Segal Consulting

100 Montgomery Street Suite 500 San Francisco, CA 94104-4308
T 415.263.8200 www.segalco.com

VIA EMAIL & USPS

March 25, 2016

Mr. Donald Kendig
Retirement Administrator
Fresno County Employees' Retirement Association
1111 H Street
Fresno, CA 93721

Re: Fresno County Employees' Retirement Association
Three-Year Phase-in of Increase in Employer Contribution Rate Starting 2017/2018
Due to Changes in Actuarial Assumptions from Actuarial Experience Study

Dear Don:

We have been requested to provide information on the three-year "phase-in" of the increase in employer contribution rate due to assumption changes adopted by the Board following our completion of the July 1, 2012 through June 30, 2015 Actuarial Experience Study. The adopted assumptions include a reduction in the annual investment return assumption from 7.25% to 7.00% and an expected improvement in life expectancy for current and future retirees, along with other assumption changes.

The table below shows the changes in the employer contribution rates with the adopted assumptions measured using the membership data reported for the June 30, 2015 valuation and broken down by membership class.

Contributions	**General**	**Safety**	**Total**
Normal Cost	0.33%	0.14%	0.30%
UAAL	4.51%	8.54%	5.14%
Total	4.84%	8.68%	5.44%

While those adopted assumptions will not be used until the next valuation as of June 30, 2016 (which sets contribution rates starting 2017/2018), this letter provides an illustration of the phased-in employer contribution rates for payment in 2017/2018 and 2018/2019 and includes an estimate of the impact of the phase-in on the ultimate employer contribution rates after the phase-in is over in 2019/2020.

Impact of Phase-in on Employer Contribution Rate

Throughout this letter, we are assuming that the phase-in would only apply to the portion of the employer contribution rate increases due to changes in actuarial assumptions and not to other changes in employer contribution rates due to investment gains or losses or other experience that may occur in the June 30, 2016 valuation.

The estimated impacts on employer contribution rates of all the demographic and economic assumption changes measured using the membership data reported for the June 30, 2015 valuation are 4.84% and 8.68% of payroll[1] for General and Safety, respectively, or 5.44% for the Association as a whole. For illustration purposes in this letter only, these are the amounts that would be phased-in over three years. The actual amounts phased-in would be determined as part of the June 30, 2016 valuation.

In general, the phase-in would work as follows:

- The portion of the employer contributions to be phased in would be determined one time, as part of the June 30, 2016 valuation. Those total fixed amounts for General and Safety would not be redetermined in later valuations. In this illustration those amounts are 4.84% and 8.68% of payroll for General and Safety, respectively.

- The actual employer contribution rates in the June 30, 2016 valuation would only reflect <u>one-third</u> of the total impact of the assumption changes (i.e., 1/3 x 4.84% or about 1.61% of payroll for General and 1/3 x 8.68% or about 2.89% of payroll for Safety in this illustration). The way this would work is that the actual employer rates would defer recognition of two-thirds of the impacts (i.e., 2/3 of 4.84% or 3.23% for General and 2/3 of 8.68% or 5.79% for Safety) by deducting 3.23% from the General employer rate and 5.79% from the Safety employer rate produced in the 2016 valuation.

- The employer contribution rates in the June 30, 2017 valuation would only reflect <u>two-thirds</u> of the total impact of the assumption changes as originally determined in the 2016 valuation (about 3.23% and 5.79% of payroll for General and Safety, respectively in this illustration). Again, the way this would work is that the actual employer rates would defer recognition of one-third of the original impacts (i.e., 1/3 of 4.84% or 1.61% for General and 1/3 of 8.68% or 2.89% for Safety) by deducting 1.61% from the General employer rate and 2.89% from the Safety employer rate produced in the 2017 valuation.

- Finally, the employer contribution rates in the June 30, 2018 valuation would reflect the <u>full</u> impact of the assumption changes shown above (4.84% and 8.68% of payroll for General and Safety, respectively). None of the original impacts would be deferred and there would be no deduction from the employer rates produced in the 2018 valuation.

---

[1] Of the 4.84% General and 8.68% Safety increases in payroll rates, about 4.2% and 6.2% of payroll rates for General and Safety, respectively are due to lowering the investment return assumption from 7.25% to 7.00%.

Note that during the phase-in period, the plan is not receiving the full Unfunded Actuarial Accrued Liability (UAAL) amortization payments. That means that in each of the next two actuarial valuations there will be an actuarial loss that will increase the future UAAL and future UAAL contributions for both General and Safety membership classes. Each of these contribution losses will be amortized and paid over a period of 15 years starting with the actuarial valuation that follows the contribution loss (i.e., following the year of the phased-in contribution). In our experience these "contribution losses" due to phase-ins are usually relatively small and so are not identified separately, but simply become part of "other gains and losses".

A comparison of the cumulative incremental contribution rates both before and after applying the phase-in is provided in the table below:

Fiscal Year	**General**		**Safety**	
	Without Phase-in	With Phase-in	Without Phase-in	With Phase-in
2017/2018	4.84%	1.61%	8.68%	2.89%
2018/2019	4.84%	3.50%	8.68%	6.27%
2019/2020 and later	4.84%	5.24%	8.68%	9.40%

The table shows that the rate impacts for the second or the third year of the phase-in are somewhat higher than simply adding another one-third to the contribution rates for the preceding year because of the contribution losses discussed earlier.

There is a technical detail that we mention here only for completeness. The increase in employer contribution rates due to these proposed assumption changes has both Normal Cost and UAAL amortization components. However, the phase-in is applied by reducing only the UAAL component of the employer contributions. This does not change the total amount of the phased-in contributions, only the allocation of the phased-in rates between Normal Cost and UAAL amortization.

Please let us know if you have any questions.

Sincerely,

Paul Angelo ay

Andy Yeung

Paul Angelo, FSA, MAAA, FCA, EA
Senior Vice President and Actuary

Andy Yeung, ASA, MAAA, FCA, EA
Vice President and Actuary

JAC/bbf

cc: Becky Van Wyk