

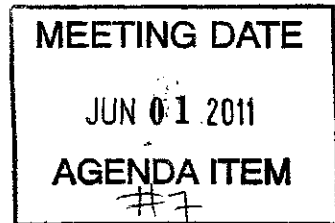
Memorandum

Date: May 24, 2011

To: Board of Retirement
Marilyn Leedom, Chief Executive Officer

From: Karen Levy, General Counsel

Subject: Request From City of Pittsburg to Modify Its Termination Agreement with CCCERA



Recommendations

- Direct staff to request the City of Pittsburg to provide information demonstrating its financial ability to meet its increased total obligations to CCCERA under the requested modification
- Direct staff to prepare a contractual amendment with the requested modification to the contract for consideration by the Retirement Board.

Background

In 2001, the City of Pittsburg withdrew from the Contra Costa County Employees' Retirement Association. The City of Pittsburg and CCCERA entered into a Termination Agreement dated July 1, 2011. In accordance with the County Employees Retirement Law of 1937 ("CERL"), the agreement set forth the City's continuing obligation to pay its future liability to CCCERA. In March of 2011, the City requested that CCCERA modify the calculation method used to determine the City's obligation from the current "market value of assets" method to a proposed "valuation value of assets." The City also requests to create an 18 month "lag" between the valuation and the date on which the contributions are due. The City's request is attached.

The Segal Company has analyzed the proposed changes. Segal's analysis dated May 16, 2011 is attached. Segal concludes that: "it is reasonable to use an asset value that reflects smoothing of investment gains and losses and to incorporate an 18-month delay between the valuation date and the date that the City's contributions are due." Segal further concludes that the proposed changes "will not impair the actuarial soundness of the funding of the plan's vested benefits."

Fiduciary counsel Harvey Leiderman of Reed Smith has reviewed the proposal and opined that it would be within the sound exercise of the Retirement Board's discretion to agree to the proposed changes, as set forth in the attached Reed Smith analysis dated May 18, 2011.

The CERL provides: "In dealing with a withdrawing district, the board of retirement shall take whatever action needed to ensure the actuarial soundness of the retirement system." (G.C. § 31564.2(d)). The CERL further provides that "no contracting agency shall fail or refuse to pay



CONTRA COSTA COUNTY
EMPLOYEES' RETIREMENT ASSOCIATION
1355 Willow Way, Suite 221, Concord, CA 94520-5728
Telephone: (925) 521-3960, Fax: (925) 646-5747

the employer's contribution required by this chapter or to pay the employer's contribution required by the chapter within the applicable time limitations." Lastly, the CERL provides that a withdrawing district's liability "shall be paid in accordance with a schedule determined by the retirement board over a period no longer than the period over which the plan's remaining unfunded actuarial liability is being amortized." (G.C. § 31564.2(c)).

The proposed revisions are therefore within the Retirement Board's authority. However, the revisions would increase the ultimate cost for the City over the long term, while decreasing the City's cost in the short term. (Segal Ltr., at page 3.) As Mr. Leiderman notes, it would be prudent for the Retirement Board to evaluate the City's financial ability to meet its increased total obligations to CCCERA prior to approving the requested changes.



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1355 Willow Way, Suite 221, Concord, CA 94520-5728
Telephone: (925) 521-3960, Fax: (925) 646-5747



City of Pittsburg

Finance Department • 65 Civic Avenue • Pittsburg, California 94565-3814
Telephone: (925) 252-4946 • Fax: (925) 252-6969 • ci.pittsburg.ca.us

MEETING DATE

APR 13 2011

AGENDA ITEM

#7

March 31, 2011

Ms. Marilyn Leedom
Chief Executive Officer
Contra Costa County Employees Retirement Association (CCCERA)
1355 Willow Way, Suite 21
Concord, CA 94520

Subject: City of Pittsburg Request to Amend the Termination Agreement with
CCCERA

Dear Ms. Leedom;


In response to CCCERA's recently calculated triennial update of the City of Pittsburg's ("the City") withdrawal liability, the City contracted with Bartel Associates to review the calculation to ensure it was accurate as well as provide the City with options to reduce its unfunded obligation. Bartel Associates confirmed that the triennial update of the City's withdrawal liability was accurately calculated.

However, as described in the attached letter from Mr. John Bartel of Bartel Associates, Mr. Bartel is recommending that the City and CCCERA amend the City's Termination Agreement to (1) allow the calculation be prepared on an Actuarial rather than Market value of assets basis, and (2) create an 18-month lag between the valuation date and the date the contribution is due. Mr. Bartel estimated that making these changes to the City's Termination Agreement with CCCERA would result in lowering the 12/31/2009 unfunded obligation from \$15.9 million to \$9.9 million and therefore lowering the City's annual payment on July 1, 2011 from \$2 million to \$1.3 million. Given this reduced unfunded obligation and annual payments to CCCERA, we respectfully request to amend the City of Pittsburg's Termination Agreement with CCCERA as suggested by Mr. Bartel.

Ms. Marilyn Leedom
CEO, CCCERA
City of Pittsburg Request to Amend Termination Agreement with CCCERA
March 31, 2011
Page 2 of 2

Thank you in advance for considering our request for these amendments. If you have any questions, please contact me at (925) 252-4848 or tolson@ci.pittsburg.ca.us.

Sincerely,

A handwritten signature in black ink, appearing to read "Tina Olson", is written over the word "Sincerely,".

Tina Olson
Director of Finance

Cc: Marc Grisham, City Manager
Marc Fox, Assistant City Manager

BARTEL ASSOCIATES, LLC

March 28, 2011

Tina Olson
Director of Finance
City of Pittsburg
65 Civic Drive
Pittsburg, CA 94565

RECEIVED

MAR 29 2011

FINANCE DEPT.

Re: City of Pittsburg – Review of CCCERA December 31, 2009 Withdrawal Liability Triennial Update

Dear Ms. Olson:

Bartel Associates has reviewed the December 17, 2010 CCCERA updated Withdrawal Liability calculation. Our comments and recommendations are:

1. We matched the Segal actuarial liability calculations very closely. This means, absent changes in the agreement, we do not disagree with the amounts in Rick Kohler's December 17, 2010 letter.
2. We suggest the City request the agreement be modified for the following reasons:
 - a. A lack of "lag" between the valuation date and the date any contribution is due creates an insurmountable budget issue.
 - b. Using the market value of assets in the calculations creates unanticipated volatility.
3. We recommend the City discuss with CCCERA the following agreement changes:
 - a. Allow the calculation to be prepared on an Actuarial rather than a Market value of assets basis.
 - b. Create a 18 month lag between valuation date and date contribution is due. For example the June 30, 2009 valuation would determine the City's 2011/12 fiscal year contribution.

We estimate the impact of our recommendations as:

- (3a) results in a lower 12/31/09 unfunded obligation of \$9.9 million rather than \$15.9 million.
- (3b) using Market value of assets results in a 7/1/11 payment of \$2.043 million rather a 1/1/10 payment of \$1.827 million.
- Combining (3a) and (3b) results in a 7/1/11 payment of \$1.271 million.

Please note:

- 5% Corridor:
 - Currently if the market value of assets are less than 105% or more than 95% of the Actuarial Accrued Liability no contribution is due.
 - If CCCERA agrees to (3a) & (3b) above they will almost certainly want to eliminate the 5% corridor around the liability.
 - We do not believe expanding the corridor will help much in mitigating future volatility.
- Amortization/payment period:
 - We do not suggest an increase in the payment period (currently 15 years).
 - Doing so would:
 - ☐ lower short term payment amounts and
 - ☐ significantly increase the interest the City will pay.
 - However, for budget reasons the City may want to make such a request.

Tina Olson
March 28, 2011
Page 2



Please feel free to call me at (650)377-1601 if you have any questions about this letter.
Sincerely,

John E. Bartel
President

c: Marc Fox, City of Pittsburgh
Bianca Lin, Bartel Associates, LLC

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THE SEGAL COMPANY
100 Montgomery Street, Suite 500 San Francisco, CA 94104-4308
T 415.263.8200 F 415.263.8290 www.segalco.com

May 16, 2011

Ms. Marilyn Leedom
Chief Executive Officer
Contra Costa County Employees' Retirement Association
1355 Willow Way, Suite 221
Concord, CA 94520

**Re: Contra Costa County Employees' Retirement Association
City of Pittsburg Request to Amend July 1, 2001 Termination Agreement**

Dear Marilyn:

As requested, we are responding to the March 28, 2011 letter that was forwarded to you by the City of Pittsburg ("City"). This letter was written by Bartel Associates, LLC and contains confirmation that they were able match our update of the City's funding obligation as of December 31, 2009 very closely. The letter also includes some recommended modifications to the City's termination agreement with CCCERA. We have been asked by you to respond to those recommended modifications from an actuarial perspective.

Summary

A more detailed discussion of the modifications to the City's termination agreement that are being recommended by Bartel Associates, LLC is provided in the body of this letter. In summary, we believe that it is reasonable to use an asset value that reflects smoothing of investment gains and losses and to incorporate an 18-month delay between the valuation date and the date that the City's contributions are due. We also believe that those changes will not impair the actuarial soundness of the funding of the plan's vested benefits.

Background

The City of Pittsburg was a contracting employer with the Contra Costa County Employees' Retirement Association (CCCERA) before it terminated on July 1, 2001 to provide CalPERS retirement benefits for its then-current and future employees. CCCERA retained the obligation to provide future benefits to the City's retirees and vested terminated members.



For purposes of determining its funding obligation, the City chose the "Second Alternative Approach" in the "Contra Costa County Employees' Retirement Association Extension of Termination Policy to Reflect Market Valuation of Assets and Continued Reassessment of Benefit Liability." This resulted in an initial funding obligation of \$31,464,761 as of June 30, 2001. This amount of assets was set aside in a bookkeeping account to provide future benefits for the City's retirees and vested terminated members. The balance of the City's allocated assets were transferred to CalPERS.

Section 4(a) of the Termination agreement requires an update of the City's bookkeeping account as of December 31 of each year. Section 4(b) of the Termination Agreement requires an update of the City's funding obligation every three years as CCCERA's triennial experience studies are completed. If the ratio of the balance of the City's bookkeeping account to its updated termination liability is below 95% or exceeds 105%, then the resulting total unfunded obligation or surplus will be amortized as a level dollar amount over 15 years.

The latest update of the City's funding obligation as of December 31, 2009 showed that the City had an unfunded obligation of about \$15.9 million. This translated into a funding ratio of 67.2% and the 15-year amortization payments amount to \$1.8 million due annually assuming payment at the end of each calendar year commencing December 31, 2010.

Recommended Modifications to Termination Agreement

The March 28, 2011 letter from Bartel Associates, LLC recommends the following changes to the City's termination agreement with CCCERA:

- a. Allow the calculation to be prepared on an actuarial rather than a market value of assets basis.
- b. Create an 18-month lag between the valuation date and date contribution is due. For example, the December 31, 2009 update of the funding obligation would determine the City's July 1, 2011 through June 30, 2012 fiscal year contribution.

Bartel Associates, LLC also notes that if CCCERA agrees to both items a. and b. above, then they will almost certainly want to eliminate the 5% corridor around the liability. We concur with that observation since the corridor functioned as a way to manage contribution volatility. That purpose would now be achieved by using the actuarial ("smoothed") value of assets instead of market value under the recommendations from Bartel Associates, LLC.

Bartel Associates, LLC estimated the impact of their recommendations as follows:

- Item a. above results in a lower December 31, 2009 unfunded obligation of \$9.9 million rather than the \$15.9 million shown earlier.
- Items a. and b. combined results in an amortization payment of \$1.271 million that would be due on July 1, 2011, rather than the \$1.8 million payment that would otherwise be due on December 31, 2010.

We believe we understand how those impact amounts were calculated and note the following:

- We would recommend that the valuation value of assets be used instead of the actuarial value of assets. Both are on a “smoothed” basis, but the valuation value excludes any non-valuation reserves (such as the post retirement death benefit) that are not part of the benefits valued in the determination of the funding obligation for the City.
- We believe that Bartel and Associates included an extra year of interest on the \$1.271 million amortization payment shown in their letter. If the intent is to have the payment due on July 1, 2011, then the payment would actually be lower by one year of interest.

If the City and CCCERA want to move forward with modifying the termination agreement, then we would determine the contribution amount based on the terms of the modified agreement.

Actuarial Perspective on Recommended Modifications to Termination Agreement

In general, we are responding to the effect of the recommended modifications on the contributions needed to fund the vested benefits and more generally on the “actuarial soundness” of the funding of those benefits.

We note that “actuarial soundness” is difficult to define, especially for actuaries. Generally, one could say it means that there is a reasonable confidence that the projected contributions together with current assets and future investment returns will be sufficient to pay all future benefits and expenses. We are generally relying upon this definition for purposes of our discussion in this letter.

It helps to go back to the basics and refer to the many previous presentations we have made to the Board that contain the basic equation “ $C + I = B + E$ ” (Contributions plus Interest Income equals Benefit Payments plus Expenses).

As the Board knows, the actuarial valuation determines the current or “measured” cost, but it does not determine the ultimate cost of the plan. The assumptions and funding policies/methods used only affect the timing of costs. In this case, that means that, if all else is equal and the current contributions are lowered (as under the combined recommendation), then there will be an increase in later contributions. We sometimes describe this as the time value of money based “No Free Lunch” rule for pension plans.

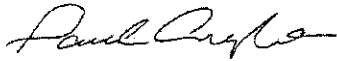
The combined recommendation described by Bartel Associates, LLC increases the ultimate cost for the City. Over the long-term, this increase in cost reflects the short term decrease, dollar for dollar plus interest, based on the time value of money.

Note that the recommendations are generally consistent with the determination of the contribution rates for employers currently participating in the retirement plan. Those contribution rates are based on the actuarial or valuation value of assets and include an 18-month delay between the valuation date and the date the contributions are implemented.

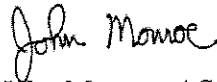
Taking all of the above into account, we believe that the changes to the termination policy that Bartel Associates, LLC are recommending will not impair the actuarial soundness of the funding of the vested benefits.

Please let us know if you have any questions.

Sincerely,



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



John Monroe, ASA, MAAA, EA
Vice President and Associate Actuary

JZM/kek

cc: Rick Koehler

Harvey L. Leiderman
Direct Phone: 415.659.5914
Email: HLeiderman@reedsmith.com

Reed Smith LLP
101 Second Street
Suite 1800
San Francisco, CA 94105
415.543.8700
Fax 415.391.8269

May 18, 2011

Marilyn Leedom, CEO
Contra Costa County Employees' Retirement Ass'n.
1355 Willow Way, Suite 221
Concord, CA 94520

Re: City of Pittsburg Request to Amend July 1, 2001 Termination Agreement

Dear Marilyn:

You have asked us to advise CCCERA on the request by the City of Pittsburg ("City"), dated March 31, 2011, to amend its July 1, 2001 Termination Agreement ("Agreement") with CCCERA. The request seeks to modify the method by which assets held by CCCERA towards payment of benefits for former City employees are calculated, and to create an 18 month "lag" between the valuation date used to determine whether additional contributions may be due and the date on which those contributions are due.

In connection with our analysis, we have reviewed CCCERA's Termination Policy to Reflect Market Valuation of Assets and Continued Reassessment of Benefit Liability, as amended November 7, 2000; the Agreement; the letter of March 28, 2011 from Bartel Associates to the City; the City's letter to CCCERA dated March 31, 2011; and the letter of The Segal Company ("Segal") to CCCERA, dated May 16, 2011.

From a legal and fiduciary viewpoint, and based particularly on Segal's conclusion that the requested amendments "will not impair the actuarial soundness of the funding of the vested benefits" of City retirees, we believe that it would be within the sound exercise of its discretion for the Board of Retirement to agree to the following amendments to the Agreement:

- Commencing with the December 31, 2009 actuarial valuation, calculate the value of the City's assets on the basis of valuation value rather than market value of assets. (Although not mentioned in any of the foregoing documents, we assume the City's liabilities will be calculated on the same basis.)
- Eliminate the 95%/105% "corridor" on the ratio of assets to liabilities in calculating necessary future contribution rate increases or decreases.
- Commencing with the December 31, 2009 actuarial valuation, establish that changes in contributions based on the actuarial valuation will be implemented with the fiscal year


commencing 18 months following the actuarial valuation date that is concurrent with the triennial experience study. This would make the first new contribution date July 1, 2011.

The consequence of moving from market value to valuation value of assets, and delaying implementation of new contribution rates, will be to defer into the future the full funding of the City's liabilities. As with many California municipalities, concerns have been raised publicly about the City's future fiscal health. We believe it would be prudent for the Board to ask the City to demonstrate its financial ability to meet its obligations to CCCERA under the proposed revisions, before approving them. Notwithstanding the "Security" provisions of the Agreement, the risk of any cash flow deficiencies, or defaults in future payments, could increase the unfunded liability of the system as a whole, potentially affecting all other participating employers.

We would be pleased to prepare the appropriate amended Agreement for consideration by the Board and the City, at your direction. In this regard, please note that there are other "clean-up" changes to the document that might be appropriate at this time (*e.g.*, eliminating recitations of how the original unfunded liability was determined.)

We also recommend a legal and actuarial review of the current Termination Policy, to determine whether any changes are appropriate under the circumstances, particularly in light of the Board's "depooling" actions taken previously.

Respectfully submitted,



Harvey L. Leiderman