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DECLINING EMPLOYER PAYROLL POLICY

PURPOSE AND BACKGROUND

1) A participating employer in the Kern County Employees' Retirement Association (KCERA) may experience an actual or expected material decline in the payroll attributable to its KCERA active members (KCERA-covered payroll). This Declining Employer Payroll Policy is intended to establish guidelines by which KCERA intends to assure that such employer will continue to satisfy its obligation to timely fund all unfunded actuarial accrued liability (UAAL) attributable to the employer's active, retired and deferred employees and their beneficiaries by reason of their prior and future service as KCERA members.

BACKGROUND AND OBJECTIVES

2) Under KCERA's practices in place prior to the adoption of this Declining Payroll Policy, KCERA generally determined employers' contribution obligations for UAAL by applying a contribution rate recommended by KCERA's actuary to the employer's KCERA-covered payroll (the percentage-of-payroll methodology). For employers whose payrolls are generally consistent with KCERA's actuarial assumptions regarding payroll growth, the percentage-of-payroll methodology is appropriate for the collection of contributions necessary to support the benefits of the employer's active, retired and deferred members.

However, for employers whose KCERA-covered payroll is declining, or is expected to decline, materially over time, the Board of Retirement has determined that the percentage-of-payroll methodology is not the appropriate means of collecting employer contributions owed to the system.

The objectives of this Declining Employer Payroll Policy are to:

(i) to ensure equitable and adequate funding of UAAL in cases involving employers with declining payrolls,
(ii) approve procedures for identifying employers who should be subject to this Policy, and
(iii) approve a different methodology for determining any UAAL attributable to such employers and setting the amount and schedule of the contributions needed to fund such UAAL.

This Policy does not change the methodology regarding how contributions for "normal cost" are determined for participating employers.

Generally, the objectives of this Policy also are to ensure compliance with County Employees' Retirement Law of 1937, California Government Code sections 31450 et seq., as amended ("CERL"), and other applicable provisions of law. Pursuant to CERL sections 31453, 31453.5, 31581, 31582, 31584, 31585, 31586, 31611, and other applicable provisions of law, a participating employer remains liable, and must make the required appropriations and transfers, to KCERA for the employer's respective share of liabilities attributable to its officers and employees who are and may be entitled to receive retirement, disability and related benefits from KCERA.

It is the Board of Retirement's primary intent to ensure the adequacy of the assets attributable to each employer to satisfy that employer's funding obligations. This will generally require redetermination of the employer's funding obligations annually until fully satisfied. In accordance with this intent, the Board of Retirement will also seek to allow an employer covered by this Policy to satisfy its funding obligation in a manner which provides the employer reasonable flexibility under the circumstances existing from time to time.

This Policy is intended to be consistent with and not supersede the terms of any other existing agreements, policies and guidelines that may be in place between KCERA and the employer.

POLICY PROCEDURES AND GUIDELINES

3) Absent exigent circumstances or unless otherwise expressly approved by the Board of Retirement at a duly-noticed public meeting, the procedures and guidelines for implementing this Policy are set forth below.

COMMENCEMENT OF COVERAGE – TRIGGERING EVENTS

4) This Policy covers only those employers for whom the Board determines, based on a recommendation from KCERA's Chief Executive Officer (CEO), that a triggering event as described in this section 4 has occurred and who are not excluded from coverage under this Policy as described in sections 5 and 6 below. The Board hereby directs the CEO to work with KCERA Staff and other KCERA service providers (e.g., the actuary) to obtain the information (e.g., KCERA-covered payroll history) needed for the Board to make determinations regarding triggering events. The CEO is further directed to report to the Board, at least annually, regarding these activities.

- ***Triggering event resulting from ceasing to enroll new hires.*** Some KCERA participating employers cease to enroll new hires with KCERA but, for a period of time, continue to have at least some previously-enrolled employees maintaining their status as active KCERA members. These employers'

KCERA-covered payroll will eventually diminish to zero as their active employees retire or otherwise terminate employment. Examples of employers in this category may include an employer that is acquired by another entity that is not a KCERA participating employer, or a KCERA employer that is taken over by a state agency whose employees are covered by another pension system such as CalPERS. There may be other examples as well.

- ***Triggering event resulting from a material and expected long-lasting reduction in KCERA-covered payroll.*** Some employers may experience a material reduction in their KCERA-covered payroll, but nevertheless continue to enroll their new hires with KCERA. The reduction may be sudden (e.g., due to a discrete event such as a partial loss of funding, or partial outsourcing), or it may be more gradual, over a period of years (due to technological advances, payroll attrition, etc.), and might not be tied to a discreet event. Generally, the Board would determine that this type of triggering event has occurred only if the Board expects that the reduction in an employer's KCERA-covered payroll is expected to be permanent, long-lasting or for an indefinite period of time that is greater than a cycle that the employer may typically experience, or a cycle similarly experienced by the other participating employers, if any, in the same KCERA cost group. Necessarily, by its nature, the determination whether this type of triggering event has occurred is more subjective than that described immediately above.

EXCLUSIONS FROM COVERAGE; TERMINATIONS OF COVERAGE

5) This Policy also covers only those employers (i) who are financially-viable entities when a triggering event occurs, and (ii) whom KCERA expects to continue indefinitely thereafter to be financially- viable entities. This Policy does not cover any other situation, including, without limitation, an employer going out of business by reason of dissolution, loss of funding, consolidation or merger (unless there is a surviving financially-viable entity that is acceptable to the Board that will make the ongoing appropriations and transfers under the Policy). This Policy also does not cover a "withdrawing employer" who ceases to provide KCERA membership for all of the employer's active KCERA members (i.e., as of a date certain, withdraws both new hires and existing actives from membership with KCERA).

The Board of Retirement recognizes that participating employers covered by this Policy will have UAAL funding obligations for several years. Therefore, if concerns arise during that period of time regarding the employer's ongoing existence as a financially-viable entity, the Board may remove the employer from coverage under this Policy and/or take any other measures that may be available to ensure the actuarial soundness of the retirement system. This includes, without limitation, assessing the projected entire amount of the employer's UAAL (as recommended by the fund's actuary and approved by the Board) in a manner consistent with KCERA's Employer Termination Policy.

PROCEDURES

6)

A. The CEO will (i) work with KCERA Staff and other KCERA service providers (e.g., the actuary), and KCERA participating employers to obtain the information (e.g., KCERA covered payroll history, employer financial reports, budgets, future financial projections, bond-rating agency submissions) needed for the Board to make determinations regarding likely triggering events and exclusions from, or terminations of, coverage and (ii) report to the Board, at least annually, regarding these activities.

B. Upon a recommendation from the CEO and notice to the affected participating employer, the Board will make a determination at a duly-noticed public meeting regarding (i) whether a triggering event has occurred for the employer, (ii) whether the employer should be excluded from coverage under this Policy, and (iii) for those employers that the Board has previously determined to be covered under the Policy, whether their coverage should be terminated under section 5 above. Employers may be required to provide KCERA with updated employee census and payroll data and financial reports. See CERL section 31543.

C. If the Board determines that a triggering event has occurred and the employer is not excluded from coverage under the Policy, then, solely for purposes of determining the covered employer's UAAL contribution obligation, KCERA will segregate on its books all assets and liabilities attributable to the employer, based upon the recommendation of KCERA actuary, and shall maintain such separate accounting for the employer until all of the participating employer's obligations to KCERA have been fully satisfied. The employer will be placed in its own cost group for purposes of determining employer and employee contributions. Consistent with section 2 above, the employer's Normal Cost will continue to be based on the active members of the covered employer.

D. KCERA's actuary will determine, and certify to the Board of Retirement, the covered employer's funding obligation for its initial UAAL, which obligation shall not be pro-rata based on payroll, but rather based on the dollar amount of the employer's actuarial accrued liability (AAL), including inactive and deferred members. The Board will generally require the employer's contributions to be paid in level, fixed-dollar amounts over a period not to exceed eighteen (18) years, beginning on July 1 of the fiscal year immediately after the year in which the triggering event occurs. In appropriate circumstances, the Board may determine, consistent with its fiduciaries duties, it is appropriate to collect the necessary contributions in a different manner.

E. The actuary will use the actuarial valuation performed for KCERA as of the end of the fiscal year immediately prior to the fiscal year in which the triggering event occurs (and based on all of KCERA's then current actuarial

assumptions and methodologies) to determine the initial AAL of the covered employer. The initial valuation value of assets (VVA), a smoothed value, will be determined using a pro-rata allocation based on the ratio of the employer's initial AAL to the AAL of all employers in the same cost group. As a result of this methodology, the initial UAAL (i.e., the initial AAL minus the initial VVA) will also be allocated pro-rata based on the covered employer's AAL in proportion to that of the other employers in the same cost group. Later values of the VVA (i.e., those used in the future valuations described below) shall be determined by rolling forward the initial VVA, adding contributions, deducting benefit payments, and crediting earnings at the actual smoothed (VVA) earnings rate on total KCERA assets.

F. Annually, after the determination of the covered employer's initial funding obligation, as part of the regular annual actuarial valuation of the plan, KCERA's actuary will measure any change in the UAAL of the participating employer due to actuarial experience or changes in actuarial assumptions. In addition to the amortized payments for the covered employer's initial UAAL funding obligation determined as of the initial valuation, the employer will be liable for, and must contribute to KCERA, any such new UAAL determined as of subsequent valuations, based upon an amortization schedule recommended by the actuary and adopted by the Board of Retirement. KCERA will hold any negative UAAL (Surplus) to be applied against any future UAAL of the covered employer.

G. If any Surplus remains after the covered employer has fully satisfied all of its UAAL obligations (Final Surplus), KCERA will distribute the Final Surplus in accordance with the terms of applicable law.

POLICY REVIEW AND HISTORY

7) This policy will be reviewed at least every five (5) years.
8) This policy was:
   a) Adopted by the Board on May 9, 2018.
   b) Amended June 8, 2022.