



Risk and Audit Committee Agenda Item 7a

November 17, 2020

Item Name: Third Party Valuation and Certification of the 2019 Annual Valuations of the Judges' Retirement System (JRS), Judges' Retirement System II (JRSII), Legislators' Retirement System (LRS), and the 1959 Survivor Benefit Program (1959 SBP)

Program: Office of Audit Services

Item Type: Information

Executive Summary

The third-party actuarial firm, Buck Global, LLC (Buck), completed its independent review of the actuarial valuations of the JRS, JRS II, LRS, and the 1959 SBP as of June 30, 2019. Overall, Buck found the actuarial process followed by CalPERS actuarial staff is thorough, complete, and complies with applicable Actuarial Standards of Practice (ASOP). The full reports summarizing the review and including findings and recommendations are in Attachments 1 through 4 of this agenda item.

Strategic Plan

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

Background

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

In November 2015, the Board selected a third-party actuarial firm, Buck, to provide the parallel valuation and certification services to the Board. Buck has completed the parallel valuation and certification services for the JRS, JRS II, LRS, and the 1959 SBP Plans as of June 30, 2019. This activity represents the completion of Task 6 of Contract 2015-8123.

The JRS provides benefits to California Supreme and Appellate Court Justices and Superior Court Judges, and Municipal Court judges appointed or elected prior to November 9, 1994 while the JRS II provides benefits to the same officials elected or appointed on or after November 9, 1994. The LRS Fund was established to provide retirement benefits to members of the Legislature elected prior to November 7, 1990, elected Constitutional Officers, the Insurance Commissioner, and Legislative Statutory Officers. The 1959 SBP provides benefits to eligible survivors of CalPERS members who are not covered by Social Security and die prior to retirement.

Analysis

Buck reviewed the actuarial assumptions and methods used in the JRS, JRS II, LRS, and the 1959 SBP valuations. Buck concluded that the assumptions used are reasonable, and the methodology used to select these assumptions is appropriate and consistent with the guidance provided in ASOP 4, 6, 27, 35, and 51.

- ASOP 4 is the standard of practice for measuring pension obligations and determining pension plan costs or contributions.
- ASOP 6, the standard of practice for measuring retiree group benefits obligations and determining retiree group benefits plan costs or contributions.
- ASOP 27 discusses the selection of economic assumptions for the measurement of pension liabilities.
- ASOP 35 discusses the selection of demographic assumptions for the measurement of pension liabilities.
- ASOP 51 applies to funding calculations and requires certain disclosures of potential risks.

Buck also completed parallel actuarial valuations for the JRS, JRS II, LRS, and the 1959 SBP valuations and compared their key results to those produced by CalPERS actuarial staff on an aggregate and individual basis in order to uncover potential discrepancies that offset each other, producing aggregate results that fall within the 5 percent tolerance level. Based on this testing, Buck reported that for all plans, all their calculations for these key results differed by less than 5 percent from the corresponding results reported by CalPERS.

During the parallel valuation and review of the JRS, JRS II, LRS, and the 1959 SBP valuations, Buck provided the following recommendations to CalPERS and an update to their previous parallel valuation and certification report recommendations by each specific plan.

Parallel Valuation and Certification Report JRS Valuation

Recommendation:

Buck provided one recommendation for inclusion in the JRS valuation report in order to more completely fulfill ASOP 27 and 35 requirements:

1. Add a statement that all assumptions represent an estimate of future experience.

In addition, Buck provided a current update to their previous parallel valuation and certification report recommendations for JRS as of June 30, 2016:

1. Add information to the reports to meet new ASOP 4 requirements. The June 30, 2019 valuation report has addressed this recommendation.
2. Consider reflecting pre-retirement mortality for all separated participants. The June 30, 2019 valuation report has addressed this recommendation.

Parallel Valuation and Certification Report JRS II Valuation

Recommendation:

Buck recommended to consider the following items for inclusion in future reports in order to more completely fulfill the requirements of ASOP 27 and ASOP 35:

1. Add information to the report to meet communication requirements.
 - a) A statement that all assumptions represent an estimate of future experience.
 - b) A description of the treatment of the Monetary Credit Account, the participation and form of payment, in the Actuarial Assumptions.

In addition, Buck provided a current update to their previous parallel valuation and certification report recommendations for JRS II as of June 30, 2016.

1. The following items may be considered for inclusion in future reports to more completely fulfill the requirements of ASOP 4:
 - a) Add enhanced description of the contribution allocation procedure, including a more detailed description of what the five-year ramp-up and ramp-down in amortizations entail. This issue is no longer applicable.
 - b) Add a statement regarding the impact of the funding policy on future contributions. The report does not have a statement regarding the impact of the funding policy on future contributions and funded status.
 - c) Include more detail on the rationale for changes in assumptions. The June 30, 2019 valuation report has addressed this recommendation.

Parallel Valuation and Certification Report LRS Valuation

Recommendation:

The following items may be considered for inclusion in future reports in order to more completely fulfill the requirements of ASOP 27 and ASOP 35:

1. A statement that all assumptions represent an estimate of future experience.
2. A disclosure of the rationale for the economic assumptions other than inflation, which may be done by referencing the experience study for all assumptions applicable and explicitly stating any assumptions the experience study is not applicable.

In addition, Buck provided a current update to their previous parallel valuation and certification report recommendations for LRS as of June 30, 2016:

1. Add a statement regarding the impact of the funding policy on future contributions and funded status to more completely fulfill the new ASOP 4 requirements. This does not appear to have been specifically addressed.

Parallel Valuation and Certification Report 1959 SBP Valuation

Recommendations:

1. The following items may be considered for inclusion in future reports to more completely fulfill the requirements of ASOP 27:
 - a) A statement that the return on investment assumption represents an estimate of future experience.
 - b) A disclosure of the rationale for the return on investment assumption.
2. Revise the treatment of the new element of the projection of the unfunded liability labeled "Changes in Contributions due to Contribution (Gain)/Loss."
3. Refine the projected unfunded liability calculation with a more precise application of interest on the projected employee contributions.
4. Provide more detail on the development of normal cost for all groups except Public Agency Indexed Level Pool.

In addition, Buck provided a current update to their previous parallel valuation and certification report recommendations for 1959 SBP as of June 30, 2016:

1. Add information to the reports to meet new ASOP 6 requirements.
 - a) An enhanced description of the contribution allocation procedure, including a more detailed description of what the five-year ramp-up and ramp-down in amortizations entail. The June 30, 2019 valuation report is the first valuation to reflect a change in the funding method; thus, this recommendation is no longer applicable as it strictly pertains to the June 30, 2016 report.
 - b) A statement regarding the impact of the funding policy on future contributions and funded status. This does not appear to have been specifically addressed.
 - c) Additional comments about the appropriateness of reported measures of the funded status of the plan. This does not appear to have been specifically addressed.
 - d) A statement regarding the potential effects of differing returns from assumptions. This does not appear to have been specifically addressed.

Budget and Fiscal Impacts

The fee for the parallel valuation and certification of the 2019 annual valuations of the JRS, JRSII, LRS, and the 1959 SBP valuations is \$53,000. Funding is identified within existing budgetary resources.

Benefits and Risks

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

Attachments

Attachment 1 – Parallel Valuation and Certification Report Judges' Retirement System Valuation as of June 30, 2019

Attachment 2 – Parallel Valuation and Certification Report Judges' Retirement System II Valuation as of June 30, 2019

Attachment 3 – Parallel Valuation and Certification Report Legislators' Retirement System Valuation as of June 30, 2019

Attachment 4 – Parallel Valuation and Certification Report 1959 Survivor Benefit Program Valuation as of June 30, 2019

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