SDCERS
San Diego City Employees' Retirement System

September 24, 2009

Jay Goldstone
Chief Operating Officer
City of San Diego
202 C Street, 11th Floor
San Diego, CA 92101

Dear Jay:

Your September 21, 2009 "Hiring Freeze" Memorandum states: "Given the City's anticipated Annual Required Contribution (pension payment) for fiscal year 2011 and the action by SDCERS' Board this past Friday, the deficit has increased by approximately $30 million."

I just want to make clear that the SDCERS Board of Administration's action last Friday did not increase the City's deficit. Rather, the Board's decision Friday simply was to take no action to change any of SDCERS' current actuarial funding practices.

Since its reformulation in 2005, the SDCERS Board has adopted some of the most conservative actuarial methods and assumptions of any public pension plan in the country. These include:

- no negative amortization of any unfunded actuarial liability (UAL);
- a corridor of 80%/120% for the relationship between actuarial and market value of assets;
- 25% asset smoothing;
- 15-year fixed amortization of gains and losses;
- Entry Age Normal funding;
- 7.75% investment assumption;
- payroll inflation assumption of 4%; and
- DROP interest crediting rates lower than the investment return assumption.

In October 2008, SDCERS provided the City with a FY2011 ARC projection of $236 million that reflected SDCERS' current actuarial methods and assumptions. In addition, a $199 million dollar projection for the FY2011 ARC was provided that reflected offsets to investment losses, including: 1) lowering the DROP interest crediting rates, 2) payroll increases lower than the actuarial assumption, and 3) the impact of the City's new pension plan for members hired on or after July 1, 2009. These two ARC projections became the basis for the City's five-year financial outlook issued in November 2008. (See, Table V, Scenarios 1 and 2 FY 2011 Forecast in the "City of San Diego 2010-2014 Five-Year Financial Outlook," November 2008.)

During his February 23, 2009 presentation to the City Council, Gene Kalwarski told Council members that the City's FY2011 ARC estimate was then in the $250 million range given investment market performance through January 2009. Again, this estimate was based upon SDCERS' current actuarial methods and assumptions.

It is also not accurate to state that the City's deficit "has increased by approximately $30 million" because until Cheiron completes its June 30, 2009 actuarial valuation for the City, the precise FY 2011 ARC will not be known. As Gene Kalwarski noted in his remarks last Friday, the FY2011 ARC projection of $224.8 million in his presentation does not reflect the effect of reduced DROP interest credit rates, lower payroll increases and the impact of the City's new pension plan (just as was noted in the City's Five-Year Financial Outlook). These factors may reduce the City's FY2011 ARC from any current estimate, but that, of course, will not be known until the valuation is complete.

If you have any questions about this or the City's FY 2011 ARC, please let me know.

Sincerely,

David B. Wescoe

cc.: Board of Administration
City Councilmembers
Andrea Tevlin, Independent Budget Analyst