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November 30, 2022

Scott Hood
Chief Executive Officer
San Mateo County Employees' Retirement Association
100 Marine Parkway, Suite 125
Redwood Shores, CA 94065-5208

Re: Analysis of Memorandum of Understanding (MOU) for Deputy Sheriff's Association (DSA)

Dear Scott:

California Government Code Section 31515.5 requires a notice be provided of the estimated financial impact that proposed benefit or salary increases would have on the funding status of the County's retirement system, administered by SamCERA.

We understand that the San Mateo County Board of Supervisors will consider a Memorandum of Understanding (MOU) with regard to employees of San Mateo County with benefits negotiated under collective bargaining agreements with the Deputy Sheriff's Association (DSA). We have been asked to provide an opinion on whether these changes will have a financial impact on the funding status of SamCERA that require notice under Section 31515.5 and provide this letter to address that question.

The changes being considered could impact the funded status of SamCERA if:

1. they increase the pension benefits of affected SamCERA members as a result of increased salary and/or benefit service, and
2. any additional pension benefits earned are not accompanied by corresponding employer and member contributions being deposited to SamCERA.

The primary financial impact of the changes is estimated to be an increase in the Unfunded Actuarial Accrued Liability (UAAL) of **$322,000**. Note that this is the impact on SamCERA funding only, and does not reflect any other cost to the County of providing these compensation features. While the UAAL of SamCERA will be higher by this amount, the funded ratio, rounded to the nearest 0.01%, will be unchanged.

Summary of changes – one-time lump sum

Our understanding is that all eligible employees will receive a one-time lump sum payment of $2,000, which will be prorated for part-time employees.

This payment is expected to increase pension benefits for all eligible employees because it will increase their pensionable compensation. Members first hired on or after January 1, 2013 are generally members of Plan 7 under the provisions of the California Public Employees' Pension Reform Act of 2013 (PEPRA) and this payment would not be includable in pensionable compensation for those employees.

Since this is a one-time lump sum payment that will not increase future years' compensation we expect it will have a relatively small impact on the funded status of SamCERA. Active employees who retire within a short timeframe after the lump sum is paid may benefit by a higher Final Average Compensation, however for employees several years from retirement we expect their Final Average Compensation will likely be based on compensation that does not include the impact of the lump sum payment.

We expect that employer and employee contributions will be deposited to SamCERA based on the lump sum payment. This will provide a partial offset to increases in the Actuarial Accrued Liability (AAL) due to the higher pension benefits. We estimate that the value of additional employer contributions is $62,000 and the value of additional employee contributions is $61,000 in fiscal year 2022 to 2023 if the lump sum is paid in that fiscal year.

We estimate that the increase in the UAAL (after the offset for the additional contributions) due to the one-time lump sum payment is approximately $18,000, summarized as follows.

Estimated Financial Impact for SamCERA of DSA Lump-Sum Payments		
Increase in Actuarial Accrued Liability (AAL):	$	141,000
Less Additional Employer Contributions in current fiscal year:		(62,000)
Less Additional Member Contributions in current fiscal year:		(61,000)
Increase in Unfunded Actuarial Accrued Liability (UAAL):	$	18,000

While the UAAL of SamCERA will be higher by this amount, the funded ratio, rounded to the nearest one basis point, will be unchanged.

Because SamCERA is a cost sharing plan, any changes in employer normal cost and UAAL amortization rates will be shared by all employers with employees in plans that include affected members. DSA members participate in the General and Safety plans. Over the longer term, we estimate that if all County non-Plan 7 active employees received this increase that, in aggregate, the employer normal cost rate for General and Safety members would be 0.01% of pay higher and the UAAL rate for General and Safety employers would be 0.01% of pay higher for 15 years. Note that the employer normal cost rate increase does not apply to payroll of members in Plan 7. Additionally, the funded ratio for SamCERA would be 0.01% lower if all County non-Plan 7 active employees received the increase.

Summary of changes – general wage increases

Our understanding is that the general wage increases under consideration includes an increase of 10.0% of pay effective November 22, 2022. Further increases will occur over the period of this agreement including increases of 3.3% plus an increase based on annual salary surveys (if applicable) in each of January 2023 and January 2024.

The annual actuarial valuation of SamCERA includes assumptions for future general wage, and merit and longevity, increases. The general wage increase assumption is 3.0% in the June 30, 2022 valuation of SamCERA.

In the actuarial valuation it is anticipated that annual general wage increases will not exactly match those expected by the assumptions, and in some years will be lower and other years will be higher than expected by the assumptions. In years when the general wage increase is greater than expected by the assumptions an actuarial loss (decrease in funded status) occurs, and in years when the increase is less than expected by the assumptions an actuarial gain (increase in funded status) occurs. However, over the long term, the assumption is expected to be roughly consistent with average annual general wage increases.

Although short-term increases or decreases in funded status may occur due to the annual deviation between actual and expected general wage increases, we believe this is within the normal operation of SamCERA and it is reasonable to conclude no impact on the funded status of SamCERA due to these increases.

We believe that wage increases for reasons other than general wage increases, or merit and longevity increases should be considered under Section 31515.5 because there is no assumption included in the valuation for other increases.

Summary of changes – longevity pay

Our understanding is that the schedule of longevity pay under consideration includes a revision to provide an increase of 2% of pay after eight (8) years of service rather than the current twelve (12) years of service.

As noted above, the annual actuarial valuation includes assumptions for longevity increases. However, since this change is a structural change rather than a difference between actual and expected experience, we have explicitly estimated its financial impact.

Current members who have at least 12 years of service are expected to be unaffected by this change. Members with 8 to 11 years of service are expected to receive a longevity increase immediately, and members with less than 8 years of service are expected to receive a longevity increase 4 years earlier than previously expected.

The following table summarizes the increase in the UAAL and employer normal cost as a result of providing a 2% increase in pay after 8 years of employment rather than after 12 years of employment for DSA members.

Estimated Financial Impact for SamCERA of revised DSA longevity pay		
Increase in Actuarial Accrued Liability (AAL):	$	59,000
Annual increase in employer Normal Cost:	$	4,000

In addition to an increase in the UAAL due to this change, the employer normal cost will also be higher each year and will vary somewhat based on plan demographics.

Because SamCERA is a cost sharing plan, any changes in employer normal cost and UAAL amortization rates will be shared by all employers with employees in plans that include affected members. DSA members participate in the General and Safety plans. Over the longer term, we estimate that if all active General and Safety members were impacted by this change in longevity pay structure that, in aggregate, the employer normal cost rate for General members would be unchanged and for Safety members would be 0.02% of pay higher. The UAAL rate would be 0.01% of pay higher for 15 years for employers of General and Safety members. The funded ratio of SamCERA would be unchanged, when rounded to the nearest 0.01%.

Summary of changes – vacation accruals

Our understanding is that an increase in per pay period vacation accruals is being considered for all employees with at least five years of service.

These changes do not increase the pension benefits of affected employees because they do not impact salary or benefit service. As such we believe they do not have a financial impact on the funded status of SamCERA that require a notice under Section 31515.5.

Summary of changes – uniform allowance

Our understanding is that an increase in uniform allowance is being considered for all employees.

These changes do not increase the pension benefits of affected employees because they do not impact salary or benefit service. As such we believe they do not have a financial impact on the funded status of SamCERA that require a notice under Section 31515.5.

Summary of changes – on-call increases

Our understanding is that all eligible employees in non-voluntary on-call positions will receive an hourly pay increase from $4.40 per hour to $5.40 per hour. Eligible employees include those who are members of legacy plans (i.e., not Plan 7).

We estimate that this change will increase the annual compensation of DSA legacy Safety plan members by 0.19% of pay, and 0.00% of pay for DSA legacy General members. If this change impacts all DSA Safety legacy members equally then we estimate that the increase in the UAAL is approximately $245,000. To the extent that DSA Safety members affected by this change have higher or lower liabilities than the legacy DSA Safety population as a whole this amount could be higher or lower.

As mentioned above, because SamCERA is a cost sharing plan, any changes in employer normal cost and UAAL amortization rate will be shared by all employers with employees in plans that include affected members. All affected DSA members are Safety members. Over the longer term, we estimate that due to this change, in aggregate, the employer normal cost rate for Safety members would be unchanged and the UAAL rate for Safety members would be 0.03% of pay higher for 15 years. Note that although the employer normal cost rate will be unchanged, the normal cost dollars will be higher due to the higher salary.

Data, methods, and assumptions

These estimates are based on the results of the June 30, 2022 actuarial valuation. For this analysis we adjusted the valuation results for all active non-Plan 7 employees with benefits negotiated under a collective bargaining agreement with DSA to include:

- a one-time lump sum payment of $2,000 payable in the fiscal year beginning July 1, 2021.
- an increase of $1 per hour on estimated on-call compensation. This increase was applied based on an approximate ratio of the total number of on-call hours and the total number of all hours of all DSA members of legacy plans in the prior year.

We also estimated the financial impact of changes in the longevity pay increase structure for all members with benefits negotiated under a collective bargaining agreement with DSA. In those calculations we assumed no longevity pay increases except for a change from the 2% increase after attainment of 12 years of service to a 2% increase after attainment of 8 years of service.

Except as noted elsewhere in this letter all other data, methods and assumptions are the same as described in the June 30, 2022 actuarial valuation.

Certification

Except as noted elsewhere in this letter, all data, methods, assumptions, and plan provisions are consistent with those described in the June 30, 2022 actuarial valuation. We have assumed that these changes would not affect future member behavior. All statements of reliance and limitations on use described in that report also apply to this work product.

The actuarial computations presented in this letter are for the specific purpose described in this letter. Determinations for other purposes may be significantly different from the results contained in this letter. Accordingly, additional determinations may be needed for other purposes. These computations are subject to the uncertainties of a regular actuarial valuation; the costs are inexact because they are based on assumptions that are themselves necessarily inexact, even though we consider them reasonable. Thus, the emerging costs will vary from those presented in this letter to the extent actual experience differs from that projected by the actuarial assumptions.

Future actuarial measurements may differ significantly from the current measurements presented in this letter due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the retirement system, and changes in plan provisions or applicable law. Due to the limited scope of our assignment, we did not perform an analysis of the potential range of future measurements.

Milliman's work is prepared solely for the internal business use of SamCERA and San Mateo County. To the extent that Milliman's work is not subject to disclosure under applicable public records laws, Milliman's work may not be provided to third parties without Milliman's prior written consent. Milliman does not intend to benefit or create a legal duty to any third-party recipient of its work product.

No third-party recipient of Milliman's work product should rely upon Milliman's work product. Such recipients should engage qualified professionals for advice appropriate to their own specific needs.

The consultants who worked on this assignment are retirement actuaries. Milliman's advice is not intended to be a substitute for qualified legal or accounting counsel.

On the basis of the foregoing, we hereby certify that, to the best of our knowledge and belief, this cost projection letter is complete and accurate and has been prepared in accordance with generally recognized and accepted actuarial principles and practices I am a member of the American Academy of Actuaries and meet the Qualification Standards to render the actuarial opinion contained herein.

Please let us know if you have any questions.

Sincerely,

Nick Collier, ASA, EA, MAAA
Consulting Actuary

Craig Glyde, ASA, EA, MAAA
Consulting Actuary

NC/CG/va

cc: Gladys Smith
Lisa Okada