



CITY OF OAKLAND

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# MEMORANDUM

**TO:** HONORABLE MAYOR &  
CITY COUNCIL

**FROM:** Katano Kasaine

**SUBJECT:** CalPERS changes to Discount rate

City Administrator  
Approval

Date

3/21/12

## INFORMATION

The purpose of this information memorandum is to provide updates to the Mayor and Council on recent changes approved by the CalPERS Board to the CalPERS discount rate assumption and the estimated impact this will have on the City's employer contribution rates.

### **Background**

In March 2011, the CalPERS Board of Administration (Board) voted to keep the current discount rate of 7.75 percent. That decision was partially made to help employers during these difficult economic times, but was also contingent upon a reassessment scheduled to be conducted this year. The CalPERS discount rate was last changed 8 years ago, when it was lowered from 8.25 percent to 7.75 percent in 2004.

The CalPERS Actuarial Office conducted its own study and hired an independent evaluator to assess economic assumptions. The discount rate assumption is calculated based on expected price inflation and real rate of return. CalPERS Actuaries recommended that the assumption for price inflation be reduced from 3.00 to 2.75 percent. Adding to the current real return assumption of 4.75 percent, the new discount rate assumption would be 7.50 percent. Public agency employer contribution rates are estimated to increase by approximately 1.0 to 2.0 percent of payroll for Miscellaneous plans and 2.0 to 3.0 percent of payroll for Safety plans. These increases are to be phased in over a period of two years beginning in fiscal year 2013-14.

The actuarial report offered the Board two options as summarized in the table below: A 7.25 percent discount rate that includes an adjustment to add an element of conservatism to further protect against lower returns, or a 7.50 percent discount rate without such an adjustment. The Board voted to lower the discount rate to 7.50 percent, but directed PERS staff to develop a plan to phase in the employer

contribution rate increases over a period of two years. While these changes will increase contributions, they are not as large as if the discount rate had been lowered to 7.25%.

**Estimated Increase in Employer Contribution Rates  
(% of Payroll)**

<b>Group</b>	<b>Discount Rate of 7.25% (Lowering Price Inflation to 2.75% with a Margin for Adverse Deviation)</b>	<b>Discount Rate of 7.50% (Lowering Price Inflation to 2.75%)</b>
State Miscellaneous	4.2%	1.6%
POFF	5.9%	2.2%
CHP	6.6%	2.4%
Schools	3.2%	1.2%
Public Agency Miscellaneous	3.5% to 4.5%	1.0% to 2.0%
Public Agency Safety	5.0% to 6.5%	2.0% to 3.0%

**Impact to the City Of Oakland**

Based on PERS' estimated payroll and assumptions listed below, the change in the discount rate is expected to cost the City of Oakland the following:

	FYE 2013	FYE 2014	FYE 2015
<b>Low End Additional Contributions Due to Assumption Changes (1% of payroll for misc, 2% for safety)</b>			
Miscellaneous	none \$	<b>1,109,863</b>	<b>2,286,317</b>
Safety	none	<b>1,650,909</b>	<b>3,400,873</b>
Total	none	<b>2,760,772</b>	<b>5,687,190</b>
<b>High End Additional Contributions Due to Assumption Changes (2% of payroll for misc, 3% for safety)</b>			
Miscellaneous	none \$	<b>2,219,725</b>	<b>4,572,634</b>
Safety	none	<b>2,476,364</b>	<b>5,101,310</b>
Total	none	<b>4,696,089</b>	<b>9,673,943</b>

**Assumptions:**

1. CalPERS FYE 2013 payroll forecast based upon 2010 actual payroll +3.25% per year. The City's actual payroll will likely be lower.
2. Payroll for FYE 2014 and 2015 uses 2013 forecast + 3.0% per year (CalPERS' new salary increase assumption).

CalPERS changes reduced inflation, salary trend and expected investment returns by 25 basis points. New assumptions are: Inflation 2.75%, Salary 3.0%, and Investment Return 7.5%.

Using City actual Payroll, the estimated increased employer contribution costs to the City is as follows:

Low End Additional Contributions Due to Assumption Changes (1% of payroll for misc, 2% for safety) - Using <b>Oakland Payroll</b>			
Miscellaneous	none	\$ 773,863	1,594,157
Safety	none	1,459,559	3,006,691
Total	none	2,233,421	4,600,848
High End Additional Contributions Due to Assumption Changes (2% of payroll for misc, 3% for safety) - Using <b>Oakland Payroll</b>			
Miscellaneous	none	\$ 1,547,726	3,188,315
Safety	none	2,189,338	4,510,036
Total	none	3,737,063	7,698,351

PERS Actuarial Office will complete the June 30, 2011 actuarial valuations in fall 2012 which will outline the impact of the changes in the discount rate assumption. The June 30, 2011 valuations will set the employer rates that take effect on July 1, 2013. Staff will continue to closely monitor PERS decisions and update Council on any new developments.

Respectfully submitted,

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/s/

KATANO KASAINÉ  
Treasury Manager, Treasury Division

For questions please contact Katano Kasaine, Treasury Manager, at (510) 238-2989.