2024 Annual Review of Funding Levels and Risks Report

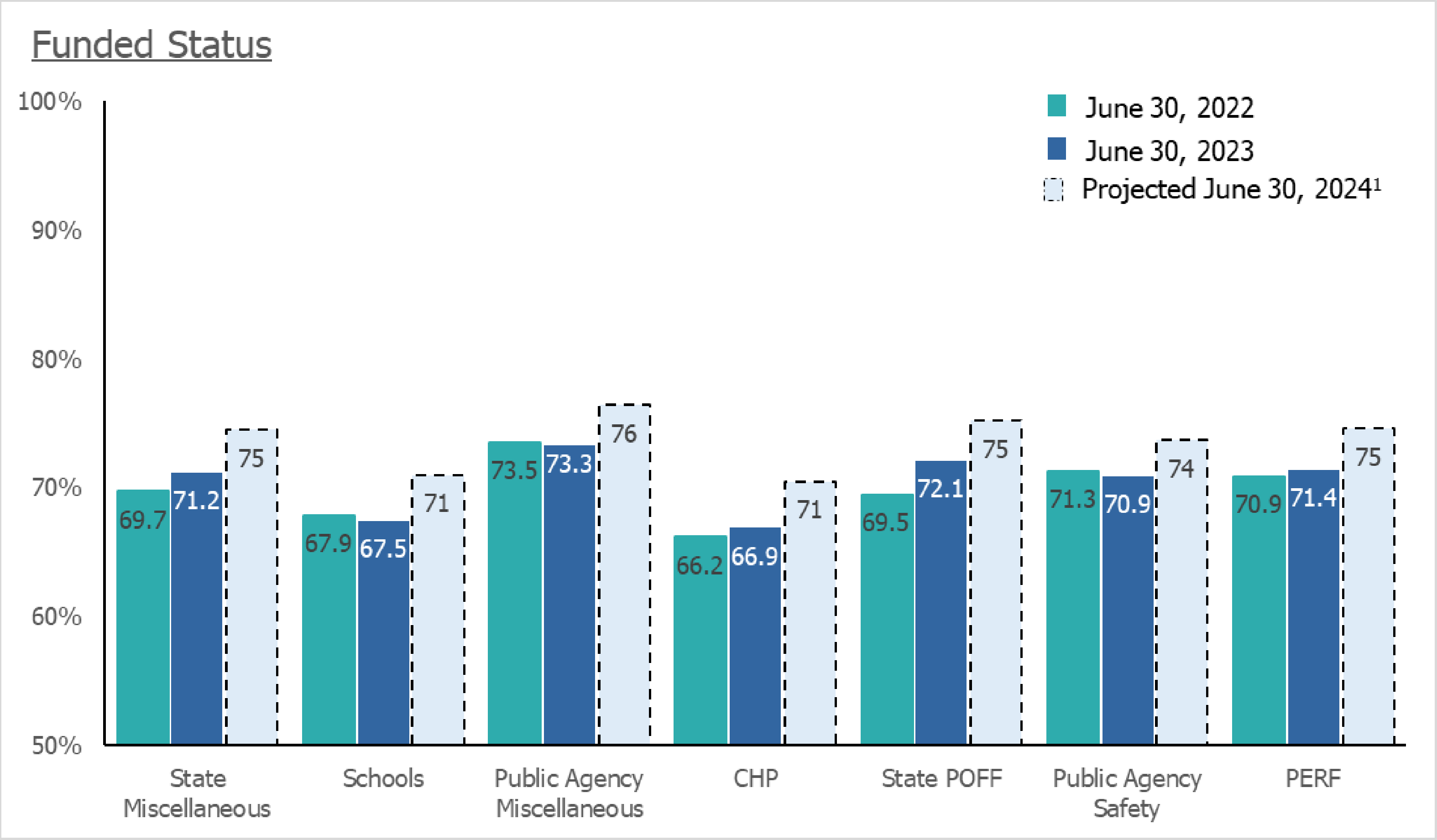
Finance and Administration Committee

November 19, 2024

Key Items

- Current Funded Status of Retirement System
- Employer Contribution Requirements
- Operation of the Funding Policies – Past and Future
- Current and Projected Contribution Requirements
- Identification of Key Risks and Potential Impacts
- Opportunities for Risk Mitigation and Improved System Sustainability – Past and Future

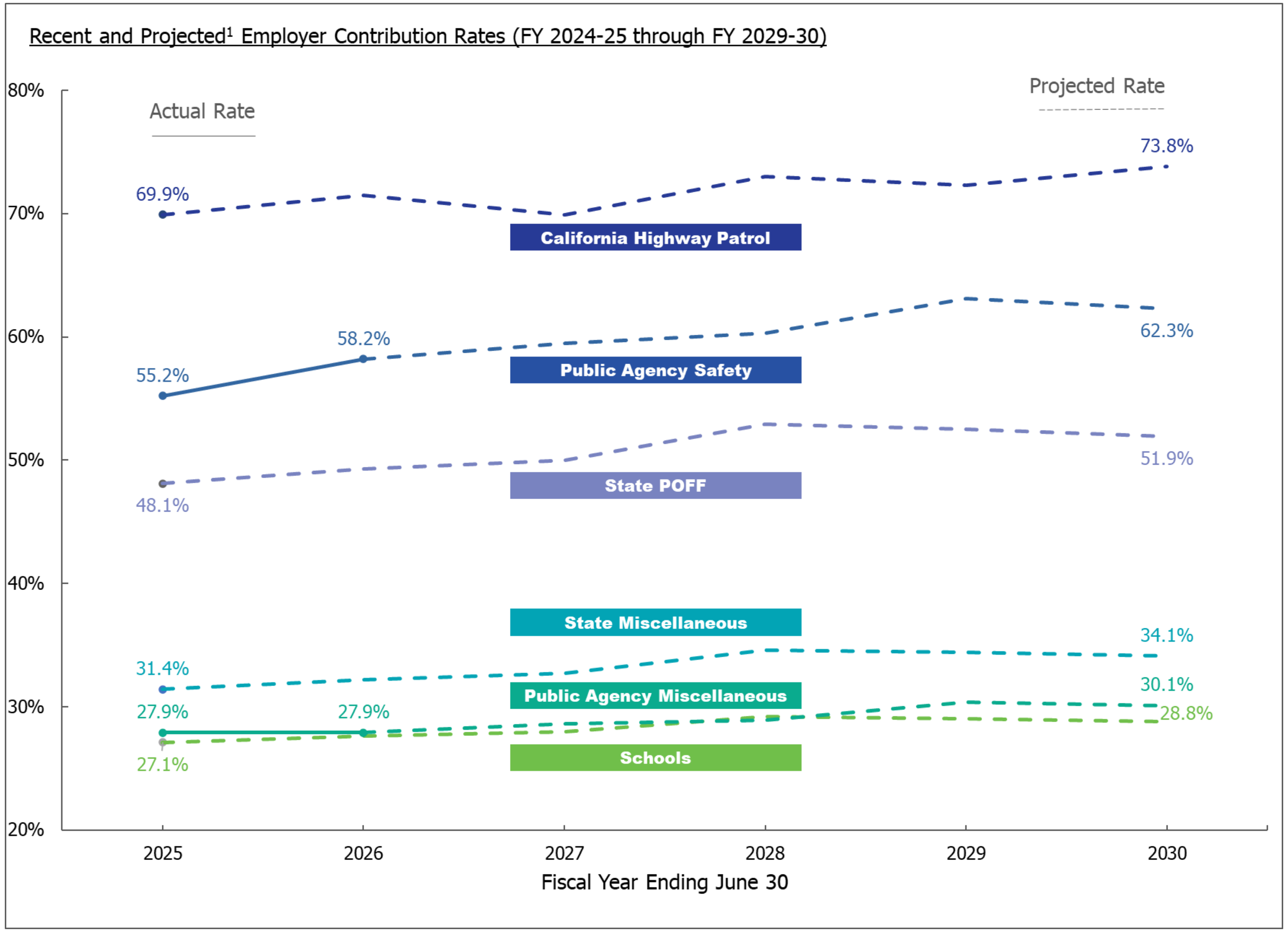
Current Funding Levels



Small improvement from 6/30/22 to 6/30/2023 even though return was slightly lower than 6.8% assumed return.

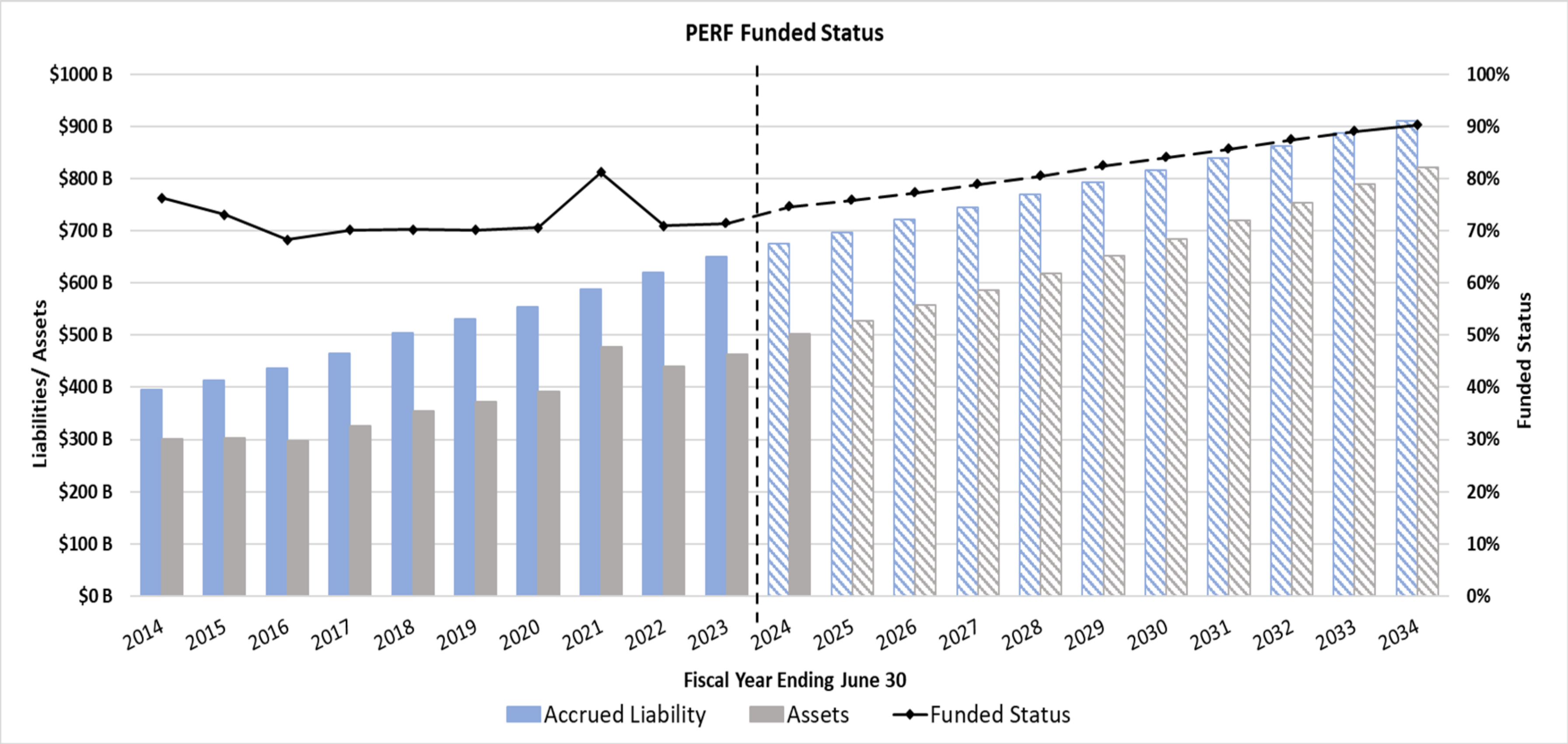
Increases in funded status as of 6/30/2024 are primarily due to the 9.5% investment return last year.

Employer Contribution Requirements



Projected contributions reflect the impact of the 9.5% investment return for the year ending June 30, 2024. This resulted in decreases to the previous projections.

Operation of Funding Policies

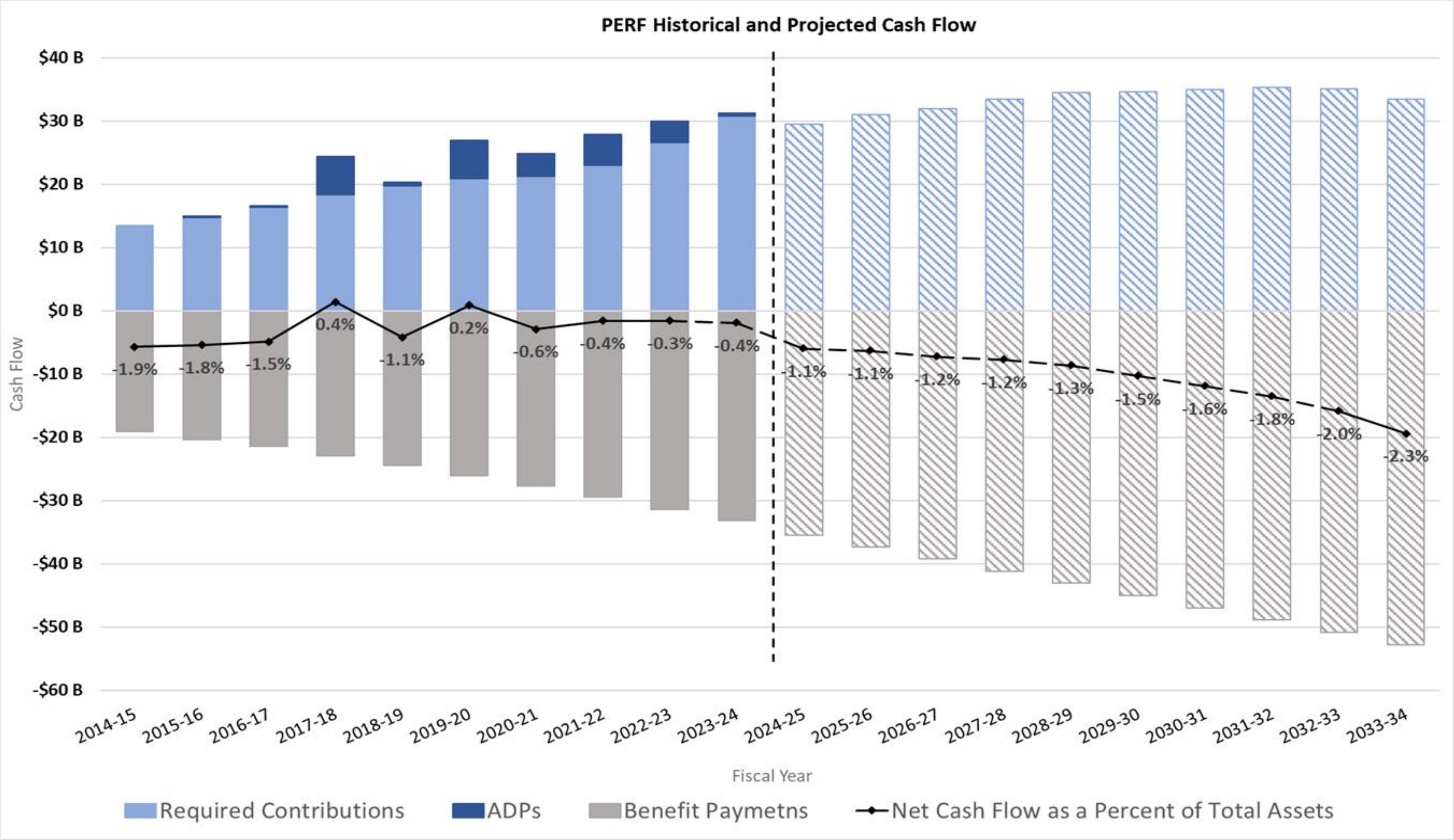


Volatile Funded Status due to uneven investment performance and assumption changes.

Projected improvement in funded status much better than improvement over last 10 years.

Operation of Funding Policies

Benefit payments are expected to continue increasing while contributions are expected to level off and then decrease over the next 10 years.



Negative cash flow is expected to grow over the next 10 years. However, this is neither unexpected nor a serious concern with regard to liquidity needs.

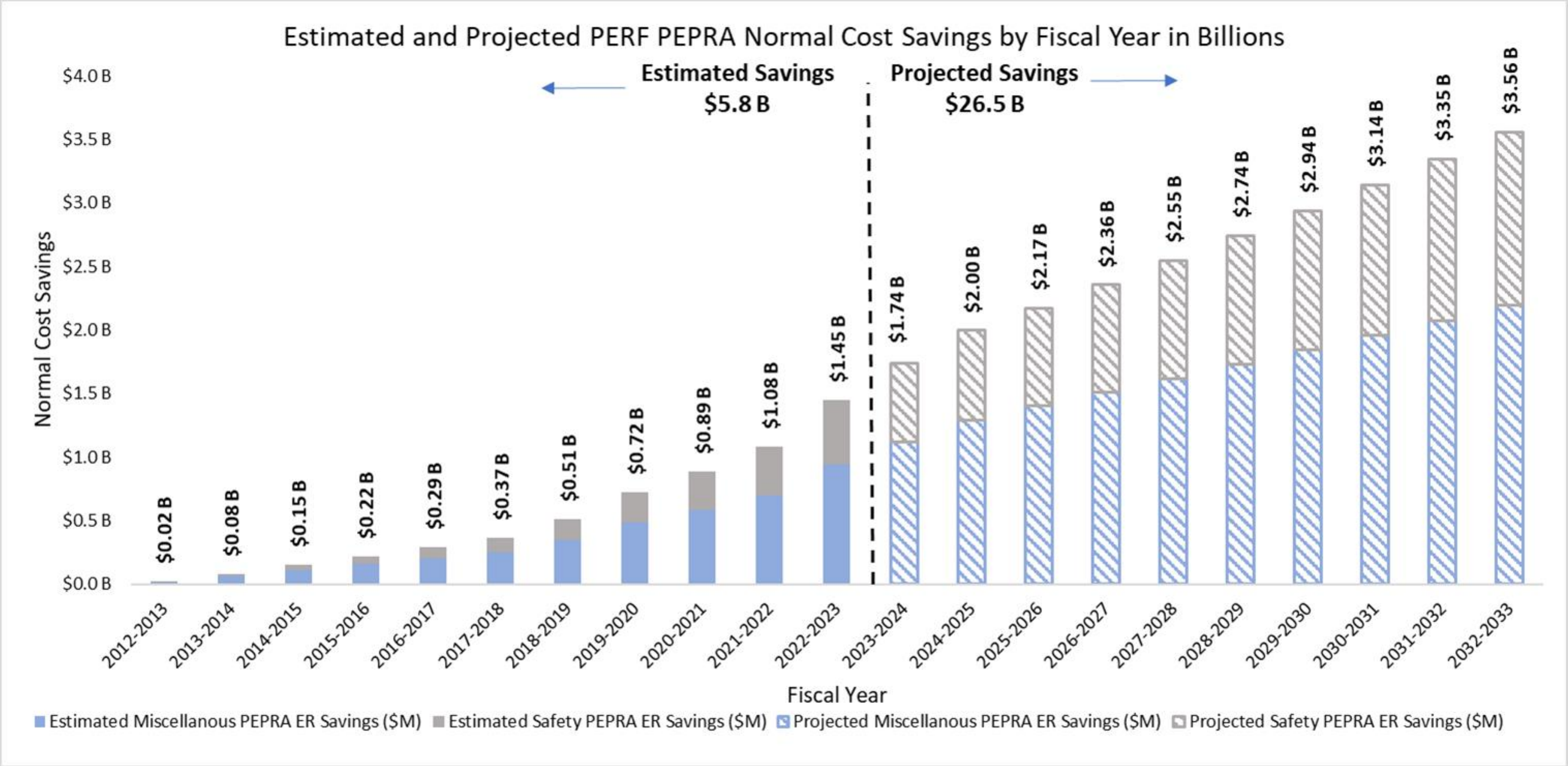
PEPRA

Plan Type	% PEPRA Members 6/30/2024	% PEPRA Payroll 6/30/2024	Estimated Cost Savings to Date	Estimated Cost Savings Next 10 Years
State	58%	47%	$1.7 billion	$8.0 billion
Schools	66%	54%	$1.1 billion	$4.3 billion
Public Agencies	65%	55%	$3.0 billion	$14.2 billion

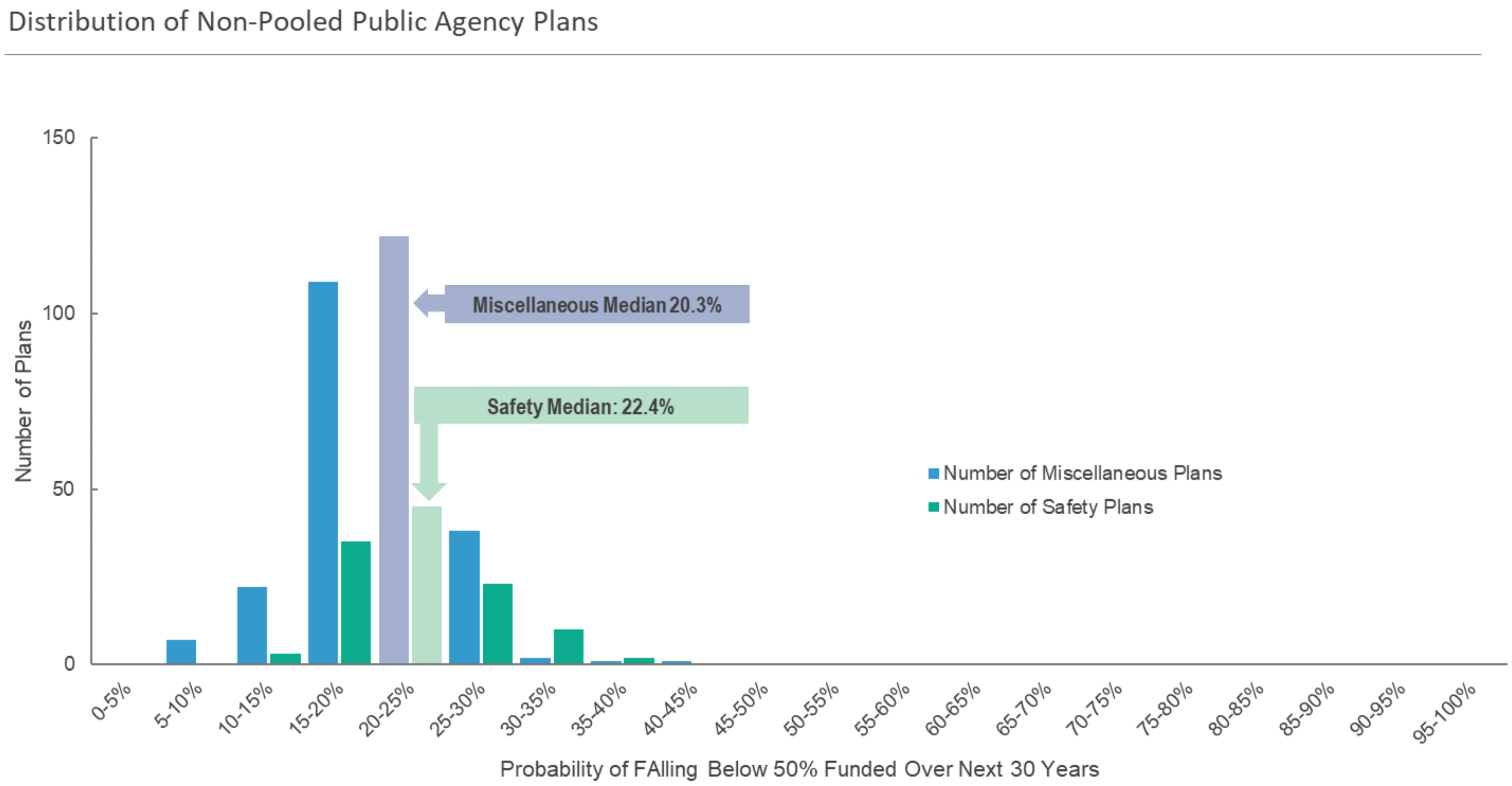
Assuming a level active population, PEPRA membership is expected to increase from about 63% today to 90% over the next 10 years.

PEPRA

While cost savings due to PEPRA began slowly, employers have saved an estimated $5.8 billion over the last 10 years and are expected to save $26.5 billion over the next 10 years.



Investment Risks – Low Funding Level



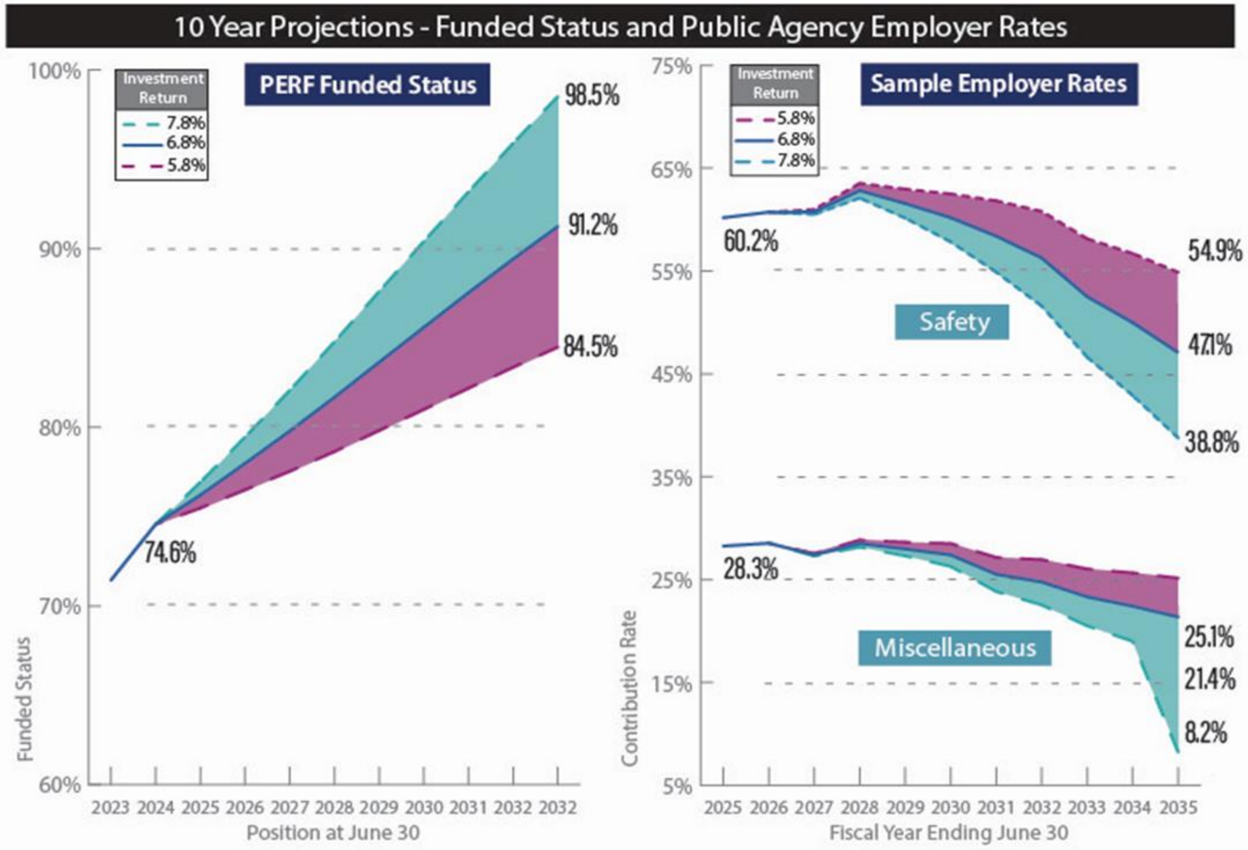
While there is no specific level to protect against, low funded status results in high employer contributions that may be hard for employers to sustain.

An asset portfolio with relatively high investment volatility can increase the likelihood of funding level decreases in the future.

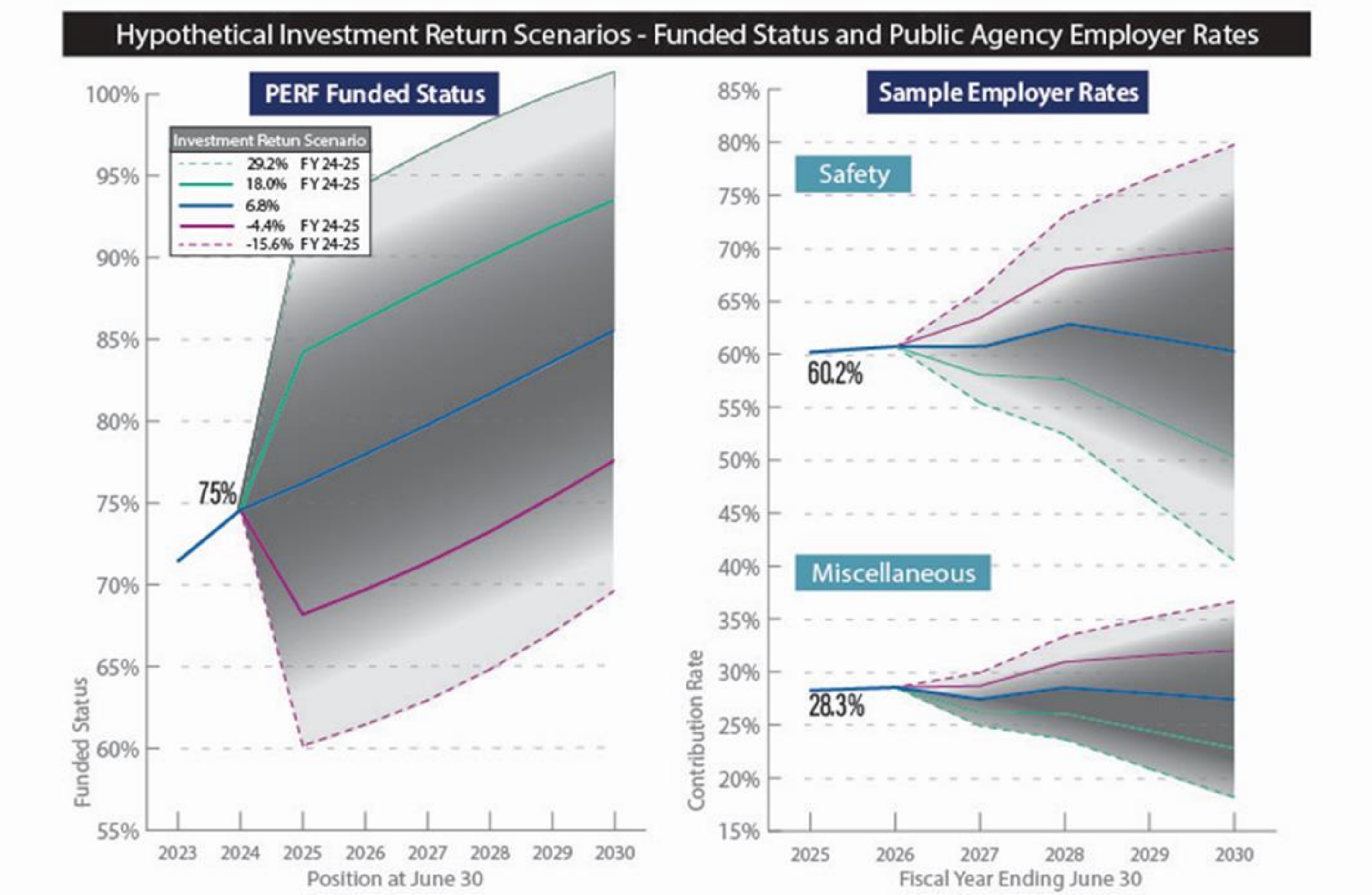
Investment Risks – Achieving 6.8% Long-Term Return

Failing to achieve an average return of 6.8% may lead to slower improvement in funded status and higher employer contributions.

While higher or lower annual investment returns immediately impact the system's funded status, impacts on employer contributions are phased-in over 5 years.



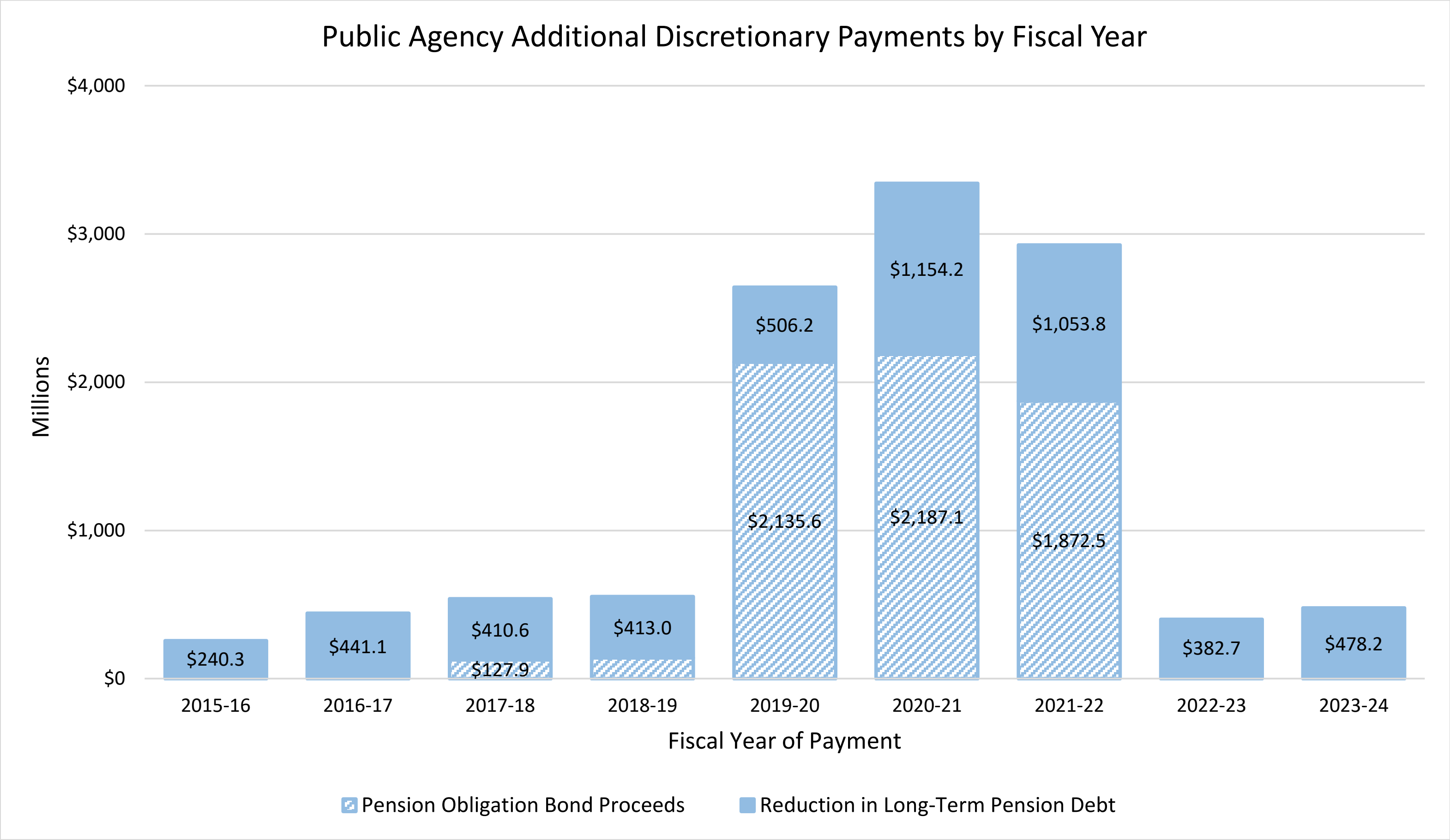
Investment Risks – High Employer Contributions



Large “shock” returns can occur in any year. Such returns can have an immediate impact on funded status.

While impacts on employer contributions can also be significant, such impacts are phased-in over 5 years.

Mitigating Risk – Additional Discretionary Payments



While CalPERS ADPs from Pension Obligation bonds have the same impact on funded status and employer contribution rates, such bonds are additional debt for the employers that issue them.

Mitigating Risk – Summary

- PEPRA changes
- Improvements to Amortization Policy
- Additional Discretionary Payments
- Additional funding through IRC section 115 trusts including the California Employers' Pension Prefunding Trust
- Employer Education
  - ➢Employer Leadership Dialogues
  - ➢Pension Outlook / Managing Employer Contributions (MEC) tools
  - ➢Educational Forum / CSMFO Presentations
  - ➢Summary of Valuation Results Tool

Areas for Future Focus

- Risk / Return balance of investment policy
- Discount rate selection for upcoming ALM process
- Possible near-term economic turmoil