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Via Email

April 19, 2023

Ms. Linda Webb
Retirement Administrator
Ventura County Employees' Retirement Association
1190 South Victoria Avenue, Suite 200
Ventura, CA 93003

**Re: Ventura County Employees' Retirement Association (VCERA)
Alameda Decision Implementation**

Dear Linda:

On July 30, 2020, the California Supreme Court issued a decision in the case of Alameda County Deputy Sheriffs' Association et al. v. Alameda County Employees' Retirement Association (ACERA) and Board of Retirement of ACERA. That decision has important implications for VCERA and its members. In this letter, we are responding to a request to calculate the impact on VCERA liabilities and contribution rates as of June 30, 2022 of potential Board action to exclude non-cashable flexible benefit credits as required by the Alameda decision, based on additional demographic information provided by VCERA.

Background[1]

The Alameda decision requires pension systems like VCERA to exclude certain pay items from a legacy member's compensation earnable, including standby pay, termination pay and certain annual leave redemptions. In addition, it also addressed in-kind benefits not payable in cash directly to the member. These in-kind benefits are also referred to as cafeteria plan allowances or flexible benefit credits. Because Ventura County's full flexible benefit credit allowance has been treated as pensionable, the exclusion of these in-kind benefits not received in cash has the most significant impact for Ventura County.

As a result of the California Supreme Court's Alameda decision, the SEIU and the County of Ventura sponsored Assembly Bill 826 which would have allowed, under specific conditions, Legacy members' compensation earnable to include a larger portion of their flexible benefit credits. However, on September 29, 2022, Governor Newsom vetoed Assembly Bill 826 therefore making only the cashable portion of the flexible benefit credits eligible to be included in the determination of compensation earnable.

At its October 24, 2022 business meeting, the VCERA Board of Retirement voted to delay the exclusion of the non-cashable flexible benefit credits from compensation earnable for Legacy

[1] This background material was prepared based on information available on VCERA's website.

members, and to revisit the item at its first business meeting in April of 2023. In the meantime, the County of Ventura has requested an actuarial study to calculate the impact as of June 30, 2022 of excluding non-cashable flexible benefit credits.

Discussion and Results

In the June 30, 2022 actuarial valuation, neither the June 30, 2022 assets provided by VCERA nor the June 30, 2022 liabilities Segal calculated using the membership data provided by VCERA reflected the financial impact of the exclusion of non-cashable flexible benefit credits.

Step One: Member Contribution Refunds

The first part of the study deals with member contributions that have already been made. As contributions are collected on pay that is included in compensation earnable, and prior to the Alameda decision non-cashable flexible benefit credits had been included in compensation earnable, members have made contributions that are now considered overpayments due to the exclusion of non-cashable flexible benefit credits from compensation earnable. Because any refund of contribution overpayments would be paid from plan assets, those refunds would directly increase the Unfunded Actuarial Accrued Liability (UAAL) and corresponding employer UAAL contribution.

VCERA provided Segal the amounts of non-cashable flexible benefit credits to be excluded by fiscal year and bargaining unit beginning in FYE 1990 and through the pay period ending May 28, 2022.[2] The amounts were broken down into the following ten categories: G1C-COURTS, G1C-DGS, G1C-NDGS, G2C-GE6, G2-COURTS, G2-DGS, G2-GE7, S1C-DS, S1C-FSM, and S1C-PS. In addition, VCERA provided the contribution rate history for each of the ten groups. Using the single entry age based rates[3] provided by VCERA and a 7.8% annual interest crediting rate[4] to accumulate past member contribution overpayments to June 30, 2022, Segal estimated that as of June 30, 2022, approximately $76.9 million in contribution refunds were due members from VCERA as a result of the exclusion of non-cashable flexible benefit credits from compensation earnable. Such refunds would increase the UAAL by an amount equal to the $76.9 million, and the ratio of the Valuation Value of Assets (VVA) to the Actuarial Accrued Liability (AAL) would decrease from 97.2% to 96.1%. In addition, the aggregate employer UAAL contribution would increase by about $6.8 million in the first year (the annual amount of contribution increase would itself increase with the 3.00% per annum payroll growth assumption in each of the subsequent 14 years).[5]

[2] Per VCERA, the following assumptions were used in compiling this information:
1. For any pay period where employer, union, or plan cannot be identified, assume County SEIU for General and County Sheriff for Safety.
2. Does not take any prior period adjustments into account, i.e., exclude earning codes.
3. Does not take plan changes into account, i.e., assume plan associated with flexible benefit credit earning code is correct.
4. Assume all flexible benefit credit records are a part of member's current VCERA membership, i.e., amounts may be overstated if member has a prior refunded membership.

[3] For this calculation, Segal used the "Reg Rate 2" and the "COLA Rate 2" from the spreadsheet provided by VCERA. These are the rates that would be paid on compensation over the first $350 for members integrated with Social Security.

[4] Based on guidance from the County.

[5] We have amortized the change in UAAL over a separate 15-year declining period based on VCERA's Actuarial Funding Policy for plan amendments.

Segal has been asked to provide a dynamic spreadsheet in which the County of Ventura can adjust various parameters. In a separate cover, Segal will provide a spreadsheet in which the following parameters can be adjusted:[6]

1. The annual interest crediting rate; and

2. The amortization period.

Step Two: Recoupment of Retiree Benefit Overpayments

The next part of the study deals with retiree benefit payments that have already been made. As benefit payments are based on pay that is included in compensation earnable, and prior to the Alameda decision non-cashable flexible benefit credits had been included in compensation earnable, retirees have received benefits that are now considered overpayments due to the exclusion of non-cashable flexible benefit credits from compensation earnable. Because any collection of benefit overpayments would increase plan assets, those collections would directly reduce the UAAL and corresponding employer UAAL contribution. Based on discussions with the County and VCERA staff, we have not included the impact of the collection of benefit overpayments in this study.[7]

Step Three: Prospective Reductions in Benefit Amounts for Current and Future Retirees

The final part of the study deals with prospective retiree benefit payments. Similar to the recoupment of retiree benefit overpayments, as benefit payments are based on pay that is included in compensation earnable, and prior to the Alameda decision non-cashable flexible benefit credits had been included in compensation earnable, retirees benefit amounts are now considered to have been overstated due to the exclusion of non-cashable flexible benefit credits from compensation earnable. In addition, active and deferred vested salaries reported to Segal for the June 30, 2022 actuarial valuation and used to project future benefit payments at retirement included the non-cashable flexible benefit amounts. Prospective reductions in retiree benefit amounts would result in a reduction in both the AAL and the UAAL as well as the corresponding employer UAAL contribution.

Note that in addition to reductions in benefit amounts, there would also be a reduction in both the employer and member normal cost contributions as the contributions would be collected over a smaller payroll.

VCERA provided Segal with the following additional demographic data as of June 30, 2022:

[6] Segal cannot vouch for the accuracy of any other estimates provided by the County of Ventura under parameters other than a 7.8% annual interest crediting rate to accumulate past member contribution overpayments to June 30, 2022 and a 15-year amortization period unless we are asked to review such alternatives. Note that any alternative amortization period would need to be approved by the Board of Retirement.

[7] It is our understanding that benefit overpayments were not to be considered in this study as it would be very time consuming for VCERA to determine these amounts, and because not considering the overpayments results in a greater net reduction in plan assets thus giving a more conservative estimate of the net cost reductions as a result of the exclusion of non-cashable flexible benefit credits from compensation earnable.

1. For active members, the following amounts were recalculated excluding non-cashable flexible benefit credits: current pensionable bi-weekly salary, current earnable bi-weekly salary, annualized bi-weekly salary, last 36-month average salary and last 12-month average salary.

2. For deferred vested members, the annualized bi-weekly salary was recalculated excluding non-cashable flexible benefit credits. Segal applied the ratio of the revised annualized bi-weekly salary to the amount originally provided for the June 30, 2022 actuarial valuation to the final average compensation amounts in the June 30, 2022 actuarial valuation.[8]

3. For retirees and beneficiaries, the following amounts were recalculated excluding non-cashable flexible benefit credits: 12-month FAC (including buydowns), 36-month FAC (including buydowns), total base benefit, base benefit eligible for regular COLA and base benefit eligible for SEIU COLA.[9]

Using the additional demographic data provided by VCERA, along with other information received as part of the June 30, 2022 actuarial valuation, Segal estimated that there would be a reduction in the AAL as of June 30, 2022 of approximately $189.0 million as a result of the exclusion of non-cashable flexible benefit credits from compensation earnable in the determination of prospective benefit amounts for current and future retirees. There would be a corresponding reduction in the UAAL equal to the $189.0 million, and the ratio of the VVA to the AAL would increase from 97.2% to 99.7%. In addition, the aggregate employer UAAL contribution would decrease by about $16.8 million in the first year (the annual amount of contribution decrease would itself increase with the 3.00% per annum payroll growth assumption in each of the subsequent 14 years).[10] Finally, the aggregate employer normal cost contribution would decrease by about $3.3 million as of June 30, 2022.

Combined Impact from Steps One through Three

Exhibit A details the net impact of the exclusion of non-cashable flexible benefit credits from compensation earnable determined earlier in Steps One and Three. As of June 30, 2022, there would be a net reduction in the UAAL of $112.1 million, and the ratio of the VVA to the AAL would increase from 97.2% to 98.6%. The aggregate employer contribution would decrease from approximately $159.2 million to $145.9 million. Finally, the aggregate member contribution rate would increase by 0.04% of payroll.[11]

[8] For conservatism, we limited the decrease in final average salary for deferred vested members to 10%.

[9] Segal used the revised base benefits eligible for respective COLAs and the original amounts eligible for respective COLAs provided for the June 30, 2022 actuarial valuation to determine the revised COLA benefit amounts.

[10] We have amortized the change in UAAL over a separate 15-year declining period based on VCERA's Actuarial Funding Policy for plan amendments.

[11] The slight increase in aggregate member contribution rate is due to the calculating a new aggregate rate by compositing the same contribution rates but using different payroll amounts after exclusion of non-cashable flexible benefit credits for Legacy members.

Exhibit B provides a 15-year projection of the Normal Cost[12] and UAAL contributions before and after reflecting the potential Board action to exclude non-cashable flexible benefit credits, as well as the total employer contribution reduction. Note those amounts are based on the assumptions outlined in this study, including a 7.8% annual interest crediting rate to accumulate past member contribution overpayments to June 30, 2022, and a 15-year declining amortization period for changes in the UAAL.

We emphasize that projections, by their nature, are not a guarantee of future results. The modeling projections are intended to serve as illustrations of future financial outcomes that are based on the information available to us at the time the modeling is undertaken and completed, and the agreed-upon assumptions and methodologies described herein. Emerging results may differ significantly if the actual experience proves to be different from these assumptions or if alternative methodologies are used. Actual experience may differ due to such variables as demographic experience, the economy, stock market performance and the regulatory environment.

Unless otherwise noted, all of the above calculations are based on the June 30, 2022 actuarial valuation results including the participant data and actuarial assumptions on which that valuation was based. That valuation and these calculations were completed under the supervision of Molly Calcagno, ASA, MAAA, Enrolled Actuary.

Segal valuation results are based on proprietary actuarial modeling software. The actuarial valuation models generate a comprehensive set of liability and cost calculations that are presented to meet regulatory, legislative and client requirements. Our Actuarial Technology and Systems unit, comprised of both actuaries and programmers, is responsible for the initial development and maintenance of these models. The models have a modular structure that allows for a high degree of accuracy, flexibility and user control. The client team programs the assumptions and the plan provisions, validates the models, and reviews test lives and results, under the supervision of the responsible actuary.

The undersigned are Members of the American Academy of Actuaries and meet the qualification requirement to render the actuarial opinion contained herein.

Please let us know if you have any questions.

Sincerely,

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

Molly Calcagno, ASA, MAAA, EA
Actuary

JY/bbf
cc: Lori Nemiroff

[12] The Normal Cost amounts are for the closed group of active members as of June 30, 2022. The exclusion of non-cashable flexible benefits would have no impact on new hires as these amounts were already excluded for PEPRA members.

Summary of Key Valuation Results as of June 30, 2022

		Before Reflecting Impact of Alameda Decision ($ in '000s)	After Reflecting Impact of Alameda Decision ($ in '000s)	Difference ($ in '000s)
Actuarial Accrued Liability:	Retired members and beneficiaries	$4,399,379	$4,368,899	-$30,480
	Inactive vested members[1]	234,807	222,916	-11,891
	Active members	2,857,141	2,710,536	-146,605
	Total Actuarial Accrued Liability	$7,491,327	$7,302,351	-$188,976
	Normal Cost for plan year beginning June 30	$180,302	$173,486	-$6,816
Assets:	Market Value of Assets (MVA)	$7,025,332	$6,948,444	-$76,888
	Valuation Value of Assets (VVA)[2]	$7,279,606	$7,202,718	-$76,888
Funded status:	Unfunded Actuarial Accrued Liability on MVA basis	$465,995	$353,907	-$112,088
	Funded percentage on MVA basis	93.78%	95.15%	+1.37%
	Unfunded Actuarial Accrued Liability on VVA basis	$211,721	$99,633	-$112,088
	Funded percentage on VVA basis	97.17%	98.64%	+1.47%

[1] Includes inactive members with member contributions on deposit.
[2] Excludes non-valuation reserves.

Summary of Key Valuation Results as of June 30, 2022 (continued)

		Before Reflecting Impact of Alameda Decision		After Reflecting Impact of Alameda Decision		Difference	
		Total Rate	**Estimated Annual Dollar Amount[1] ($ in '000s)**	**Total Rate**	**Estimated Annual Dollar Amount[1] ($ in '000s)**	**Total Rate**	**Estimated Annual Dollar Amount ($ in '000s)**
Employer Contribution Rates:[2]	• General Tier 1	22.64%	$397	22.03%	$371	-0.61%	-$26
	• General Tier 2	10.91%	21,549	10.14%	18,759	-0.77%	-2,790
	• General PEPRA Tier 2	10.92%	14,084	10.09%	13,014	-0.83%	-1,070
	• General Tier 2 w/COLA[3]	17.91%	32,088	17.37%	28,014	-0.54%	-4,074
	• General PEPRA Tier 2 w/COLA[17]	17.84%	30,183	17.23%	29,151	-0.61%	-1,032
	• General Combined	14.53%	98,301	13.82%	89,309	-0.71%	-8,992
	• Safety	31.74%	45,381	30.52%	41,758	-1.22%	-3,623
	• Safety PEPRA	29.04%	15,530	27.77%	14,851	-1.27%	-679
	• Safety Combined	31.00%	60,911	29.75%	56,609	-1.25%	-4,302
	All Categories Combined	**18.23%**	**$159,212**	**17.44%**	**$145,918**	**-0.79%**	**-$13,294**

1 Based on projected compensation for each scenario.
2 Before reflection of any member rate that may be "picked-up" by the employer. Contributions are assumed to be paid throughout the year.
3 This category represents those Tier 2 members who contribute a negotiated 2.63% of compensation for a fixed 2% COLA pursuant to Government Code 31627 that applies to service after March 2003.

Segal

Projection of Employer Contributions as of June 30, 2022 ($ in '000s)[1]

	Before Reflecting Impact of Alameda Decision						After Reflecting Impact of Alameda Decision		
Fiscal Year[2]	**Employer Normal Cost Contribution[3]**	**Employer UAAL Contribution**	**Total Employer Contribution**	**UAAL[4] Contribution Impact of Refunding Contributions**	**NC Contribution Impact of Prospective Changes**	**UAAL[4] Contribution Impact of Prospective Changes**	**Employer Normal Cost Contribution**	**Employer UAAL[5] Contribution**	**Total Employer Contribution**
2022/2023	$88,725	$70,466	$159,191	$6,849	-$3,256	-$16,833	$85,469	$60,482	$145,951
2023/2024	84,854	72,579	157,433	7,054	-3,167	-17,338	81,687	62,295	143,982
2024/2025	82,397	42,163	124,560	7,266	-3,063	-17,858	79,334	31,571	110,905
2025/2026	79,688	12,791	92,479	7,484	-2,949	-18,394	76,739	1,881	78,620
2026/2027	76,501	7,564	84,065	7,708	-2,813	-18,946	73,688	0	73,688
2027/2028	73,374	7,169	80,543	7,939	-2,678	-19,514	70,696	0	70,696
2028/2029	70,405	5,161	75,566	8,177	-2,549	-20,099	67,856	0	67,856
2029/2030	67,750	5,316	73,066	8,422	-2,425	-20,702	65,325	0	65,325
2030/2031	64,627	5,475	70,102	8,675	-2,291	-21,323	62,336	0	62,336
2031/2032	61,458	5,705	67,163	8,935	-2,149	-21,963	59,309	0	59,309
2032/2033	58,437	0	58,437	9,203	-2,012	-22,622	56,425	0	56,425
2033/2034	55,365	8,226	63,591	9,479	-1,869	-23,301	53,496	0	53,496
2034/2035	52,278	0	52,278	9,763	-1,720	-24,000	50,558	0	50,558
2035/2036	49,569	0	49,569	10,056	-1,585	-24,720	47,984	0	47,984
2036/2037	47,428	0	47,428	10,358	-1,470	-25,462	45,958	0	45,958

1 Does not reflect the recognition of $254.3 million in net deferred investment losses as of June 30, 2022.
2 In practice there is a 12-month delay between the date contributions are determined and the date those contributions are paid. We have not reflected that delay in these illustrations.
3 Does not include normal cost contributions attributable to payroll for new hires after June 30, 2022.
4 Since VCERA does not track assets separately by employer, the UAAL contribution impact would be allocated across all VCERA employers.
5 The employer UAAL contribution cannot be a negative (credit) amount.