SDCERS
San Diego City Employees' Retirement System

June 30, 2012 Actuarial Valuation for the City of San Diego

At the request of the Board of Administration, Cheiron performed the June 30, 2012 actuarial valuation (Valuation) of San Diego City Employees' Retirement System. The purpose of the actuarial valuation is to report on the financial condition of the System's Defined Benefit Plans for its three Plan Sponsors – the City of San Diego, the San Diego Unified Port District and the San Diego County Regional Airport Authority. The following FAQ is intended to provide SDCERS' Plan Sponsors and Members with information regarding the Valuation's results for the City of San Diego.

The Valuation and its contents were prepared in accordance with generally recognized and accepted actuarial principles and practices consistent with the Code of Professional Conduct and applicable Actuarial Standards of Practice set out by the Actuarial Standards Board.

FREQUENTLY ASKED QUESTIONS

1. Based on the June 30, 2012 Actuarial Valuation for the City of San Diego, what is the City's Unfunded Actuarial Liability (UAL)?

Using the Entry Age Normal ("EAN") funding method, the City's UAL as of June 30, 2012 was $2.279 billion.

2. How does the 2012 UAL compare to the 2011 UAL?

The City's UAL has increased by $101.5 million, from $2,177.8 million to $2.279.3 million. The primary cause of this increase was a return on assets less than expected. The rate of return on the actuarial value of assets was 6.4%, or 1.1% below the assumed return, leading in large part to the $62.2 million increase in the UAL.

3. What is the City's 2012 funding ratio?

As of June 30, 2012, the City's funding ratio -- the system's actuarial value of assets to actuarial liabilities -- is 68.6%.

4. How does this compare to the City's 2011 funding ratio?

The City's 2012 funding ratio is 0.1% higher than the 2011 funding ratio. As of June 30, 2011, the City's funding ratio was 68.5%.

5. What is the City's Annual Required Contribution (ARC) for FY 2014?

The ARC is the amount the City of San Diego will have to contribute to SDCERS on or after July 1, 2013. If paid in full in July 2013 as expected, the City's ARC for FY 2014 will be $275.3 million.

6. What was the City's ARC payment for FY 2013?

The City's FY 2013 ARC was $231.1 million.

7. Did Proposition B affect the City's Annual Required Contribution (ARC)?

Yes, Proposition B increased the City's ARC payment by $27.0 million, but did not increase the City's UAL. Proposition B closed the plan for General Members and for Fire and Lifeguard Safety Members; however, the plan remains open for sworn Police Officers. The Governmental Accounting Standards Board rules require the UAL associated with the closed General and Fire/Lifeguard Safety plan to be paid off more quickly. A level dollar amortization was applied to the closed plan portion of the UAL to follow present GASB standards. That portion of the UAL associated with the open Police plan will continue to be amortized as a level percentage of pay.

8. How is the City's FY 2014 ARC calculated?

The City's employer contributions are comprised 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, 2012) of the portion of the employee's projected retirement benefit assigned to FY 2014. 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 2014, the City's Normal Cost is $51.0 million (approximately 10.6% of payroll). 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, 2012 UAL of $2.279 billion is split into several tiers, each using a different amortization period. These tiers are comprised of:

- $1.564 billion remaining from the closed General and Fire Safety plans, amortized over 15 years ($163.4 million of the 2014 ARC);
- $368.4 million remaining from the City's June 30, 2007 UAL, amortized over 15 years ($30.8 million of the FY 2014 ARC);
- $29.8 million remaining from the 2008 changes in actuarial assumptions, amortized over 26 years ($1.8 million of the FY 2014 ARC);
- $4.3 million remaining from the FY 2008 experience loss, amortized over 11 years ($0.5 million of the FY 2014 ARC);
- $264.0 million remaining from the FY 2009 experience loss, amortized over 12 years ($25.8 million of the FY 2014 ARC);
- $8.6 million remaining from the FY 2010 experience loss, amortized over 13 years ($0.8 million of the FY 2014 ARC);

- $15.2 million remaining from the FY 2010 experience gain from the PSC correction adjustment, amortized over 12 years (negative $1.5 million of the FY 2014 ARC);
- $47.5 million remaining from the FY 2011 experience gain, amortized over 14 years (negative $4.2 million of the FY 2014 ARC);
- $63.3 million remaining from the impact of 2011 changes in actuarial assumptions, amortized over 29 years ($3.5 million of the FY 2014 ARC);
- $36.8 million due to the FY 2012 experience loss, amortized over 15 years ($3.3 million of the FY 2014 ARC); and
- $2.5 million due to the FY 2012 changes in actuarial method, amortized over 30 years ($0.1 million of the FY 2014 ARC).
- Adding the amortization of each tier results in a FY 2014 UAL amortization payment of $224.3 million.

City contributions were determined under full compliance with the Governmental Accounting Standards Board (GASB) Statement Number 25, defining the annual required contribution (ARC) for the City for fiscal year July 1, 2013 through June 30, 2014 (FY 2014).

9. What was the market value of SDCERS' Trust Fund on June 30, 2012, and the City's portion of this amount?

The market value of the assets in SDCERS' Trust Fund on June 30, 2012 was $5.164 billion. The City's portion of this amount was $4.800 billion.

10. How does this compare to the June 30, 2011 market values for the City's portion?

The June 30, 2012 values are 1.0% lower. The June 30, 2011 market value for the SDCERS Trust Fund was $5.204 billion, and the City's portion of the Trust Fund was $4.848billion ($48.2 million more than at June 30, 2012). This decrease for FY2012 is due to contribution revenue and investment earnings being slightly less than payments of member benefits and plan expenses.

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

For the 2012 Valuation, SDCERS' actuary assumed a long-term average investment return of 7.5% for Trust Fund assets.

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

SDCERS' annualized investment returns at market value for the one, three and ten year periods ended June 30, 2012, as reported by Hewitt EnnisKnupp, SDCERS' Investment Consultant, were 0.9%, 12.4%, and 7.3%, respectively. Annualized investment returns are different from the actuarial rate of return calculated by the actuary (e.g., the actuarial investment return was 6.4% for the year ended June 30, 2012) because the actuary computes the actuarial return using the Expected Value of Assets smoothing method.

13. 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. Assets are assumed to be used exclusively for the provision of retirement benefits and expenses.

The actuarial value of assets each year is equal to 100% of the expected actuarial value of San Diego City Employees' Retirement System June 30, 2012 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. In the June 30, 2012 valuation, the City's actuarial value of assets of $4.982 billion was 104% of the City's market value of assets of $4.800 billion.

14. Are the City's retiree health care expenses included in the 2012 Valuation?

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