

Approval of a Lump Sum Payment to the California Public Employees Retirement System (CalPERS) to Payoff the Authority's Unfunded Actuarial Accrued Liability (UAAL)



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What is the discount rate?

The discount rate is the long-term interest rate used to fund future pension benefits. It is one of the key components of the **Asset Liability Management (ALM)** cycle that CalPERS uses to balance assets with future pension obligations. The discount rate is also known as the assumed rate of return because it's what CalPERS expects its investments to earn during the fiscal year.

Why the Discount Rate Change?

CalPERS Board of Administration, in December 2016, approved lowering the CalPERS discount rate assumption, the long-term rate of return, **from 7.50 percent to 7.00 percent** over a three-year period starting with the valuation date of June 2016.

Subsequently, in July 2021 the CalPERS Board of Administration **voted to lower the discount rate from 7% to 6.8%** due to the Funding Risk Mitigation Policy. This policy lowers the discount rate in years of good investment returns to reduce risk in the portfolio. The policy automatically lowered discount rate when CalPERS achieved an investment return of 21.3% for fiscal year (FY) 2020-21. The next review of this policy by CalPERS will occur in 2025.

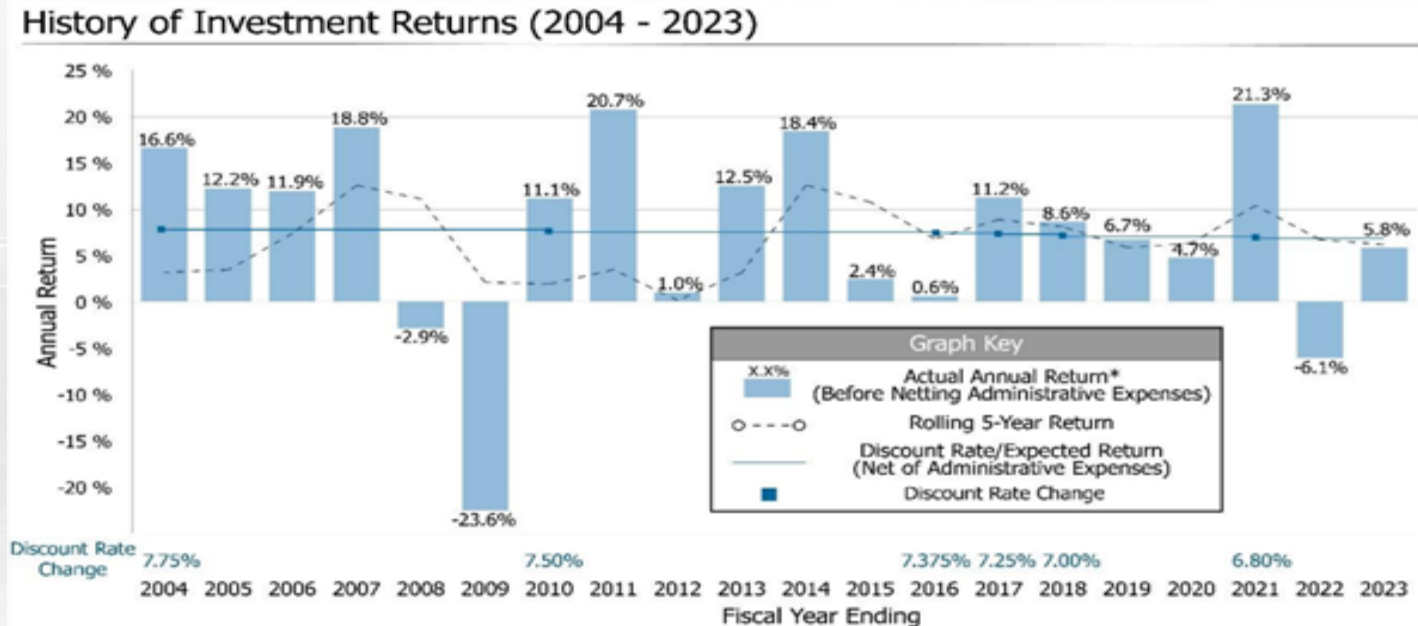
CalPERS projects the benefits of reducing discount rate include:

- Strengthening the long-term sustainability of the fund,
- reducing negative cash flows,
- **additional contributions from participating agencies will help to offset the cost to pay pensions,**
- reducing the long-term probability of funded ratios falling below undesirable levels,
- improving the likelihood of CalPERS investment earning their assumed rate of return
- reducing risk of contribution increases in the future from volatile investments markets.

Effect on CCTA?

Lowering the discount rate means plans will see increases in both normal costs (the cost of pension benefits accruing in one year for active members) and the accrued liabilities. These increases will result in higher required employer contributions. The Authority has seen an increase in employer contribution rates over the last ten years. The Authority's contribution rate has increased from 8.377% in 2016-17 to 11.94% scheduled for 2025-26.

The investment and assets held by CalPERS are in excess of \$530 billion and are well diversified. These investment and asset returns can fluctuate year-to-year and play a role in the current funding of the pension plan.



Funding History

In May of 2015, the Authority approved Resolution 15-17-A for the payoff amount of **\$2,210,110** which eliminated the UAAL as of June 2015. In February of 2019, the Authority approved Resolution 19-05-A for the payoff amount of **\$1,238,094** which eliminated the UAAL as of June 2018. As a result of these contributions, changes in the discount rate assumptions and the long-term rate of return on assets held by CalPERS, the Authority's current funding values as of June 30, 2023, now reflect a pension liability of **\$2,428,000** or a funded status of 87%. **(Classic \$2,356,000 & PEPRA \$72,000)**

Valuation	Accrued	Share of Pool's	Unfunded		CalPERS	LAIF
Date	Liability (AL)	Market Value of Assets (MVA)	Accrued Liability (UAL)	Funded Ratio	Investment Returns	Investment Returns
6/30/2014	\$10,938,262	\$9,014,721	\$1,923,541	82.40%	18.400%	0.249%
6/30/2015	11,724,167	11,441,044	283,123	97.60%	2.400%	0.269%
6/30/2016	12,520,097	11,295,894	1,224,203	90.20%	0.600%	0.434%
6/30/2017	13,386,252	12,278,478	1,107,774	91.70%	11.200%	0.754%
6/30/2018	14,502,714	12,897,608	1,605,106	88.90%	8.600%	1.376%
6/30/2019	16,274,939	15,679,803	595,136	96.30%	6.700%	2.266%
6/30/2020	17,749,923	16,645,443	1,104,480	93.80%	4.700%	1.934%
6/30/2021	19,161,104	20,152,054	-990,950	105.20%	21.300%	0.500%
6/30/2022	20,280,131	18,199,868	2,080,263	89.70%	-6.10%	0.371%
6/30/2023	21,005,875	18,366,140	2,639,735	87.40%	5.800%	2.170%

Asset Liability Management (ALM)

The goal of the ALM process is to balance the expected cost of future pension payments with the expected future investment returns. During the process, the CalPERS board reviews its overall risks, taking into consideration the long-term sustainability of the system.

This formal process runs on a four-year cycle and includes a review of CalPERS' investment portfolios and retirement plan liabilities. Liability projections are based on demographic and economic factors and trends, including membership dynamics, future salary and payroll growth, retirement ages, inflation, and life expectancy.

ALM Key Risk Tradeoffs

Asset Liability Management (ALM) Timeline

2025

January

- Board Education Day: Risk Tradeoff Activity TPA Considerations

February

- Risk Activity Follow Up and Risk Appetite
- *ALM Strategy Session**

March

- ALM Governance
- *ALM Strategy Session**

June

- ALM Education Session
- *ALM Strategy Session**

July

- Board Offsite: ALM Education Session

September

- First Reading: Proposed Reference Portfolio and Active Risk, Experience Study, Actuarial Assumptions, and Discount Rate
- *ALM Strategy Session**

November

- Final Approval of Proposed Reference Portfolio and Active Risk, Experience Study, Actuarial Assumptions, and Discount Rate
- *ALM Strategy Session**

2026

July 1 Effective Date

Stakeholder Engagement Throughout Cycle

Amortization Schedule and Alternatives (continued)

CalPERS Amortization of Unfunded

CLASSIC - CalPERS Actuarial Valuation - June 30, 2023

CalPERS applies a twenty-year amortization schedule that outlines the annual payments necessary to pay the unfunded liability on an annual basis. Should the Authority elect to follow this schedule or the fifteen-year, current projections would total \$4,619,712 and \$1,683,868 would be accumulated interest payments over fifteen-year years.

PEPRA CalPERS Actuarial Valuation - June 30, 2023

Projections would total \$144,858 and \$52,800 would be accumulated interest payments over fifteen-year years.

Date	Current Amortization Schedule		Alternative Schedules			
	Balance	Payment	20 Year Amortization		15 Year Amortization	
			Balance	Payment	Balance	Payment
6/30/2025	2,935,844	152,260	2,935,844	264,002	2,935,844	307,981
6/30/2026	2,978,129	198,619	2,862,651	264,001	2,817,201	307,981
6/30/2027	2,975,381	244,980	2,784,482	264,002	2,690,491	307,981
6/30/2028	2,924,534	291,340	2,700,996	264,001	2,555,164	307,981
6/30/2029	2,822,319	294,262	2,611,834	264,001	2,410,635	307,981
6/30/2030	2,710,134	294,261	2,516,609	264,002	2,256,278	307,981
6/30/2031	2,590,322	294,261	2,414,908	264,001	2,091,425	307,981
6/30/2032	2,462,362	294,262	2,306,292	264,001	1,915,362	307,981
6/30/2033	2,325,700	294,262	2,190,290	264,001	1,727,326	307,980
6/30/2034	2,179,745	294,260	2,066,400	264,002	1,526,505	307,981
6/30/2035	2,023,868	294,262	1,934,085	264,001	1,312,027	307,980
6/30/2036	1,857,388	294,260	1,792,773	264,002	1,082,966	307,981
6/30/2037	1,679,590	294,262	1,641,851	264,001	838,328	307,981
6/30/2038	1,489,700	294,262	1,480,667	264,001	577,054	307,980
6/30/2039	1,286,898	294,261	1,308,523	264,001	298,015	307,981
6/30/2040	1,070,306	294,261	1,124,673	264,002		
6/30/2041	838,986	294,261	928,320	264,001		
6/30/2042	591,936	294,261	718,616	264,001		
6/30/2043	328,086	294,262	494,652	264,001		
6/30/2044	46,293	47,841	255,459	264,002		
6/30/2045						
6/30/2046						
6/30/2047						
6/30/2048						
6/30/2049						
<hr/>						
Total		5,348,960		5,280,027		4,619,712
Interest Paid		2,413,116		2,344,183		1,683,868
Estimated Savings				68,933		729,248

Proposed Lump Sum Payment

In January 2025, staff worked with the CalPERS Actuarial Office to determine the estimated pay-off assumptions that include the preliminary fiscal year 2023-24 investment return of 9.3%. Including the recent fiscal year investment return will reduce the pay-off amount to necessary to \$2,428,000. CalPERS information is based on the most recent Lump Sum Payment Request Form(s).

Classic Employees Amount	\$2,356,000.00
PEPRA Employees Amount	<u>\$ 72,000.00</u>
Total Lump-sum payment	\$2,428,000.00

Proposed Savings Accrued Interest

The proposed lump sum payment will reduce the Authority's UAAL and represent a cost reduction on future interest amortization in the amount of \$1,693,868 for the Classic Plan and \$52,800 on the PEPRA Plan based on the fifteen-year amortization schedules.

Proposed Source of Funds

The proposed source for the lump sum payment of \$2,428,000 is an accumulation of investment income earned in the Authority's Measure C contingency reserve. The reserve balance is in excess of programed amounts for remaining Measure C projects.

Staff Recommends

- Staff seeks approval of Resolution 25-05-A which will allow for a lump sum payment to CalPERS in the amount of \$2,428,000 to pay off the Authority's UAAL as of June 30, 2023.
- **Questions**