are the 1990s would retire. So it temporarily may increase.

COMMITTEE MEMBER JONES: Okay. But eventually it will be --

BENEFIT SERVICES DIVISION CHIEF SUINE: -- but eventually it will decrease not only for PEPRA, but some other contribution limits that were put in place in 1996.

COMMITTEE MEMBER JONES: I see. Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: That will help decrease the increase in participants.

COMMITTEE MEMBER JONES: Okay. So the law says that this provision cannot be provided after -- anyone that's hired after 2013 or anyone after the date of 2013?

BENEFIT SERVICES DIVISION CHIEF SUINE: Yeah, new members --

COMMITTEE MEMBER JONES: New members only. Okay.

BENEFIT SERVICES DIVISION CHIEF SUINE: -- who came in on or before.

COMMITTEE MEMBER JONES: So in the long term, it will go down --

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct.

COMMITTEE MEMBER JONES: -- not soon. But the bottom line is that it is funding itself.

BENEFIT SERVICES DIVISION CHIEF SUINE: That's correct.

COMMITTEE MEMBER JONES: Okay. Well, I could support status quo with that.

CHAIRPERSON COSTIGAN: Okay. We'll get to a motion in a second. We have Ms. Johnson from CSAC first.

MS. JOHNSON: Yes. Good afternoon. Dorothy Johnson with the California State Association of Counties. We are here today in support of Option 2 to maintain the status quo. And we appreciate the dialogue and discussion from the Board and the questions for, again many of the reasons that were already stated. And this isn't just an issue of CalPERS versus employers, us/them, but what will be the eventual outcome for the participants and the members who may potentially have to reach out to multiple employers, who may not have the expertise that CalPERS has to administer such program.

Also want to readjust the lack of fee authority or the administration fee for locals. We currently don't have that authority. I don't think we'd be able to recoup any of the costs for maintaining a customer service line, let alone the processing of these -- of these checks.

So for these reasons we're pleased to support 2, and again really appreciate the comments that were shared here today.

Thank you.

CHAIRPERSON COSTIGAN: Thank you, Ms. Johnson.

MR. LENNOX: Good afternoon, Chair and Members. Derick Lennox on behalf of the School Employees Association of California --

CHAIRPERSON COSTIGAN: Hang on a second.

Okay. Go ahead.

MR. LENNOX: School Employers Association of California, as well as the Small School Districts Association here in support of Option 2.

Having worked directly with retired members and stakeholder employers who participate in the Replacement Benefit Plan, I want to encourage the Board to keep the status quo. And so in the spirit of offering some stakeholder feedback, I just want to make a couple of points.

The first is that CalPERS retired members are best served by CalPERS continuing to run the program. You all have thousands of members agencies. And CalPERS is really the hub in the proverbial wheel when it comes to this program. And there's no question that you are doing a better job in administering it at a low cost than -- and I speak respectfully about our own clients -- the employers that we work with.

And so when you think about the thousands of spokes in the wheel, it really becomes a difficult problem for retired members to be able to get those contributions and payments.

But it's not just a cost efficiency issue, you know, as many members have mentioned, those truly harmed in a more decentralized Option 1 would be those retired members. And approximately 40 percent of those in the Replacement Benefit Plan currently have two or more employers that they'd have to hunt down across the state, and sometimes not just in the schools pool. They could be a city employee at one point in their career, and a school employee at a different point in their career.

So I can tell you from experience that unfortunately the members aren't always successful, sometimes due to the employers. And that's a challenge.

And, you know, the result is them having to spend tens of thousands of dollars in legal fees, not only suing, you know, the school districts, in our case, but also CalPERS, unfortunately to try and recoup those costs.

And, you know, for those who are earning $20 a month on it, it just doesn't make a lot of sense to create more instances you could see that sort of issue occurring.

The second point I want to raise in the spirit of collaboration is that to the extent the Board is interested in reducing complexity within the system, Strategic Objective number 3, I also want to remind the Board that the purpose of that is, of course, to ensure benefit payment timeliness and customer satisfaction.

And to that end, I am really pleased to report that last year we were able to work very productively with your staff on a piece of legislation to increase the likelihood of collection and transmittal by county offices across the State to make sure that retired members are able to receive those contributions after their career.

And the bill that eventually was signed into law will have no associated expenses for CalPERS, but hopefully act in a way to reduces that complexity, and better serve those retired members.

And with that, I'll close.

Thank you.

CHAIRPERSON COSTIGAN: All right. Thank, Mr. Lenox. And also we received a letter from Peter Kutras on this item as well, where he is asking that the Board adopt -- or the Committee adopt Option 2.

Mr. Slaton, would you push your microphone, please?

All right. Mr. Slaton

COMMITTEE MEMBER SLATON: I move Option 2.

CHAIRPERSON COSTIGAN: Okay. It's been moved by Slaton.

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: Succeeded by Taylor to adopt Option 2.

Any further discussion?

All right. Hearing none.

All in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed?

Motion carries.

Thank you.

Oh, Ms. Lum. I'm sorry.

DEPUTY EXECUTIVE OFFICER LUM: Thank you, Mr. Chair. I just wanted to share our appreciation for the discussion and the dialogue that has occurred today. And just as a reminder, when we presented the CEM report in

October, we did share with the various committees that periodically we would be bringing items such as this and other pieces of legislation or non-legislative items for consideration, as they do increase the complexity of the system.

And so this is one of those items, and it's a very difficult decision to make. However, I do appreciate all the feedback and the comments with regards to the manner in which we do serve our members.

And so just as reminder, you will see other items that come forward to the Committee, whether it's here or ore Pension and Health Benefits Committee that are really aimed at complexity. And sometimes, there's going to be a very difficult choice, between cost and service and complexity.

So again, I just wanted to remind you of that, and to thank you for the discussion today.

CHAIRPERSON COSTIGAN: Ms. Lum, and thank you. I mean, I'd encourage you to continue to bring it. I mean, the goal is to reduce complexity -- the complex nature of the system.

And without having these dialogues and discussions in the work that Jan and Anthony have done, we'll further it. I mean, so this is great work. It shouldn't be taken which way the Committee went. But, you know, again fantastic work. And I also want to thank Ms. Johnson and Mr. Lennox for their comments and it looks as though the engagement between your folks and them, we're seeing an increase. That's a benefit of these discussions.

CHAIRPERSON COSTIGAN: All right. So we're going to go onto Item 7b. But, Scott, before we begin, is it a 1-hour discussion, a 30-minute discussion, or a two-minute discussion?

All right. I think what we're going to do is break for lunch. It's 12:42. We could -- yeah, why don't -- if it's okay with the Committee, could we come back at 1:15? Is that enough time?

So we're going to just recess until 1:15 and then we'll come back and we will take up our Chief Actuary with Item 7.

Thank you all.

(Off record: 12:43 p.m.)

(Thereupon a lunch break was taken.)

A F T E R N O O N S E S S I O N

(On record: 1:16 p.m.)

CHAIRPERSON COSTIGAN: Okay. All right. Good afternoon. We're going to reconvene the Finance and Administration Committee.

We're going move to on to Item 7a. We're going to hear from our Chief Actuary.

Scott.

(Thereupon an overhead presentation was presented as follows.)

CHIEF ACTUARY TERANDO: Good afternoon, Mr. Chair, Members of the Committee. Scott Terando, CalPERS team member.

Item 7a is an action item that goes over the review of the actuarial assumptions and the selection of the discount rate. Yesterday, the Investment Committee made a decision in the ALM process on the asset allocation. Today, we're going to continue the other half of that ALM process where we look at the discount rate selection, as well as the adoption of the economic and demographic assumptions.

At this point, I'll pass it along to Randy Dziubek who will run through some of our analysis, as well as the recommendations that we have.

DEPUTY CHIEF ACTUARY DZIUBEK: Good afternoon.

Randy Dziubek, CalPERS actuarial team. As Scott said, 7a is an action item. We're going to be asking for approval of our proposed actuarial assumptions, both demographic and economic, as a result of an extensive analysis of the assumptions and a full experience study. These assumptions would be effective for the June 30, 2017 actuarial valuations, with the exception of a 1-year delay for the schools plan on just the economic assumptions that are being recommended.

Okay. My slide is not advancing.

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DEPUTY CHIEF ACTUARY DZIUBEK: There we go.

So as you probably recall in November, we brought most of these proposed assumption changes to you as an information item, all of them in fact, except the discount rate, because at the time we didn't know which portfolio the Investment Committee would recommend. We now know that, and so we will be including a discussion of the discount rate today.

We don't want to duplicate the discussion from November with regard to the assumptions other than the discount rate. So what we've prepared is a few slides that just give a nice summary and recap of how each of the individual assumption changes are expected to impact different employee groups.

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DEPUTY CHIEF ACTUARY DZIUBEK: And I think the slides are fairly self-explanatory, but the downward arrows would indicate that the proposed change is expected to decrease the normal cost for that group. An up arrow indicates an expected increase. And then the net result, with all the assumption changes combined, is shown in the right-hand column.

So a couple points about some of these assumptions. First of all, with regard to mortality, you may remember from the November discussion that we are recommending some changes to our mortally assumption, but they're generally very minor in terms how far they will impact costs going forward.

You can see some up arrows, some down arrows. Of course, the arrows don't indicate the magnitude. But with regard to mortality, those are all very small impacts.

Now, the reason we think that our mortality change this year is so small is that for the first time during the last experience study, we adopted not only new mortality rates, but also an assumption for future improvement in mortality rates. And so this year, we did see improvement in mortality over the last four years, but we had already anticipated some improvement in our existing rates. So that's why our new proposal is very close to what the rates were that we were using previously.

With regard to terminations, we saw a pretty consistent trend of seeing fewer terminations than our assumptions would have predicted. And so by changing our assumptions to more accurately reflect that, that will drive some small increases in costs going forward.

The less chance somebody has of terminating, the greater their chances of obviously reaching retirement where the higher cost benefits are.

Salary increases, for the most part, ended up pretty close to what our assumptions would have predicted. There were a couple groups where we saw slightly higher than expected salary increases, but many of the groups the increases came out very close to our assumptions.

Service retirement was a bit of mixed bag for some of the groups. We saw fewer retirements than we expected. People delaying retirement to later ages. For example, the State miscellaneous group, schools group. So our changes are to reduce retirement rates and predict later retirements, which is having a bit of a cost decrease on the plans results. But there a couple groups, State CHP, State POFF, where we actually aw more retirements than we expected. And so the effect is going to be the opposite and slightly increase costs.

Disability retirements, we saw pretty consistently fewer disability retirements than were expected. And so our proposed assumptions will reflect that and reduce costs somewhat. And with regard to inflation, as the heading of table says, all of these assumptions, we don't have any reflection here of any change to the discount rate. That will come on the slides to come.

So for inflation here, we are just talking about the impact due to how our inflation assumption will affect projected cost of living increases, salary increases. And because we're recommending a decrease of 25 basis points, that's going to have a downward effect on contributions going forward.

And as you can see, the net results, there's only one of these groups that's over a percent, and that's the State industrial group, and that's primarily because they're one group that didn't see the lower numbers of terminations as the others did. So all of the other changes are all in the downward direction, and so they're getting a -- about a one percent decrease in normal cost. The other are all up or down, but within a half percent.

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DEPUTY CHIEF ACTUARY DZIUBEK: And then the next two slides goes over the same information but for public agency miscellaneous plans on slide 5.

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DEPUTY CHIEF ACTUARY DZIUBEK: Public agency, safety plans on slide 6.

And again, pretty much all the same information and you can see the net results in all of these cases is less than a half percent.

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DEPUTY CHIEF ACTUARY DZIUBEK: So something else that it's important to look at when we're changing actuarial assumptions is the impact on the PEPRA normal cost. Because as we all know, the law requires that PEPRA members are required to pay half of the PEPRA normal cost. So the results we saw in the previous slides was for the total normal cost, classic and PEPRA members combined. If we look at just the PEPRA normal cost, we're again seeing generally very small changes in the PEPRA normal costs, either positive or negative, ranging from minus 1 percent to a positive 0.1 percent.

So these changes on their own are not expected to result in any increases or decreases in the PEPRA member contribution rates. Now, the discount rate change is much more significant in terms of the normal cost changes. Phasing into the 7 percent discount rate, if that is, in fact, what is approved would likely result in some increases to PEPRA member rates.

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DEPUTY CHIEF ACTUARY DZIUBEK: One of the assumptions that we didn't really touch on in November, we wanted to be sure to have a slide this month, is on the mortality contingency load. And this is a load that we use only for plans that are moving into our Terminated Agency Pool.

And when that happens, the Actuarial Office performs a termination valuation as of the termination date, and determines the termination liabilities using all of the normal actuarial assumptions, except for the discount rate. And then we add this load on the chance that even though we're using our best guess for mortality experience, there's also a chance that people will out live that assumption.

And unlike public agency active plans, where when that happens, it's just an actuarial loss, and we amortize it and we slightly increase the agency's contributions, we don't have that ability once a plan is in the Terminated Agency Pool.

So we have historically had this load to protect us against, the possibility of people living longer than our mortally assumption.

Now, because we have started to build in future improvements in our mortality assumption, and we've gotten 2 cycles of looking at this now, we felt it was appropriate to lower that contingency load from 7 percent to 5 percent. So this will only affect plans going into the TAP and will result in slightly lower termination liabilities for those plans.

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DEPUTY CHIEF ACTUARY DZIUBEK: Okay. So let's move into the discount rate assumption.

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DEPUTY CHIEF ACTUARY DZIUBEK: When we put this presentation together -- yes, sorry.

COMMITTEE MEMBER JELINCIC: I have a couple of questions on what we've covered so far. And believe me, I'll have some on the discount rate. But the mortality load, reducing it from 7 to 5, I understand that if we've built improved mortality into the assumption, but I -- I don't have the PERL memorized, but isn't that 7 percent currently in statute.

DEPUTY CHIEF ACTUARY DZIUBEK: The contingency load is in the statute. I didn't think it specified 7 percent. Maybe Scott can speak to that.

CHIEF ACTUARY TERANDO: I didn't it specifically mentioned 7 percent either. We could take a look at that.

COMMITTEE MEMBER JELINCIC: Okay. If it does, then I assume you're going to come back with a legislative change.

The other question I have is about the inflation assumption. Every central bank in the world is trying to reignite inflation. We are -- so we are betting that over the next 60 years, because it's a 60-year assumption, that they're going to fail. And I've spent enough time in the investment business to know that betting against the Fed and the rest of the world banks is probably not a good idea.

I've had a conversation, and, you know, part of the assumption is, well, we've been in this low inflation environment for a while now, but I also remember Paul Volcker, and as an industry we have a problem with an anchor bias. That which is true today will always be true.

So just because we're currently in a low inflation environment, I'm not sure we want to assume it's going to continue for 60 years, especially given that the world bank -- the central banks around the world have said we want more inflation. So what's really your rationale for saying, where we are today is going to continue?

DEPUTY CHIEF ACTUARY DZIUBEK: That's a good question. First of all, let's be clear. And I think we probably all clear -- are clear that we're not assuming that inflation is going to decrease from where we are today. We are looking at our current inflation assumption of 2.75, which was set 4 years ago. And we are looking at the available information, and saying that we think 2 and a half percent is better going forward.

You know, we would all agree that inflation is increasing slightly over the recent years, and the Fed has been increasing their rates, and perhaps are likely to continue to do that next year.

We're currently at around 2 percent. The last few years have had seen inflation of less than 2 percent. And so our 2 and a half percent proposal is very much based on the same type of logic we use for the discount rate, where we're looking at it in both short-term and long term, and taking an average of those two.

So we do believe inflation will be increasing from where we are today, and we see that happening. It's just under 2 percent -- or just around 2 percent, and certainly we think that that will continue.

As far as our long-term assumption, we're basing some of that on what we hear from our investment advisors, what we see in the Social Security trustee's annual report, where they predict long-term inflation every year. The 2017 report predicted 2.6 long term. And so based on those kinds of higher long-term assumptions with the lower short-term, we ended up at 2 and a half.

COMMITTEE MEMBER JELINCIC: Well, except we've got a long, long history that says on average it runs close to 3. And so we're basically betting that the central banks of the world can't get the inflation to where we're not to that long-term average. I mean currently they've got lower targets, that I will tell you as they hit that target, they're going to raise the target.

So how -- you know, so I'm just not -- I mean, it will be what it will be. And we can rest assured that it will not be 2 and a half, and it will not be 2.75, but I'd like to hear more confidence on why we ought to assume that it -- you know, that 2.75 is too high?

CHIEF ACTUARY TERANDO: I mean, if you take a look at -- if you look at the 5, 10, 15, 20, even up to the 30-year average, the average has been under 30 -- or it's been under 2 and a half. So not only has it been you know, short term, but the long term -- relatively long term, for the last 30 years, inflation has been low.

You also take a look at, you know, as Randy mentioned, current inflation, even if it goes up a half a percent, will get up to where we are saying inflation should be at 2 and a half. We're starting at a higher -- we've -- we're at a higher position right now, an so we're kind of bringing it -- our assumption in line with where the Fed is targeting it, along with the Social Security administration.

And keep in mind, you know, we review these assumptions every 4 years. So it's not like we're going to lock in 2 and a half and we're never going to look at it again for 10, 20 years. We review this every 4 years. And again, we have a mid-cycle review. So it's not like we are locked into a particular assumption. But right now, from what we see, we see it as being the most reasonable assumption on the inflation side.

COMMITTEE MEMBER JELINCIC: Okay.

DEPUTY CHIEF ACTUARY DZIUBEK: Recognizing reasonable and intelligent people can disagree on this assumption and any assumption.

CHIEF FINANCIAL OFFICER ASUBONTEN: Mr. Jelincic, Charles Asubonten, CalPERS CFO. As you know, there's always a lag from the Feds, from the central banks. So as they're saying, it will take some time. And of course, this is not the end of it. We'll get time to look at it again.

COMMITTEE MEMBER JELINCIC: Okay. May Paul Volcker have Mercy on your soul. Thank you.

CHAIRPERSON COSTIGAN: Well, I mean, Mr. Jelincic, I think you raise a good point. But if you look at some of the data that came out of the Fed's meeting last week, they're still projecting, at least for the next 10 years Inflation under 2.6 percent. I mean, I think one of the things -- and I know this is probably more of a political policy discussion, is Americans have gotten used to very low inflation. There's been a paradigm shift in the last 10 or 15 years. And you see that every time there's pressure to raise interest rates, you get the realtors and others coming back saying we're going to see a decline in housing markets.

And so I think you're right, when you look at it historically. The question is 10 years ago, 5 years ago when folks were getting loans, who would of thought in 2017 you'd still be borrowing money at 2 and a half percent.

I can assure you in 2008 no one assumed that. And so I think it's a great point, but we will come back and revisiting this. I mean, I was just looking at the Feds out of Cleveland are projecting, at least through 2022, a 2.5 percent.

And so it looks like we're somewhere in the targeted. And quickly reading this latest report, running out till 2060, no one seems to see significant, including the Central Bank, is that U.S. CPI is going to be between 2 and 2.7 and average around 2.3 through '18. And then going forward through 2022, 2.3.

So, I mean, it's a guess. I mean, again as I said In Investment Committee, I wish I had bought Tesla and couple other things before, so well points.

Anything on this item? I'm sorry, on the measure of inflation?

DEPUTY CHIEF ACTUARY DZIUBEK: Nothing from us.

CHAIRPERSON COSTIGAN: Unless -- and our economist is not here, right? Okay -- from investments.

Anything else, Mr. Jelincic, on that item?

COMMITTEE MEMBER JELINCIC: No.

CHAIRPERSON COSTIGAN: All right. Discount rate.

DEPUTY CHIEF ACTUARY DZIUBEK: Sure. So moving on to discount rate. We wanted to mention that, of course, the discount rate is made up of two components, inflation and our real return assumption. We've just had a good discussion on inflation, so I won't continue that, other than to say, that if we -- if you approve the current 7 percent discount rate recommendation, which is on a phased-in schedule, we would recommend that we also phase in the change in the inflation assumption, just to be consistent with that and maintain level costs over the next few years.

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DEPUTY CHIEF ACTUARY DZIUBEK: So again, when we put this material together, we didn't know which of the portfolios would be recommended by the Investment Committee. We now know that they have selected Portfolio C. So actually some of this information it's been talked about in a lot of previous meetings.

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DEPUTY CHIEF ACTUARY DZIUBEK: We will just say that given that Portfolio C is roughly maintaining the portfolio that we have now, we are recommending that we continue with the discount rate decisions that the Board made in December of 2016, which is to drop to 7.25 for the 2015 valuations, and then 7 percent for the 6/30/18 valuations.

Now, the next slide has some cost information.

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DEPUTY CHIEF ACTUARY DZIUBEK: Again, this was primarily to show you costs or savings if something other than Portfolio C was selected. The base that we started with was Portfolio C and all the new demographic assumptions. And so -- but on the chance that you would -- or the Investment Committee would have picked one of the other portfolios, we wanted to give some information with regard to how much that would increase or decrease costs.

So there really is no change in costs from what have been previously communicated to the Committee members to our agencies on the 7 percent.

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DEPUTY CHIEF ACTUARY DZIUBEK: So as I indicated, if these are approved -- yes --

CHAIRPERSON COSTIGAN: I'm sorry, I thought you were pushing your microphone, Mr. Jelincic. No?

COMMITTEE MEMBER JELINCIC: No

CHAIRPERSON COSTIGAN: Okay. Sorry.

DEPUTY CHIEF ACTUARY DZIUBEK: If these assumptions are approved, they would be effective for the June 30, 2017 valuations. Other than, as I mentioned, there will a 1-year lag on the economic assumptions for the schools plan. These new assumptions will also immediately be used for benefit option factors or service purchase calculations.

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DEPUTY CHIEF ACTUARY DZIUBEK: So with that, we're happy to take another other questions.

CHAIRPERSON COSTIGAN: Okay. I see -- Mr. Jelincic, you might want to push your microphone.

I see no questions, but Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Okay. I -- yesterday, we listened to the employers tell us the most important thing is that we have the money to pay the benefits. And the -- I also encouraged us to take more risk. And the response is we can't take more risk, because we're only 68 percent funded.

Although, quite frankly, if we raise the discount rate to 10, suddenly we're fully funded or maybe it's 12. I mean, the truth of the matter is we owe what we owe. We don't know what it is. We're going to write an unknown number of checks, in an unknown amount, to unknown people, for an unknown period of time.

Now, we've got some actuaries who are pretty smart, and they take advantage of the law of large numbers, and say this is our best guess on what we owe.

We look at our assets, and, you know, one would think, well, really know what we own. But if you look at real estate, which is 10 percent of our portfolio, it's based on appraisals with at least a quarter lag. I will point out that, you know, in '07, '08 real estate values were based on appraisals. They were people's best guess. In '09, people said what were they smoking? So we've got an uncertainty in that asset class.

We've got 8 percent of our portfolio in private equity. And when we look at the realized volatility in that portfolio, everybody says, well, that's nuts, it's just -- it doesn't make any sense, which is really kind of proof that we don't really know what the value of those portfolios are.

Much of the value is based on the estimate of the general partner, who gets paid in part based on the Assets under management. So his bias is not to low-ball it. So we've got some doubts on the liability -- or the asset side as well.

We really need to pay the benefit. And quite frankly, if we -- we can't take more risk because of the unfunded liability, then we should not adopt a program that, even if it performs as expected, makes us more unfunded 10 years from now, than it is today.

That's not prudent, it's not reasonable, and it's not fiduciarily sound. We adopted a portfolio that has a expected return over the next 10 years of 6.1. We do a regression to the mean to make it get up to 7. And I've looked at the formula, and, you know, we kind of tweak the formula to get where we want to get.

So if we really want to pay the benefits, if we are really concerned about not increasing the unfunded liability, then we should adopt a discount rate of 6.25, and that's what I move.

CHAIRPERSON COSTIGAN: All right. We have a motion before us to adopt a discount rate of 6.25.

I will just say, since I cannot second the motion, I'm not going to disagree with what Mr. Jelincic has been saying. I've been advocating for the last couple years for a lower discount rate. I know why we settled at 7. I think the concerns you've raised are there.

But given that, does anybody want to speak on the motion?

No I'm asking. That's -- I mean --

VICE CHAIRPERSON TAYLOR: There has to be a second.

CHAIRPERSON COSTIGAN: That's right. There's no second?

Okay. Okay. Now, that's why I've got two folks.

All right, Mr. Jelincic, your motion fails for lack of a second.

COMMITTEE MEMBER JELINCIC: I am shocked.

CHAIRPERSON COSTIGAN: ALl right. Thank you, Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: I absolutely didn't expect that to come.

(Laughter.)

CHAIRPERSON COSTIGAN: Thank you, Mr. Jelincic.

Mr. Jones.

COMMITTEE MEMBER JONES: Yeah. Thank you Mr. Chair. In agenda Item 7a, review of actuarial assumptions and discount rate selection, I move that we adopt recommendation 1, 2, and 3.

CHAIRPERSON COSTIGAN: Okay. We have a motion.

COMMITTEE MEMBER JELINCIC: You need to put a number in 2.

CHAIRPERSON COSTIGAN: I know. Hang on a second.

So Mr. Jones has moved that we adopt Item 7a as outlined in the recommendations, items 1, 2, and 3.

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: It's been seconded by Taylor.

And, Ms. Taylor, do you want to speak on the motion or speak on the item.

VICE CHAIRPERSON TAYLOR: I'm going to speak on the item.

CHAIRPERSON COSTIGAN: Speak on the item. Okay.

Okay. Hang on a second. Mr. Jelincic, push your microphone.

VICE CHAIRPERSON TAYLOR: I was -- why are we doing that?

CHAIRPERSON COSTIGAN: Hang on a second. Let me just -- he's got a point of order.

Yes, Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: Two needs a number in it. It ought to be 7.

CHAIRPERSON COSTIGAN: Sorry, you're correct.

COMMITTEE MEMBER JELINCIC: But it needs a number.

CHAIRPERSON COSTIGAN: All right. Approve the discount rate.

COMMITTEE MEMBER JONES: I will modify my motion to include 7 percent --

CHAIRPERSON COSTIGAN: Hang on a second, Mr. Jones.

COMMITTEE MEMBER JONES: -- discount rate.

VICE CHAIRPERSON TAYLOR: Second that.

CHAIRPERSON COSTIGAN: All right. Ms. Taylor.

VICE CHAIRPERSON TAYLOR: So I just want to say that while I understand, sort of, J.J.'s recommendation and concern, the long-term assumptions are much better. And so I don't agree that it's not within our fiduciary duty to adopt the 7 percent rate. And I think that was a stretch.

So I will say, however, that the -- there are many other factors that we have to consider besides just the rate. And one of that -- much of that is whether or not we put the fund in a unfunded liability status that we can't recover from, if we lower the rate that low. So there are many, many reasons to stick with the 7 percent, just as there are many reasons to go down to 6.1 percent. I just want to voice my support for 7 percent, as I had said before in Investment Committee. I wasn't on board for the 7 percent to begin with.

But since we are here, I am willing to stay at the 7 percent, and have it instituted within the next 3 years.

Thank you.

CHAIRPERSON COSTIGAN: Thank you, Madam Vice Chair.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: I will just again point out that it's not reasonable or prudent to say we can't take more risk because we are underfunded, and adopt a program that makes sure that even if it operates as expected, the dollar amount of our unfunded status increase.

Thank you.

CHAIRPERSON COSTIGAN: Ms. Paquin.

ACTING COMMITTEE MEMBER PAQUIN: Thank you, Mr. Chair.

Thank you very much for all the work through the ALM process and for this final report. I had one question on the materials. In the Cheiron report talked about mortality projections and recommended looking at generational and benefits-weighted approaches for the next experience study. Is that something that you are working on?

DEPUTY CHIEF ACTUARY DZIUBEK: Yeah. As far as the generational mortality -- and for those who might not be familiar with that term, right now our approach is to build in a certain number of years of mortality improvement. And we're using 15 years, and we're building that into our base table and just applying it now.

On a generational approach, your computer software would be smart enough to year by year build in a little of improvement each year out into the future. We are updating our software as we speak. And by the time we come to you with the next experience study, we'll be able to use generational mortality, and we will do that.

Now, I will say though that the 15 years that we selected was selected to approximate what we would get as results if we used fully generational mortality.

On the benefits weighting, we think that's an interesting topic of conversation. There's been a lot of research done lately into that topic. I think -- I think most people would agree there is a relationship between income and mortality. The question is for us, and our population, given that they have fairly high access to good health care, the pays are perhaps not as disparate as other plans, how do we reflect that into our mortality assumption? We will continue to look at that and we appreciate Cheiron's suggestion to do that.

ACTING COMMITTEE MEMBER PAQUIN: Great. Thank you.

CHAIRPERSON COSTIGAN: Okay. Before I call on Mr. Jelincic, I just want to say just a couple things in response to our fiduciary obligation. This is a process that we've worked on for over 2 years, both through ALM, working on the discount rate. The Investment Committee, Chaired by Mr. Jones, has spent a considerable amount of time along with the Investment Office designing the portfolio, and how we arrived at what we did on Monday.

I want to give credit to our Chief Actuary and his team for the work that you have done. We have spent well over a year just to arrive to where we are today. I know our outside consultants, our advisors, our Committee staff, our CFO, our CEO are all in agreement that should the Committee adopt the 7 percent, that is the prudent and reasonable standard for the system at this time.

I know that reasonable minds, Mr. Jelincic, can disagree. And as I said, there are times I have -- I think a more conservative portfolio, but I believe, as for this Committee that the 7 percent rate that this -- that we have adopted or we're going to is prudent and reasonable. And I know this is not -- again not the end of this discussion, because we will continue to evaluate.

As we raised in the Investment Committee with Mr.

Jones yesterday, about whether we overperform or underperform on it. So I just want it not to leave addressed, because we throw the term fiduciary around quite a bit. And as you know, Mr. Jelincic, like you, we take that very seriously.

With that, Mr. Jelincic, I will call on you right now, sir.

COMMITTEE MEMBER JELINCIC: Okay. I would just like to split the question, because I would actually like to vote yes on 1 and 3, and vote no on 2.

CHAIRPERSON COSTIGAN: All right. So in consultation with my Vice Chair, I don't believe we can split the question the way you want, because 1 is predicated upon adoption of number 2. So your motion actually would not work, because you're voting -- because if you read it, the new actuarial assumptions are presented. You were correct to point, and 2, that we needed to adopt a rate.

And I understand the concern you have, sir, is that you want a lower discount rate. And by voting on the entire motion -- or voting against the entire motion, you'd be voting against the items that you agree with, is that correct?

COMMITTEE MEMBER JELINCIC: Yes.

CHAIRPERSON COSTIGAN: So, Mr. Jacobs --

COMMITTEE MEMBER JELINCIC: Can we vote on 2 first?

CHAIRPERSON COSTIGAN: Well, let me ask our counsel from just a position standpoint. I just want to make sure we get the motion correct.

So, Mr. Jacobs, what Mr. Jelincic is proposing is to have items 1 and 3 voted on, of which I believe he would be a yes vote. That we would then adopt item 2, which is to approve the discount rate at 7 percent, where we currently are, of which he would be a no vote.

So can that question be split? Ms. Taylor, your help here would be --

GENERAL COUNSEL JACOBS: Were you waiting for me or --

CHAIRPERSON COSTIGAN: Go ahead.

GENERAL COUNSEL JACOBS: Yes, it can be split that way.

CHAIRPERSON COSTIGAN: All right. So you believe the question can be split?

GENERAL COUNSEL JACOBS: Yes.

CHAIRPERSON COSTIGAN: Hang on one second.

We have a question, Mr. Jacobs.

Ms. Taylor.

VICE CHAIRPERSON TAYLOR: So in my reading of it, it looks like number 1 specifically relies on number 2, because it says contribution rates due to changes in assumptions for the State and schools will be impacted at FY 2018 and '19, and contribution rates for public agencies will be impacted in 2019 and '20.

So it relies on passing number 2 for that to be true, if I'm correct.

GENERAL COUNSEL JACOBS: What's our actuary's view on that?

(Laughter.)

CHIEF ACTUARY TERANDO: Well, if you look at number 1, we talk about the assumptions presented in the experience study, and the discount rate was actually not part of the experience study. So from that perspective, we can -- it makes sense that we could split the items.

VICE CHAIRPERSON TAYLOR: Okay. And then my only other question is because the 7 percent was agreed to prior to this, right, which is where number 1 comes from, because we already had a time frame within which we were supposed to implement that, and that's what number 1 is.

So I think if we vote on number 1 without number 2, we are putting ourselves at risk.

CHAIRPERSON COSTIGAN: We vote in number 2 first. So we're going to revise the motion.

VICE CHAIRPERSON TAYLOR: There you go.

CHAIRPERSON COSTIGAN: Mr. Jones.

COMMITTEE MEMBER JONES: Yes. I would like to modify my motion.

CHAIRPERSON COSTIGAN: Yes, sir.

COMMITTEE MEMBER JONES: Okay. The first part of the -- the first motion in Agenda Item 7a, review of actuarial assumptions and discount rate, I move we adopt recommendations -- recommendation number 2.

VICE CHAIRPERSON TAYLOR: Second.

CHAIRPERSON COSTIGAN: Which would be to approve the discount rate --

COMMITTEE MEMBER JONES: At 7 percent.

VICE CHAIRPERSON TAYLOR: At 7 percent.

CHAIRPERSON COSTIGAN: -- at 7 percent.

It has been moved by Jones. Seconded by?

VICE CHAIRPERSON TAYLOR: Me.

CHAIRPERSON COSTIGAN: Taylor.

Any further discussion?

Hearing none.

All in favor?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed?

(No.)

COMMITTEE MEMBER JELINCIC: Record my no vote.

CHAIRPERSON COSTIGAN: So number two.

COMMITTEE MEMBER JONES: I move in Agenda Item 7a review of actuarial assumptions and discount rate selection, I move that we adopt Recommendations 1 and 3.

CHAIRPERSON COSTIGAN: It's been moved by --

VICE CHAIRPERSON TAYLOR: I'll second it.

I seconded it.

CHAIRPERSON COSTIGAN: Seconded by Taylor.

VICE CHAIRPERSON TAYLOR: Yeah, because I originally seconded it.

CHAIRPERSON COSTIGAN: Any further discussion?

Hearing none.

All in support?

(Ayes.)

CHAIRPERSON COSTIGAN: Opposed?

Motion carries. Thank you. Thank you, Mr. Jacobs. You earned your pay today.

All right. Anything else on that item?

All right. Item 8a, which is an information agenda item.

(Thereupon an overhead presentation was presented as follows.)

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Good afternoon, Arnita Paige CalPERS team member. The purpose of our quarterly report on participating employers is to keep you updated on our employer population as it relates to termination and collection activity.

Today's report includes the Committee's direction provided in September to update headers on the agencies with no active members report, and provide the final benefit reduction rates for Trinity County Waterworks District and Niland Sanitary District.

Let me grab the --

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: On slide 2, we provide Trinity Waterworks District's final benefit reduction rate is 68.55 percent for two retirees. This reduction became effective on their first pay period in December 2017.

We did hear from Trinity's board. And they stated this they plan to pay the members directly for the reduction amounts. So this contract was a total of five members, the two retirees and then three additional members that are eligible for benefits in the future.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: On slide 3, we provided Niland Sanitary District's final benefit reduction which is 92.49 percent. This reduction represents -- is for one retiree that becomes effective in January 2018.

The reduction amount for the one PEPRA member is

100 percent. So the total for this total con -- total members in this contract is five.

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CHAIRPERSON COSTIGAN: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: You say total is five. Does that include the PEPRA?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yes. And so there's one member that when you subtract the one member who's not totally vested.

COMMITTEE MEMBER JELINCIC: Okay. So there are three vested --

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

COMMITTEE MEMBER JELINCIC: -- Inactives.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

COMMITTEE MEMBER JELINCIC: And I was going to make the point later, but while I have it, I might as well. When you do these reports in the future, I think it might be worthwhile to point out not only for the inactives, how many vested inactives there are, just so it has a context.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you.

COMMITTEE MEMBER JELINCIC: Thank you.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Out joint powers of authority summary report provides information on the number of contracts we have with JPAs, and whether their JPA agreements include language obligating their member agencies to help the JPA with their pension liabilities. Since the last time, we reported in September, we reviewed an additional 14 agreements to bring our total to 149. And to date, in total, we have 162 contracts with joint powers of authority.

The number of agreements that include liability language for member agencies remain at 10, and we increase the member agencies identified as a State by one to the -- to 6.

CHAIRPERSON COSTIGAN: Can I ask you a question on that?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Sure.

CHAIRPERSON COSTIGAN: So again, I appreciate this data. I guess the one data point I'd have in the middle column, where it says number of agencies with financial liability obligations reverting to member agencies, I want to -- at one point, we had a discussion. The concern was whether or not the JPA had its own independent revenue source, because East San Gabriel was a contractual -- the revenue was based upon a contract.

At some point, can we break this down and determine -- because I know you have in here fair and exposition -- pollution control districts, which have the authority to raise fees, mosquito abatement districts things of that nature.

Because I think we need one more column, because what we were trying to get to is the addressing of the East San Gabriel issue, which was again -- it was a contractual issue -- the revenue was contractual. It wasn't based upon an independent revenue source.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

CHAIRPERSON COSTIGAN: So again, this is great data on it, and appreciate it. It seems to be getting larger than we thought it was. And right now, we have, what is that, 8 percent actually revert back to the parent agency -- the creation agency.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

CHAIRPERSON COSTIGAN: And so we probably want to break that 149 down and see who would be at risk if it's just contractual versus revenue, because I think that's -- Ms. Taylor, if we were correct, that was our concern was what was the revenue? How would those members -- it's not so much that they're JPA, it was what would happen to their revenue source. And if they're a -- like a pollution control agency, or a utility district, they have the ability to raise revenues and fees as opposed to the contract. So just something down the road.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you. Point taken. We can do that.

CHAIRPERSON COSTIGAN: Ms. Paquin.

ACTING COMMITTEE MEMBER PAQUIN: Thank you, Mr. Chair. I had a question on this slide. So you identify nine in the other category as having liability revert to member agencies. And of the nine, does that include the six that were identified as having a State as members?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: They're separate.

ACTING COMMITTEE MEMBER PAQUIN: So it's a total of 14 then?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

ACTING COMMITTEE MEMBER PAQUIN: Okay. Thank you.

CHAIRPERSON COSTIGAN: Yes. Please continue.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: This report is our update on agencies with no active member population. We did change the report title based on your advice to improve clarity, and we also changed the reporting column. In our last update, we reported 59 agencies. Since then, two -- we've had two voluntary terminations, and one involuntary termination. It was completed and removed from the report.

We added four new cases, to bring our total to 60. These cases are current on their pension obligations, and we are in communications -- we have communicated with all of them and continue to do so on a case-by-case basis.

And in our next four slides, we provide an update on each of the columns that were here.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: In terms of the dissolved cases, we have seven -- I mean, excuse me, we have five agencies who have decided to terminate. And we've sent them termination cost estimates. We have seven agencies who have required education on the termination process, who are still having internal discussions. And we are working with one agency to merge their contract with another agency.

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CHAIRPERSON COSTIGAN: I'm sorry. Ms. Taylor.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yes.

VICE CHAIRPERSON TAYLOR: I'm sorry to interrupt. This is a good report. I just want to know these -- I'm glad we're seeing this now ahead of time. How close are these agencies, either in the termination -- and is this inclusive of Niland and Trinity, first of all?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: No, those were the ones that were removed from the report.

VICE CHAIRPERSON TAYLOR: Okay. So these five terminations are coming up?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

VICE CHAIRPERSON TAYLOR: Okay. And then we have a possible seven more?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Well, they're discussing termination. Right now, they've dissolved, so the member agency is looking at --

VICE CHAIRPERSON TAYLOR: All seven of them have dissolved?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

VICE CHAIRPERSON TAYLOR: Okay. So they're not necessarily -- I'm trying to think of a nice way to word this through -- driven out through our costs.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF

PAIGE: Well, correct. I mean, they've dissolved for various reasons. The majority of the reasons is they've -- they're not longer performing those functions.

CHAIRPERSON COSTIGAN: Can I ask a -- I'm sorry. Can I just ask a clarification on what Ms. Taylor is racing? The title is dissolved 13 agencies, but we've got five that are in process --

VICE CHAIRPERSON TAYLOR: No. Yeah, five that are currently in process.

CHAIRPERSON COSTIGAN: -- and we have seven -- and seven that are potential?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

CHAIRPERSON COSTIGAN: So they're not dissolved yet.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Well, they are dissolved, but we're working with the member agency -- excuse me, the successor agency. They're looking at whether they can terminate the contract. So they're having internal discussions regarding that issue.

CHAIRPERSON COSTIGAN: Okay. So these seven agencies have already gone through termination?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Well, they're dissolved and they terminated from a ceased operation perspective.

VICE CHAIRPERSON TAYLOR: Are they paying?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yeah, we -- none of them owe money at this time, so their contract is current.

VICE CHAIRPERSON TAYLOR: Okay. But they will eventually end up in our Terminated Agency Pool.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: There's a strong chance of that.

VICE CHAIRPERSON TAYLOR: Even though they don't currently owe money.

Do you foresee the five terminated agencies or the seven potentials within the next few months terminating their payments?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Well, these agencies it's best they continue making payments -- I mean, the duration. Some say they have funds for the next few years. So I think there's varying responses to that.

I will say that the five agencies that -- out of the five -- the top five agencies, four of those agencies, when we look at their actuary reports, they're at a superfunded status at a hypothetical termination.

So that one remaining agency that we're working with, they do have some funds, and where having discussions with them in terms of how they're going to settle their termination costs.

VICE CHAIRPERSON TAYLOR: I'm not sure if we don't want this a little more specific maybe.

I'm wondering if maybe we could get a little more specific in term of -- I don't know if we want to do that in public session. That's up to you. Maybe we do it in closed session.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Okay.

VICE CHAIRPERSON TAYLOR: If we could get a little more specificity in the report.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Okay.

VICE CHAIRPERSON TAYLOR: Thank you.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you.

CHAIRPERSON COSTIGAN: Because I'm -- go ahead. Sorry.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Okay. In terms of our function mergers, basically we have two -- excuse me, we have two agencies that can -- we're working on merging with another existing contracting agency here at CalPERS. And then we have three agencies that are having internal discussions on terminating.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: In terms of our outsourcing category, our membership program requested and reviewed agreements from agencies who've outsourced, and service agreements. And we have a high percentage of those who have valid outsource agreements and we're continuing to monitor those. And then we have two members -- I mean, two agencies who have expressed interest in possibly terminating. And the remainder we're working with them as we receive information.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: In terms of the stopped reporting payroll issues, we have two members that we're looking at -- I mean, excuse me, two agencies that are potential terminations for compliance. And then we're waiting for additional responses from one, and we also need information from seven additional ones to continue our review.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: And that's it. And we'll move on to our terminations to provide you an update on those members who -- those agencies who have sent us their notice to --

of intent to terminate. California Redevelopment Association, who's been on this report, and Central Sierra Planning Council, that is the member agencies that I -- I mean, that agency is one that was part of our members with no active -- I mean, agencies with no active members. They're included in that five that I talked -- that's the agency that I'm working with.

CHAIRPERSON COSTIGAN: So just a question. On the California Redevelopment Association Foundation, that was a result of the elimination three years ago of the redevelopment agencies.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Correct.

CHAIRPERSON COSTIGAN: And it's my understanding that they're currently 100 percent funded.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Currently, correct. They're not in termination.

CHAIRPERSON COSTIGAN: But there are no additional payments coming, because there's no --

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Right, at this time.

CHAIRPERSON COSTIGAN: When will -- oh, they have several employees. When will we -- when we will -- when we will -- I can't speak. When will we see them?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF

PAIGE: Actually, we had conversations with them a few days ago. What they're doing is they're outreaching their sources to see if they can raise funds. And at that time they want to have a discussion with us and they plan to voluntary terminate after that.

CHAIRPERSON COSTIGAN: Okay. And then Central Sierra Planning Council?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yes, that's the agency that I referred to in the dissolved category, the fifth -- that is our fifth agency who we're working with to provide termination costs. And then we have a discussion on selling the total cost of the termination. And they're moving forward.

CHAIRPERSON COSTIGAN: And then you're going to get to Herald Fire Protection District?

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yes. So we'll go ahead and we'll move on to Herald Fire. Herald Fire, we just -- we just completed the termination valuation on them, and they received that information last month. We invoiced them on November 30th for the termination costs, and their bill is actually due on January 20th.

So they're not yet delinquent. We have been in discussions with them about the termination costs, and we plan to continue those discussions. We don't have a resolution at this point, but we are having discussions.

CHAIRPERSON COSTIGAN: All right. It's my understanding - and I appreciate you having conversations with the fire district - is there was a question over reports. We were keep -- we had the data. They didn't have the data about what was reporting. So just maybe in February just have an update on that, because --

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Absolutely.

CHAIRPERSON COSTIGAN: -- I know that the fire protection district has just -- it was just a paper -- paperwork issue in the past that we're trying to work through.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Yes, we'll do that.

CHAIRPERSON COSTIGAN: All right. Thank you.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Um-hmm.

This is our new collections report. And what we're doing here, we wanted to provide more transparency in terms of what our collection activity looks like. This quarter represents from September 1st to November 30th. And on the far left column, that represents all the types of payments that we collect. And on top, the header of the report provides the days delinquent, how we review them. And under the -- each column, the number of occurrences we have, and the number of cases resolved.

And we've actually also footnoted under the resolved the total amounts outstanding under each of those categories. And our message here is our delinquency is relatively low. We believe all the amounts on here are solvable, and we are working with these employers.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: And then last -- and then in terms of our legislative strategy, we'll continue to -- this was approved in November by the Board. We're continuing to pursue improving final -- excuse me, continuing to pursue shortening our voluntary time frame to terminate for our employers as well as improving member notification.

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PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: And then lastly, we plan to continue our discussions with the inactive agencies, pursue the legislative strategies. And we'll be back in February to provide a report to the Board.

And this concludes our presentation

CHAIRPERSON COSTIGAN: Thank you.

Mr. Jones.

COMMITTEE MEMBER JONES: Yeah. Thank you, Mr. Chair. I just wanted to thank you for an excellent report.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Oh, thank you.

CHAIRPERSON COSTIGAN: Yeah. Again, you guys have been doing a fantastic job from where we were 2 years. I mean, the information -- the feedback I'm getting just great work. And again providing the information early and available to those that are impacted on both sides is much appreciate.

So any further discussion on this item?

I have no -- Mr. Lennox, you're going to speak on 8b on the next item.

Okay. All right. Thank you.

PENSION CONTRACT & PREFUNDING PROGRAMS CHIEF PAIGE: Thank you.

CHAIRPERSON COSTIGAN: All right. On to 8b, health care administrative expenses.

And before you get started, Liana, I just want to acknowledge my Executive Officer from the State Personnel Board, Ms. Ambrose, sitting in the back. Good to have you here.

Good afternoon.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: Good afternoon, Mr. Chair and members of the Committee. Liana Bailey-Crimmins, CalPERS team member.

Today's health care administrative expense information item covers three points. The first is insight to the recent PEMHCA statute changes that affect two health care funds. Second is to highlight the findings from a recent impact assessment report requested by the legislature. And then lastly, based on the findings of the impact assessment, we want to emphasize here at CalPERS that at this time, CalPERS is not pursuing any changes to the method we currently perform in order to collect the administrative expenses.

Present with me today is Mr. Robert Jarzombek. He is the Chief of the Health Account Management Division. And he oversees the public billing and marketing group. And his team is actually the ones that perform this analysis, so it's -- it's prudent that he's the one that's presenting with me today.

And before we go into a lot of details, I'd like to give you some background on how CalPERS collects the administrative expenses. So we collect a total of $73 million annually to fund both direct and indirect expenses to run the $8.19 billion Health Care Program. Happy to report in 2018, we will increase this program to 9.3 billion on behalf of the 1.4 million total covered lives.

As you can see, administrative expenses account for less than 1 percent of the CalPERS Health Program. In fact, it's 0.8 percent, which is significantly lower than other large employers, and including other State employer purchasers, such as Covered California.

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CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: There are two health program funds that are used to collect the administrative expenses via the Contingency Reserve Fund, also as you can see on the slide is CRF. We collect approximately $30 million, which is an employer contribution model only.

The regulation allows CalPERS to collect up to 2 percent, but we have never gone anywhere close to that amount. In 2017, we collected from employers 0.0 -- 0.31 percent. And this current fiscal year, we are collecting 0.33 percent.

The Health Care Fund, also known as HCF, we collect $43 million via premiums, which is shared both between employers and employees. These costs are collected to support the administrative expenses, specifically for self-funded plans and flex-funded plans. And in 2017, this equated to approximately $4.68 per member per month.

Also, if there is any excess reserves collected, this amount may vary from year to year to ensure that we are not collecting more than what is needed. So with that, I'd like to now turn it over to Mr. Robert Jarzombek to give you more details on the analysis that was performed.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: All right. Thank you, Liana. Good afternoon, Mr. Chair, Committee members --

CHAIRPERSON COSTIGAN: Hang on a second. I'm sorry.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: In the analysis, when you're talking about the CRF administrative fee is billed at 0.32 percent of what?

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: Of the entire set of premiums.

COMMITTEE MEMBER JELINCIC: Of premiums.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: Yes.

COMMITTEE MEMBER JELINCIC: Okay. Thank you

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: Thank you.

CHAIRPERSON COSTIGAN: All right. Thank you. Sorry, sir.

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF

JARZOMBEK: Okay. Good afternoon, Mr. Chair, Committee member Rob Jarzombek CalPERS team member.

As Liana mentioned, I'll share some recent statutory changes, including a control language mandate for CalPERS to complete.

But before I begin, I'd like to point out that at this -- at the time this item was published online, we've added an additional analysis and that -- to Attachment 1. A revised Attachment 1 is available in the back and will be posted online at the conclusion of Board week.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: So as some of you may be aware, in the past couple of years, there were statutory changes that happened as part of the past two State Budget Acts.

Prior to July 2016, only the expenditure of monies deposited into the CRF for administrative expenses required appropriation approval through the annual State Budget Act.

In June 2016, as part of the 16-17 State Budget Act, expenditure from the HCF for admin expenses now also require this same administrative -- appropriation approval through the annual Budget Act as well.

This change was made late in the process and not through a policy bill. What this means for CalPERS is that the health teams must exclusively go through the State's budget change proposal process, if additional funding or positions are needed, and not through CalPERS own formal budget request process.

This change was strongly supported by the Department of Finance, and as such, DOF has requested improved transparency and efficiency in accordance with its new shared role with the legislature in overseeing the expenditure of funds in the HCF.

A second change came this year, and that was to lower the CRF's reserves for CalPERS operations from three months to 1 month. This means that if the State's budget is not approved timely, CalPERS will only have sufficient funding in reserve to pay up to one month of administrative expenses instead of three.

Please note this for CalPERS internal operational expenses related to health program only. This does not impact our ability to pay carriers.

The third change we'd like to talk about involves a requirement for CalPERS to conduct an employer and employee impact analysis, regarding administrative fees for the CalPERS Health Program. Department of Finance has expressed an interest in funding all of the CalPERS Health Program administrative expenses through the CRF, which is the employer only contribution model.

A requirement was added to this year's State Budget Act for CalPERS to report to the legislature the fiscal effect on the State, local government agencies, and their employees if all health benefit administrative costs were paid through the CRF and not through health premiums.

This report is required to be submitted by January 10th, and I'm here to present our analysis to you today. To develop this, we worked closely with the Department of Finance to validate methodology and assumptions used to fulfill this requirement.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: While DOF may gain increased transparency into how administrative fees are collected if this approach were to move forward. CalPERS is not pursuing this change. We are simply fulfilling the control language requirement.

And as required, we performed our impact analysis, and it's attached to this agenda item. To do this, we looked at the current CRF for collecting administrative fees, the current HCF method for collecting admin fees, and then what would happen if we were to use a proposed CRF-only method for collecting the same administrative fees.

When we began this effort, we wanted to use the most recent data available to us. And that was information from October of this year. So for this exercise, we're using the total covered lives information from that month, as well as the gross health insurance premiums from October as well, and then annualizing them so we can determine the annual fiscal impact on an employee as well as employers.

So as Liana mentioned, the CRF uses an administrative fee, which is applied to the gross health insurance premiums of each employer to cover -- for internal administrative expenses. For this exercise, we used a CRF admin rate of 0.32 percent, as this is the average of last fiscal year's rate of point 0.31 percent and the current fiscal year rate of 0.33 percent.

As shown on the summary page in Attachment 1, this generates approximately $28.5 million, which is close to the $30 million the CRF needs to generate to cover administrative expenses.

Then we looked at the HCF. Also as Liana shared, the HCF collects administrative fees via a per member per month method, which collected through premiums. For 2017, that rate was $4.68 for self-funded and flex-funded plans. This generates approximately $44.2 million, which it too is close to the $43 million the HCF needs to generate to cover administrative expenses. We then removed the per member per month fees from the gross health insurance premiums of each employer. So by doing this, a reduction in premiums can be shown.

Finally, into the revised premium amounts, we applied a CRF admin rate of 0.82 percent, as this is the amount needed to generate approximately $73 million to cover administrative expenses for the CalPERS Health Program.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Now to the employer impact. This approach would increase the administrative fees for our employers on average by approximately 150 percent. This results in an annual increase of administrative fees who are approximately $25.5 million to the State and $18.7 million to our public agency and school employers.

And as I mentioned, since the time this was first published, we've added an additional analysis to show the overall net impact to employers.

To determine the net impact employers, we first had to learn how the costs of premiums is being split between the employer and employee, as this is needed to gain insight on what employers are paying on the HCF side. So based on the data we have available to us, reported from employers through my|CalPERS, we learned that on average the State is paying 85 percent of premiums, and the State employee is paying 15 percent of premiums.

For public agencies and schools, the split is different. Public agency and school employers pay on average 31 percent of premiums, and their employers pay the -- employees pay the balance, or 69 percent of those premiums.

So to determine the net impact on employers, we removed the previous employer payments to the CRF, so what they're paying today. And then as well, we also remove the portions employers are paying towards the HCF, so what portions are praying of that $4.68.

Using this approach, we show an average annual net increase of $2.3 million to the State, which is about 6 percent more than they're paying today, and it shows an average annual net increase of $13.2 million to our public agency and school employers, which is a 75 percent increase compared to what they're paying today.

A breakdown of all agencies is in Attachment 1. Based on this information, we think the impacts to employers, and in particular to public agency and school employers, is moderate to significant and will not provide any new additional value.

As we know, many of our employers are already expressing their concerns with rising costs in the health care industry, as well as in their pension worlds. This would increase pressure on employers to find other alternatives to provide health benefits to their employees and retirees.

Additionally, the more financial impacts that are shifted to the employer, the less employers have available to them during labor negotiations.

Now, to the employee impact. To determine the employee impact, we use the same percentages regarding how much of premiums are paid by the employer versus the employee. We then took the 2017 per member per month rate of $4.68 multiplied it by 12 and then multiplied it by the percentage employees are paying of premiums, so 15 percent for State, 69 percent for public agencies and schools.

This results in an annual employees impact of a savings to the State employee of approximately $8 a year. For public agency or school employee, the average annual savings would be $39 a year. This information is also in Attachment 1.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: In addition to the employer and employee impacts, this change would have risk for the CalPERS Health Program as well. With increased cost to employers and a net increase of 75 percent to contracting agencies, CalPERS would lose our competitive advantage over brokers who are constantly working to sell benefits to our public agencies and schools.

Each year we have to work hard not to just bring on new agencies, but to simply retain the agencies we currently have. Losing employers would mean losing members, and that would reduce the 1.4 million total covered lives we have today. This would put at risk CalPERS leadership and market influence and holding the line health care premium increases as well as reduce our ability to bring change and innovation in this critical arena.

Finally, we would see an erosion in stakeholder confidence in our ability to deliver high quality affordable health care to members in a consistent and stable manner.

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HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Based on our analysis, the cost to employers is moderate to significant. We recommend not making any changes to the current methods used to collect administrative fees. The completed impact analysis will be delivered to the legislature as required on or before January 10th.

This concludes our presentation, and we're happy to answer any questions.

CHAIRPERSON COSTIGAN: All right. Thank you. Excellent presentation. I assume that you've been working with the Department of Finance and have expressed the concerns about the increases cost to them?

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Yes.

CHAIRPERSON COSTIGAN: All right. Mr. Jones.

COMMITTEE MEMBER JONES: Yeah. Thank you, Mr. Chair. The first question is on slide number 9, where you represent the 150 percent increase, 25 million for the State and 18.7 for public agencies. So once that money is collected who benefits from those resources, the State?

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Once that money is collected, that is just for CalPERS internal operational expenses. So there would be -- I'm not sure I understand the question.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: So, Mr. Jones, currently the administrative expenses totally is $73 million. Those are for direct. So the Health Program personnel and then indirect costs for like building expenses, and IT projects. So there's 73 million total that's needed.

So what you see on the first one is currently we collected in two means. One is a 0.33 percent, which is taken from the total health care premiums. And then for flex funding and for our self-funded, because there's more administrative cost for us, there's a $4.68 per member per month. What that is saying is it would shift and no longer be collected in premium, so we would actually have to have increase the 0.33 to be 0.82 to collect the full 73 million. And that would represent 150 percent increase.

But as Department of Finance and public agencies have asked is, well, what I'm already paying, so what's the offset. And so that is what the net that Robert was talking about.

COMMITTEE MEMBER JONES: Okay. So the State is not really impacted as much as these numbers would suggest then?

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: The State is impacted. This would be the total administrative fee impact to the State. So right now they're paying some of that money in premiums. This would have to -- they would -- they would not be paying it that way.

COMMITTEE MEMBER JONES: That's what --

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: The total -- by there is still an overall net impact to the State of 2.3 percent.

COMMITTEE MEMBER JONES: Sure. Sure. But it's a reduction though. No?

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: It's 2.3 million increase --

COMMITTEE MEMBER JONES: Okay. Thanks.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: -- for the State

CHAIRPERSON COSTIGAN: Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: This convoluted thing is a good argument against trailer bills. But isn't this already the law that we do this. We bring them both together?

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: The law -- the way the statute -- the statutes are written is that we have the CRF and HCF operate separately. So there's two funds there. This proposal is to basically not use the HCF anymore for -- to fund administrative expenses.

COMMITTEE MEMBER JELINCIC: Okay. But didn't the trailer bill --

CHAIRPERSON COSTIGAN: So this is current law.

COMMITTEE MEMBER JELINCIC: I already acknowledged that.

CHAIRPERSON COSTIGAN: We're saying two different things here, because you just said proposal and trailer bill.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: So there's two things. So, one, currently, we collect administrative expenses at per statute via two means, administrative expenses via the CRF and HCF.

There was a trailer bill this last year that was actually shot down by the Senate Assembly that was to take and all merge it into the CRF only, which is an employer-only contribution model.

But that -- since that was actually shut down, there was control language that was added to ask us to do the analysis for the legislature, so they could truly see the impact to public agencies and schools. So this is satisfying their analysis request. There is no current trailer bill or policy bill that's moving forward.

CHAIRPERSON COSTIGAN: So back to Mr. Jones' question. What's the fiscal impact? If there was no change in the statute, and this is just reporting language --

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: There is none. We're just --

CHAIRPERSON COSTIGAN: So the chart that shows a net increase is based upon what, because nothing has changed in the statute?

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: It was based on the assessment that the legislature asked us to do an impact analysis. So we're just showing what the impact analysis would be.

CHAIRPERSON COSTIGAN: So that's why we need to be clear. This is a potential cost to what Mr. Jones was asking. There is no cost at this point. All we had was reporting language that was inserted into the trailer bill last year.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: You got it.

CHAIRPERSON COSTIGAN: I used to do this for a living.

Mr. Brown.

COMMITTEE MEMBER JELINCIC: Wait.

CHAIRPERSON COSTIGAN: I'll come back to you.

Oh, hang on a second. Sorry.

Mr. Jelincic.

COMMITTEE MEMBER JELINCIC: So why? I mean, why is this being proposed or sought by the Department of Finance? I mean, it making no sense to me.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: In discussions with them when they received the appropriation and oversight responsibilities of HCF last year, because CalPERS collects it in two different manners, it's difficult to provide oversight. And so this would create more transparency. So we are working with Department of Finance to see if there's other means to achieve this same goal. But we still have to satisfy the requirement in the control language to provide the assessment.

COMMITTEE MEMBER JELINCIC: Okay. Thank you.

CHIEF HEALTH DIRECTOR BAILEY-CRIMMINS: You're welcome.

CHAIRPERSON COSTIGAN: Mr. Brown.

ACTING BOARD MEMBER BROWN: Thank you, Mr. Chair. I just want to thank you for adding the net annual increase into Attachment 1. I think that did address some of our questions. I also maybe make the suggestion to include that information in the paragraph above to maybe make it more transparent.

I did have a follow-up question on the public agencies. You said you came up with a split through your -- through your data the 31.69. And I was just wondering did that somehow include the fact that many employers may use cafeteria plans and may reimburse public employees on the back end, so they're not technically paying 69 percent of the premium.

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: No, so it does not include that. So we don't have insight into that. This is just what employers are reporting to us. So we do know that public agencies typically have something else that's happening internally, but we don't have info -- we're not privy to that information and weren't able to incorporate it into this analysis.

ACTING BOARD MEMBER BROWN: So the annual increase on the public agency is kind of worst case scenario. It could be lower, because they could already be paying some of that cost, already or reimbursing the employees.

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Correct. And again, that 31.69 is an average of all of our agencies, so the there -

ACTING BOARD MEMBER BROWN: So some may be impacted more than others.

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF JARZOMBEK: Correct.

ACTING BOARD MEMBER BROWN: Thank you.

CHAIRPERSON COSTIGAN: Mr. Lennon, why don't you come on down, sir.

Mr. Jelincic,

COMMITTEE MEMBER JELINCIC: Yeah, I just want to point out that we typically think of public agencies and schools as separate groups. In this analysis, the schools are grouped with public agencies.

HEALTH ACCOUNT MANAGEMENT DIVISION CHIEF

JARZOMBEK: That is correct.

CHAIRPERSON COSTIGAN: All right. No further discussions on this one.

Mr. Lennox, you have three minutes, sir.

MR. LENNOX: Thank you Chair and members. Derick Lennox on behalf of the School Employers Association of California. Part of what we do is very similar to what CalPERS does in terms of helping our employers provide health benefits to employees. We are one of the only statewide associations in K-12 education that has a full-time individual, a consultant, who actually helps districts understand the costs and benefits of different employer-provided health programs.

And in many cases, we direct them right here to this building to CalPERS, because of the quality of the plan. So I just wanted to speak, rather than talk about the parade of horribles that we've been talking about on the employer fiscal side, about where I think the Venn Diagrams of CalPERS and what we do overlap. And it really goes to slide 10, I believe.

And this is exactly what we'll tell the legislature and finance if they happen to inquire with us as well that as consumers in this very competitive health marketplace, it's not very difficult for employers to go from one organization to another in terms of providing health benefits.

So we'd really like to see CalPERS be as competitive as possible, because so many of our members in the association are in CalPERS. And so adding those extra costs, there are already so many reasons to, you know, choose something else or be persuaded by a broker one way or another, it's one good reason to stay in CalPERS.

And to the extent that we're already users of the CalPERS Health Benefits Program, we certainly don't want to see CalPERS losing its market influence when it comes to the size and scope of, you know, the number of lives that you cover. So we want to make sure that your market influence and control over premiums and drug prices and all the rest are as strong as possible, because in that sense our interests are totally aligned.

Thank you very much.

CHAIRPERSON COSTIGAN: Thank you, Mr. Lennox.

Okay. Nothing further on that item.

All right. I believe, Pam, we have no other public comment on any other item, if my list is correct. So that brings us to Committee direction, Charles.

CHIEF FINANCIAL OFFICER ASUBONTEN: Yes, sir. Yes. Charles Asubonten CFO. Mr. Chairman, I have three main directions.

And the first one is for CEO, working with Public

Relations, to draft legislation no later than February to exempt schools employees from current membership requirements and require enrollment upon hire into the -- into a calPERS position.

CHAIRPERSON COSTIGAN: That's to come back with proposed legislation, that's correct.

CHIEF FINANCIAL OFFICER ASUBONTEN: Yes.

CHAIRPERSON COSTIGAN: That was Mr. Feckner's request.

Next item.

CHIEF FINANCIAL OFFICER ASUBONTEN: The next item miscellaneous items from the participating employers. One, to include vested members on affected -- on the slides that we saw earlier. The second one is update reporting on participating employers on the JPA to slides to include or separate contractual versus revenue funding.

The next item is -- I'm not sure if it's direction per se, but to have closed session to include more detailed information --

CHAIRPERSON COSTIGAN: Is that -- and we'll be working with Mr. Jacobs on that, because I believe that could either be a litigation or an employment issue related to the termination of agencies, but that's something that we'll work with Mr. Jacobs on. So, yes.

CHIEF FINANCIAL OFFICER ASUBONTEN: Okay. And lastly to continue to provide an update on Herald Fire Protection District status.

CHAIRPERSON COSTIGAN: I do believe that is it. Committee members, in agreement? Did we miss anything?

Oh, I'm sorry Mr. Jones. Hang on a second.

COMMITTEE MEMBER JONES: Mr. Chair, on the proposed legislation that Mr. Feckner, I don't remember him asking that proposed legislation. I thought he wanted the CEO to meet with the legislative staff.

CHAIRPERSON COSTIGAN: He is. And I think, as we discussed, she would have that meeting. If we were going to do anything, we'd have to bring it back in February to meet the legislative deadline.

COMMITTEE MEMBER JONES: Okay. Oh, I see. Okay

CHAIRPERSON COSTIGAN: And the problem is we don't have a meeting in January. We have an offsite.

COMMITTEE MEMBER JONES: Yeah. Okay.

CHAIRPERSON COSTIGAN: And so you're absolutely right, but to move on timelines.

Anything else, Charles?

CHIEF FINANCIAL OFFICER ASUBONTEN: That's it.

CHAIRPERSON COSTIGAN: Anything from this side of the dais?

Anything?

Mr. Bilbrey.

BOARD MEMBER BILBREY: Okay. Finance and Admin is adjourned. We will meet at 2:50?

Did you say -- 2:50 Perf and Comp.

Thank you all. This meeting is adjourned.

(Thereupon the California Public Employees' Retirement System, Board of Administration, Finance & Administration Committee meeting adjourned at 2:32 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 December 2017.

JAMES F. PETERS, CSR
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