Joint Hearing
Senate PE & R and Assembly PE, R & SS Committees

January 10, 2018

John E. Bartel
Member, California Actuarial Advisory Panel

Agenda

- Brief History of CAAP
- Government Code §20229
- Main Results
- Role of Investment Return
- Role of Amortization Period

California Actuarial Advisory Panel (CAAP)

- Panel was established with enactment of SB 1123 in 2008
- Pursuant to Government Code §7507.2(a):

  …the panel shall provide impartial and independent information on pensions, other postemployment benefits, and best practices to public agencies…
- Housed in the State Controller's Office

CAAP Accomplishments

- Historical
  - Model Disclosure elements for Actuarial Valuation Reports — December 2011
  - Actuarial Funding Policies and Practices for Benefit Changes in Public Pension and OPEB Plans — February 2014
  - Evaluating Public Sector Actuarial Services — February 2015
  - Actuarial Funding Policies and Practices for Public Pension and OPEB Plans and Level Cost Allocation Model — February 2013 Updated November 2015

CAAP Accomplishments

- 2017
  - Response to SCO Government Compensation Database Questions — October 2017
  - Response to DOF SB 84 Questions — November 2017
  - Annual PEPRA Compensation Limit Letter — November 2017

Government Code §20229

- Requires CalPERS Board provide annual report which includes certain information for State employees
  - Liabilities and contribution rates using an investment return assumption that is 2% higher and 2% lower than assumed
  - Contribution rates calculated by paying down unfunded liability over the average remaining service period of State employees
- Requirement met with publication of the State June 30, 2016 Actuarial Valuation Report

  https://www.calpers.ca.gov/docs/forms-publications/2016-state-valuation.pdf

Government Code §20229

- Requires CAAP Chair (or designee) present information to this joint legislative hearing
  - Explain the role played by the investment return assumption and amortization period in the calculation of contribution rates.
  - Describe the consequences to future State budgets if the investment return assumptions are not realized.
  - Report whether the Board's amortization period exceeds the estimated average remaining service periods of employees covered by the contributions.

Main Results from State Valuation Report

- Most recent valuation report is June 30, 2016
- Report covers five different retirement plans:
  - State Miscellaneous (Tier 1 and Tier 2)
  - State Industrial
  - State Safety
  - State Peace Officers and Firefighters
  - California Highway Patrol

Main Results from State Valuation Report

As of June 30, 2016

All State plans combined:

■ Actuarial Accrued Liability	$170.7 billion
■ Market Value of Assets	111.1 billion
■ Unfunded Liability	59.5 billion
■ Funded Ratio (based on a 7⅜%)	65.1%
■ Estimated funded ratio on June 30, 2017 (based on 7%)	65.3%

Main Results from State Valuation Report

2017/18 Fiscal Year Employer Contribution Rates:

State Miscellaneous	28.3%
State Industrial	19.5%
State Safety	19.4%
State Peace Officers & Firefighters	42.6%
California Highway Patrol	52.8%
Average	30.6%

Changes Since the Prior Year's Valuation to Actuarial Methods and Assumptions

- On December 21, 2016 CalPERS Board lowered the discount rate from 7½% to 7% over next 3 valuations:

	Rate	Initial	Full
• 6/30/16 val.	7.375%	17/18	21/22
• 6/30/17 val.	7.25%	18/19	22/23
• 6/30/18 val.	7.00%	19/20	23/24

  - Risk mitigation suspended until after 6/30/18
- Future analysis may result in a change to this discount rate schedule.

Role Played By Investment Return

- Assets to pay benefits come from two sources
  - Contributions (both employer and employee) and
  - Investment earnings
- Actual returns are unknown so must use an assumption
- If investment returns are ***higher*** than expected then contributions can be ***lower***
- If investment returns are ***lower*** than expected then contributions must be ***higher***
- Liability reflects only the portion of benefits anticipated to be paid by contributions (cash)
- See Risk Analysis Section of Valuation Report – Pages 36-50

Role Played By Amortization Periods

- Goal is to be 100 % funded i.e. no unfunded liability
  - Target not a certainty
- Time to get to 100% funded is amortization period
- Shorter Period
  - Higher contribution rates
  - Current taxpayers pay more toward current unfunded liability
- Longer Period
  - Lower contribution rates
  - Future taxpayers pay more toward current unfunded liability

Role Played By Amortization Periods

	Average Amortization Period*	Estimated Average Remaining Service Period
■ State Miscellaneous	26	10
■ State Industrial	34	11
■ State Safety	31	10
■ State Peace Officers & Firefighters	30	11
■ California Highway Patrol	27	12

* Periods may exceed 30 years due to the inclusion of a 5-year ramp in the amortization policy. However, all unfunded liability is scheduled to be paid off within 30 years.