



## **TOWN OF LOS GATOS CALPERS MISCELLANEOUS & SAFETY PLANS**

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### **CalPERS Analysis – 6/30/21 Valuation**

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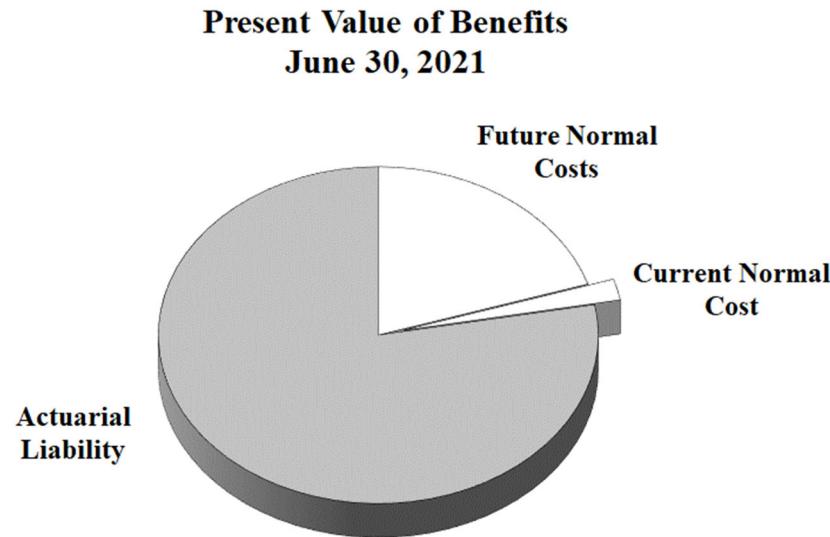
**March 7, 2023**

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# DEFINITIONS

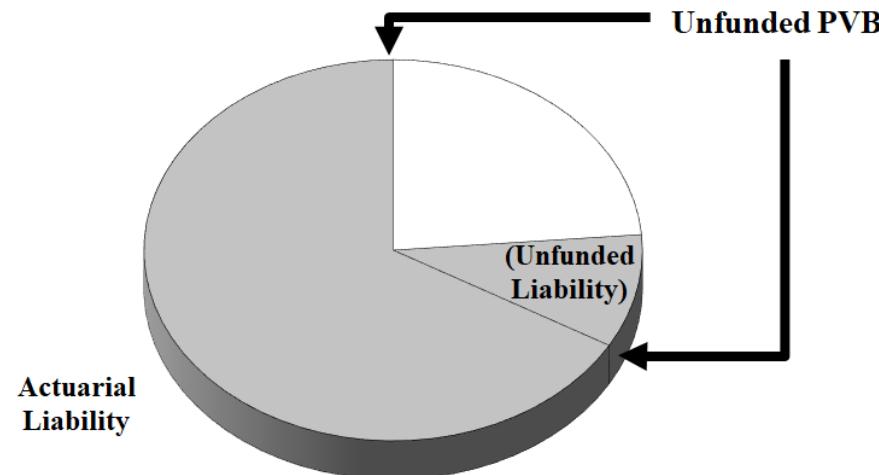


- **PVB - Present Value of all Projected Benefits:**
  - The value now of amounts due to be paid in the future
  - Discounted value (at valuation date - 6/30/21), of all future expected benefit payments based on various (actuarial) assumptions
- **Current Normal Cost (NC):**
  - Portion of PVB allocated to (or “earned” during) current year
  - Value of employee and employer current service benefit
- **Actuarial Liability (AAL):**
  - Discounted value (at valuation date) of benefits earned through valuation date [value of past service benefit]
  - Portion of PVB “earned” at measurement



# DEFINITIONS

## Present Value of Benefits June 30, 2021



- **Target**- Have money in the bank to cover Actuarial Liability (past service)
- **Unfunded Liability (UAAL or UAL)** - Money short of target at valuation date
  - If all actuarial assumptions were always exactly met, then the plan assets would always equal AAL
  - Any difference is the unfunded (or overfunded) AAL
  - Every year, the actuary calculates the difference between the expected UAAL and Actual UAAL. This is a new layer or amortization base
  - Each new layer gets amortized (paid off) over a period of time as part of the contribution [rate]

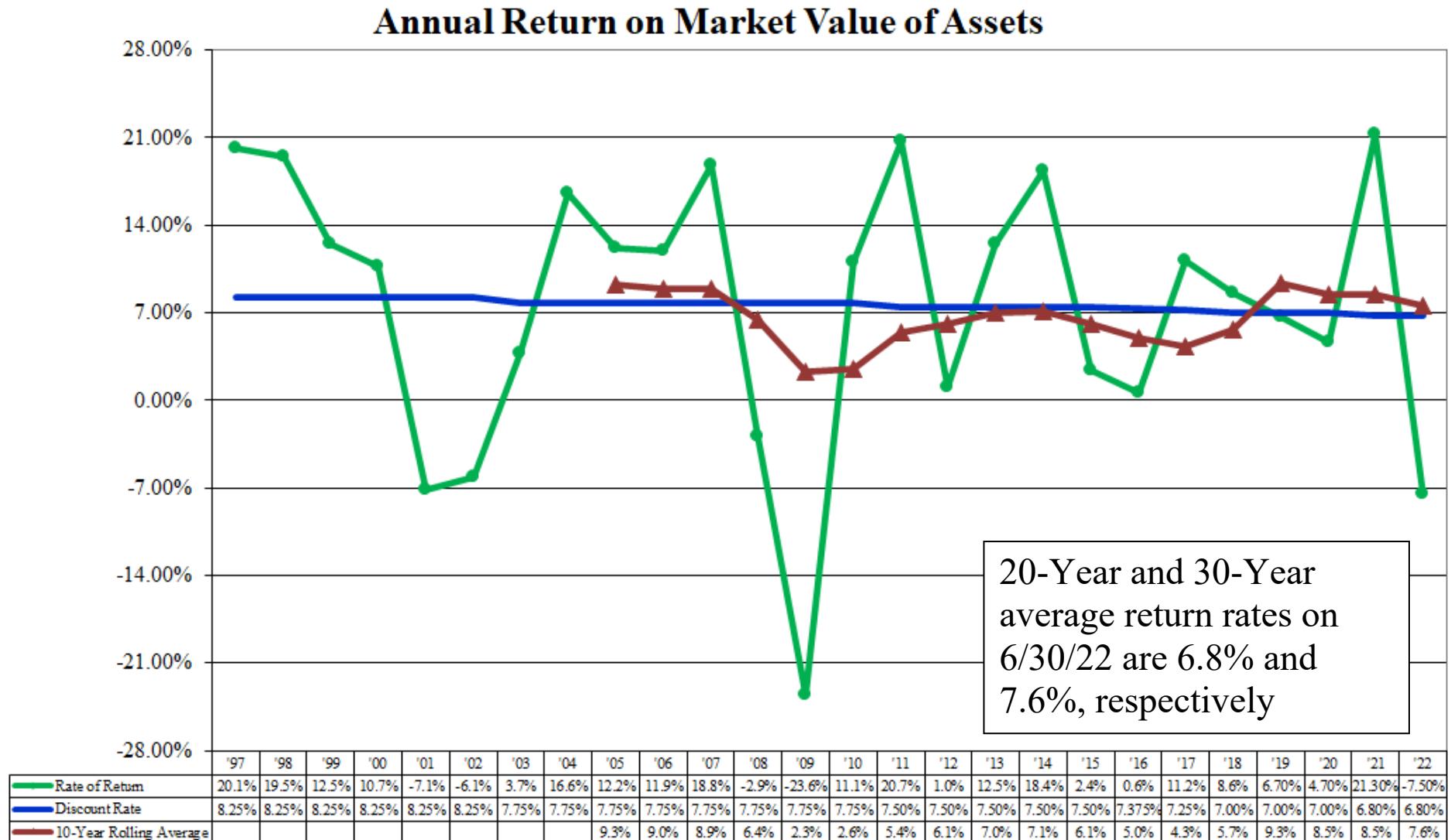


## HOW WE GOT HERE

- Investment Losses
- CalPERS Contribution Policy
- Enhanced Benefits
- Demographics



## HOW WE GOT HERE – INVESTMENT RETURN



Returns (after 2001) shown are gross returns, unreduced for administrative expenses, from CalPERS valuation reports, when available. The discount rate is based on expected returns net of administrative expenses.



## HOW WE GOT HERE – OLD CONTRIBUTION POLICY

- Effective with 2003 valuations:
  - Slow (15 year) recognition of investment losses into funded status
  - Rolling 30 year amortization of all (primarily investment) losses
- Designed to:
  - First smooth rates and
  - Second pay off UAL
- Mitigated contribution volatility



## HOW WE GOT HERE – ENHANCED BENEFITS

- At CalPERS, Enhanced Benefits implemented using all (future & prior) service
- Typically not negotiated with cost sharing
- Town of Los Gatos

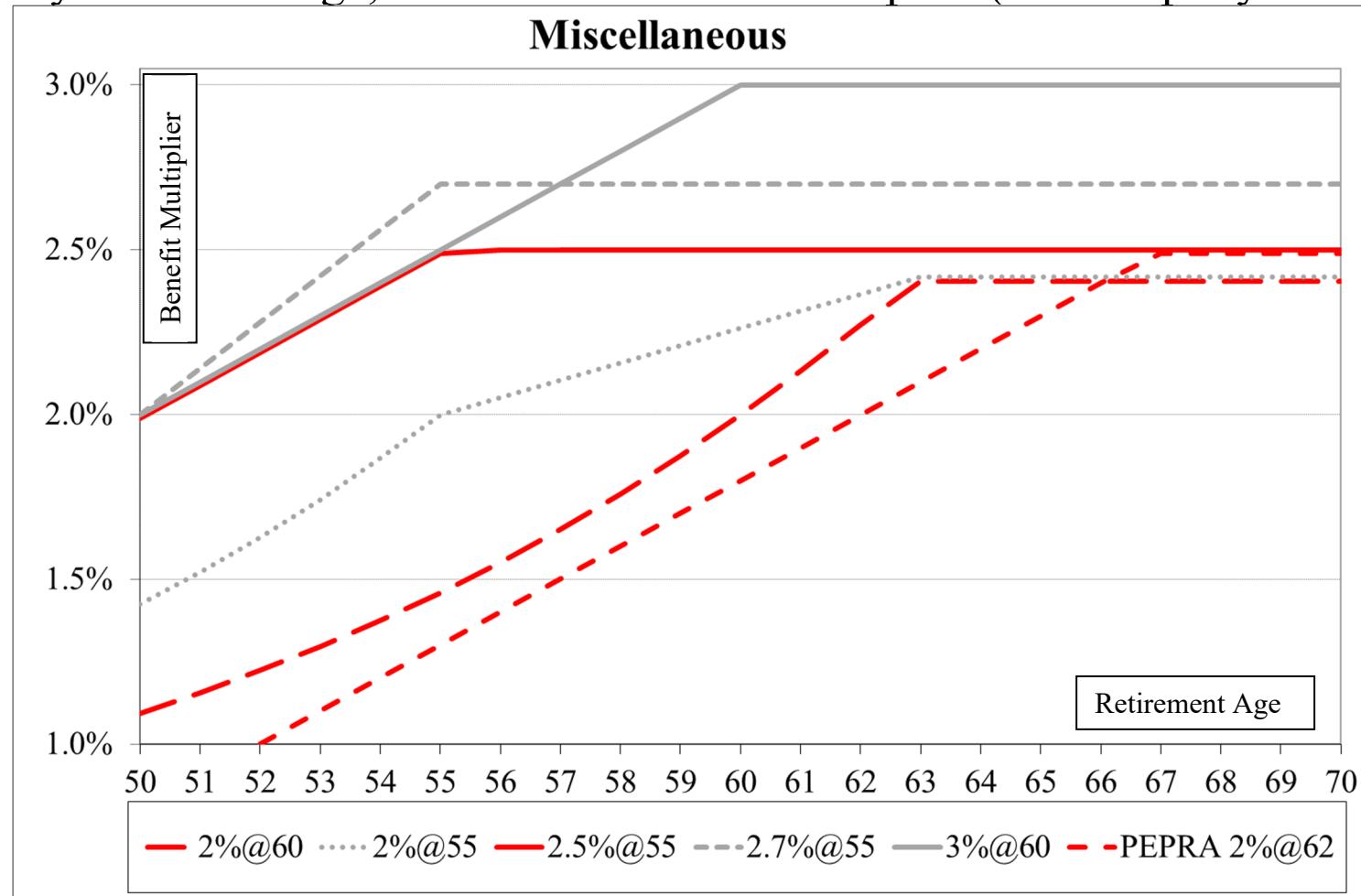
	<b>Tier 1</b>	<b>Tier 2</b>	<b>PEPRA</b>
● Miscellaneous	2.5%@55 FAC1	2%@60 FAC3 9/15/12	2%@62 FAC3
● Safety	3%@50 FAC1	N/A	2.7%@57 FAC3

- Note:
  - FAC1 is highest one year (typically final) average earnings
  - FAC3 is highest three years (typically final three) average earnings
- PEPRA tier implemented for new employees hired after 1/1/13
  - Employee pays half of total normal cost
  - 2023 Compensation limit
    - Social Security participants: \$146,042
    - Non-Social Security participants: \$175,250

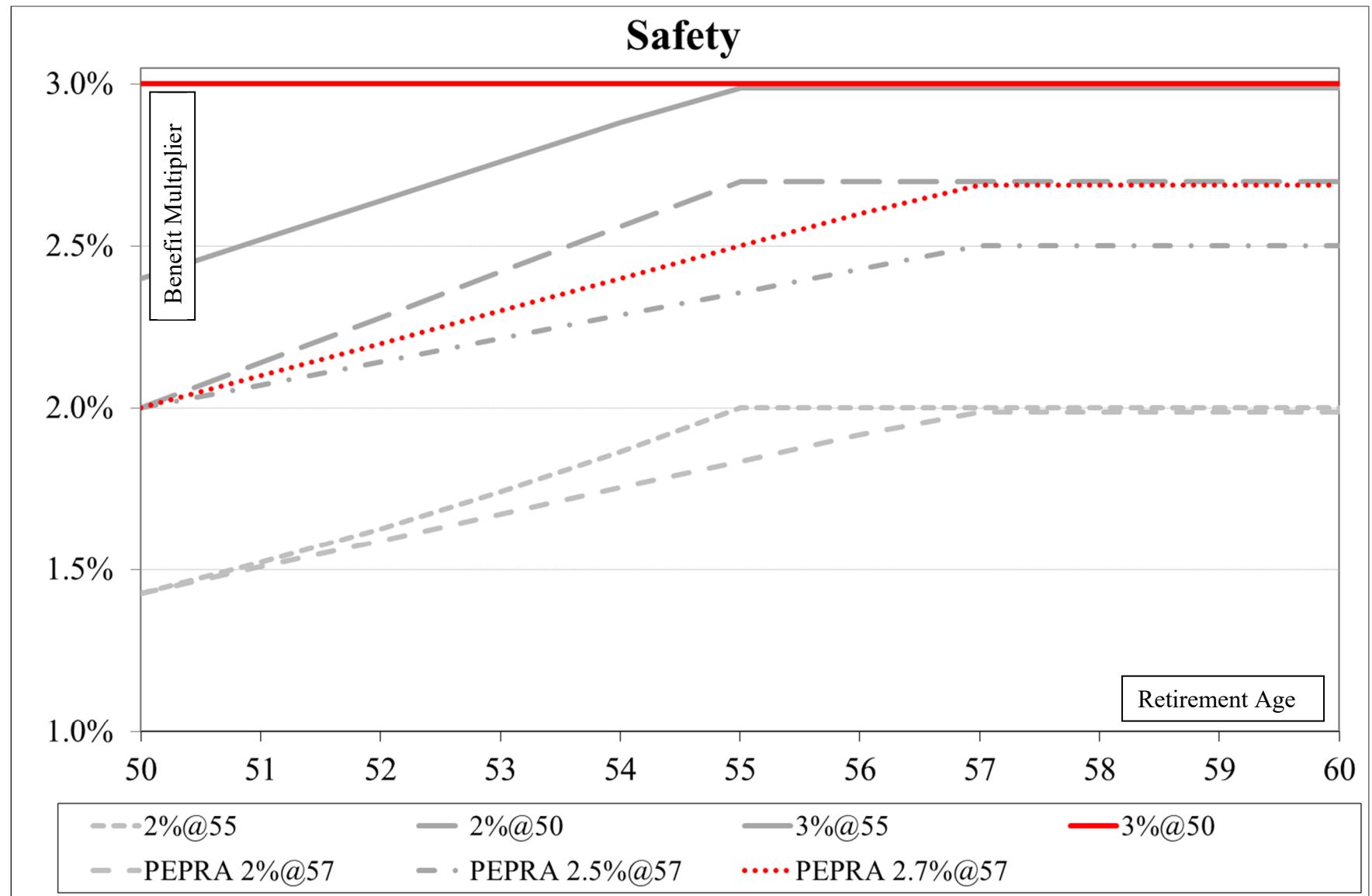


## HOW WE GOT HERE – ENHANCED BENEFITS

- Available CalPERS Benefit formulas. Town's formulas shown in red.
- For any retirement age, chart shows benefit multiplier (% FAE per year of service)



## HOW WE GOT HERE – ENHANCED BENEFITS



## HOW WE GOT HERE – DEMOGRAPHIC

- Around the State
  - Large retiree liability compared to actives
    - Public Agency average: 59% for Miscellaneous, 67% for Safety
  - Declining active population and increasing number of retirees
  - Higher percentage of retiree liability increases contribution volatility
- Town of Los Gatos percentage of liability belonging to retirees:
  - Miscellaneous 65%
  - Safety 74%



## CALPERS CHANGES

- April 2013: CalPERS adopted new contribution policy
  - No asset smoothing or rolling amortization
- February 2018: New amortization policy for 2021/22 contributions
  - Fixed dollar (level) 20-year amortization rather than % pay (escalating)
  - 5-year ramp up (not down) for investment gains and losses
- CalPERS Board changed the discount rate to 7%, still phasing in to rates:

	<u>Rate</u>	<u>Initial Impact</u>	<u>Full Impact</u>
● 6/30/16 valuation	7.375%	18/19	22/23
● 6/30/17 valuation	7.25%	19/20	23/24
● 6/30/18 valuation	7.00%	20/21	24/25
- In the November 2021 meeting, CalPERS Board adopted new
  - Discount rate and investment allocation
    - Discount rate: 6.8% for 6/30/2021. UAL impact matches investment gain amortization (5-year ramp-up). Initial impact in 23/24 and full impact in 27/28.
    - Asset allocation has higher investment risk than current portfolio
  - Experience study (Demographic assumptions)



## CALPERS CHANGES

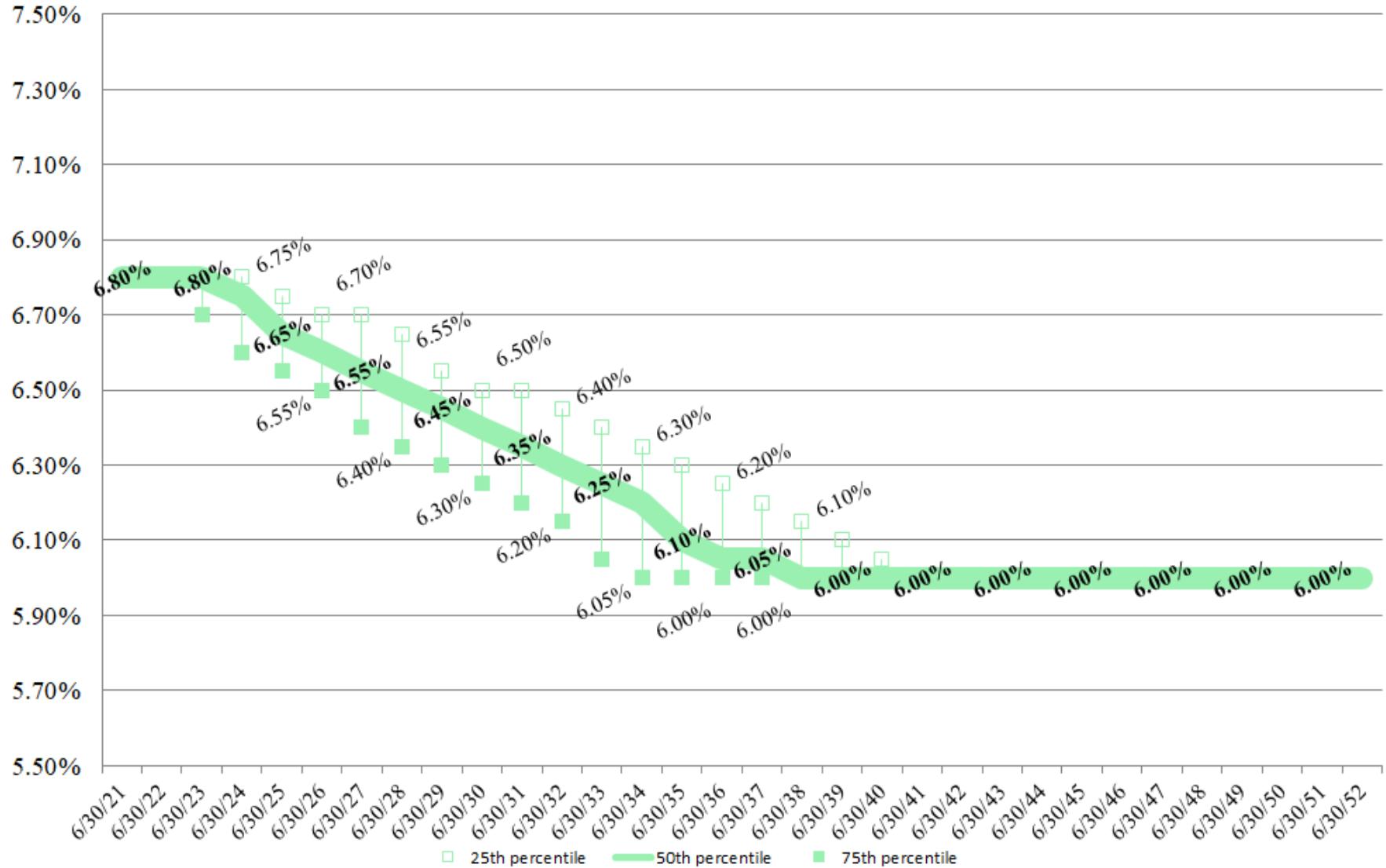
### ■ Risk Mitigation Strategy

- Move to more conservative investments over time to reduce volatility
  - Only when investment return is better than expected
  - Lower discount rate in concert
  - Essentially use  $\approx 50\%$  of investment gains to pay for cost increases
- Likely get to 6.0% discount rate over 20+ years
  - Risk mitigation suspended from 6/30/16 to 6/30/18 valuation
  - Did not trigger for 6/30/19 or 6/30/20 valuations
- First triggered for 6/30/21 valuation – 6.8% discount rate



# CALPERS CHANGES

## Discount Rate used as of Actuarial Valuation Date



# CALPERS CHANGES

## Capital Market Assumptions

Asset Class	Asset Segment	Near-Term Return (5-year)	Long-Term Return (20-year)	Volatility (20-year)
Growth	Global Equity – Cap Weighted	6.8%	6.8%	17.0%
	Global Equity – Non-Cap Weighted	5.1%	6.1%	13.5%
	Private Equity	8.9%	9.6%	30.1%
Income	Long U.S. Treasuries	0.1%	2.6%	12.4%
	Mortgage-Backed Securities	1.2%	2.8%	3.1%
	Investment Grade Corporates	0.1%	3.9%	8.5%
	Spread Product – High Yield	2.2%	4.7%	9.2%
	Spread Product – Sovereigns	3.2%	4.5%	10.4%
	High Yield Segment	2.2%	4.6%	9.0%
Real Assets	Real Estate	5.3%	5.5%	12.2%
Liquidity	Liquidity	0.3%	1.7%	0.8%
Other	Private Debt	6.8%	5.9%	9.9%
	Emerging Market Debt	2.7%	4.8%	10.3%



# CALPERS CHANGES

## Portfolio Target Allocations

	Prior Portfolio	11/17/21 Portfolio
<b>Asset Classification</b>		
Liquidity	1%	-
Real Assets	13%	15%
Private Debt	-	5%
EM Sov Bonds	1%	5%
High Yield	4%	5%
Investment Grade Corp.	6%	10%
Mtge-backed Securities	7%	5%
Treasury	10%	5%
Private Equity	8%	13%
Global Equity <sup>1</sup>	50%	42%
Leverage	<u>-</u>	<u>(5)%</u>
Total	100%	100%
<b>Standard Deviation</b>	11.2%	12.0%

<sup>1</sup> Cap and non-cap weighted combined for this table; actual portfolios have specific allocations for each classification.



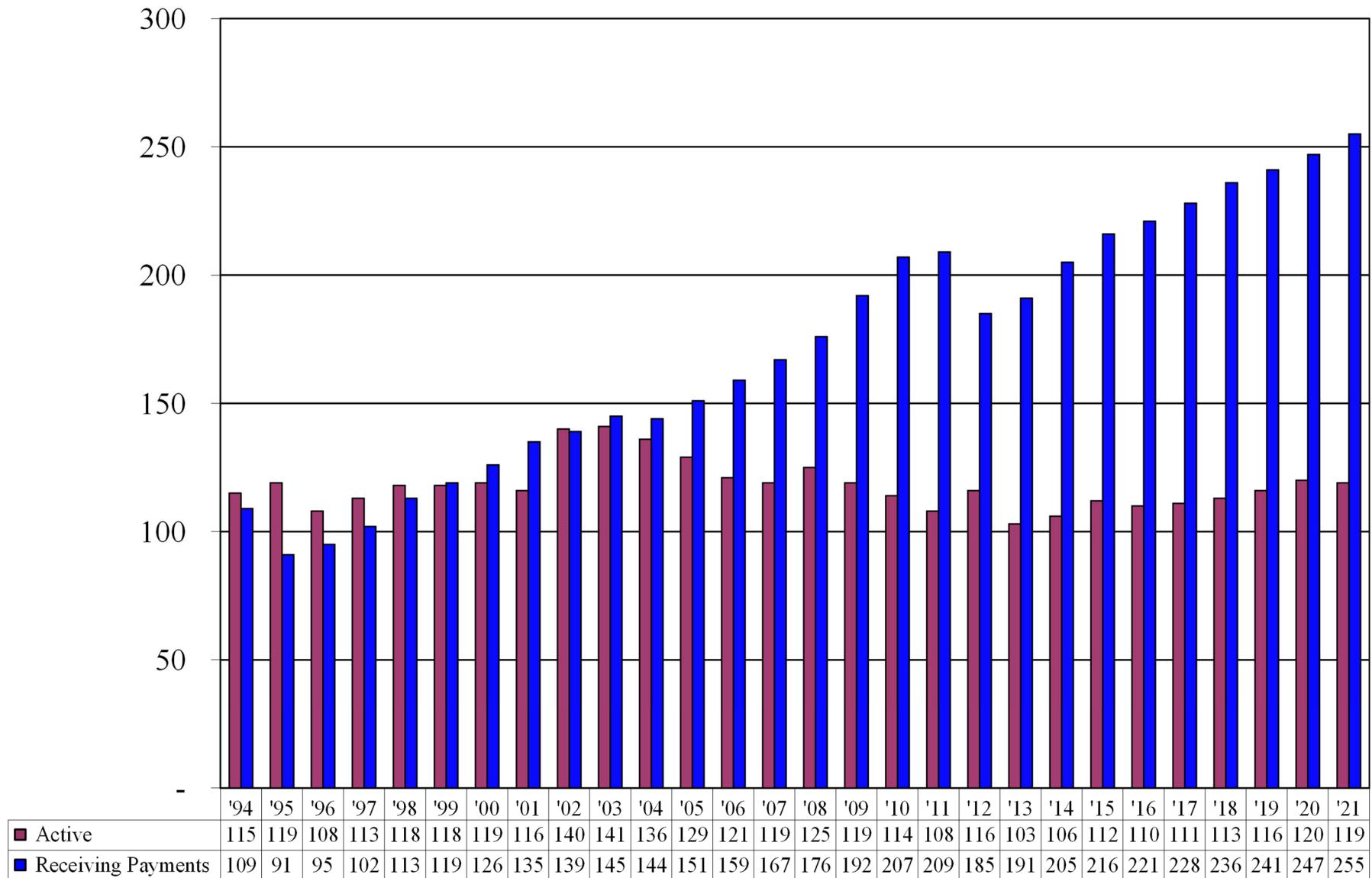
## SUMMARY OF DEMOGRAPHIC INFORMATION - MISCELLANEOUS

	2001	2011	2020	2021
<b>Actives</b>				
■ Counts	116	108	120	119
■ Average				
• Age	46	48	45	45
• Town Service	9	10	8	8
• PERSable Wages	\$ 56,900	\$ 79,800	\$ 98,000	\$ 100,600
■ Total PERSable Wages	6,600,000	8,600,000	11,800,000	12,000,000
<b>Inactive Members</b>				
■ Counts				
• Transferred	76	88	101	101
• Separated	67	72	88	91
• Retired				
□ Service	109	178	213	220
□ Disability	9	11	12	13
□ Beneficiaries	<u>17</u>	<u>20</u>	<u>22</u>	<u>22</u>
□ Total	135	209	247	255
■ Average Annual Town Provided Benefit for Service Retirees <sup>2</sup>	9,700	18,300	26,600	27,000

<sup>2</sup> Average Town-provided pensions are based on Town service & Town benefit formula, and are not representative of benefits for long-service employees.



## SUMMARY OF DEMOGRAPHIC INFORMATION - MISCELLANEOUS



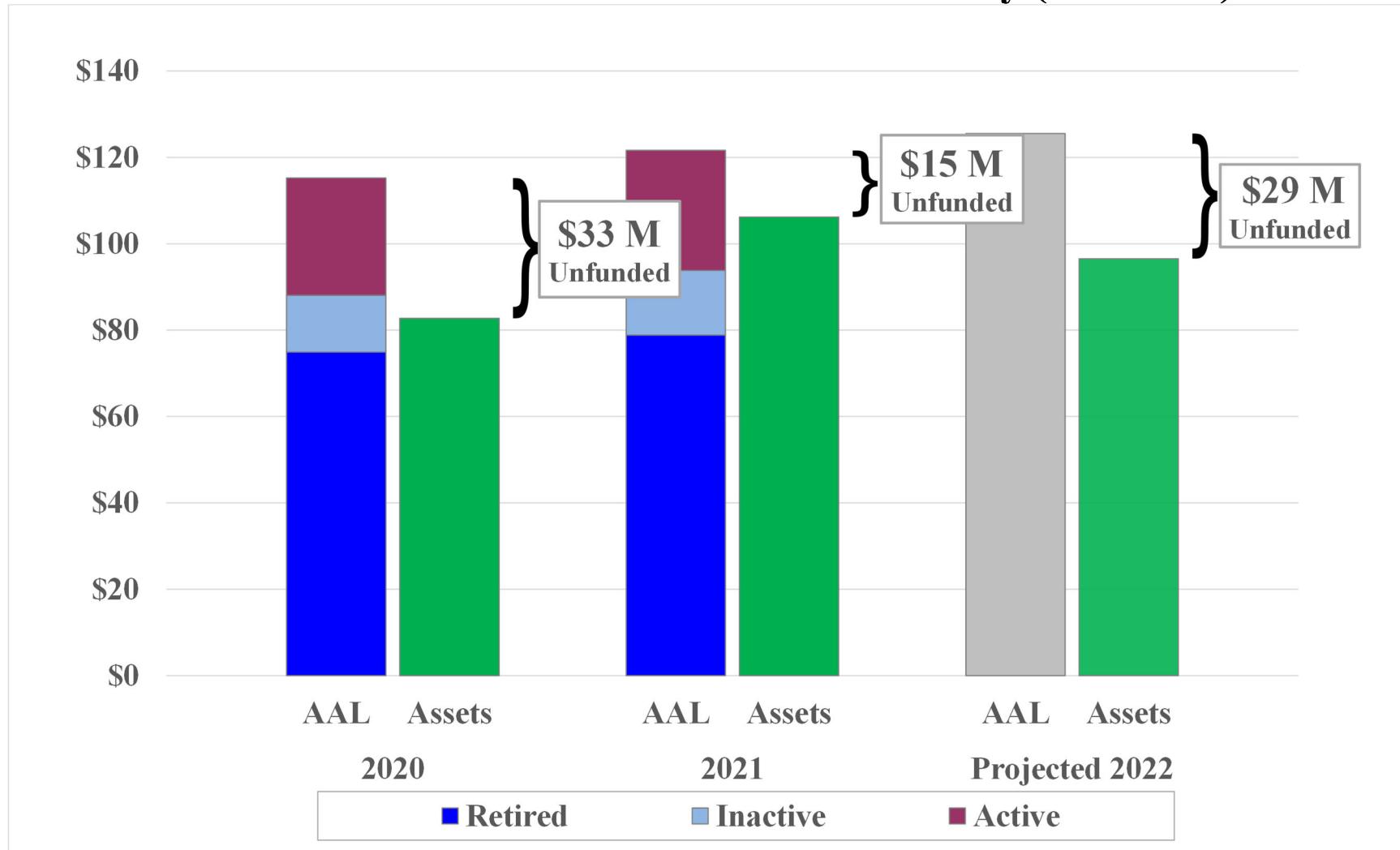
## PLAN FUNDED STATUS - MISCELLANEOUS

	<u>June 30, 2020</u>	<u>June 30, 2021</u>
<b>■ Actuarial Accrued Liability</b>		
● Active	\$27,200,000	\$27,800,000
● Retiree	74,900,000	78,800,000
● Inactive	<u>13,100,000</u>	<u>15,000,000</u>
● Total	115,200,000	121,600,000
<b>■ Assets</b>	<u>82,700,000</u>	<u>106,200,000</u>
<b>■ Unfunded Liability</b>	32,500,000	15,400,000
<b>■ Funded Ratio</b>	71.8%	87.3%
<b>■ Average funded ratio for CalPERS Public Agency Miscellaneous Plans</b>	72.3%	83.7%



## PLAN FUNDED STATUS - MISCELLANEOUS

### Town CalPERS Assets and Actuarial Liability (\$Millions)<sup>3</sup>



<sup>3</sup> Projected 2022 assets reflect -7.5% CalPERS investment return for 2021/22.



## PLAN FUNDED STATUS - MISCELLANEOUS

### Discount Rate Sensitivity

June 30, 2021

	<b>Discount Rate</b>		
	<u>6.80%</u>	<u>6.30%<sup>4</sup></u>	<u>5.80%</u>
<b>AAL</b>	\$121,600,000	\$129,700,000	\$137,700,000
<b>Assets</b>	<u>106,200,000</u>	<u>106,200,000</u>	<u>106,200,000</u>
<b>Unfunded Liability</b>	15,400,000	23,500,000	31,500,000
<b>Funded Ratio</b>	87.3%	81.9%	77.1%

<sup>4</sup> Estimated by Foster & Foster.



## PLAN FUNDED STATUS - MISCELLANEOUS

### Unfunded Accrued Liability Changes

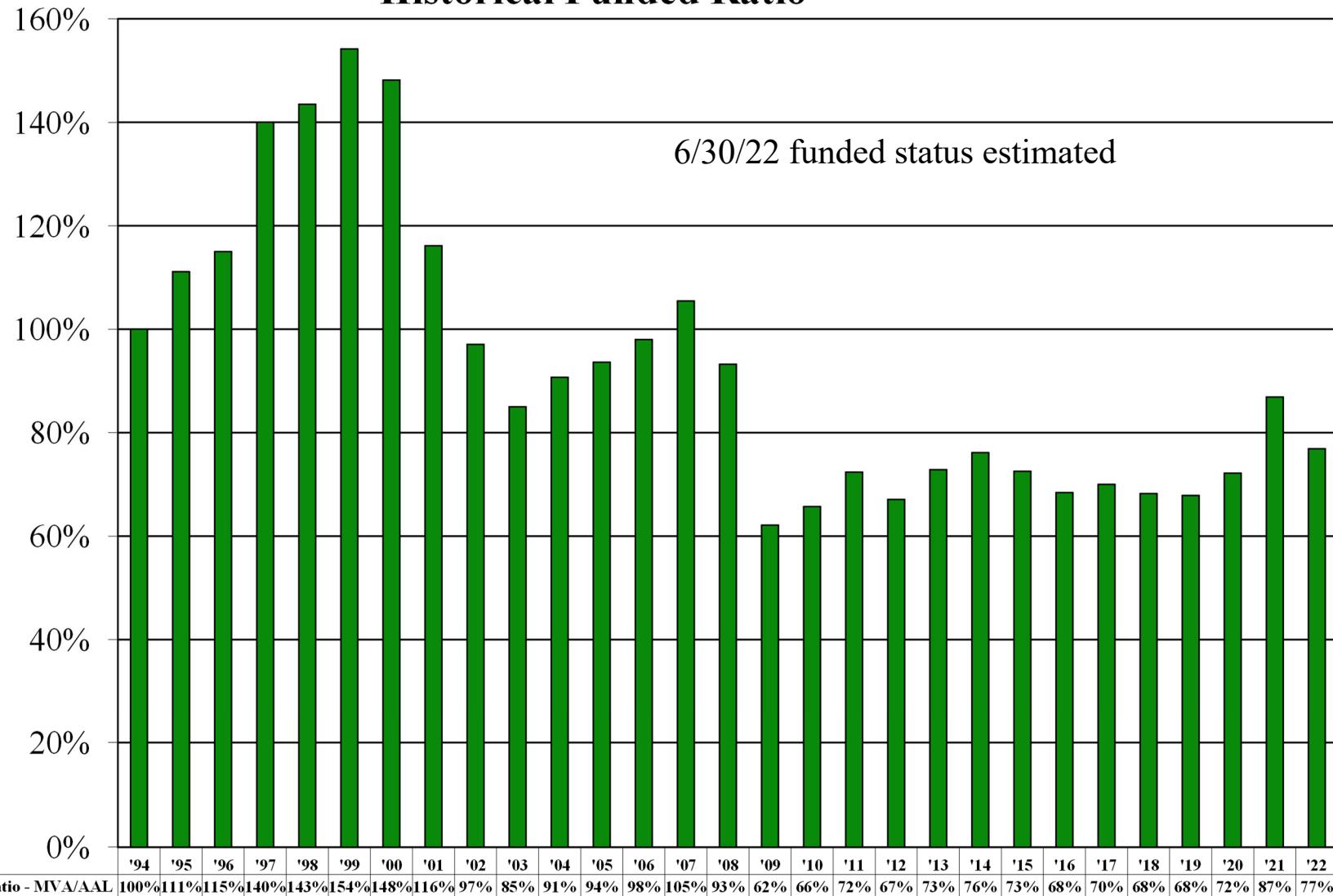
■ <b>Unfunded Accrued Liability on 6/30/20</b>	\$ 32,500,000
■ <b>Expected 6/30/21 Unfunded Accrued Liability</b>	26,400,000
■ <b>Changes</b>	
• Assumption Change (demographics)	0
• Discount Rate 7% to 6.8%	2,800,000
• Asset Loss (Gain) (21.3% return for FY 2021)	(13,700,000)
• Contribution & Experience Loss (Gain)	<u>(100,000)</u>
• Total	<u>(11,000,000)</u>
■ <b>Unfunded Accrued Liability on 6/30/21</b>	15,400,000
■ <b>Projected Unfunded Accrued Liability on 6/30/22<sup>5</sup></b>	29,000,000

<sup>5</sup> Projected UAL reflects -7.5% CalPERS investment return for 2021/22.

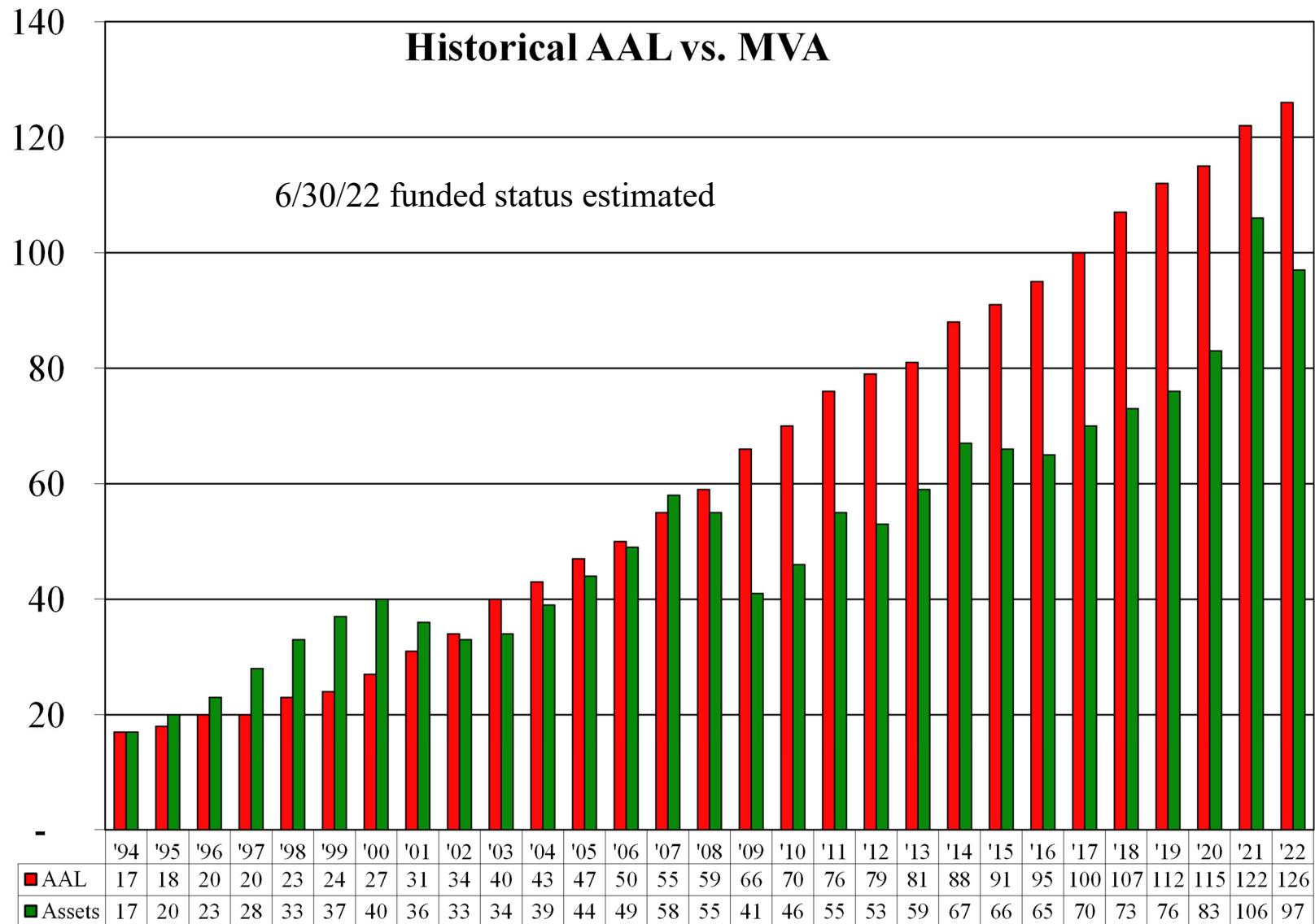


## FUNDED RATIO - MISCELLANEOUS

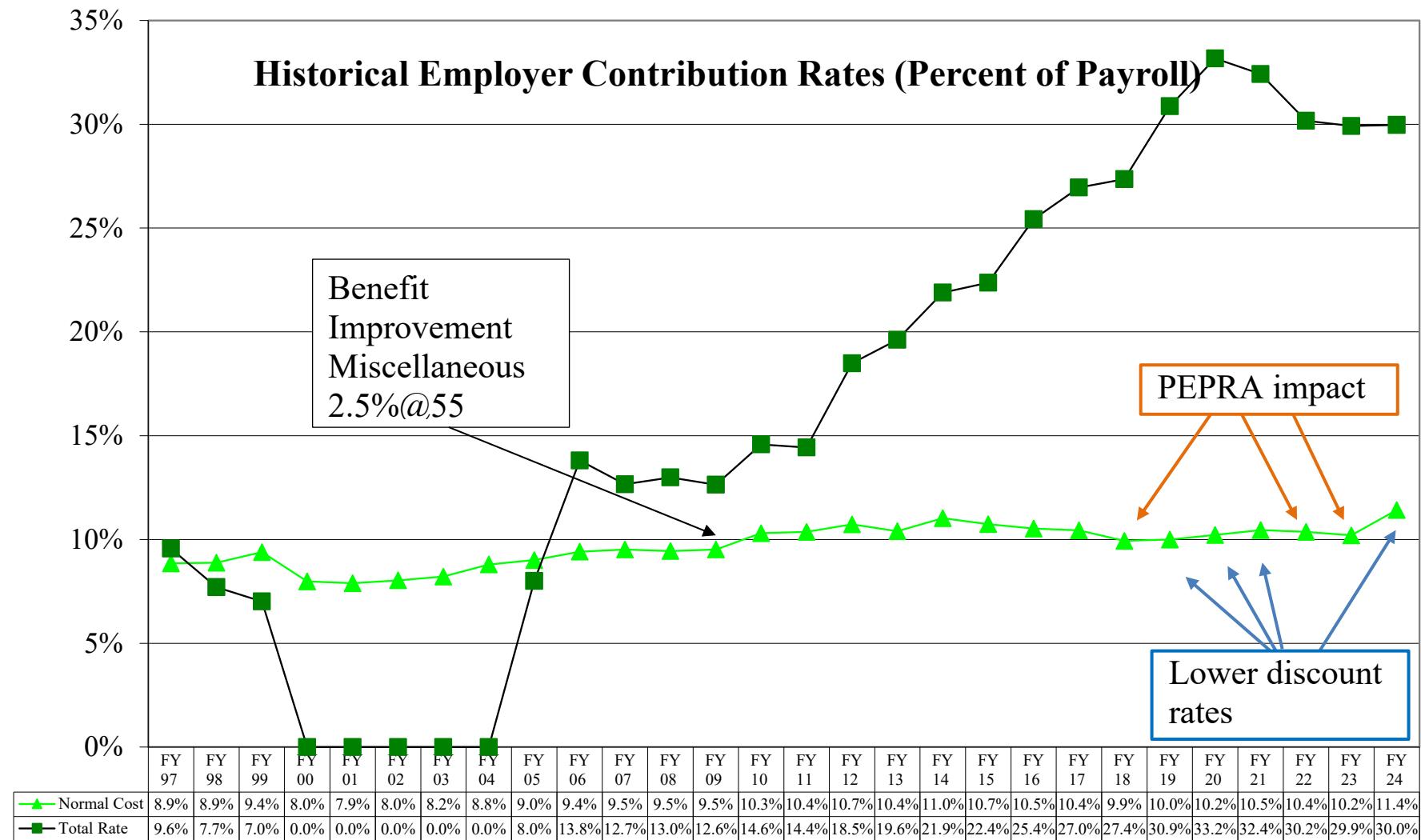
### Historical Funded Ratio



## FUNDED STATUS (MILLIONS) - MISCELLANEOUS



## CONTRIBUTION RATES - MISCELLANEOUS



FY21 & FY22 Total Rates reflect Additional Discretionary Payments (ADPs) of \$4,753,965 made October 2019, \$3,580,365 made July 2020, and \$2,050,942 in April 2021.



## CONTRIBUTION RATES - MISCELLANEOUS

	<u>6/30/20</u>	<u>6/30/21</u>
	<u>2022/2023</u>	<u>2023/2024</u>
■ Total Normal Cost	17.6%	18.8%
■ Employee Normal Cost	<u>7.4%</u>	<u>7.4%</u>
■ Employer Normal Cost	10.2%	11.4%
■ Amortization Payments	<u>19.7%</u>	<u>18.5%<sup>6</sup></u>
■ Total Employer Contribution Rate	29.9%	30.0%
■ 2022/23 Employer Contribution Rate		29.9%
● Payroll Changes		0.2%
● 6/30/17 Discount Rate & Inflation (5 <sup>th</sup> Year)		0.2%
● 6/30/18 Discount Rate change (4 <sup>th</sup> Year)		0.6%
● 6/30/21 Demographic Assumption change (no ramp)		0.7%
● 6/30/21 Risk Mitigation (6.8%) (Normal Cost change)		0.8%
● Other (Gains)/Losses mainly net investment gain		<u>(2.4%)</u>
■ 2023/24 Employer Contribution Rate		30.0%

<sup>6</sup> Equivalent to 18.8% of UAL. One year, 6.8% interest on the UAL is 6.7% of payroll. 2023/24 amortization payment exceeds interest on the UAL, so there is no “negative amortization.”



## CONTRIBUTION PROJECTIONS - MISCELLANEOUS

- Investment returns:
  - June 30, 2022 (7.5%)<sup>7</sup>
  - Future returns based on stochastic analysis using 1,000 trials
  - Single year returns<sup>8</sup> with current investment mix, no risk mitigation
- Assumes investment returns will generally be lower over the next 10 years and higher beyond that.
- Discount Rate decreases due to Risk Mitigation policy – Ultimate rate 6.0%
- No Other: Gains/Losses, Method/Assumption Changes, Benefit Improvements
- Different from CalPERS projection
- Impact of Risk Mitigation Policy:
  - Net impact of investment gain and discount rate change amortized over 20 years with 5 year ramp up; same amortization method for all future years
- Projected payroll FY 2023-2027 from City budget projections

<sup>7</sup> Final return based on CalPERS 2022 ACFR.

<sup>8</sup> N<sup>th</sup> percentile means N percentage of our trials result in returns lower than the indicated rates.



## CONTRIBUTION PROJECTIONS - MISCELLANEOUS

- New hire assumptions:
  - All new hires assumed PEPRA members and none are Classic members
- 6/30/21 employee distribution:

Benefit Tier	Count	% of Total	20/21 Payroll	% of Total
● 2.5%@55 FAC1	32	26.9%	\$3,511,394	29.3%
● 2%@60 FAC3	25	21.0%	3,344,416	27.9%
● 2%@62 FAC3 (PEPRA)	62	52.1%	5,114,292	42.7%

- Town provided payroll for contribution years:

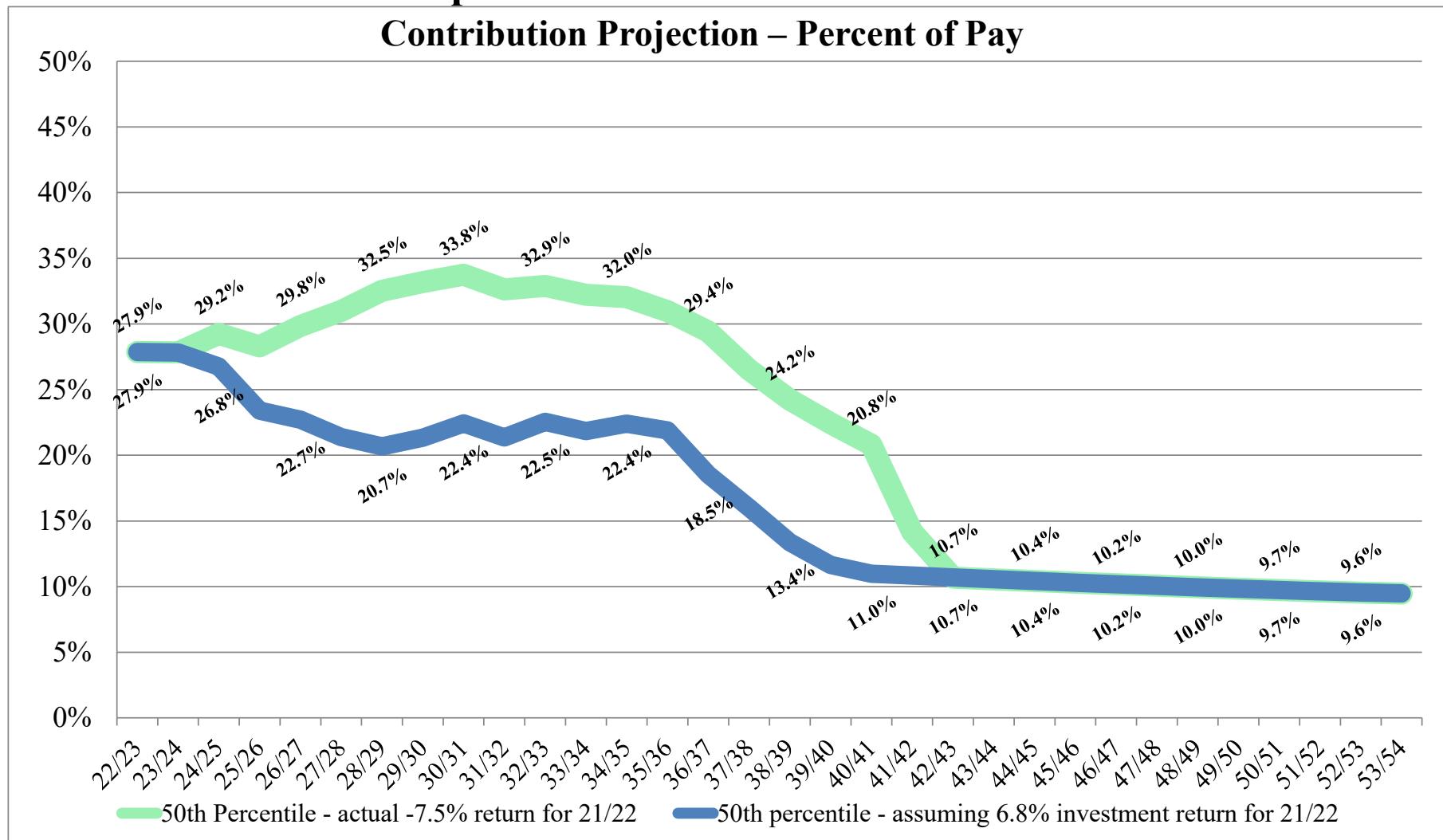
FYE	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29
Payroll (000s)	\$14,241	\$14,695	\$15,128	\$15,388	\$15,747	\$16,111	\$16,439



## CONTRIBUTION PROJECTIONS - MISCELLANEOUS

### Impact of 21/22 Investment Return

#### Contribution Projection – Percent of Pay

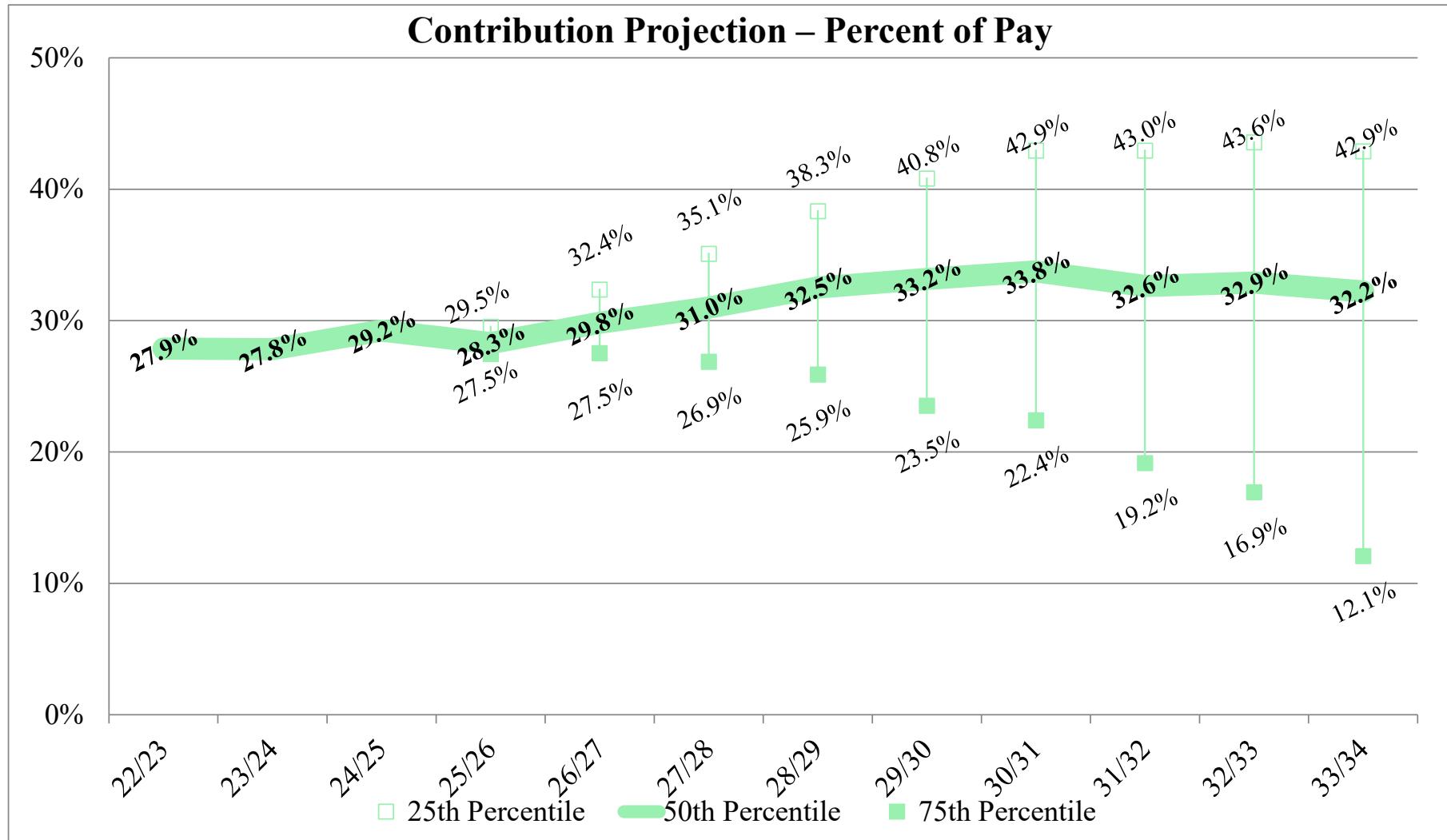


## CONTRIBUTION PROJECTIONS - MISCELLANEOUS

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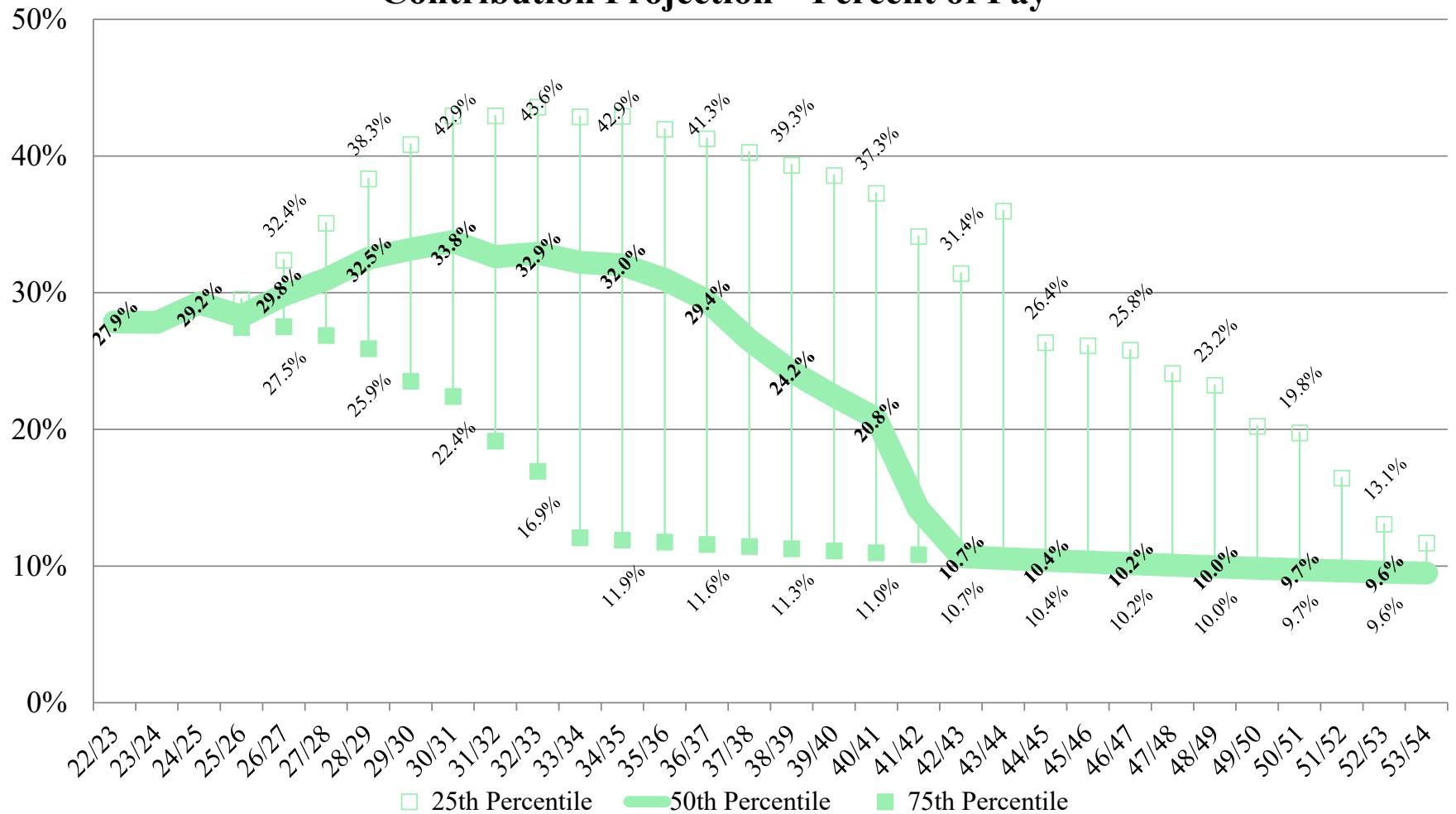


## CONTRIBUTION PROJECTIONS - MISCELLANEOUS



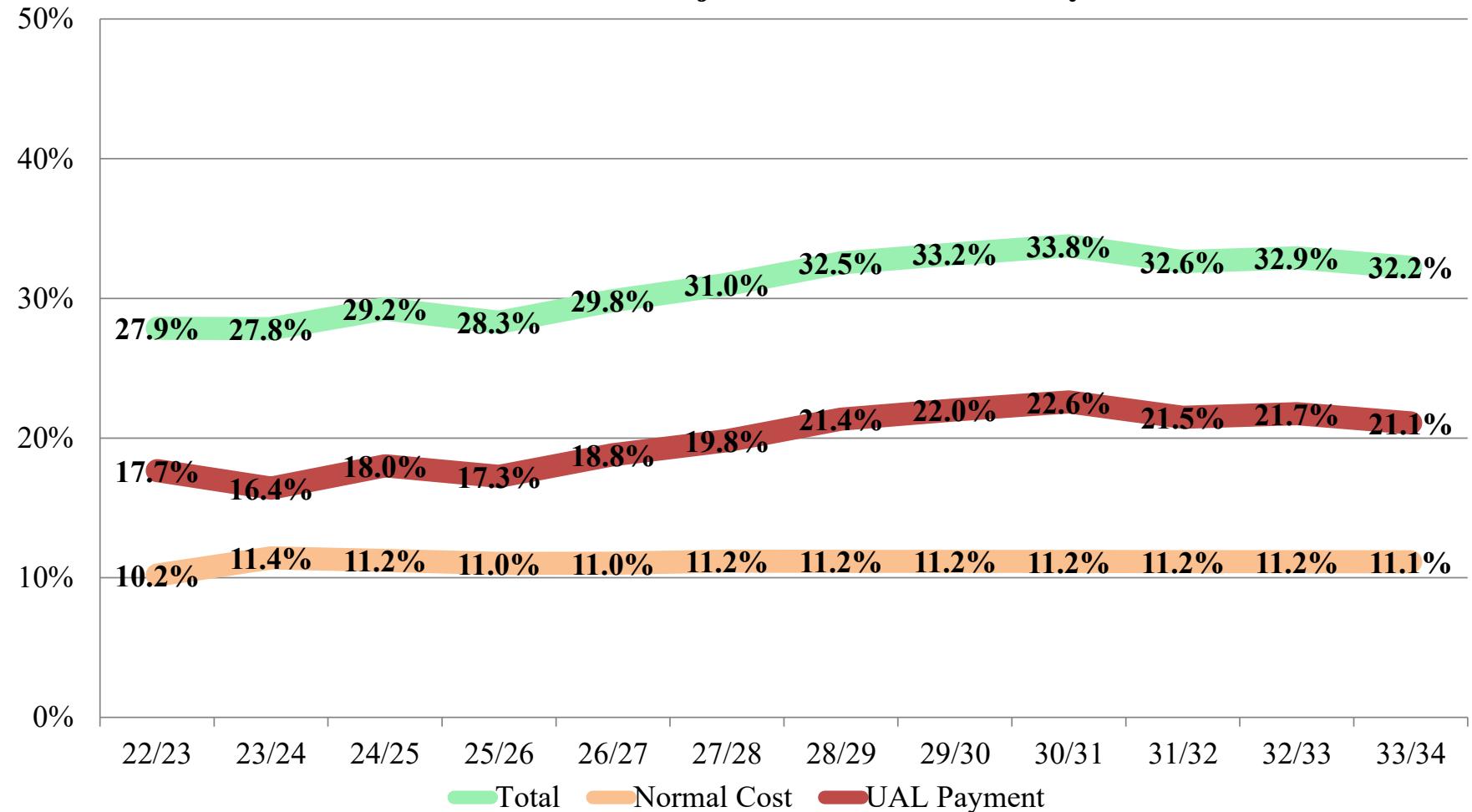
# CONTRIBUTION PROJECTIONS - MISCELLANEOUS

## Contribution Projection – Percent of Pay

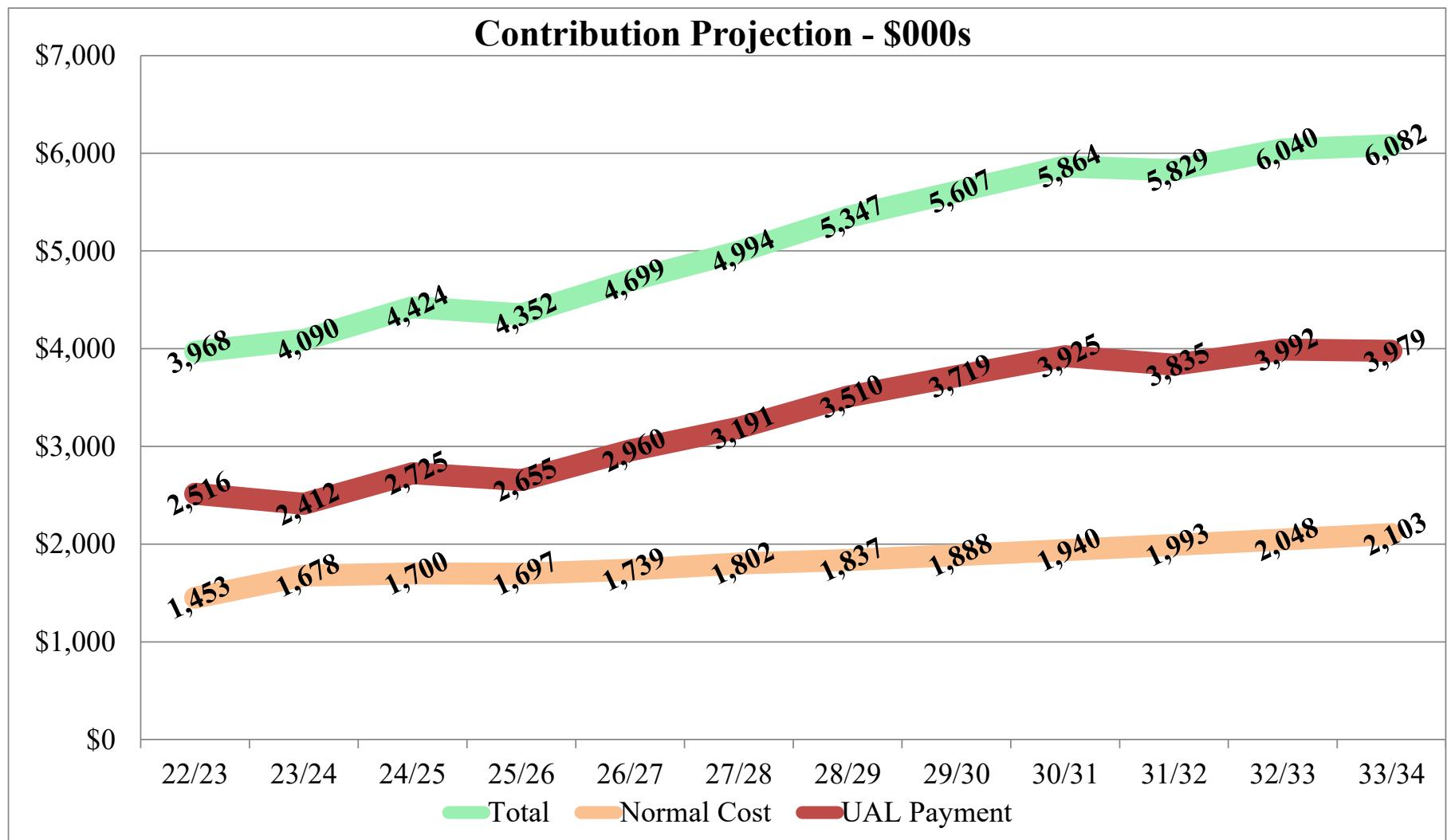


## CONTRIBUTION PROJECTIONS - MISCELLANEOUS

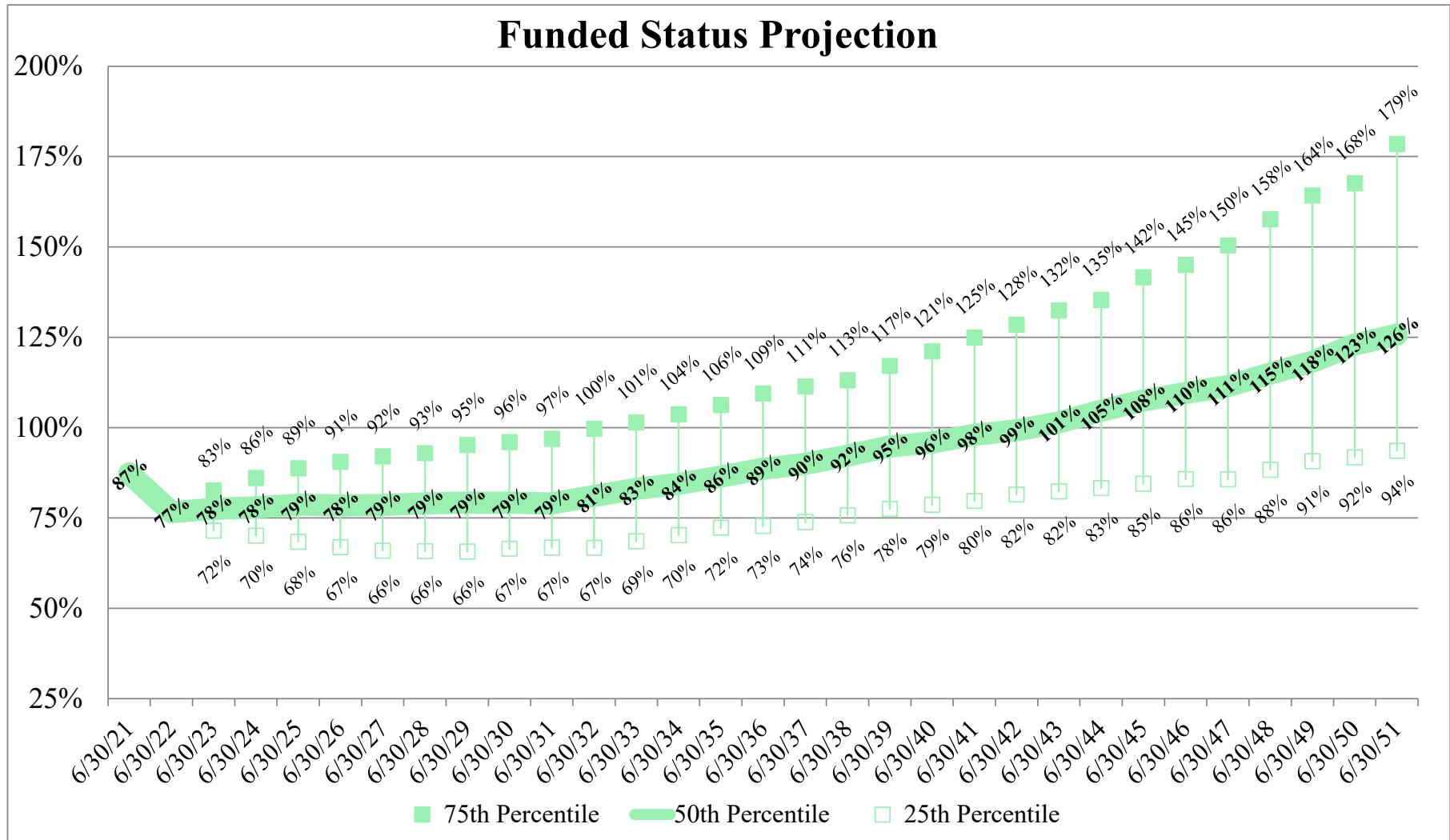
### Contribution Projection – Percent of Pay



## CONTRIBUTION PROJECTIONS - MISCELLANEOUS



# FUNDED STATUS - MISCELLANEOUS

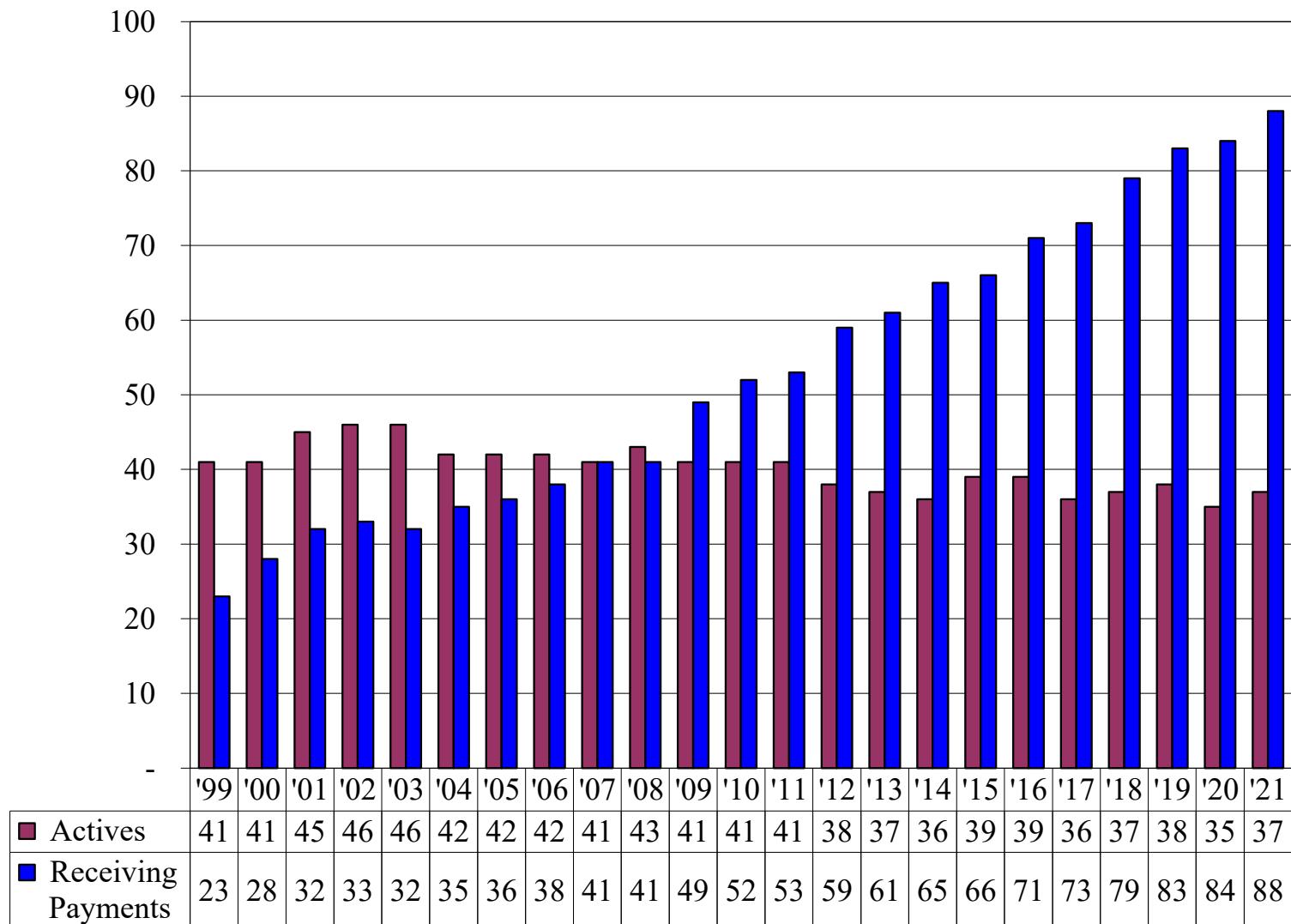


## SUMMARY OF DEMOGRAPHIC INFORMATION - SAFETY

	2012	2016	2020	2021
<b>Actives</b>				
■ Counts	38	39	35	37
■ Average PERSable Wages	\$ 128,000	\$ 129,000	\$ 152,900	\$ 149,900
■ Total PERSable Wages	4,900,000	5,000,000	5,300,000	5,500,000
<b>Inactive Members</b>				
■ Counts				
• Transferred	15	14	13	13
• Separated	3	2	3	3
• Receiving Payments	59	71	84	88



## SUMMARY OF DEMOGRAPHIC INFORMATION - SAFETY



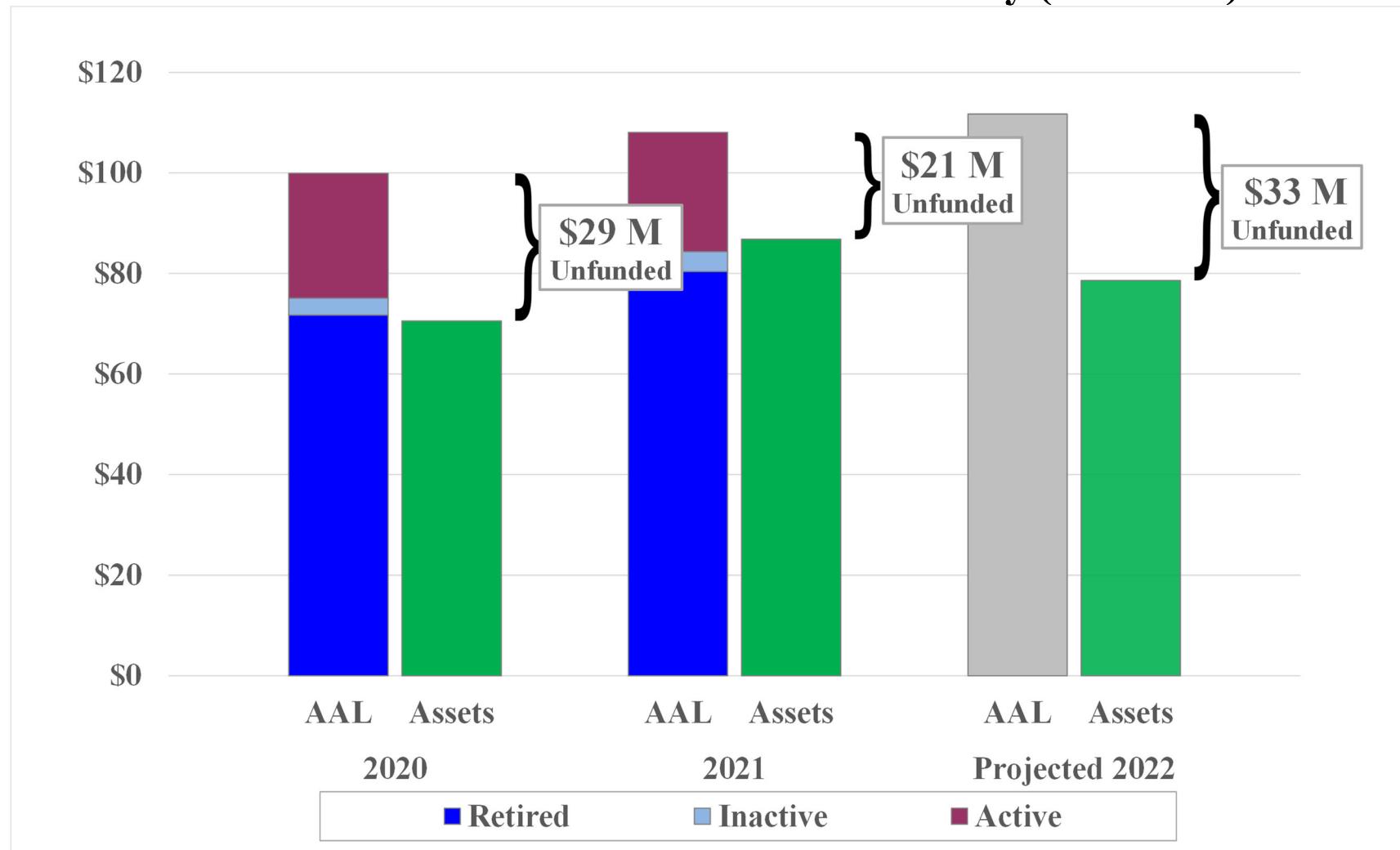
## PLAN FUNDED STATUS - SAFETY

	<u>June 30, 2020</u>	<u>June 30, 2021</u>
<b>■ Actuarial Accrued Liability</b>		
● Active	\$24,800,000	\$23,700,000
● Retiree	71,700,000	80,400,000
● Inactive	<u>3,400,000</u>	<u>4,000,000</u>
● Total	99,900,000	108,100,000
<b>■ Assets</b>	<u>70,500,000</u>	<u>86,800,000</u>
<b>■ Unfunded Liability</b>	29,400,000	21,300,000
<b>■ Funded Ratio</b>	70.6%	80.3%
<b>■ Average funded ratio for CalPERS Public Agency Safety Plans</b>	69.2%	80.9%



## PLAN FUNDED STATUS - SAFETY

### Town CalPERS Assets and Actuarial Liability (\$Millions)<sup>9</sup>



<sup>9</sup> Projected 2022 assets reflects -7.5% CalPERS investment return for 2021/22.



## PLAN FUNDED STATUS - SAFETY

### Discount Rate Sensitivity

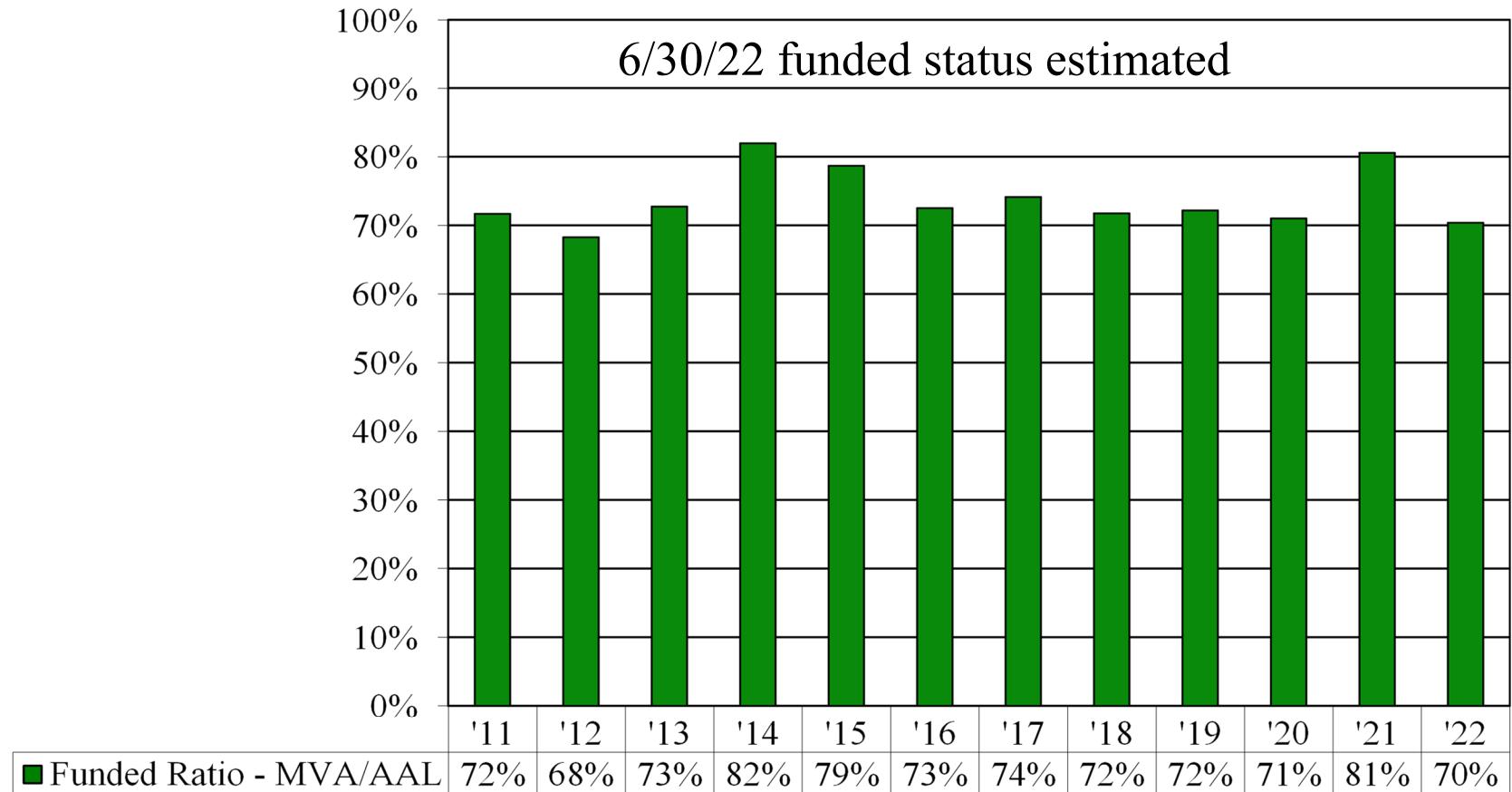
June 30, 2021

	<b>Discount Rate</b>		
	<u>6.80%</u>	<u>6.30%</u> <sup>10</sup>	<u>5.80%</u>
<b>AAL</b>	\$108,100,000	\$115,500,000	\$122,900,000
<b>Assets</b>	<u>86,800,000</u>	<u>86,800,000</u>	<u>86,800,000</u>
<b>Unfunded Liability</b>	21,300,000	28,700,000	36,100,000
<b>Funded Ratio</b>	80.3%	75.2%	70.6%

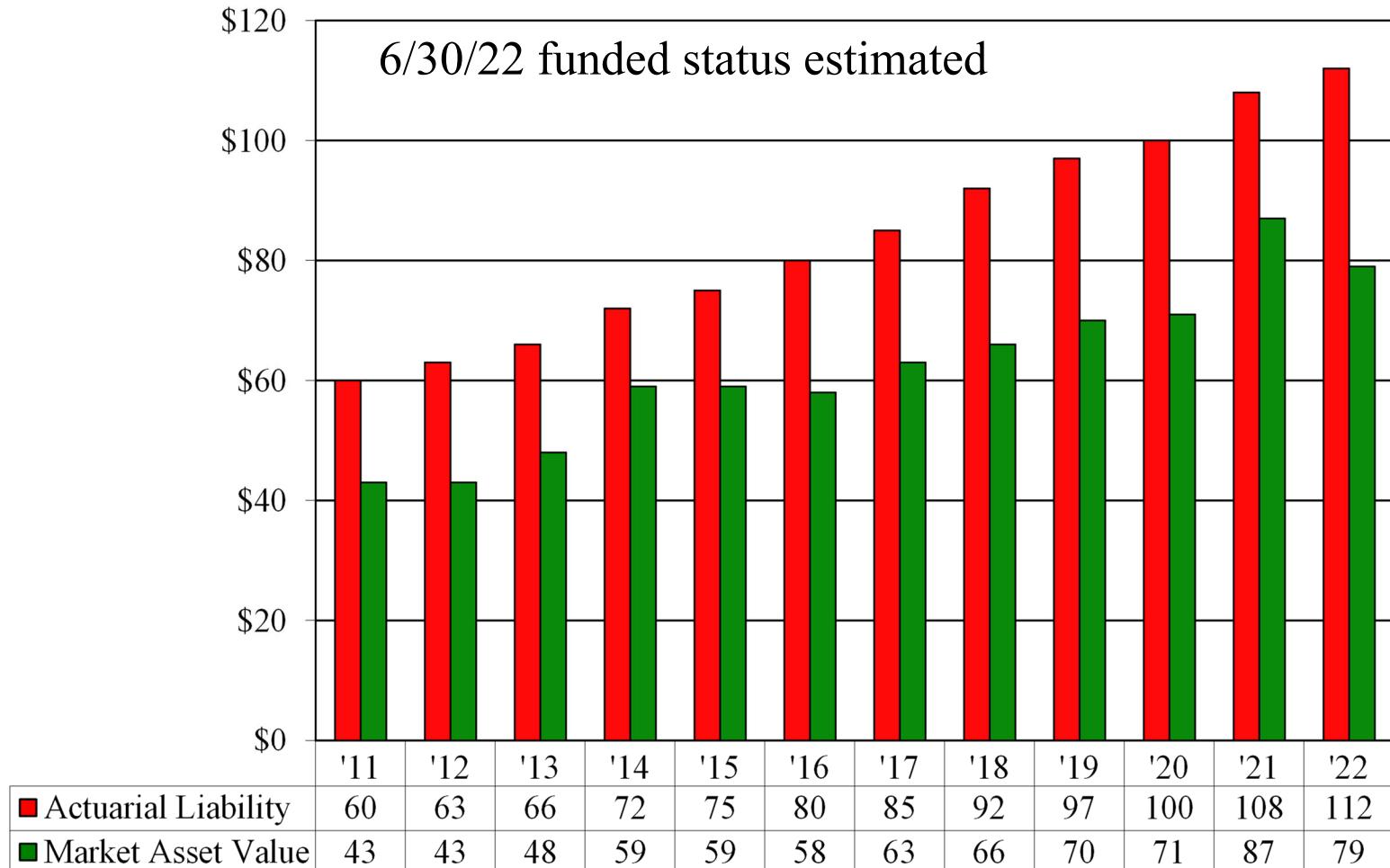
<sup>10</sup> Estimated by Foster & Foster.



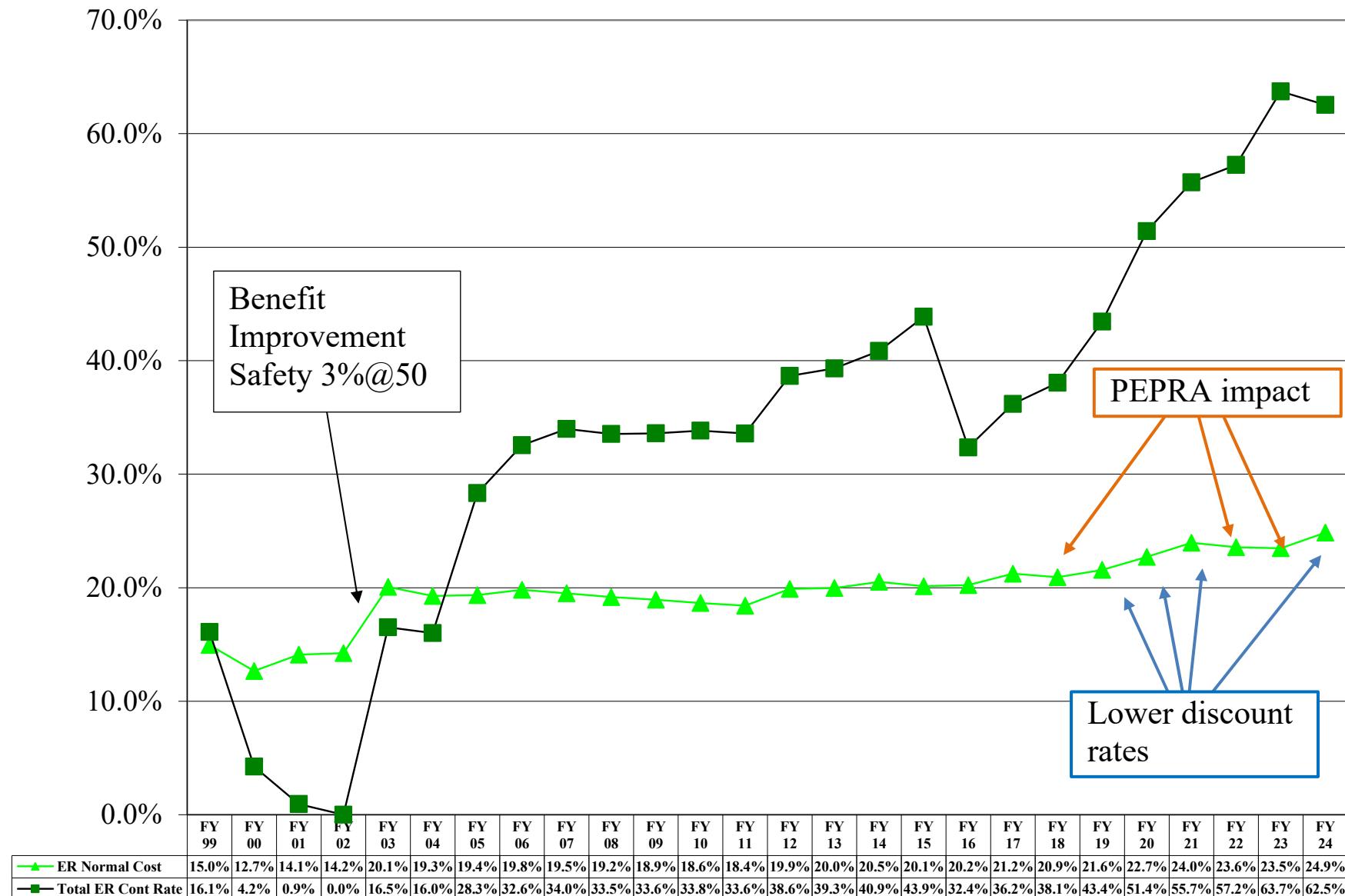
## FUNDED RATIO - SAFETY



## FUNDED STATUS (MILLIONS) - SAFETY



# CONTRIBUTION RATES - SAFETY



## CONTRIBUTION RATES - SAFETY

<b>6/30/21 Valuation</b>			
<b>2023/2024 Contribution Rates</b>			
	<b>Total<sup>11</sup></b>	<b>Tier 1</b>	<b>PEPRA</b>
	<b>3%@50</b>	<b>2.7%@57</b>	
■ Base Total Normal Cost	32.5%	34.60%	27.3%
■ Class 1 Benefits			
● Final One Year Compensation	1.0%	1.50%	-
● PRSA	<u>1.9%</u>	<u>2.00%</u>	<u>1.7%</u>
■ Total Normal Cost	35.4%	38.10%	29.0%
■ Formula's Expected EE Contr. Rate	<u>10.6%</u>	<u>9.00%</u>	<u>14.5%</u>
■ Employer Normal Cost	24.9%	29.10%	14.5%
■ Amortization Payment	37.7%	53.10%	-
■ Amortization of Side Fund	-	-	-
<b>■ Total Employer Contribution</b>	<b>62.5%</b>	<b>82.20%</b>	<b>14.5%</b>
■ Employee counts	37	24	13
■ Employee payroll (in 000's)	\$ 6,026	\$4,276	\$ 1,751
<b>■ Total ER Contribution \$ (in 000's)</b>	<b>\$ 3,769</b>	<b>\$3,515</b>	<b>\$ 254</b>

<sup>11</sup> Weighting of total contribution based on projected classic and PEPRA payrolls



## CONTRIBUTION RATES - SAFETY

	<u>6/30/20</u>	<u>6/30/21</u>
	<u>2022/2023</u>	<u>2023/2024</u>
■ Total Normal Cost	33.3%	35.4%
■ Employee Normal Cost	<u>9.9%</u>	<u>10.6%</u>
■ Employer Normal Cost	23.5%	24.9%
■ Amortization Payments	<u>40.3%</u>	<u>37.7%</u> <sup>12</sup>
■ Total Employer Contribution Rate	63.7%	62.5%
■ 2022/23 Employer Contribution Rate		63.7%
● Payroll Changes		(0.4%)
● 6/30/17 Discount Rate & Inflation (5 <sup>th</sup> Year)		0.7%
● 6/30/18 Discount Rate change (4 <sup>th</sup> Year)		1.0%
● 6/30/21 Demographic Assumption change		1.8%
● 6/30/21 Risk Mitigation (Normal Cost change)		0.7%
● Other (Gains)/Losses mainly net investment gain		<u>(5.0%)</u>
■ 2023/24 Employer Contribution Rate		62.5%

<sup>12</sup> Equivalent to 11.4% of UAL. One year, 6.8% interest on the UAL is 22.4% of payroll. 2023/24 amortization payment exceeds interest on the UAL, so there is no “negative amortization.”



## CONTRIBUTION PROJECTION - SAFETY

- Investment returns:
  - June 30, 2022 (7.5%)<sup>13</sup>
  - Future returns based on stochastic analysis using 1,000 trials
  - Single year returns<sup>14</sup> with current investment mix, no risk mitigation:

	Percentile		
	25 <sup>th</sup>	50 <sup>th</sup>	75 <sup>th</sup>
First 10 years	<b>-1.8%</b>	<b>6.0%</b>	<b>14.7%</b>
After 10 years	<b>-0.7%</b>	<b>7.5%</b>	<b>16.4%</b>
- Assumes investment returns will generally be lower over the next 10 years and higher beyond that.
- Discount Rate decreases due to Risk Mitigation policy – Ultimate rate 6.0%
- No Other: Gains/Losses, Method/Assumption Changes, Benefit Improvements
- Different from CalPERS projection
- Impact of Risk Mitigation Policy:
  - Net impact of investment gain and discount rate change amortized over 20 years with 5 year ramp up; same amortization method for all future years
- Projected payroll FY 2023-2027 from City budget projections

<sup>13</sup> Final return based on CalPERS 2022 ACFR.

<sup>14</sup> N<sup>th</sup> percentile means N percentage of our trials result in returns lower than the indicated rates.



## CONTRIBUTION PROJECTION - SAFETY

- New hire assumptions:
  - All new hires assumed PEPRA members and none are Classic members
- 6/30/21 employee distribution:

Benefit Tier	Count	% of Total	20/21 Payroll	% of Total
● 3%@50 FAE1	24	64.9%	\$3,935,891	71.0%
● 2.7%@57 FAE3 (PEPRA)	13	35.1%	1,611,346	29.0%

- Employee Cost Sharing of Employer Contribution:
  - 3% of pay employee share for Classic members
- Town provided payroll (000s) for contribution years:

FYE	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29
Classic	\$3,982	\$4,113	\$4,204	\$4,290	\$4,375	\$4,462	\$4,551
PEPRA	2,438	2,586	2,712	2,810	2,869	2,927	2,985



# CONTRIBUTION PROJECTION - SAFETY

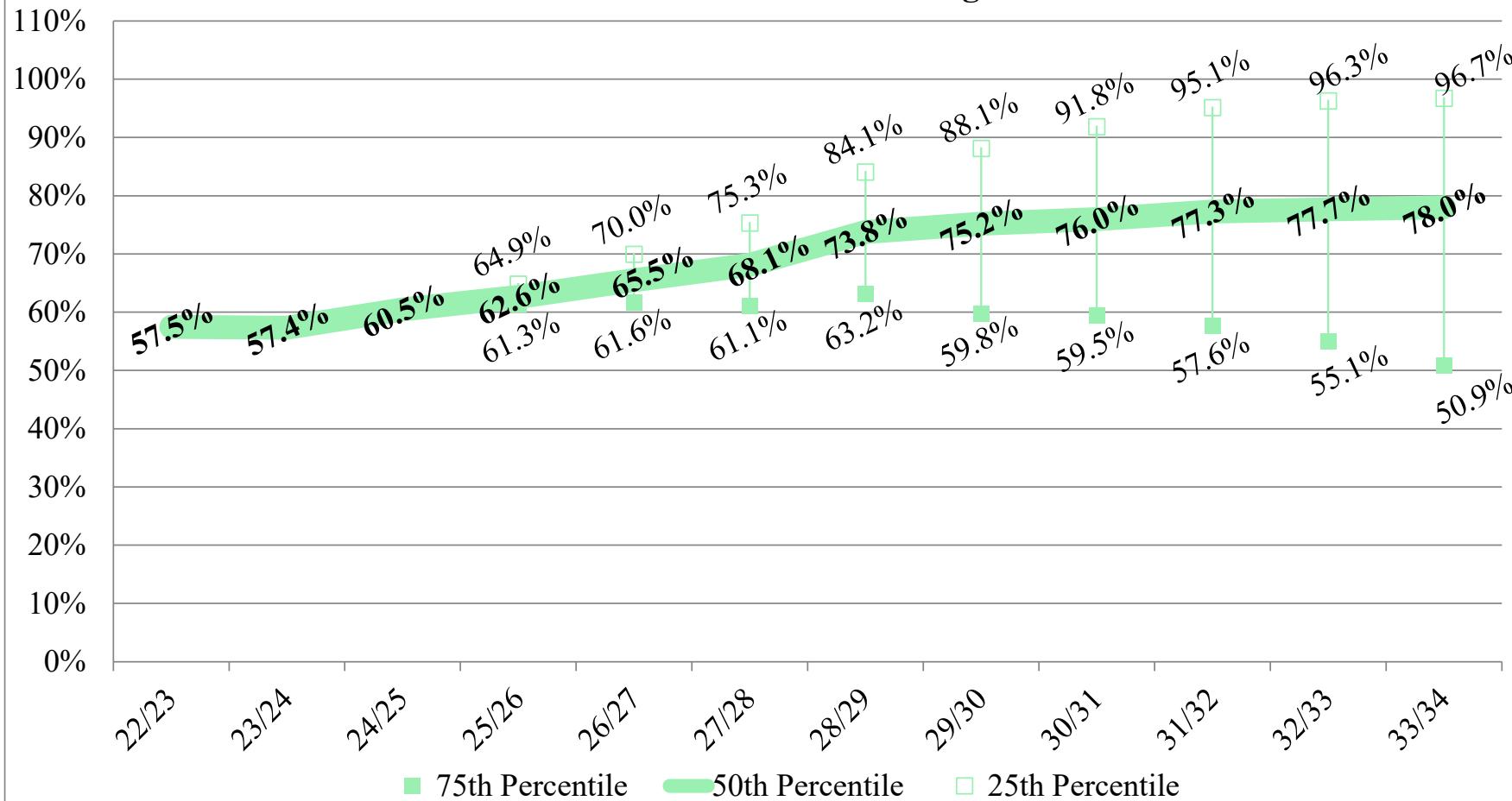
## Impact of 21/22 Investment Return

### Contribution Projection – Percent of Pay With EE Cost-Sharing



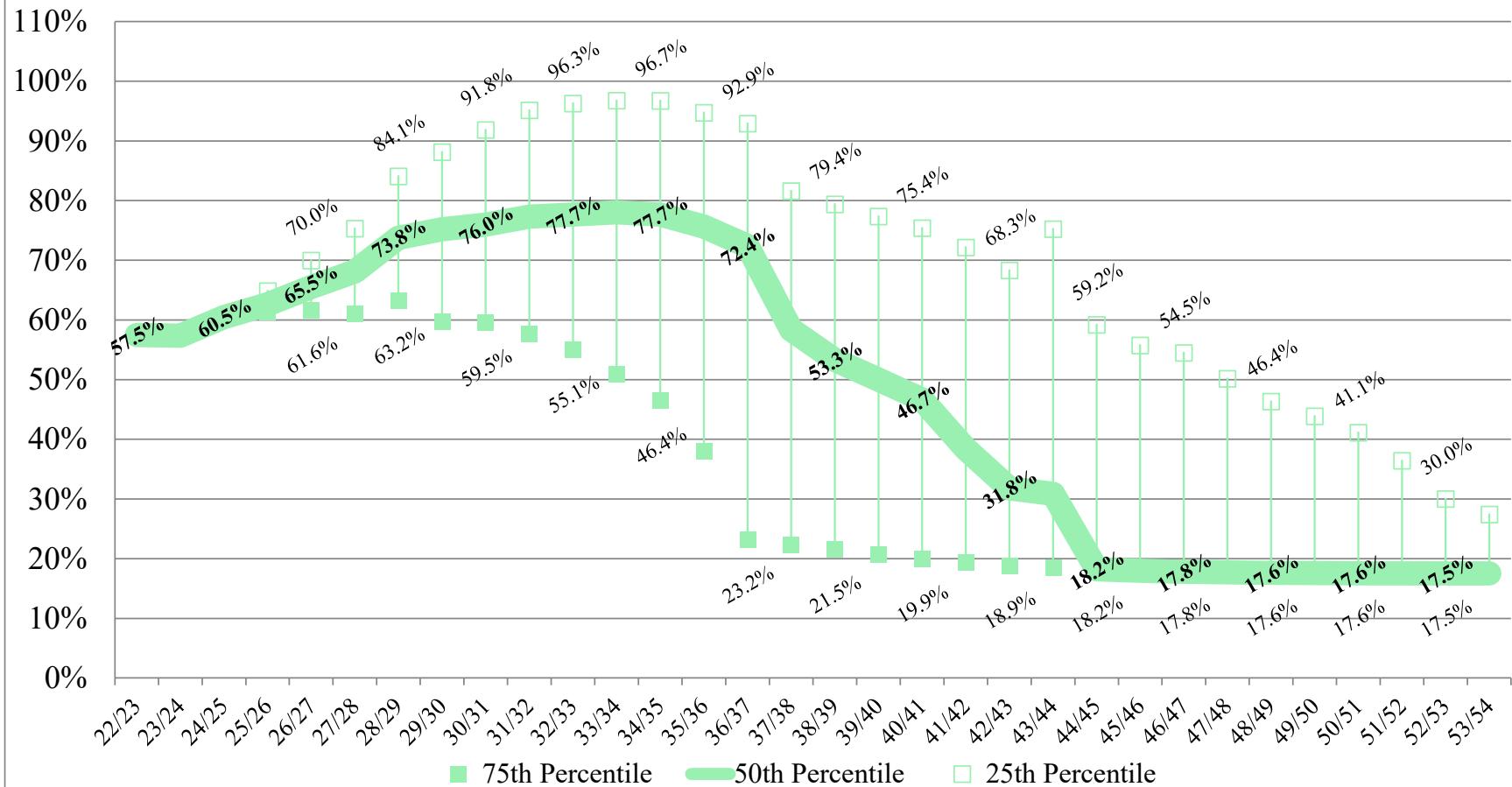
## CONTRIBUTION PROJECTION - SAFETY

### Contribution Projection – Percent of Pay Without EE Cost-Sharing



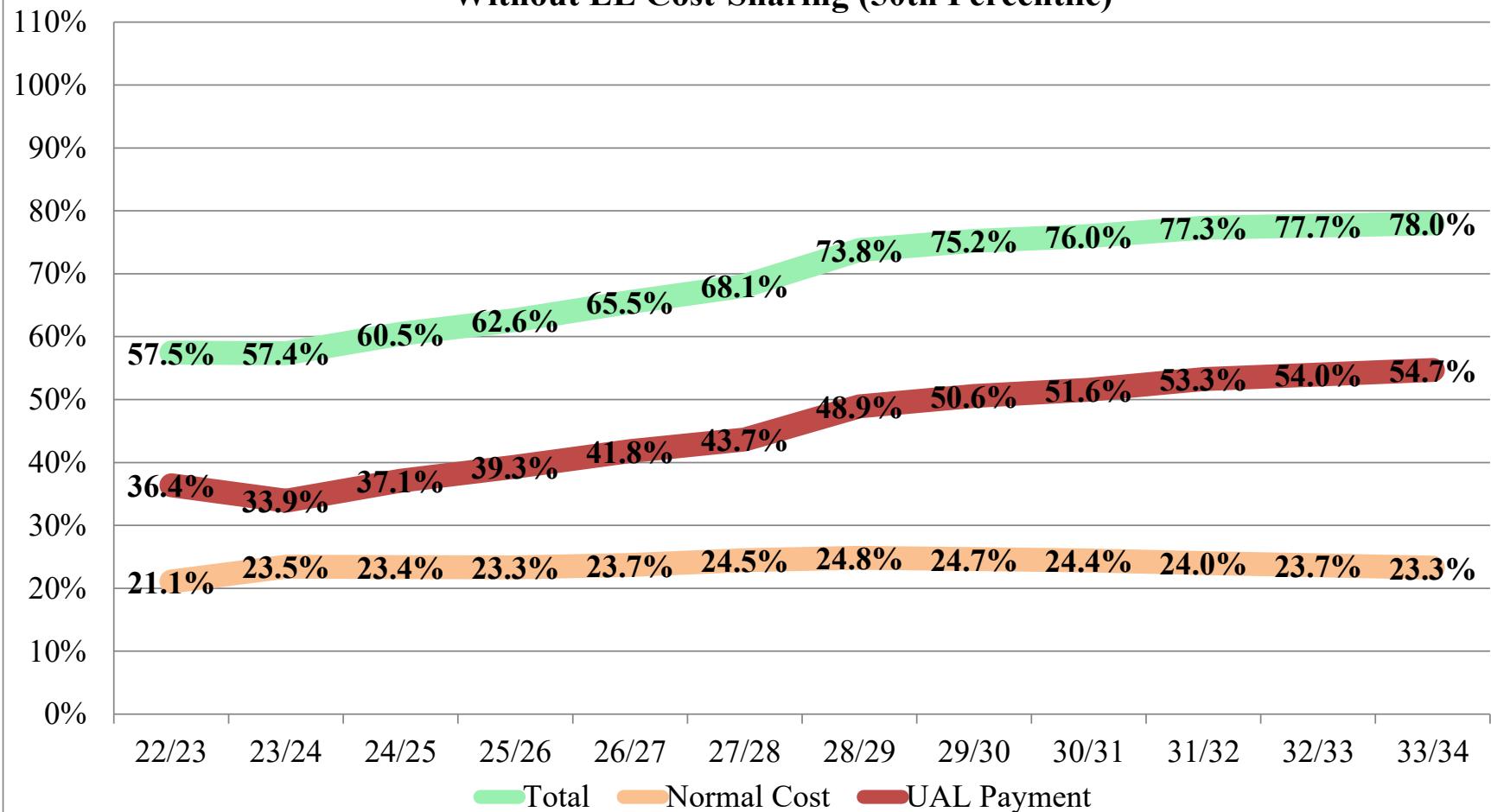
# CONTRIBUTION PROJECTION - SAFETY

## Contribution Projection – Percent of Pay Without EE Cost-Sharing



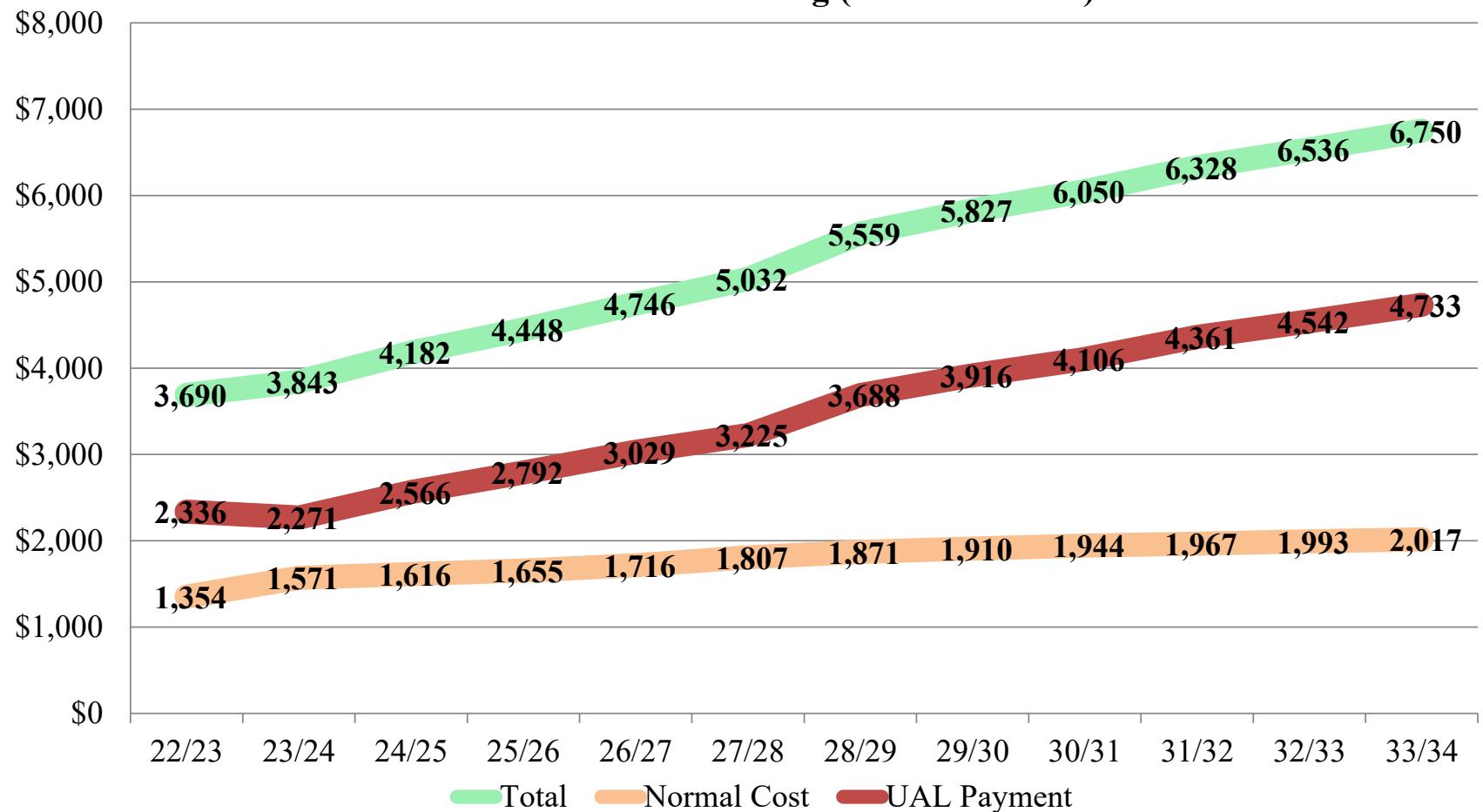
## CONTRIBUTION PROJECTION - SAFETY

### Contribution Projection – Percent of Pay Without EE Cost-Sharing (50th Percentile)



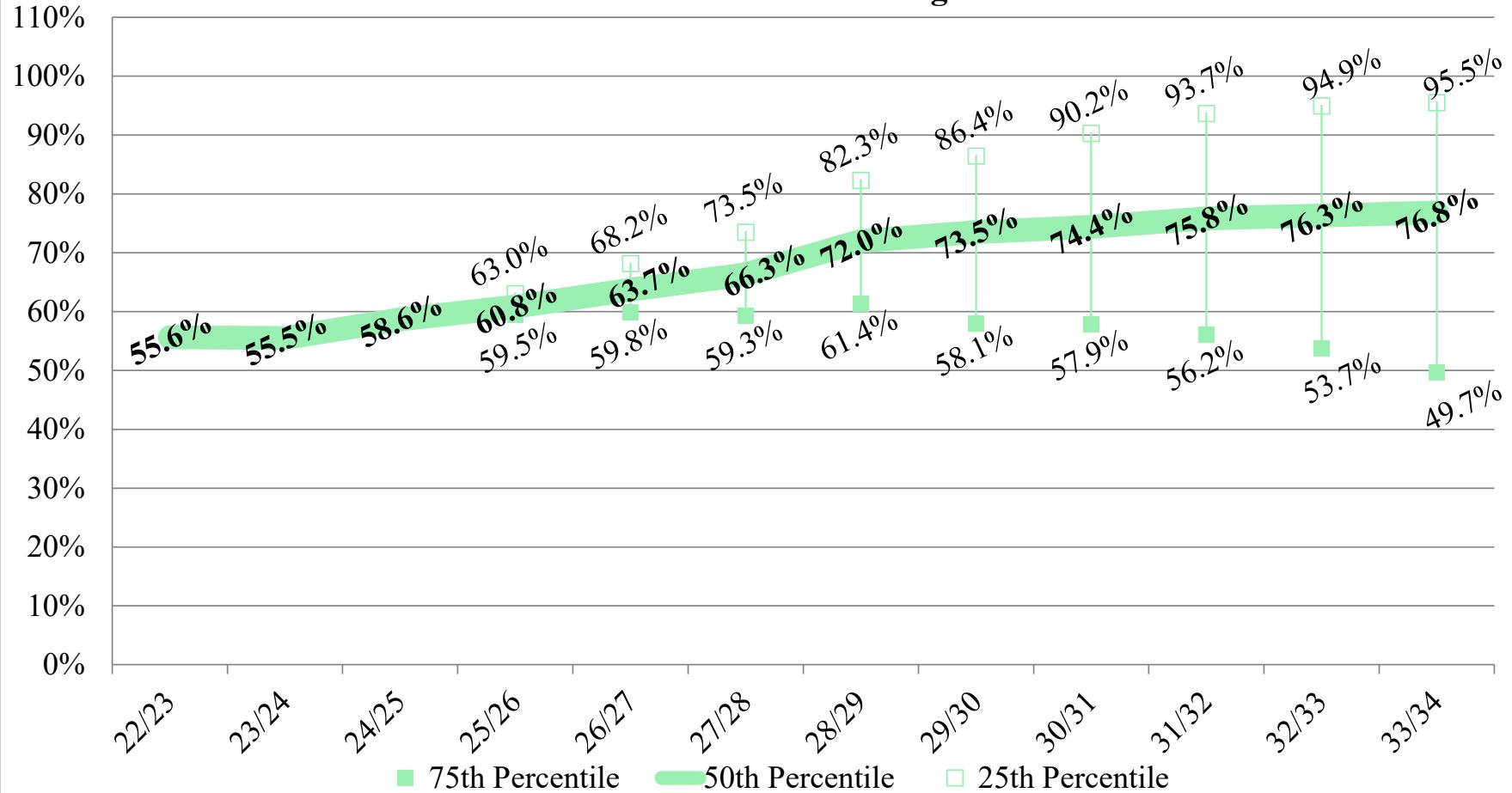
## CONTRIBUTION PROJECTION - SAFETY

Contribution Projection - \$000s  
Without EE Cost-Sharing (50th Percentile)



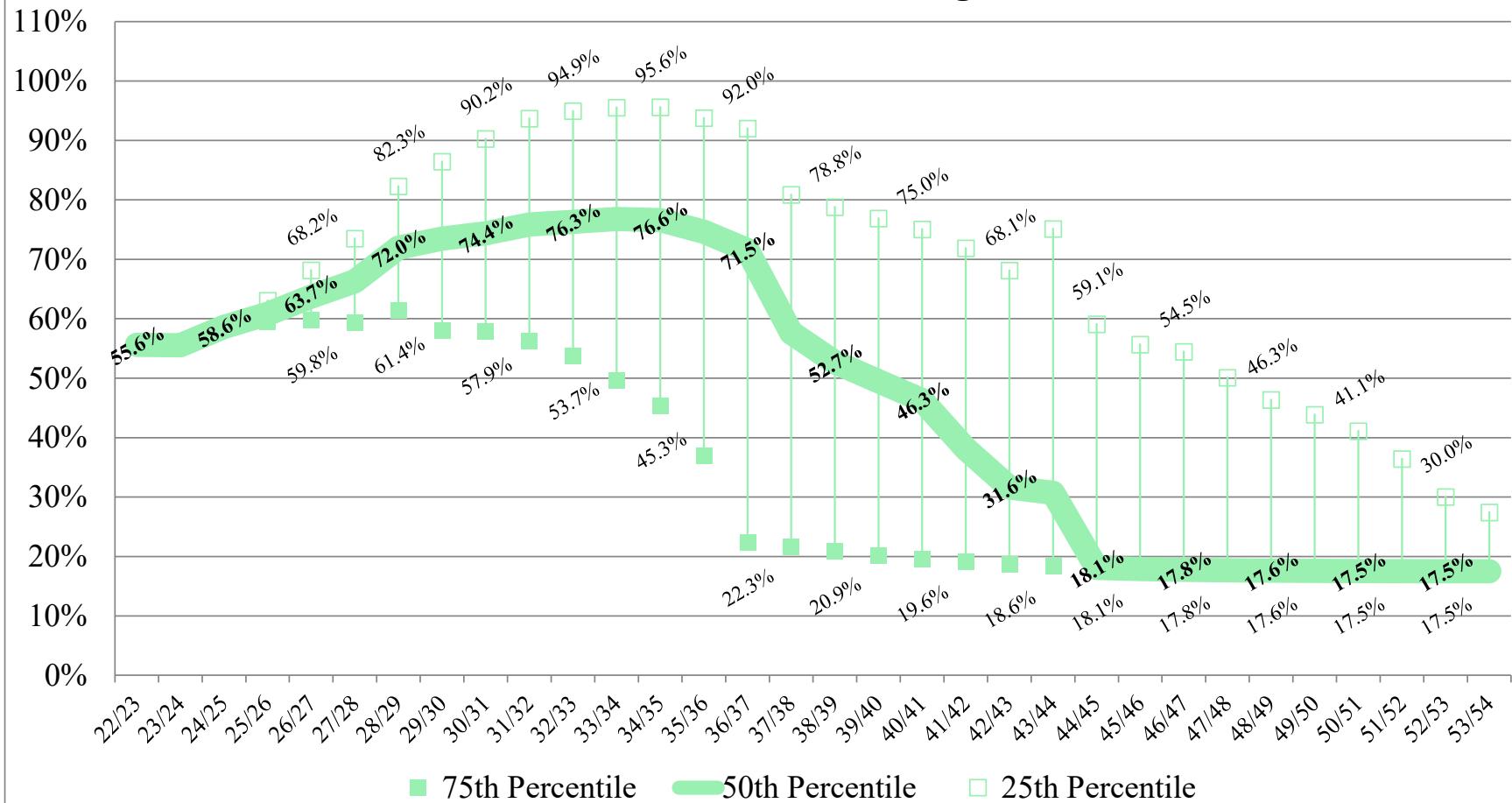
## CONTRIBUTION PROJECTION - SAFETY

### Contribution Projection – Percent of Pay With EE Cost-Sharing



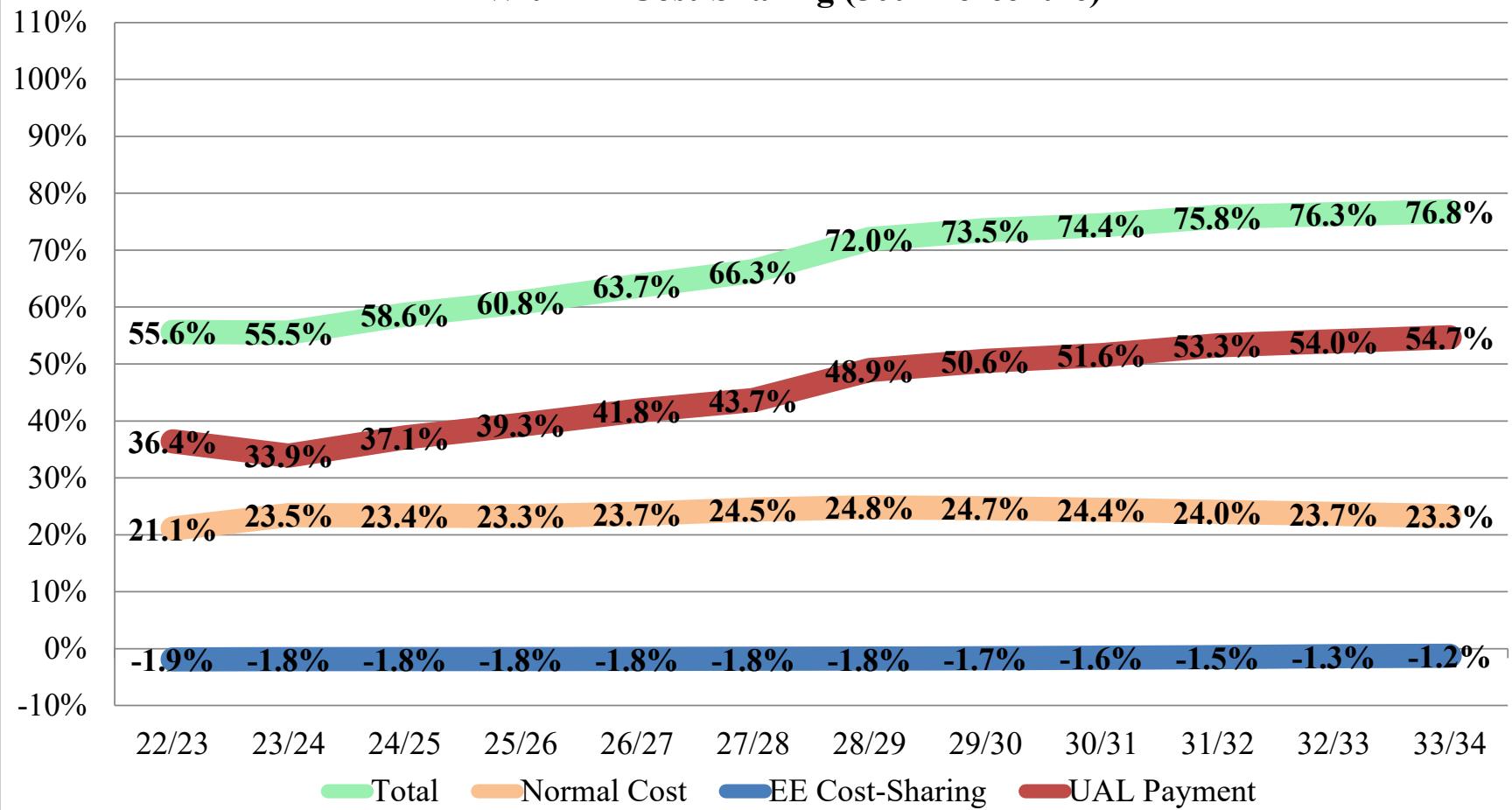
# CONTRIBUTION PROJECTION - SAFETY

## Contribution Projection – Percent of Pay With EE Cost-Sharing



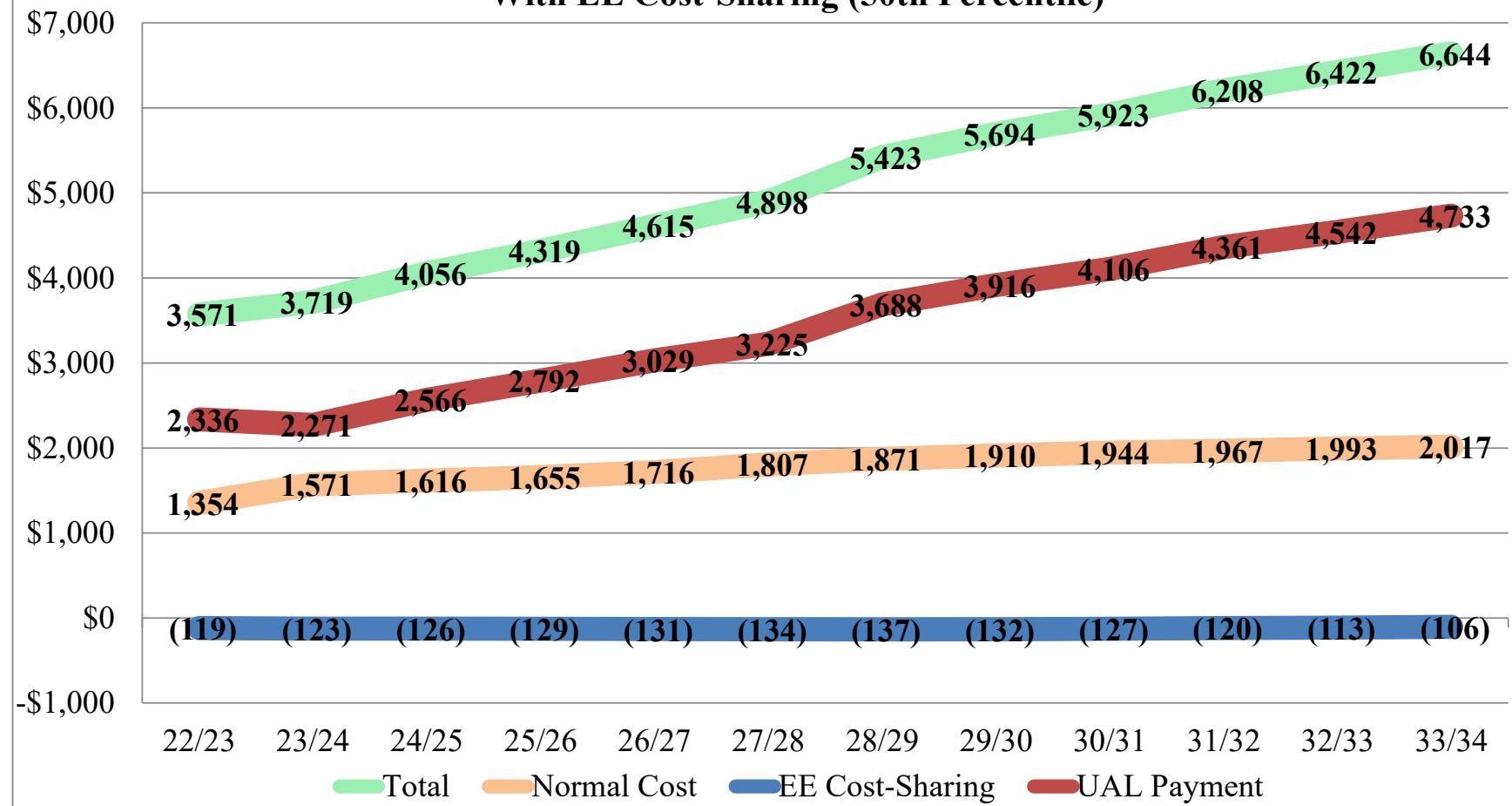
# CONTRIBUTION PROJECTION - SAFETY

## Contribution Projection – Percent of Pay With EE Cost-Sharing (50th Percentile)



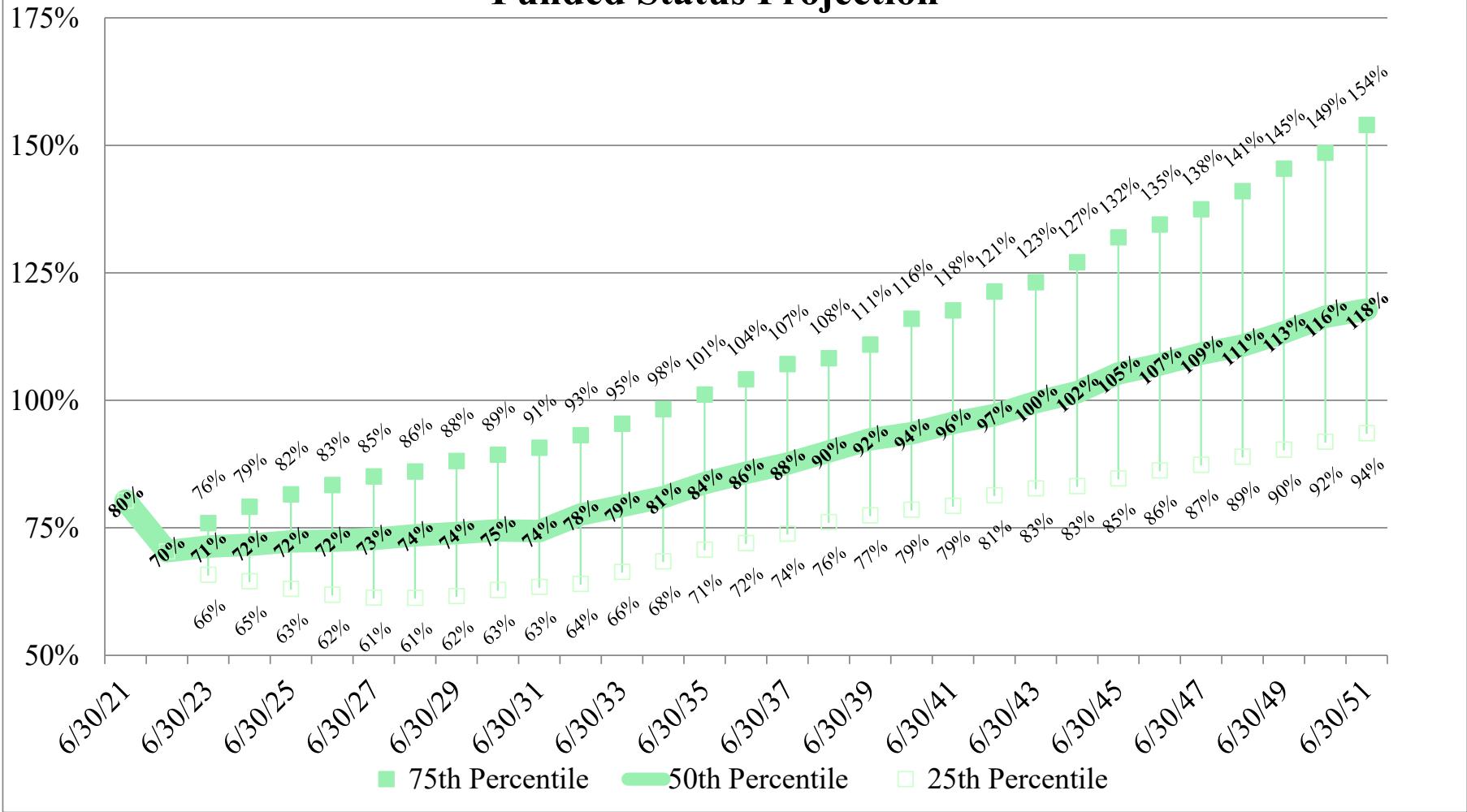
## CONTRIBUTION PROJECTION - SAFETY

Contribution Projection - \$000s  
With EE Cost-Sharing (50th Percentile)



# FUNDED STATUS - SAFETY

## Funded Status Projection



March 7, 2023



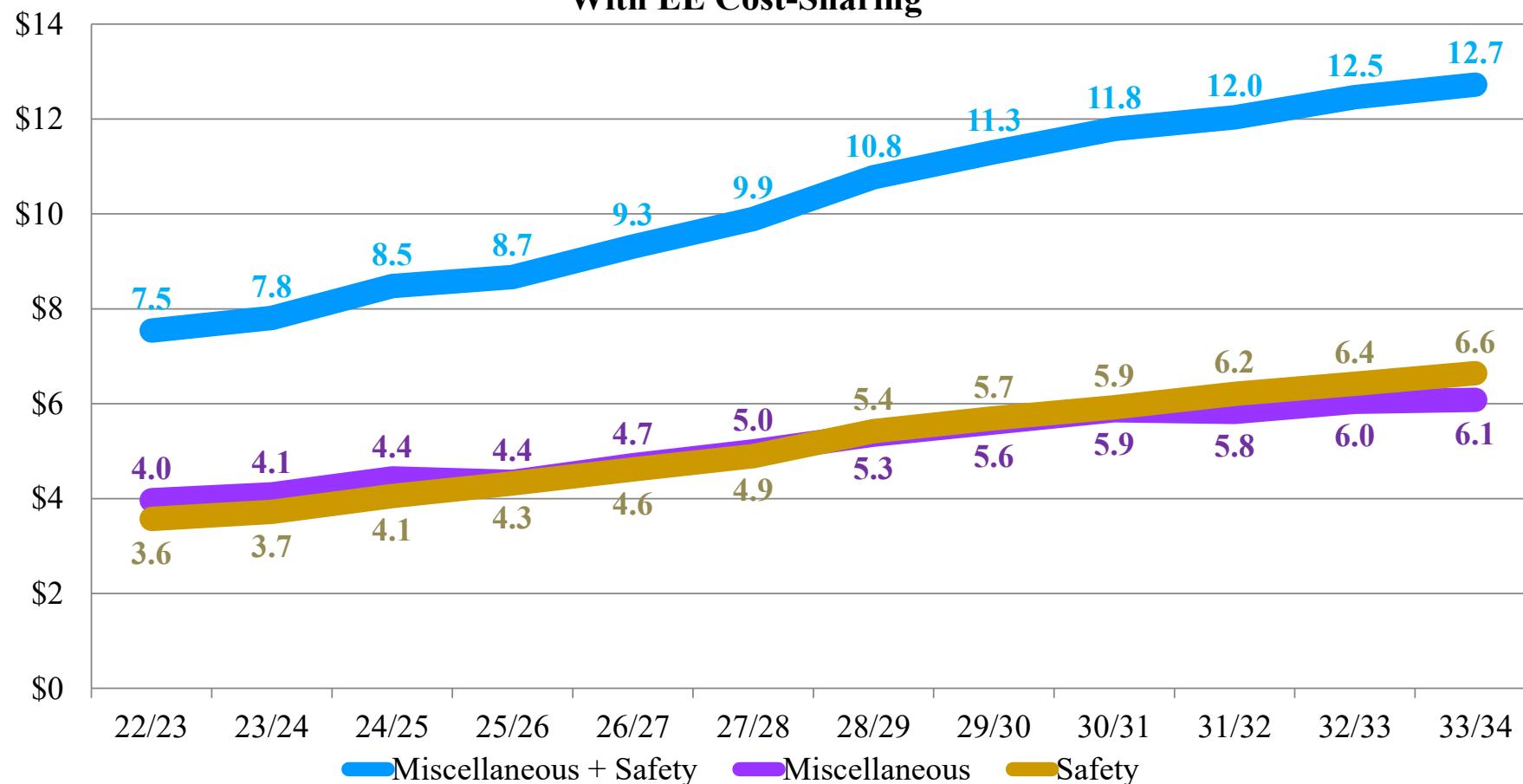
## FUNDED STATUS - SAFETY

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## COMBINED MISCELLANEOUS AND SAFETY

### Contribution Projection (\$Millions) Miscellaneous & Safety With EE Cost-Sharing



## COMBINED MISCELLANEOUS AND SAFETY

### Funded Status Summary on June 30, 2021 (Amounts in \$Millions)

	<b>Miscellaneous</b>	<b>Safety</b>	<b>Total</b>
■ <b>AAL</b>	\$ 121.6	\$ 108.1	\$ 229.7
■ <b>Assets</b>	<u>106.2</u>	<u>86.8</u>	<u>193.0</u>
■ <b>Unfunded AAL</b>	15.4	21.3	36.7
■ <b>Funded Ratio</b>	87.3%	80.3%	84.0%

### Projected Funded Status Summary on June 30, 2022<sup>15</sup> (Amounts in \$Millions)

	<b>Miscellaneous</b>	<b>Safety</b>	<b>Total</b>
■ <b>AAL</b>	\$ 125.5	\$ 111.6	\$ 237.1
■ <b>Assets</b>	<u>96.1</u>	<u>78.6</u>	<u>174.7</u>
■ <b>Unfunded AAL</b>	29.4	33.0	62.4
■ <b>Funded Ratio</b>	76.6%	70.4%	73.7%

<sup>15</sup> Projected 2022 assets reflects -7.5% CalPERS investment return for 2021/22.



## LEAVING CALPERS

- Participation in CalPERS is governed by State law and CalPERS rules
- The following are considered “withdrawing” from CalPERS:
  - Exclude new hires from CalPERS & giving them a different pension
  - Stop accruing benefits for current employees
- “Withdrawal” from CalPERS:
  - Treated as plan termination
  - Liability increased for conservative investments
  - Liability increased for future demographic fluctuations
  - Liability must be funded immediately by withdrawing agency
  - Otherwise, retiree benefits are cut



# LEAVING CALPERS

## CalPERS Termination Estimates on June 30, 2021 (Amounts in Millions)

<b>Discount Rate</b>	<b>Ongoing Plan</b>	<b>Termination Basis</b>	
	<b>6.80%</b>	<b>1.00%</b>	<b>2.25%</b>
<b>Miscellaneous</b>			
Actuarial Accrued Liability	\$ 121.6	\$ 270.8	\$ 223.9
Assets	<u>106.2</u>	<u>106.2</u>	<u>106.2</u>
Unfunded AAL (UAAL)	15.4	164.6	117.7
<b>Safety</b>			
Actuarial Accrued Liability	\$ 108.1	\$ 258.1	\$ 210.9
Assets	<u>86.8</u>	<u>86.8</u>	<u>86.8</u>
Unfunded AAL (UAAL)	21.3	171.3	124.1
<b>Total</b>			
Unfunded AAL (UAAL)	\$36.7	\$335.9	\$241.8
Funded Ratio	84.0%	36.5%	44.4%



## PEPRA COST SHARING

- Target of 50% of total normal cost paid by all employees
- *PEPRA members* must pay greater of 50% of total normal cost or bargained amount if higher
- Employer cannot pay any part of *PEPRA member* required employee contributions
- Employer may impose current employees pay 50% of total normal cost (limited to 8% of pay for Miscellaneous and 12% for Safety) if not agreed through collective bargaining
- Miscellaneous Plan 2023/24:

	<u>Classic Members</u>		<u>New Members</u>
	Tier 1 <u>2.5%@55 FAC1</u>	Tier 2 <u>2%@60 FAC3</u>	PEPRA <u>2%@62 FAC3</u>
● Employer Normal Cost	13.8%	14.3%	7.93%
● Member Normal Cost	<u>8.0%</u>	<u>7.0%</u>	<u>7.25%</u>
● Total Normal Cost	21.8%	21.3%	15.18%
● 50% Target	10.9%	10.7%	7.59%



## PEPRA COST SHARING

### ■ Safety Plan 2023/24:

	<u>Classic Members</u>	<u>New Members</u>
	Tier 1	PEPRA
	<u><b>3%@50 FAC1</b></u>	<u><b>2.7%@57 FAC3</b></u>
● Employer Normal Cost	29.1%	14.50%
● Member Normal Cost	<u>9.0%</u>	<u>14.50%</u>
● Total Normal Cost	38.1%	29.00%
● 50% Target	19.1%	14.50%

### ■ PEPRA Member Contributions:

Group	2022/23		2023/24			
	Total NC (Basis)	Member Rate	Total Normal Cost	Change	Member Rate	Method
Miscellaneous	14.43%	7.25%	15.18%	<b>0.75%</b>	<b>7.25%</b>	PEPRA Members
Safety	27.63%	13.75%	29.00%	<b>1.37%</b>	<b>14.50%</b>	PEPRA Members



## PAYING DOWN THE UAL & RATE STABILIZATION

- Where do you get the money from?
- How do you use the money?



## WHERE DO YOU GET THE MONEY FROM?

- POB:
  - Usually thought of as interest arbitrage between expected earnings and rate paid on POB
  - No guaranteed savings
  - PEPRA prevents contributions from dropping below normal cost
    - Savings offset when investment return is good
  - GFOA Advisory
- Borrow from General Fund similar to State
- One time payments
  - Governing body resolution to use a portion of one time money, e.g.
    - 1/3 to one time projects
    - 1/3 to replenish reserves and
    - 1/3 to pay down unfunded liability



## ADDITIONAL PAYMENTS TO CALPERS

- Internal Service Fund
  - Typically used for rate stabilization
  - Restricted investments:
    - Likely low (0.5%-1.0%) investment returns
    - Short term/high quality, designed for preservation of principal
  - Assets can be used by governing body for other purposes
  - Does not reduce Unfunded Liability



## ADDITIONAL PAYMENTS TO CALPERS

Make payments directly to CalPERS:

- Likely best long-term investment return
- Must be considered an irrevocable decision
  - Extra payments cannot be used as future “credit”
  - PEPRA prevents contributions from dropping below normal cost
- Option #1: Request shorter amortization period (Fresh Start):
  - Higher short term payments
  - Less interest and lower long term payments
  - Likely cannot revert to old amortization schedule
    - Savings offset when investment return is good (PEPRA)



## ADDITIONAL PAYMENTS TO CALPERS

- Make payments directly to CalPERS (continued):
  - Option #2: Target specific amortization bases with an Additional Discretionary Payment “ADP” :
    - Extra contribution’s impact muted by reduced future contributions
      - CalPERS can’t track the “would have been” contribution
    - No guaranteed savings
      - Larger asset pool means larger loss (or gain) opportunity
    - Paying off shorter amortization bases: larger contribution savings over shorter period:
      - e.g. 10 year base reduces contribution 13.7¢ for \$1
      - Less interest savings vs paying off longer amortization bases
    - Paying off longer amortization bases: smaller contribution savings over longer period:
      - e.g. 25 year base reduces contribution 8.2¢ for \$1
      - More interest savings vs paying off shorter amortization bases
    - Maintaining the current payment schedule – not letting payments reduce due to extra payment – gives the greatest long-term savings



## IRREVOCABLE SUPPLEMENTAL (§115) PENSION TRUST

- Can only be used to:
  - Reimburse Town for CalPERS contributions
  - Make payments directly to CalPERS
- Investments significantly less restricted than Town investment funds
  - Fiduciary rules govern Trust investments
  - Usually, designed for long term returns
- Assets don't count for GASB accounting
  - Are considered Employer assets
- Over 100 trusts established, mostly since 2015
  - Trust providers: PARS, PFM, Keenan
  - California Employers' Pension Prefunding Trust (CEPPT) effective July 2019
    - Strategy 1: 48% stocks / 52% bonds
    - Strategy 2: 22% stocks / 78% bonds



## IRREVOCABLE SUPPLEMENTAL (§115) PENSION TRUST

- More flexibility than paying CalPERS directly
  - Town decides if and when and how much money to put into Trust
  - Town decides if and when and how much to withdraw to pay CalPERS or reimburse Agency
- Funding strategies typically focus on:
  - Reducing the unfunded liability
    - Fund enough to make total CalPERS UAL = 0
    - Make PEPRA required payments from Trust when overfunded
  - Stabilizing contribution rates
    - Mitigate expected contribution rates to better manage budget
  - Combination
    - Use funds for rate stabilization/budget predictability
    - Target increasing fund balance to pay off UAL sooner



## IRREVOCABLE SUPPLEMENTAL (§115) PENSION TRUST

- Consider:
  - How much can you put into Trust?
    - Initial seed money?
    - Additional amounts in future years?
  - When do you take money out?
    - Target budget rate?
    - Year target budget rate kicks in?
      - Before or after CalPERS rate exceeds budgeted rate?



## PREFUNDING OPTION

### Direct Payment to CalPERS Prefunding Option

- Following illustrates savings from an additional \$1 million contribution to CalPERS on June 30, 2023:
- Miscellaneous Plan
  - Shortest Base: 2003 Assumption Change (2 years, \$0.6 million on 6/30/23) and 2007 Benefit Change (5 years, \$1.0 million on 6/30/23)  
Less interest savings, largest short-term contribution impact
  - Longest Base: 2013 Gain/Loss (22 years, \$8.7 million on 6/30/23)  
Greater interest savings, smallest short-term contribution impact

Target Bases	Estimated Interest Savings	2023/24 Contribution Impact
<b>Shortest Bases</b>		<b>\$1 million</b>
\$ Savings (000's)	\$114	\$(400)
PV Savings @ 3% (000's)	60	
<b>Longest Base</b>		<b>\$1 million</b>
\$ Savings (000's)	\$954	\$(73)
PV Savings @ 3% (000's)	430	



## PREFUNDING OPTION

### ■ Safety Plan<sup>16</sup>

- Shortest Base: 2014 Assumption Change (13 years, \$3.9 million on 6/30/23)  
Less interest savings, largest short-term contribution impact
- Longest Base: 2018 Non Asset Gain/Loss (27 years, \$0.4 million on 6/30/23), 2017 Non Asset Gain/Loss (26 years, \$0.07 million on 6/30/23) and 2016 Asset Gain/Loss (25 years, \$5.5 million on 6/30/23)  
Greater interest savings, smallest short-term contribution impact

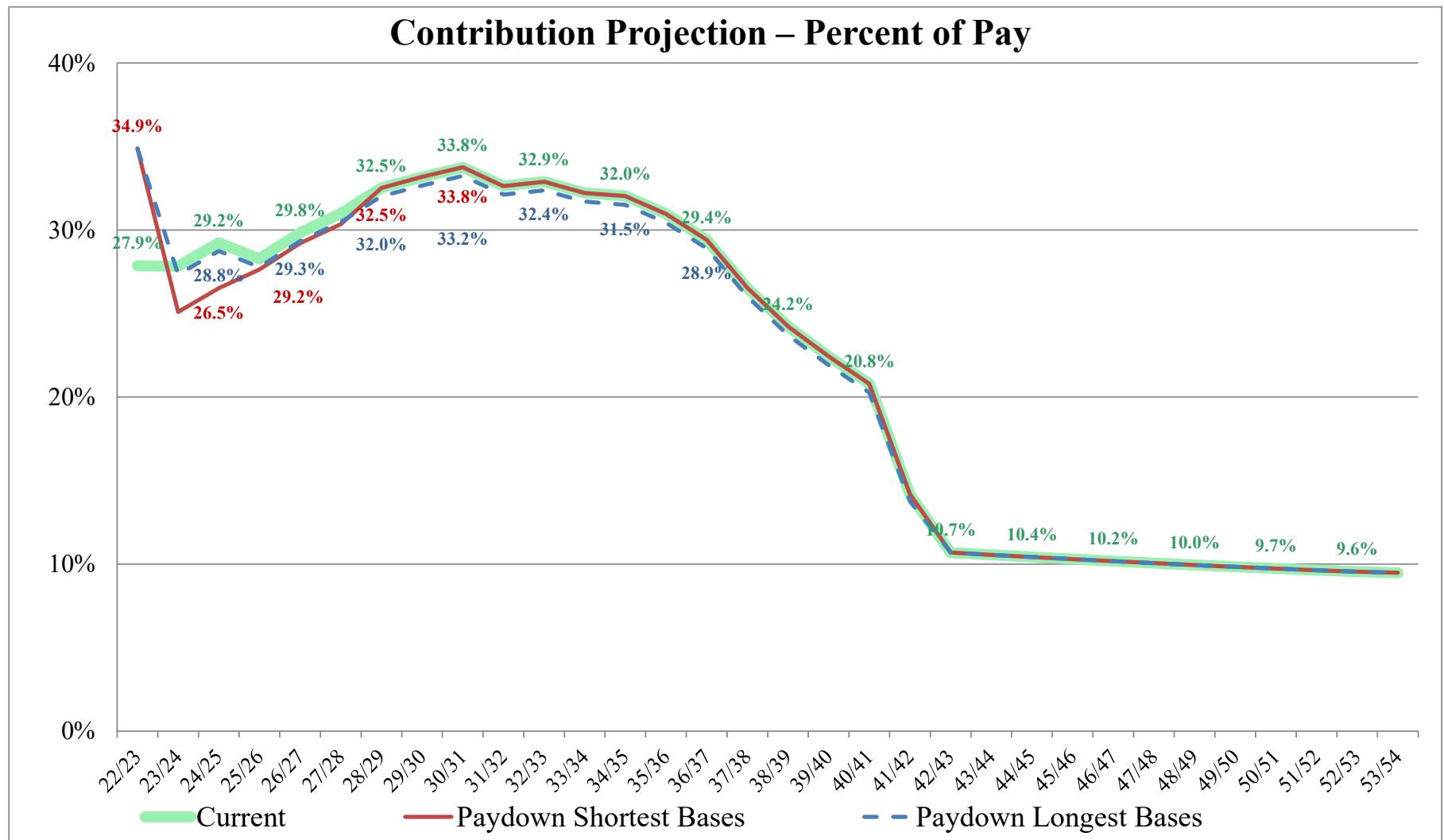
Target Bases	Estimated Interest Savings	2023/24 Contribution Impact
<b>Shortest Bases</b>		<b>\$1 million</b>
\$ Savings (000's)	\$439	\$(113)
PV Savings @ 3% (000's)	215	
<b>Longest Base</b>		<b>\$1 million</b>
\$ Savings (000's)	\$1,035	\$(60)
PV Savings @ 3% (000's)	452	

<sup>16</sup> All of the target bases are in Safety Classic plan. PEPRA plan has only one credit base.



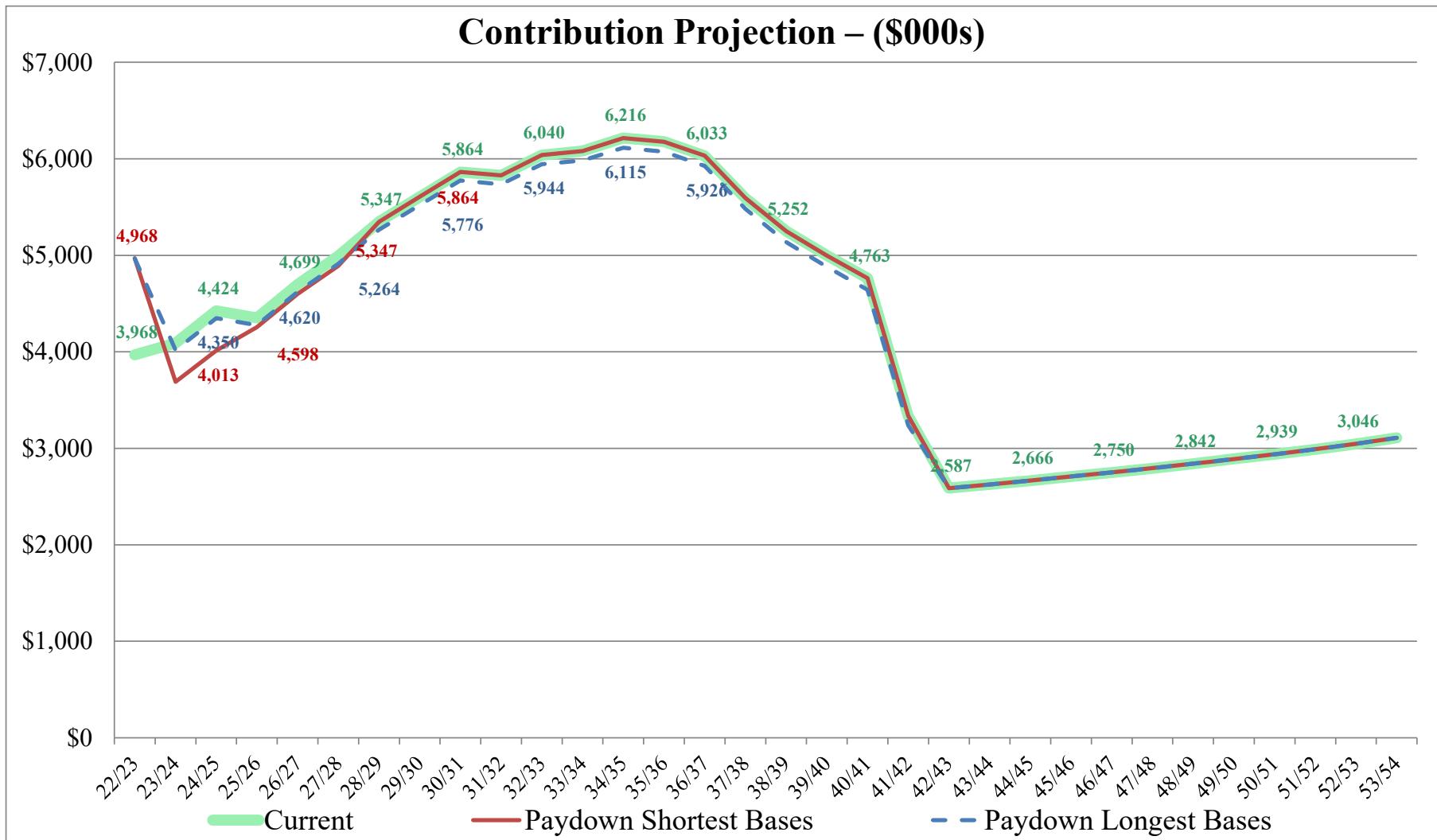
## PREFUNDING OPTION

### Direct Payment to CalPERS Miscellaneous



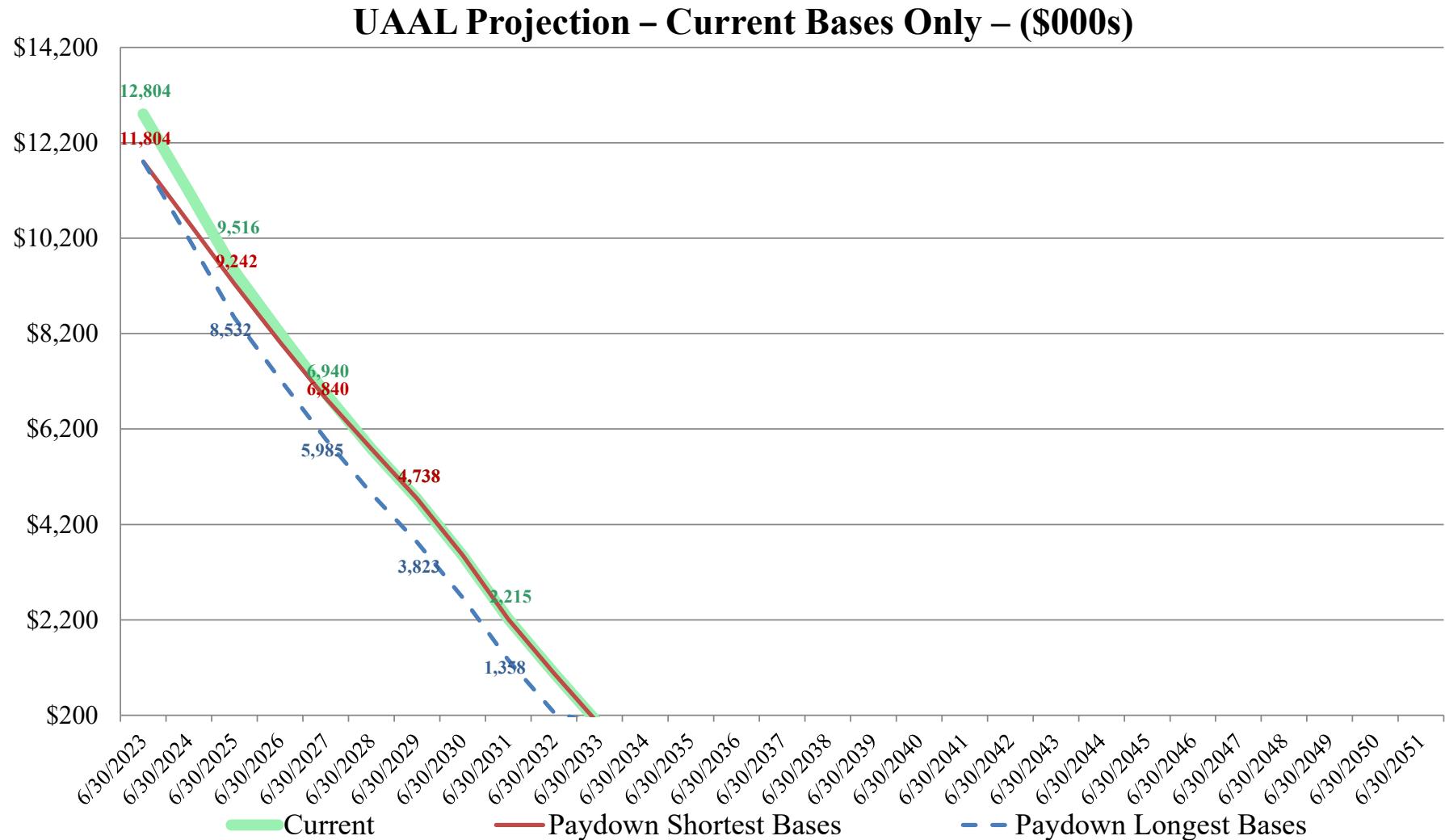
## PREFUNDING OPTION

### Direct Payment to CalPERS Miscellaneous



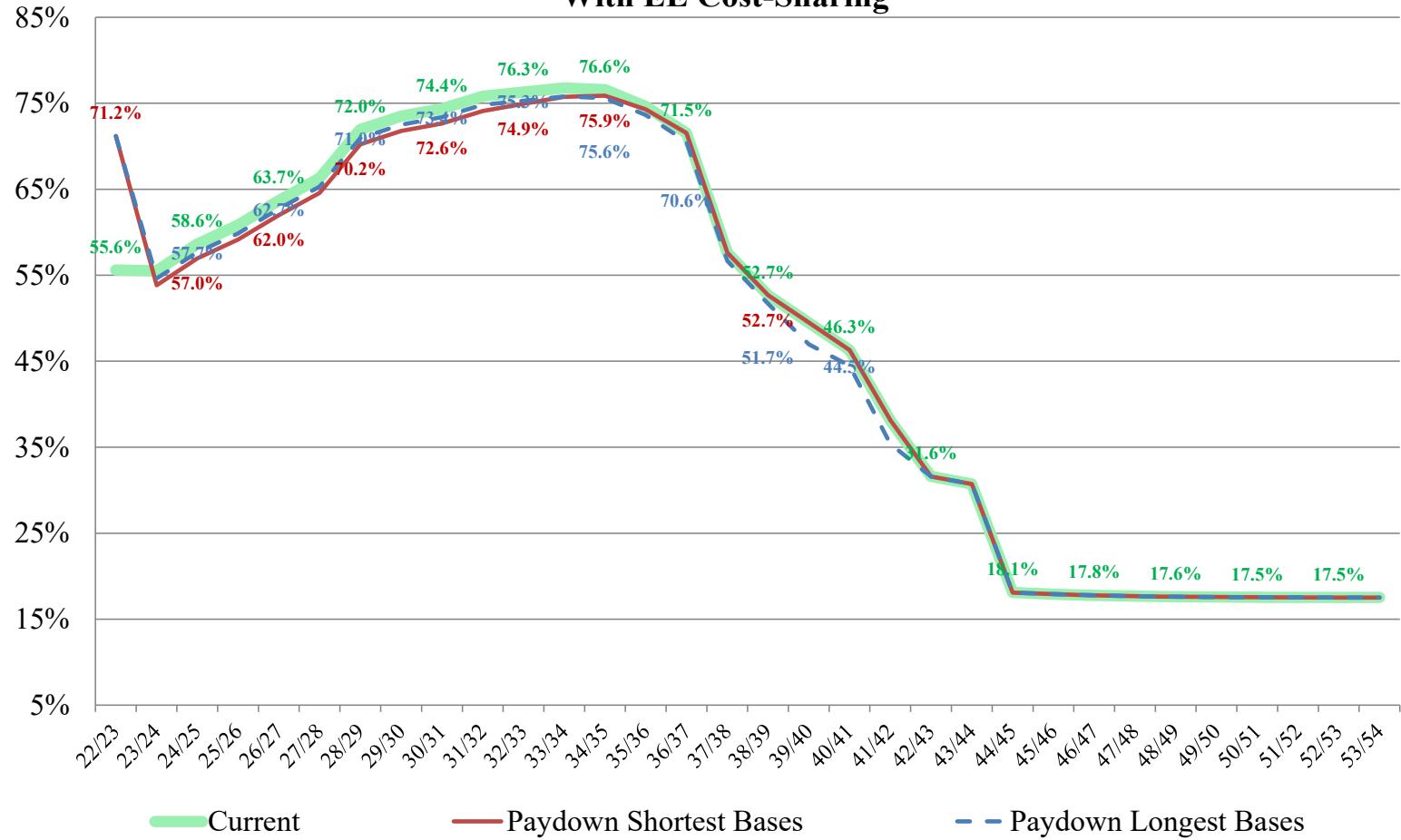
## PREFUNDING OPTION

### Direct Payment to CalPERS Miscellaneous



## PREFUNDING OPTION

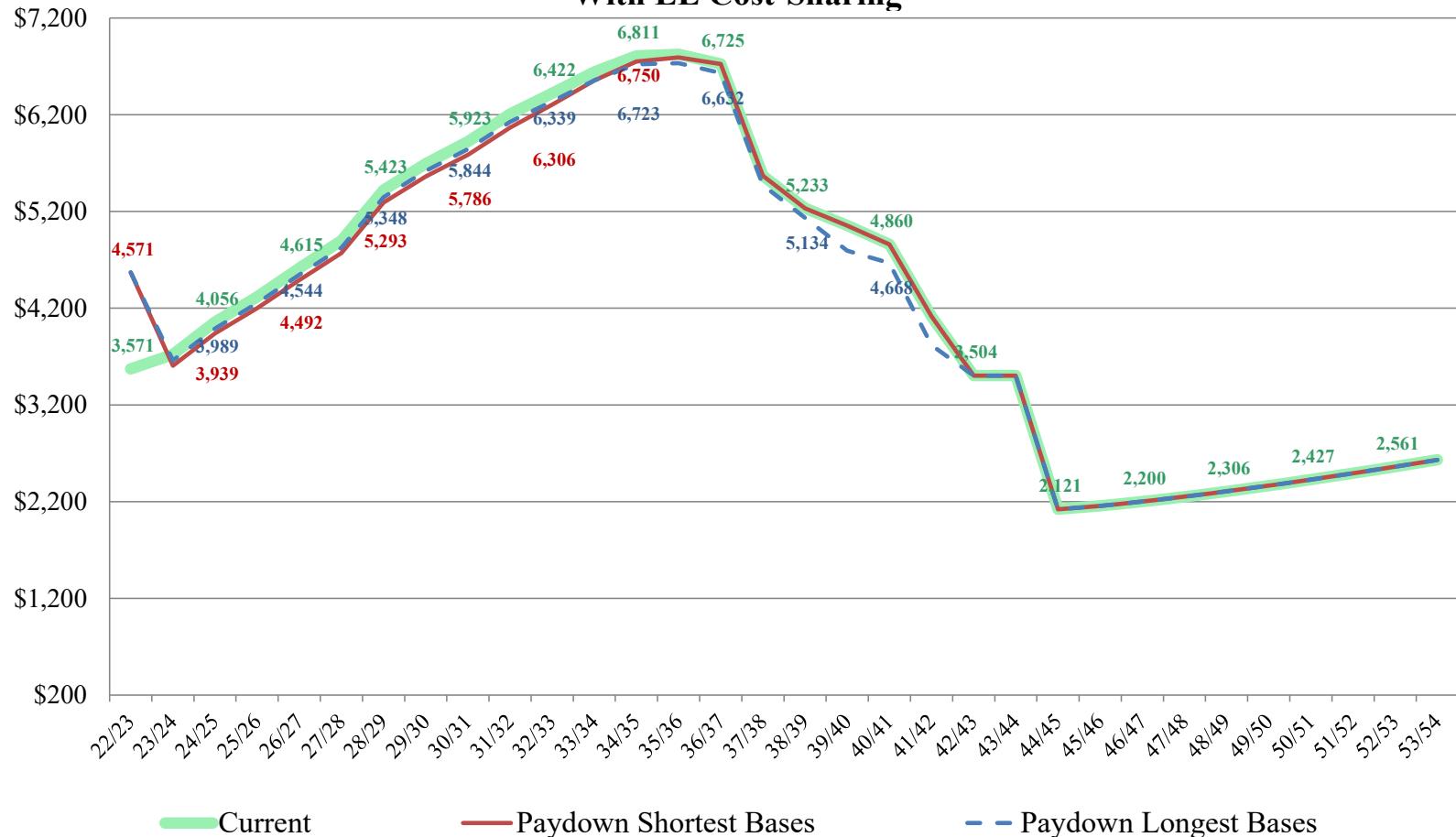
### Direct Payment to CalPERS Safety Contribution Projection – Percent of Pay With EE Cost-Sharing



## PREFUNDING OPTION

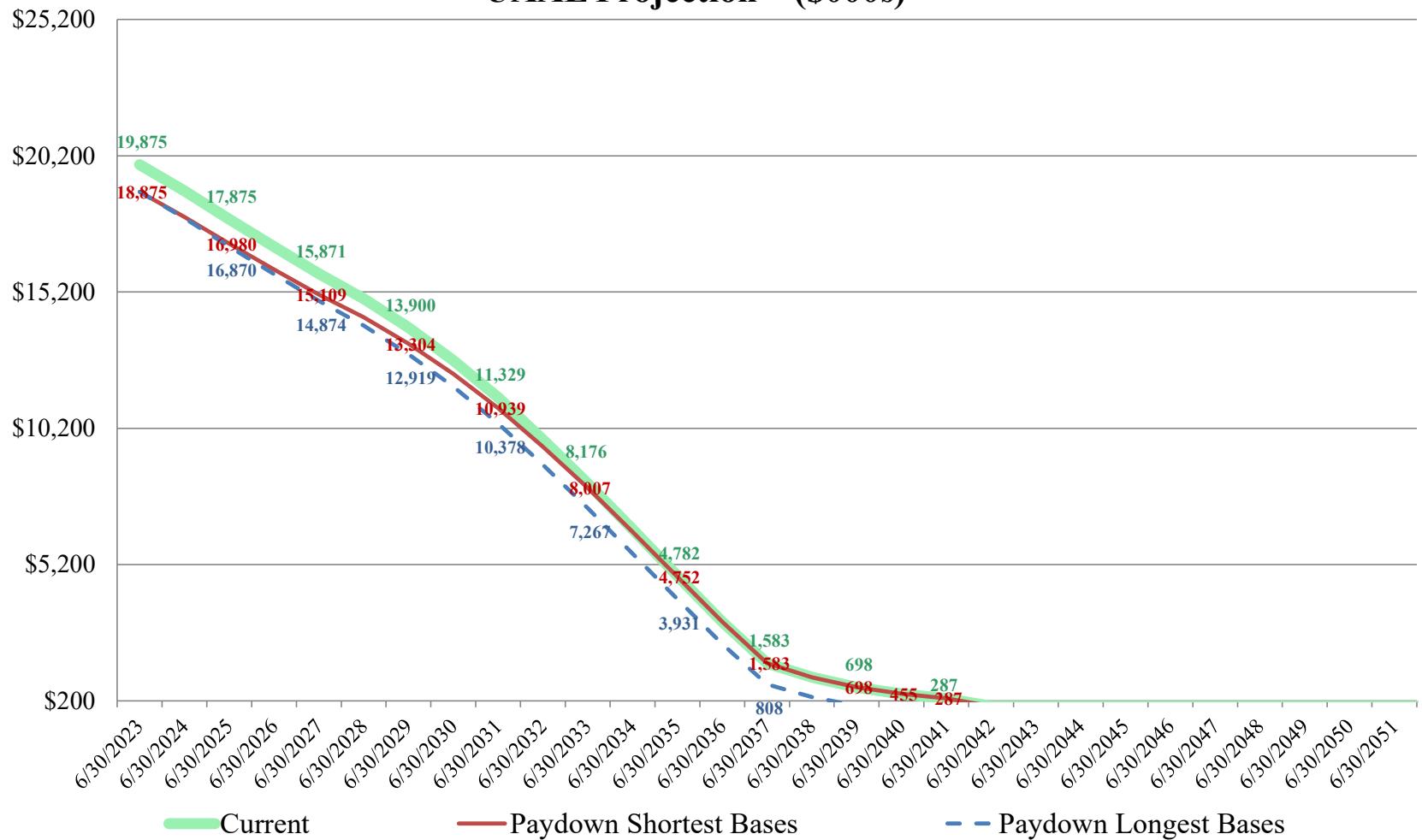
### Direct Payment to CalPERS Safety

#### Contribution Projection – (\$000s) With EE Cost-Sharing



## PREFUNDING OPTION

### Direct Payment to CalPERS Safety UAAL Projection – (\$000s)



## COMPARISON OF OPTIONS

### ■ Supplemental Trust

- Flexible
- Likely lower long-term return
- Investment strategy choice
- Does not reduce net pension liability for GASB reporting
- More visible

### ■ CalPERS

- Locked In
- Likely higher long-term return
- No investment choice
- Reduces net pension liability for GASB reporting
- More restricted



# ACTUARIAL CERTIFICATION

This report presents analysis of the Town of Los Gatos's CalPERS pension plans. The purpose of this report is to provide the Town:

- Historical perspective on the plan investment returns, assets, funded status and contributions.
- Projections of likely future contributions and the impact of investment volatility

The calculations and projections in this report are based on information contained in the Town's June 30, 2021 and earlier CalPERS actuarial valuation reports. We reviewed this information for reasonableness, but do not make any representation on the accuracy of the CalPERS reports.

Future investment returns and volatility are based on Foster & Foster's Capital Market model which results in long term returns summarized on pages 25 and 57.

Future results may differ from our projections due to differences in actual experience as well as changes in plan provisions, CalPERS actuarial assumptions or methodology. Other than variations in investment return, this study does not analyze these.

To the best of our knowledge, this report is complete and accurate and has been conducted using generally accepted actuarial principles and practices. As members of the American Academy of Actuaries meeting the Academy Qualification Standards, we certify the actuarial results and opinions herein.

Respectfully submitted,



Mary Elizabeth Redding, FSA, EA, MAAA  
Foster & Foster, Inc.  
March 7, 2023



Bianca Lin, FSA, EA, MAAA  
Foster & Foster, Inc.  
March 7, 2023



March 7, 2023

