



Summary and Answers to Frequently-Asked Questions about the June 30, 2009 Actuarial Valuation for the City of San Diego

Updated July 9, 2010

SUMMARY

The June 30, 2009 Actuarial Valuation for the City of San Diego (the “2009 Valuation”) incorporates the same benefit provisions and actuarial methods used in the City’s June 30, 2008 actuarial valuation. With the actuarial method and assumption changes that were implemented in prior valuations, SDCERS has completed the transition to using the most widely-accepted, industry-standard actuarial methods used by public pension plans.

FREQUENTLY ASKED QUESTIONS

- 1. Based on the June 30, 2009 Actuarial Valuation for the City of San Diego (the “2009 Valuation”) what is the City’s 2009 Unfunded Actuarial Liability (UAL)?**
Using the Entry Age Normal (“EAN”) funding method, the City’s UAL as of June 30, 2009 was \$2,106.4 million. *[See the 2009 Valuation Letter of Transmittal.]*
- 2. How does the 2009 UAL compare to the 2008 UAL?**
It is \$803.2 million, or 61.6%, higher. The primary cause of the increase was the FY 2009 actuarial investment experience loss of \$811.4 million. FY 2009 liability experience losses of \$6.2 million were largely offset by gains in member contributions. *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at page 4.]*
- 3. What is the City’s 2009 funding ratio?**
As of June 30, 2009, the City’s funding ratio, which is the ratio of the actuarial value of assets (after smoothing) over total actuarial liabilities, was 66.5%. *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at page 3.]*
- 4. How does this compare to the City’s 2008 funding ratio?**
It is 11.6% lower. As of June 30, 2008, the City’s funding ratio was 78.1%. *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at page 3.]*
- 5. What is the City’s Annual Required Contribution (ARC) for FY 2011? (The ARC is the amount the City will have to contribute to SDCERS on or after July 1, 2010.)**
If paid in full in July 2010 as expected, the City’s ARC for FY 2011 will be \$229.1 million (approximately 40.7% of payroll). If the City pays the ARC evenly throughout FY 2011, the contribution will be \$237.8 million (approximately 41.75% of payroll). *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at page 5.]*
- 6. What was the City’s ARC payment for FY 2010?**
The City’s FY 2010 ARC was \$154.2 million, and it was paid in full on July 1, 2009. *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at page 5.]*

7. How is the City's FY 2011 ARC calculated?

The City's employer contributions are composed of two components: the Normal Cost contribution and the UAL contribution.

Normal Cost represents, for each active City employee, the present value (as of June 30, 2009) of the portion of the employee's projected retirement benefit assigned to FY 2011. By paying the Normal Cost, the City pays a fixed percentage of salary to fund SDCERS for the value of benefits over each participant's career. If paid at the beginning of FY 2011, the City's Normal Cost is \$61.3 million.

The UAL portion of the employer contribution is an amount the City pays each year to pay down unfunded liabilities accrued over past years. The UAL is paid-off ("amortized") over a period of years. The City's total June 30, 2009 UAL of \$2,106.4 million is split into several tiers, each using a different amortization period. These tiers are comprised of:

1. the \$1,190.9 million remaining balance of the City's June 30, 2007 UAL now amortized over 18 years (\$87.8 million of the FY 2011 ARC);
2. the \$90.3 million UAL due to the impact of 2008 changes in actuarial assumptions that is amortized over 29 years (\$5.0 million of the FY 2011 ARC);
3. the \$14.6 million UAL due to the FY 2008 experience loss that is amortized over 14 years (\$1.3 million of the FY 2011 ARC); and
4. the \$810.6 million UAL due to the FY 2009 experience loss that is amortized over 15 years (\$73.7 million of the FY 2011 ARC).

Adding the amortization amounts of each tier together results in an FY 2011 UAL amortization payment of \$167.8 million. *[See the 2009 Valuation Letter of Transmittal and the 2009 Valuation at pages 1 and 5.]*

8. What was the market value of SDCERS' Trust Fund on June 30, 2009, and what was the City's portion of this amount?

The market value of the assets in SDCERS' Trust Fund on June 30, 2009 was \$3.715 billion. The City's portion of this amount was \$3.479 billion. *[See the 2009 Valuation at page 15.]*

9. How does this compare to the June 30, 2008 market values?

The June 30, 2009 values are 21% lower. The June 30, 2008 market value for the SDCERS Trust Fund was \$4.696 billion, and the City's portion of the Trust Fund was \$4.409 billion (\$929 million more than at June 30, 2009). This decrease is almost entirely due to the decline in the market value of investments, net of investment income, of \$898 million. This reflects an investment return of -19.2% for the year. *[See the 2009 Valuation at page 15 and 17.]*

10. What is the actuary's assumed investment return for the SDCERS Trust Fund?

For the 2009 Valuation, SDCERS' actuary assumes a long-term average investment return of 7.75% for Trust Fund assets. *[See the 2009 Valuation at page 43.]*

11. What were the annualized investment returns of Trust Fund assets?

SDCERS' annualized investment returns at market value for the one, three, five and ten-year periods ended June 30, 2009, as reported by Callan Associates, SDCERS' Investment Consultant, were -19.2%, -3.5%, 2.3% and 4.6%, respectively. Annualized investment returns are different from the actuarial rate of return calculated by the actuary (e.g., -6.18% for the year ending June 30, 2009) because the actuary computes the actuarial return using the Expected Value of Assets smoothing method. *[See the 2009 Valuation at pages 16 and 17.]*

12. How does the Expected Value of Assets smoothing method work?

The Expected Value of Assets smoothing method dampens the volatility in asset values that can occur because of fluctuations in market conditions. Use of an asset smoothing method is consistent with the long-term nature of the actuarial valuation process.

The actuarial value of assets each year is equal to 100% of the expected actuarial value of assets plus 25% of the difference between the current market value of assets and the expected actuarial value of assets. In no event will the actuarial value of assets ever be less than 80% of the market value of assets nor greater than 120% of the market value of assets. This 120% factor applied in the June 30, 2009 valuation, as the City's actuarial value of assets is now \$4.175 billion, which is 120% of the City's market value of assets of \$3.479 billion.

Unlike many other public pension funds, SDCERS' Board voted to make no changes to the 120% ceiling of actuarial value of assets as compared to market value, nor to amortize the FY 2009 investment losses over a longer period of time, in spite of the extraordinary global investment market decline during Fiscal Year 2009. *[See the 2009 Valuation at page 16.]*

13. Are the City's retiree health care expenses included in the 2009 Valuation?

No. Health care expenses are a separate obligation of the City, and they are not paid from retirement assets in the SDCERS Trust Fund.

14. How were the 2009 DROP interest rate changes handled in the 2009 Valuation?

For DROP members still working, the liability for the account balances in the asset information was adjusted to assume average distribution in 2 ½ years and an interest crediting rate of 3.54%. Thereafter, it was assumed the account balance would be converted to an annuity at an interest rate of 5% over 10 years, reflecting the average period of payout options. Pre-2006 DROP account balances still left on account were valued assuming they would be paid out until age 70 ½, with an interest crediting rate of 3.54%. The remaining account balances were valued at asset value.