SB cera
San Bernardino
County Employees' Retirement Association

Information presented to the Commission at the 7-17-13 LAFCO hearing.

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LAFCO
San Bernardino County

June 12, 2013

Ms. Kathleen Rollings-McDonald, Executive Officer
Local Agency Formation Commission
215 North D Street, Suite 204
San Bernardino, CA 92415-0490

RE: LAFCO Liability Calculations

Dear Ms. Rollings-McDonald:

At your request, SBCERA has conferred with our actuaries at The Segal Company about determining the unfunded liability of the Local Agency Formation Commission (LAFCO) as of June 30, 2013, as well as the termination liability that would become owed upon the hypothetical withdrawal of LAFCO from SBCERA. Attached is a copy of the actuaries' letter which explains their methodology for performing this work.

As the letter also explains, the fee for the actuaries' services will be approximately $10,000 to $15,000, to be paid by LAFCO. Please let us know if you would like the actuaries to proceed with this work. If LAFCO actually withdraws from participation in SBCERA, the calculation of the precise termination liability would require an additional $5,000. See the "Estimated Fees and Delivery of Study" section in the attached. For whatever services LAFCO desires the actuaries to perform, we will send you a bill for their actual time.

Regarding your question about the accounting of assets for the non-County agencies who did not issue Pension Obligation Bonds (POB's), all plan sponsors who have not issued POB's are accounted for in the actuarial cost groups called 'Other General' and 'Other Safety'. LAFCO is part of the 'Other General' group. The assets and liabilities for each actuarial cost group are tracked separately by our actuaries, but the assets for each employer within each group are not tracked separately.

If you have any questions, please feel free to contact Julie Underwood, Chief of Fiscal Services, or me at (909) 885-7980.

Sincerely,

Norman L. Ruggles
Chief Executive Officer

Enclosure

SEGAL

THE SEGAL COMPANY
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June 11, 2013

Mr. Norm Ruggles
Chief Executive Officer
San Bernardino County Employees' Retirement Association
348 W Hospitality Lane, Third Floor
San Bernardino, CA 92415-0014

**Re: San Bernardino County Employees' Retirement Association
Local Agency Formation Commission - Proposed Project Plan**

Dear Norm:

We understand that the Local Agency Formation Commission (the District) is requesting a hypothetical determination of their obligation in the event that they were to withdraw from SBCERA pursuant to Government Code Sections 31564 and 31564.2. As requested, this letter provides a proposed methodology for determining the obligation to SBCERA if the District were to terminate its participation agreement, along with our proposal to calculate that obligation. Note that the District has also requested an estimate of their Unfunded Actuarial Accrued Liability (UAAL) (on a non-termination basis). Since this information (as of June 30, 2012) is calculated as part of Step 2 shown on page 3 of this letter, it would also be included in our study.

GENERAL DISCUSSION

In order to determine a withdrawing District's funding obligation, it is necessary to attribute a portion of SBCERA's liabilities and assets to the District. The liability is determined by performing a separate actuarial valuation using the District's member data and termination benefits. However, because SBCERA is a cost sharing multiple-employer plan, there is no ongoing separate accounting of SBCERA's assets attributable to the District.

Section 31564.2 provides a default method for determining a withdrawing District's funding obligation; however, because the default methodology is based only on contribution history, it overlooks important benefit level and membership classification distinctions that are critical to the determination of a fair and equitable funding obligation. For that reason, we advise our client retirement systems to adopt a methodology that is the least disruptive to and the most consistent with the contribution obligations of the remaining employers.

Some systems have adopted a formal employer termination policy. However, considering this may be a rare event for SBCERA, the termination procedure described herein could be effectively followed by SBCERA for the termination of the District. We defer to you as to whether the adoption of a formal policy is appropriate for your system.

This letter provides a description of a methodology we have seen employed by other 1937 Act retirement systems. This policy dictates the use of the market value of assets and market based actuarial assumptions for projecting liabilities of members of a district, so that no further assessments or measurements of the District's liabilities will be necessary after the termination date. We understand that this is the preferable approach to take based on the circumstances involved.

TERMINATION CONDITIONS

Based on our discussions, we understand that the following approach would be taken by the (hypothetically) terminating employer with regard to member's benefits:

- All active members on the termination date would receive SBCERA benefits for their credited service and compensation up to the termination date. As a result, they will take on the same status as terminated members without reciprocal benefits.

- All vested terminated and retired members (and beneficiaries) would continue to receive their future benefits from SBCERA.

DETERMINATION OF FUNDING OBLIGATION

The District's funding obligation as of the termination date is equal to:

- The present value of all future benefits expected to be paid by SBCERA to the District's employees, retirees, beneficiaries, and terminated members as of termination date

MINUS

- The value of assets allocated to the District as of the termination date.

As noted earlier, the valuation of the liabilities would be on a market basis. Under this approach, the present value of future benefits would be calculated using all the same actuarial assumptions utilized in the most recent actuarial valuation except that future benefit payments will be discounted to the present date using market based interest rate assumptions. The market based interest assumptions we recommend for this purpose are the discount rates used by the Pension Benefit Guaranty Corporation (PBGC) to measure the sufficiency of assets for a corporate employer who is terminating its single-employer defined benefit pension plan. These PBGC rates are generally lower than the interest rate used in SBCERA's actuarial valuation. For example, in May 2013, the PBGC rates are 2.50% per annum for the next 20 years and 3.20% per annum, thereafter. Under this approach, there will be no ongoing reassessment of the benefit liability after the District's termination date.

Because SBCERA is a cost sharing multiple-employer plan, there is no ongoing separate accounting of SBCERA's assets by employer. The SBCERA assets attributable to contributions of the District and its employees would be determined as follows:

Step 1: Determine the Actuarial Accrued Liability of the District as of SBCERA's most recent actuarial valuation.

Step 2: Determine the UAAL of the District as of the most recent actuarial valuation by dividing the District's annual UAAL contribution requirement by the UAAL amortization factor. The District's UAAL contribution rate, annual payroll, and average UAAL amortization factor would be determined as of the most recent actuarial valuation date.

Step 3: Determine the non-investment change in assets from the most recent actuarial valuation date to the actual date of termination as:

- The total contributions by the District from the most recent actuarial valuation date to the date of termination; plus
- The total contributions by the District's employees from the most recent actuarial valuation date to date of termination; minus
- The total benefit and refund payments from the most recent actuarial valuation date to the date of termination to retirees, beneficiaries, and former employees of the District as a result of their years of service with the District for which they are entitled to SBCERA benefits.

Step 4: Determine the accumulated market value of assets at the termination date as:

(Step 1 – Step 2) x Ratio A x (1 + j) + Step 3 x (1 + j/2)

Where:

Ratio A = (Total SBCERA assets at market value as of the most recent actuarial valuation date) divided by (Total SBCERA assets at actuarial value as of the most recent actuarial valuation date)

j = the return on the market value of SBCERA's total assets from the most recent actuarial valuation date to the date of the employer's termination

If the result is a net liability, then the District would be required to pay off that amount as a lump sum or other terms acceptable to SBCERA.

The terminating employer's assets would be adjusted if there is any portion of SBCERA's reserves or designations from which the terminating employer will not benefit as a result of the termination. However, we do not believe that there are any such reserves or designations that the terminating employer will not benefit from.

DATA REQUIRED FOR FUNDING OBLIGATION CALCULATION

The following data will be needed to determine the District's funding obligation at termination.

1. Confirmation that the hypothetical date of termination is June 30, 2013.
2. Demographic data on the District's members as of the date of termination.
3. Confirmation that the termination benefits to which active members are entitled are the same as those for terminated members without reciprocal benefits.
4. Confirmation that all future benefits for members who are vested terminated or retired as of the termination date will continue to be paid by SBCERA.
5. The District's actual and expected contributions from the most recent actuarial valuation date through the date of termination.
6. District members' actual and expected contributions from the most recent actuarial valuation date through the date of termination.
7. Benefit payments and refunds made to the District's terminated and retired members (and beneficiaries) from the most recent actuarial valuation date through the date of termination.

ESTIMATED FEES AND DELIVERY OF STUDY

We propose that we first prepare preliminary results based on the process previously described earlier in this letter. These preliminary results would be based on the June 30, 2012 actuarial valuation and reflect estimated investment and demographic experience through the termination date. This will provide a good idea of the magnitude of the funding obligation and will accelerate delivery of the results. We expect that the fees associated with completing the preliminary results will be approximately $10,000 to $15,000. Actual fees will be billed on a time and charge basis according to actual hours worked. An invoice will be prepared once all the preliminary results are completed. We expect that the preliminary results can be delivered four to six weeks after all the necessary data is received.

In the event that the District decides to proceed with the termination and SBCERA requires the termination funding obligation to be finalized, then we estimate than the fees to complete a final report would be around $5,000. The final results would also be based on the June 30, 2012 actuarial valuation, but would reflect actual investment and demographic experience through the termination date. As with the preliminary results, actual fees will be billed on a time and charge basis according to actual hours worked. An invoice will be prepared once the final results are completed.

Please let us know if you have any questions.

Sincerely,

Paul Angelo, FSA, MAAA, FCA, EA
Senior Vice President and Actuary

John Monroe, ASA, MAAA, EA
Vice President and Associate Actuary

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