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San Bernardino
County Employees' Retirement Association

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Chair of the Board

Subject: **PARTICIPATING EMPLOYER TERMINATION AND TERMINAL FUNDING OBLIGATION**

PARTICIPATING EMPLOYER TERMINATION AND TERMINAL FUNDING OBLIGATION

I. PURPOSE

The Board of Retirement (Board) has a duty to establish the funding obligations of participating employers that terminate their participation in SBCERA pursuant to California Government Code Sections 31564 and 31564.2, and/or a participating employer ceasing to have employees appointed to a regular position included in SBCERA membership with the no intent of filling such positions. This policy establishes the calculation methodology for the terminating participating employer, as well as the basis for calculating member benefits.

The general principle applied in this policy is to establish the funding obligation of terminating participating employers as:

- The present value of all future benefits expected to be paid by SBCERA to the terminating participating employer's employees, retirees, beneficiaries, and terminated members as of the termination date; minus
- The value of SBCERA assets allocated to the terminating participating employer as of the termination date.

This policy provides the specific procedures to be used in determining the above two components.

The Board's primary consideration is to ensure that the funding obligation of the terminating participating employer is properly determined and settled. In particular, it is the Board's intent that:

- The SBCERA liabilities attributable to the terminating employer will be determined in a manner that is consistent with the fact that, because there will be no reassessment of the terminating participating employer's funding obligation after the termination date, all risks are being retained by SBCERA and no risks are being retained by the terminating participating employer. To accomplish this intent, the present value of all future benefits will be determined using a market-based discount rate.

- The SBCERA assets attributable to the terminating participating employer will be determined in a manner that is consistent with the contribution obligations of the remaining participating employers. To accomplish this intent, assets will be allocated to the terminating participating employer so that the contribution rate toward the Unfunded Actuarial Accrued Liability (UAAL) will be left substantially unchanged for all of SBCERA's remaining participating employers.

II. CALCULATION METHODOLOGY

A. Summary

This policy establishes a market based approach as of the termination date. This approach dictates the use of market value of assets and requires a valuation of the liabilities on a market-consistent basis. Under this approach, the liabilities for retirees and terminated members will be calculated using all the same actuarial assumptions utilized in the most recent actuarial valuation except that the future benefit payments will be discounted to the present date using a market-based discount rate. Themarket-based discount rates for this purpose are the discount rates used by the Pension Benefit Guaranty Corporation (PBGC) to measure the sufficiency of assets for a corporate employer who is terminating its single-employer defined benefit pension plan.

B. Termination Conditions

The Board shall require the terminating participating employer to reimburse SBCERA for the actuarial consulting fees incurred to determine its terminal funding obligation. In the event there is a dispute over the amount of those actuarial consulting fees, the Board will have sole authority to resolve the dispute. In addition to the valuation work performed by SBCERA's consulting actuary, the terminating participating employer may contract with an actuary of its own choice, at its own expense, to review the results from SBCERA's consulting actuary. The Board will have sole authority to resolve any dispute over the calculation of the terminal funding obligation.

The termination date must be at the end of a calendar month to allow a proper determination of the market value of the SBCERA assets.

As part of the termination process, the Board and the terminating participating employer will enter into an agreement stipulating the provisions for the settlement of the terminal funding obligation.

C. Present Value of Future Benefits

The benefits payable by SBCERA to current and former employees of the terminating participating employer will be as follows:

- All active members of the terminating participating employer on the termination date will receive SBCERA benefits for their credited service time up to the termination date. As a result, they will take on the same status as terminated members.

- All vested terminated and retired terminated members (and beneficiaries) will continue to receive future benefits from SBCERA.

The future benefits to be paid to SBCERA members of the terminating participating employer will include those payable to:

- Current retirees and/or beneficiaries of retirees with service while employed at the terminating participating employer prior to the termination date;

- Current members of the terminating participating employer as of the termination date; and

- Former members of the terminating participating employer entitled to either deferred vested benefits or a refund of their accumulated contributions plus credited interest.

The present value of benefits will be determined based on:

- The service retirement and or other benefits associated with the members' years of service with SBCERA as of the termination date, for which they are entitled to SBCERA benefits;

- Expected future cost-of-living adjustments on those benefits;

- For employees and deferred vested members, expected final average compensation (including the effect of any reciprocity benefits);

- For employees and deferred vested members, their expected age at retirement; and

- For retired members and beneficiaries of the retirees, the SBCERA benefits earned for service with the terminating participating employer.

The determination of the present value of future benefits will be based upon the actuarial assumptions most recently adopted by the Board at the time of the determination, except that future benefit payments will be discounted to the termination date using market-based interest rate assumptions.

No consideration will be given to future Board provided benefits.

D. Market-Based Approach for Valuing Liabilities with No Reassessments

1. The determination of the present value of future benefits will be based upon the actuarial assumptions most recently adopted by the Board at the time of the determination, except that future benefit payments will be discounted to the termination date using market-based interest rate assumptions. The market-based interest assumptions selected for this purpose are the discount rates used by the Pension Benefit Guaranty Corporation (PBGC) to measure the sufficiency of assets for a corporate employer who is terminating its single-employer defined benefit pension plan. These PBGC rates are generally lower than the expected earnings based on the discount rate used in SBCERA's actuarial valuation.

2. There will be no reassessment of the terminating participating employer's terminal funding obligation after the termination date under this approach.

E. Determination of Terminating Participating Employer's Assets

SBCERA is a cost-sharing multiple-employer plan defined benefit pension plan. As a result, there is no ongoing separate accounting of SBCERA's assets by employer except in instances when, in the Board's opinion, separate accounting is necessary to maintain equity among employers. The SBCERA assets attributable to contributions of the terminating participating employer and its employees as of the termination date will be determined as follows:

Step 1: Determine the Actuarial Accrued Liability of the terminating participating employer as of SBCERA's most recent actuarial valuation irrespective of the participating employer's termination.

Step 2: Determine the UAAL of the terminating participating employer as of the most recent actuarial valuation by dividing the terminating participating employer's annual required UAAL contribution amount by the UAAL amortization factor. The amortization factor will generally equal the UAAL contribution amount for the cost group that includes the terminating participating employer divided by the UAAL for that cost group. The terminating participating employer's UAAL contribution rate, annual payroll, and UAAL amortization factor will be determined as of the most recent actuarial valuation date. The UAAL contribution rate will be determined before any rate adjustments resulting from distribution from the Cost-of-Living Reserve to provide for future cost-of-living benefits.

Step 3: Determine the non-investment change in assets from the most recent actuarial valuation date to the actuarial termination date as:

- The total contributions by the terminating participating employer since the most recent actuarial valuation date; plus
- The total contributions by employees of the terminating participating employer since the most recent actuarial valuation date; minus
- The total benefit and refund payments since the most recent actuarial valuation date to retirees, beneficiaries, and former employees of the employer.

Step 4: Determine the accumulated assets as of the termination date as:

(Step 1 – Step 2) X Ratio A X (1 + j) + Step 3 X (1 + j/2)

Where:

j = The net rate of return on the market value of SBCERA's total assets from the most recent actuarial valuation date to the date of the participating employer's termination.

Ratio A = (Total SBCERA assets at market value as of the most recent actuarial valuation date) divided by (Total SBCERA assets at actuarial value date as of the most recent valuation date)

Step 5: Determine the portion of any of SBCERA's reserves or designations from which the terminating participating employer will not benefit because of the termination. An adjustment will be made as appropriate to include these reserves or designations in the terminating employer's assets.

F. Settlement of Terminal Funding Obligation

The terminating participating employer's terminal funding obligation will be the excess, if any, of the present value of future benefits over the employer's accumulated assets, as determined under this policy. Settlement of the terminal funding obligation will be made either in a lump sum or, if allowed by the Board, annual installment payments by the employer over a period of up to five years following termination unless the Board determines a longer installment period is appropriate. Annual installment payment arrangements are subject to interest. The rate of interest used shall be the then-current actuarial assumed discount rate less 0.50%, unless the Board deems otherwise.