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ACTUARIAL FUNDING POLICY

PURPOSE

The purpose of this Actuarial Funding Policy is to record the funding objectives and policy set by the Board of Retirement (Board) for the Kern County Employees' Retirement Association (KCERA). The Board establishes this Actuarial Funding Policy to help ensure the systematic funding of future benefit payments for members of KCERA. In addition, this document records certain policy guidelines established by the Board to assist in administering KCERA in a consistent and efficient manner.

This Actuarial Funding Policy supersedes any previous Actuarial Funding Policies. It is a working document and may be modified as the Board deems necessary.

BACKGROUND

KCERA is a public employee retirement system that was established on January 1, 1945 to provide retirement allowances and other benefits to all permanent general and safety employees of the County of Kern and participating special districts.

These benefits are financed through a combination of employee and employer contributions along with the investment return on those contributions. Benefit and contribution level may vary within KCERA depending on the member's classification (General or Safety), tier and by participating employer (County or one of the Special Districts).

KCERA is governed by the provisions of the County Employees Retirement Law of 1937 (1937 Act). Kern County adopted Article 5.5 of the 37 Act. This Article creates a Supplemental Retiree Benefit Reserve (SRBR) through which the Board may pay supplemental benefits to retirees and beneficiaries.

An actuarial valuation is performed annually as of June 30 of each year to determine the contribution rates for the following fiscal year that begins 12 months after the valuation date.

This funding policy applies to "regular benefits" which refer to the retirement, disability, survivor and withdrawal benefits, and all cost-of-living increases that were adopted by the County of Kern (or the special districts) and whose payments are guaranteed by those agencies. This policy does not cover benefits financed by the SRBR, except in instances when the benefits have been guaranteed by the County and special districts.

GOALS OF ACTUARIAL FUNDING POLICY

1. To achieve long-term full funding of the cost of benefits provided by KCERA;

2. To seek reasonable and equitable allocation of the cost of benefits over time; and,

3. To minimize volatility of the plan sponsor's contribution to the extent reasonably possible, consistent with other policy goals.

In addition, to the extent that it does not conflict with the above goals, the Board will try to pool risks across all portions of KCERA to the extent that those groups have similar benefit provisions, contribution provisions and contribution histories. Separate cost groups will be set up to recognize meaningful differences in benefit structure (e.g., Safety or General), employee contribution levels (e.g., whether the employer pays employee contributions after five years of service), employer contribution history (e.g., payment of extraordinary contributions like Pension Obligation Bond payments) and benefit changes (for prior service or not).

FUNDING REQUIREMENT AND POLICY COMPONENTS

KCERA annual funding requirement for "regular benefits" is comprised of a payment of the Normal Cost and a payment on the Unfunded Actuarial Accrued Liability (UAAL). The Normal Cost and the amount of payment on UAAL are determined by the following three components of this funding policy:

I. Actuarial Cost Method: the techniques to allocate the cost/liability of retirement benefit to a given period;

II. Asset Smoothing Method: the techniques that spread the recognition of investment gains or losses over a period of time for the purposes of determining the Actuarial Value of Assets used in the actuarial valuation process; and

III. Amortization Policy: the decisions on how, in terms of duration and pattern, to reduce the difference between the Actuarial Accrued Liability and the Valuation Value of Assets in a systematic manner.

I. Actuarial Cost Method:

The Entry Age Normal method shall be applied to the projected retirement benefits in determining the Normal Cost and the Actuarial Accrued Liability. The Normal Cost shall be determined on an individual basis for each active member.

II. Asset Smoothing Method:

The investment gains or losses of each valuation period, as a result of comparing the actual market return and the expected market return, shall be recognized semi-annually in level amounts over 5 years in calculating the Actuarial Value of Assets. Deferred investment gains or losses cannot exceed 50% of the Market Value of Assets. Note that the Valuation Value of Assets is the Actuarial Value of Assets reduced by any applicable Non-Valuation Reserves.

III. Amortization Policy:

- The UAAL, (i.e., the difference between the Actuarial Accrued Liability and the Valuation Value of Assets), as of June 30, 2011 shall be amortized separately from any future changes in UAAL over a period of 24.5 years from June 30, 2011.
- Any new UAAL as a result of actuarial gains or losses identified in the annual valuation as of June 30 will be amortized over a period of 18 years.
- Any new UAAL as a result of change in actuarial assumptions or methods will be amortized over a period of 18 years.
- Unless an alternative amortization period is recommended by the Actuary and accepted by the Board based on the results of an actuarial analysis:

  a. with the exception noted in b., below, the change in UAAL as a result of any plan amendments will be amortized over a period of 15 years or less;

  b. the increase in UAAL resulting from a temporary retirement incentive, including the impact of benefits resulting from additional service permitted in Section 31641.04 of the 1937 CERL (Golden Handshake), will be funded over a period of up to 5 years. For Golden Handshakes, the employer has the choice of two methods:

     i. Payment in full for the UAAL attributable to the Golden Handshake in the first month of the fiscal year following the fiscal year in which the Golden Handshake was granted.

     ii. Payment according to a five-year amortization period which will be invoiced (payable in 30 days) to the employer in the first month of the fiscal year following the fiscal year in the which the Golden Handshake was granted. The amortization schedule will be based upon the valuation interest rate used in the most recently completed valuation at the time that the amortization schedule is created. The employer may complete payment of the Golden Handshake at any time during the five-year amortization period.

        If the amortization method is used, then the outstanding balance will generally be recorded as a receivable asset to be included with the Actuarial Value of Assets. All Golden Handshakes provided by an employer during any fiscal year will be bundled together and will be invoiced in one transaction in the first month following the fiscal year in which the Golden Handshakes were granted.

- UAAL shall be amortized over “closed” amortization periods so that the amortization period for each layer decreases by one year with each actuarial valuation.

- UAAL shall be amortized as a level percentage of payroll so that the amortization amount in each year during the amortization period shall be expected to be a level percentage of covered payroll, taking into consideration the current assumption for general payroll increase.

- If an overfunding exists (i.e., the total of all UAAL becomes negative so that there is a surplus), such surplus and any subsequent surpluses will be amortized over an "open" amortization period of 30 years. Any prior UAAL amortization layers will be considered fully amortized, and any subsequent UAAL will be amortized over 18 years as the first of a new series of amortization layers.

- These amortization policy components will apply separately to each of KCERA's UAAL cost sharing groups.

OTHER POLICY CONSIDERATIONS

- Timing of Contributions

  a. In order to allow the employers to more accurately budget for pension contributions and other practical considerations, the contribution rates determined in each valuation (as of June 30) will apply to the fiscal year beginning 12 months after the valuation date. The UAAL contribution rates in the actuarial valuation are adjusted to account for this one-year delay.

  b. Any change in contribution rate requirement that results from a plan amendment (including a change in member contribution rates) is generally implemented as of the effective date of the plan amendment or as soon as administratively feasible.

  c. For purposes of calculating employer contributions, we assume that the employer and member contributions will be made during consistent intervals throughout the year.

- Cost Groups

  Separate cost groups will be set up in order to recognize differences in benefit structure (e.g., General Tier I, General Tier II or Safety), member contribution levels, employer contribution history (e.g., payment of extraordinary contributions like Pension Obligation Bond (POB) payments), and other differences that the Board deems significant, such as benefit changes on a prospective basis only.

  This structure is based on the assumption that all General members have similar benefit provisions (Tier I and II separately), and that all Safety members have similar benefit provisions. However, additional separate employer cost groups may be established by the Board as needed. An employer may be contributing to one or more different cost groups depending on the benefit structure adopted for its employees.

a. KCERA's Total (employer and member) Normal Cost is determined separately for each group of members that have the same benefit formula (on a prospective basis) based on the Actuarial Cost Method described above. This means that to the extent that members have the same plan provisions for future benefit accruals, then the Total Normal Cost (as a percentage of payroll) for those employers will be the same.

b. The net employer Normal Cost is calculated by reducing the Total Normal Cost for expected member contributions. This is done separately for each of the different member contribution arrangements and benefit structures that exist at the various employers. The various member contribution arrangements are described in more detail in the actuarial valuation report.

c. KCERA's UAAL is determined separately based on contribution and benefit history. This means that there could be separate calculations of AAL for cost groups that have significantly different contribution histories, or prior benefit accrual provisions (e.g., General County and Courts, General Districts and Safety). Plan assets are tracked separately for groups with different UAAL contribution histories unless otherwise established by the Board.

d. There is a further adjustment made to the UAAL contribution rate to account for District Category IV adopting the 3% @ 60 formula on a prospective basis only. This adjustment is described in more detail in the actuarial valuation report.

- Transfers

When employees transfer from one participating employer to another KCERA participating employer, recognition needs to be made of the employee's prior service within KCERA on an equitable basis. For each employee that transfers within KCERA the funding for the employee's benefits will be determined as follows:

a. The employee will be reported and funded as a vested terminated employee for the former participating employer with reciprocal benefits the same as any other vested terminated employee who moves to a reciprocal retirement system other than KCERA.

b. The employee will be reported and funded as an active employee for the new participating employer but with reciprocal service credits for the prior service in KCERA for purposes of benefit eligibility and entry age. Benefit amounts will be funded only for the service provided to the new participating employer.

c. Upon retirement from KCERA, the employee's total retirement benefit will be determined based on service with each KCERA participating employer and the employee's Final Average Salary.

The entire liability for the retired employee's KCERA benefit payments will be allocated to the latest participating employer's cost group. The employee will be reported as a retired employee for the latest participating employer with the full KCERA retirement benefit amount.

GLOSSARY OF FUNDING POLICY TERMS

Present Value of Benefits (PVB) or total cost: the present value at a particular point in time of all projected future benefit payments for current plan members. The future benefit payments and the present value of those payments are determined using actuarial assumptions as to future events. Examples of these assumptions are estimates of retirement patterns, salary increases, investment returns, etc. Another way to think of the PVB is that if the plan has assets equal to the PVB and all actuarial assumptions are met, then no future contributions would be needed to provide all future service benefits for all current members, including future service and salary increases for current active members.

Actuarial Cost Method: allocates a portion of the total cost (PVB) to each year of service, both past service and future service.

Normal Cost (NC): the cost allocated under the Actuarial Cost Method to each year of active member service.

Entry Age Normal Actuarial Cost Method: A funding method that calculates the Normal Cost as a level percentage of pay over the working lifetime of the plan's members.

Actuarial Accrued Liability (AAL): the value at a particular point in time of all past Normal Costs. This is the amount of assets the plan would have today if the current plan provisions, actuarial assumptions and participant data had always been in effect, contributions equal to the Normal Cost had been made and all actuarial assumptions came true.

Market Value of Assets (MVA): the fair value of assets of the plan as reported in the plan's audited financial statements.

Actuarial Value of Assets (AVA) or smoothed value: a market-related value of the plan assets. The AVA tracks the market value of assets over time and smoothes out short-term fluctuations in market values.

Valuation Value of Assets (VVA): the value of assets used in the actuarial valuation to determine contribution rate requirements. It is equal to the Actuarial Value of Assets reduced by the value of any applicable Non-Valuation Reserves as defined in KCERA's Statement of Interest Crediting Policy. In particular, the VVA will not include assets allocated to the SRBR, unless those assets have been set aside within the SRBR to help fund a benefit guaranteed by the County and other employers.

Unfunded Actuarial Accrued Liability (UAAL): the positive difference, if any, between the AAL and the VVA.

Surplus: the positive difference, if any, between the VVA and the AAL.

Actuarial Value Funded Ratio: the ratio of the VVA to the AAL.

Market Value Funded Ratio: the ratio of the MVA to the AAL.

Actuarial Gains and Losses: changes in UAAL or surplus due to actual experience different from what is assumed in the actuarial valuation. For example, if during a given year the assets earn more than the investment return assumption, the amount of earnings above the assumption will cause an unexpected reduction in UAAL, or "actuarial gain" as of the next valuation. These include contribution gains and losses that result from actual contributions made being greater or less than the level determined under the policy.

Valuation Date: June 30 of every year.

POLICY REVIEW AND HISTORY

1) This policy shall be reviewed at least every five (5) years.
2) This policy was:
   a) Adopted by the Board on May 16, 2012.
   b) Amended on June 8, 2022.