POLICY NUMBER:	POLICY TITLE: Pension Funding Policy	
ORIGINAL ISSUE DATE: March 2017		
REVISION DATE: April 20, 2021	POLICY CONTACTS: County Administrative Office	
RELATED DOCUMENTS: Resolution 15-98 Bartel Associates Valuation CalPERS Annual Valuations	RELATED POLICIES:	

Contents

SECTION I – PURPOSE

This policy statement pertains to the actuarial, funding and cost recovery aspects of Pension Benefits. This policy does not purport to address the sustainability of established pension benefits under current defined benefit formulas. This policy may also be referred to, in brief, as "Pension Policy."

This policy will be updated periodically in light of actuarial valuation results, changes in benefits, or other material changes to the County's fiscal position.

SECTION II – APPLICABILITY

This policy is an update to the Pension Policy (adopted in 2017) and an extension of the Debt Policy (adopted 2017) and is generally consistent with best practices recommended by the Government Finance Officers Association (GFOA). Variances from best practices are identified herein together with the underlying reasons.

This policy is applicable to the County's two key defined benefit plans, which are administered by the California Public Employees' Retirement System (CalPERS):

- Miscellaneous Plan of the County of Humboldt hereafter referred to as the "Miscellaneous Plan." The Miscellaneous Plan includes employees of the County and employees of the Humboldt County Superior Court.
- Safety Plan of the County of Humboldt hereafter referred to as the "Safety Plan."

The County receives actuarial valuations prepared by the actuarial office of CalPERS on an annual basis. The report provides a determination of the minimum required contributions, often referred to as the Actuarially Determined Contribution (ADC). As a CalPERS member agency, the County is obligated to fund the ADC by state statute each year.

SECTION III – DEFINITIONS

Key actuarial or accounting terms related to pensions are defined below:

Accrued Liability (also called Actuarial Accrued Liability, Entry Age Actuarial Accrued Liability or Total Pension Liability): The total dollars needed as of the valuation date to fund all benefits attributed to the past for *current* members.

Actuarial Assumptions: Assumptions made about certain events that will affect pension costs. Assumptions are generally broken into two categories: demographic and economic. Demographic assumptions are those that relate to future actions by people, and include such things as mortality, termination, disability, and retirement rates. Economic assumptions are those that relate to money, and include discount rate, salary growth, and inflation.

Actuarially Determined Contribution (ADC): The amount actuarially calculated each year that is required to be contributed to a pension plan’s pool of assets in order to ensure there will be enough funds to pay promised pension benefits. The contribution rate can be reported either in dollars or as a percent of salary. Actuaries annually determine how much should be paid by employers in a given year in order to properly fund a pension plan. This amount is a combination of the employer’s share of Normal Cost plus the unfunded liability amortization payment.

Actuarial Valuation: The determination, as of a point in time (valuation date), of the Normal Cost, Accrued Liability, and related actuarial present values for a pension plan.

Funded Status: A measure of how well funded, or how “on track” a pension plan is with respect to having sufficient assets to fund liabilities. A ratio greater than 100% means the plan has more assets than liabilities, in other words, it is ahead of schedule. A ratio of less than 100% means liabilities are greater than assets, meaning the agency is behind schedule on funding.

Internal Pension Management Account: An internal account or fund used for the purpose of depositing, collecting or transferring deductions, fines, fees or other funds for a specific purpose. In 2015, the Board of Supervisors via Resolution 15-98 authorized creation of the Pension Management Trust Fund to accumulate assets for the purpose of meeting future pension obligations, along with other post-employment benefit obligations, as authorized by the Board. Changes in accounting standards may necessitate this account be changed from a trust fund to another type of account, or a combination thereof, but the purpose will remain.

Normal Cost: The annual cost of service attributed to a fiscal year for current active employees. The portion that is allocated to future years of service is referred to as Future Normal Costs.

Pension Benefit: Pension benefits are provided pursuant to a defined benefit formula. The formula used by the retirement system will be based on key factors such as the benefit factor, service credit and final pensionable compensation. A simplified example is below:

Service Credit (Years)	X	Benefit Factor (% per year)	X	Final Pensionable Compensation (dollars)	=	Pension Benefit

Pensionable Compensation: Pensionable compensation is defined in government code and retirement law and generally refers to the normal monthly rate of pay or base pay of the member paid in cash for employment rendered on a full-time basis during normal hours according to publicly available pay schedules.

Pension Rate Stabilization Program: The County recognizes that pension assets are exposed to significant market volatility. The County has set funds aside in trust to mitigate the budgetary impact of rapid increases in the minimum required employer contribution.

Present Value of Benefits (PVB): The total dollars needed as of the valuation date to fund all benefits earned in the past or expected to be earned in the future for current members.

Section 115 Trust (External Pension Trust): An irrevocable external trust fund established in accordance with Internal Revenue Code (IRC) § 115. Income derived from the trust is exempt from income taxation but these assets can only be used to pay post-employment retirement benefits.

Unfunded Accrued Liability (UAL): When the value of the plan's assets is less than its Accrued Liability, the difference is the plan's Unfunded Accrued Liability (or unfunded liability). If there is an unfunded liability, the plan will have to pay contributions exceeding the Normal Cost.

SECTION IV – GUIDING PRINCIPLES

A. Intergenerational Equity

Pension benefits are offered as part of a compensation package for employees as a benefit of the County of Humboldt for a career of public service. The employee accumulates (or earns) the benefit through accrual of years of service with the agency over their service life (or career).

1. The County as a matter of principle strives to comply with maintaining intergenerational equity.

2. As this relates to pension benefits, the objective is to ensure that adequate employee and employer contributions are made to the pension system during the service life of employees to avoid shifting the cost or burden to future generations of employees and taxpayers.

B. Financial Sustainability

Financial Sustainability is the overarching principle in Humboldt County financial operations.

1. Within the context of pension funding, this principle expresses that the County provides and fund benefits to its employees within available means while proactively taking measure to build and preserve its ability to continue providing these benefits in the long run.

SECTION V – POLICY

A. Governance and Transparency

CalPERS, as the pension plan administrator, establishes actuarial assumptions for all pension plans under their administration.

1. In accordance with best practices and generally accepted accounting principles (GAAP), the County will receive an Actuarial Valuation and related reports for both (1) funding and (2) accounting for pension benefits annual from the Actuarial Office of CalPERS.

   The County Administrative Officer (CAO) shall annually review the actuarial report to evaluate the funding progress and changes since the prior valuation.

2. The CAO shall transmit the actuarial report, together with a lay summary regarding the Funded Status of the pension plans, cost trends, major changes in actuarial assumptions, significant experience gains/losses, any noted deviations from best practices, and any additional recommendations to the Board of Supervisors. The CAO shall post actuarial valuations to the County website annually.

3. The CAO shall use the actuarial valuation and supplemental accounting report(s) as the basis for financial reporting in accordance with the GAAP.

   a. The CAO should allocate the liability to participating agencies and enterprise or internal service funds based on eligible employee payroll to show their respective share of the Unfunded Accrued Liability (UAL).
   b. The CAO, at their discretion, may contract an external auditor or other appropriate party, to opine on the allocation of the UAL to other agencies or segments of the governmental agency.

4. The CAO shall evaluate opportunities and implement procedures to

enhance transparency to the public, employees and other interested parties on the employee and employer share of current and future pension contributions, with the purpose of identifying clearly any significant financial impact of any proposed salary or benefit modification.

5. Future benefit modifications (including those that affect the key pension benefit factors of the defined benefit formula) for members and beneficiaries should be carefully considered and impacts of such proposed changes on the County's pension plan shall be evaluated by the CAO (utilizing actuaries if required) and presented to the Board of Supervisors prior to adoption so the effect of the modifications can be understood and considered in relation to the plan's Accrued Liability, funded ratio, and current and future contribution rates for both employees and the County.

B. Funding Goal

It is always the County's intention to pay all benefits promised.

1. **Long-Term Funding Target**
   As such, over the long-term, the target Funded Status is 100% (full funding) of the Accrued Liability related to the County's pension plans. The County's goal is to accumulate sufficient assets to fund all projected benefit payments.
2. **Long-Term Perspective**
   Pension benefits are paid out over a time horizon that can stretch out over 30 years, or even longer. As such, while the long-term goal is to be 100% funded, it is not necessary to meet that goal in every year. The County will strive to move toward that target whenever the funded percentage is less than 100%.

C. Funding

1. **Actuarially Determined Contribution (ADC)**
   The ADC is determined annually by the pension plan administrator CalPERS for subsequent fiscal years (for example: CalPERS Actuarial Valuation report as of June 30, 2019 determines the 2021-22 required contributions).
   a. The CAO shall each year budget the Actuarially Determined Contribution to CalPERS and establish and maintain the necessary reserve to ensure that this obligation is met annually.

2. **Prepayment of Minimum Required Contribution**
   The pension plan administrator (CalPERS) at times may provide an incentive (or discount) for the County to pay all or a portion of the employer's share of the minimum required contribution at the beginning

of the fiscal year, rather than remitting the contribution with each monthly period during the fiscal year.

   a. The CAO shall prepare a financial analysis on an annual basis when a financial incentive is offered to make a prepayment of the UAL contribution to determine whether this is in the best interest of the County.
      i. The analysis should take into account the savings and cash flow impact from remitting the pension contribution in advance compared to any costs of borrowing or financing.
      ii. This recommendation shall be submitted as part of the County's recommended budget.

3. Target Contribution

The CAO shall set Target Contribution Rates for the Miscellaneous and Safety Plans at a percentage of pay that is projected to fully fund the County's UAL over a period of no more than 20 years, unless otherwise allowed by CalPERS. These targets will also be updated periodically to reflect expected changes in CalPERS assumptions, actuarial valuations or market conditions. Such amounts may be in excess of the ADC.

   a. To achieve the Target Contribution Rate, the CAO may recommend funding the costs through employer and employee contributions, contributions from the Pension Trust, other funding sources, or a combination thereof.

4. Payment of UAL

Over the years CalPERS has utilized various amortization methodologies over a term of up to 30 years to methodically repay the UAL arising from past experience differing from expectations (investment gains or losses, or other experience gains or losses), or changes in future expectations (change in actuarial assumptions; change in actuarial methodology; change in benefit, etc.) that occurred prior to June 30, 2018. Without any additional action, provided that the actuarial assumptions are an accurate reflection of future experience, the plan would move to a fully funded status within 30 years of the last event that created the liability. In line with industry best practices, CalPERS revised its amortization policy to shorten the period for amortizing future actuarial gains and losses to 20 years, beginning from the actuarial report for June 30, 2019, and effective in Fiscal Year 2021-22 for Humboldt County.

CalPERS new amortization policy does not affect any Unfunded Accrued Liability established prior to June 30, 2019, which are still being amortized over periods up to 30 years. CalPERS has offered alternative 20- and 15-year amortization schedules available for voluntary election that would result in substantial long-term savings to the County.

a. As part of long-term financial planning and taking into consideration cash flow needs, County staff should periodically evaluate the feasibility and cost-benefits of following one of these alternative amortization schedules and make appropriate recommendations to the Board of Supervisors. This may occur either formally, by adopting a revised amortization schedule through CalPERS, or virtually, by making additional discretionary contributions to shorten the term of the payment schedule and or achieve additional cost savings.

5. **Pension Funding Stabilization Program**
Although there is no legal requirement to make a pension contribution above the Actuarially Determined Contribution (ADC), the Board of Supervisors has determined that fulfilling its full pension obligation is a primary objective of the County and that making additional contributions before they are required can help stabilize future pension contributions, and can often be expected to provide long-term savings to the County. As such, based on staff research and recommendation, the Board has approved a Pension Funding Stabilization Program. The program focuses on stabilizing the County's pension contribution and lowering long-term pension contribution requirement through the tactical use of additional discretionary contributions to CalPERS, as well as to an irrevocable trust, hereafter referred to as the External Pension Trust or Section 115 Pension Trust.

D. Additional Discretionary Payments (ADP)

1. **Use of Target Contribution**
The Target Contribution will first be used to make the Actuarially Determined Contribution (ADC) required by CalPERS for that fiscal year. Any remaining amounts of the Target Contribution will be allocated by the Board between:
    a. Additional discretionary contributions to CalPERS – These contributions may be used to lower the projected contribution rate down to the Target Contribution Rate for future years, or to lower long-term contribution requirements.
    b. Additional payments to the Pension Trust – These contributions will first be used to bring the Pension Trust to the Minimum Balance. After that has been done, additional contributions can be sent to the Pension Trust in order to pre-fund future contributions.

2. **Prepayment Savings**
    a. During the annual budget process, the CAO shall provide a

recommendation to the Board of Supervisors on the amount to transfer from savings generated by prepayment of the annual contribution to the Pension Funding Stabilization Program.

3. **Additional Contributions**
   a. In years when there are budget surpluses or other one-time revenues, the CAO will also recommend what portion of these revenues, if any, should be used to further speed up the payment of UAL. Priority should be given to those items that relieve budget or financial operating pressure in future periods.

E. External Pension Trust (Section 115 Pension Trust)

1. **Establishment of the Trust**
   The County established an external irrevocable post-employment benefits trust program, also known as a Section 115 trust, which was adopted via Resolution 15-98 by the Board of Supervisors on Sept. 15, 2015. This trust, which is exempt from federal income taxes, will be a vehicle to accumulate assets for the purpose of meeting future pension obligations, along with other post-employment benefit obligations, as authorized by the Board.

2. **Objective of Trust**
   The purpose of the External Pension Trust is to set aside funds for the pre-funding of the County's CalPERS pension contributions. A similar Section 115 OPEB Trust will be used to set aside funds to prefund Other Post-Employment Benefits obligations.

3. **Section 115 Pension Trust Administrator**
   a. The Board of Supervisors delegates the Section 115 Pension Trust Administrator function to the CAO and Treasurer-Tax Collector, who may contract with third party providers.

4. **Minimum Balance Target (MBT)**
   a. The recommended Minimum Balance Target of the pension funding stabilization program will be an amount equivalent to 1/6th of the County's Actuarially Determined Contribution (ADC).
   b. The MBT will be determined annually by the Section 115 Pension Trust Administrator.
   c. After the MBT is achieved, it shall be maintained every year unless the County is in the Restoration of Trust Balance process after drawn down, and shall be used to ensure sufficient funding for the Actuarially Determined Contribution or Target Contribution Rate.
   d. Balances accumulated above the MBT may be utilized for the purpose of stabilizing future contribution rates, to help achieve the

Target Contribution Rate, or to further reduce the County's UAL, upon Board approval.

5. **Funding Trust**
    a. To provide a dedicated on-going source for the External Pension Trust, a supplemental pension charge will be applied to all departments as a percentage of salary. This provision does not prohibit additional contributions to the External Pension Trust, as authorized by the Board.
    b. The charge (described in the County's financial statements as Section 115 Pension Trust) will be set annually as part of the County budget process, or anytime during the year, as authorized by Board. Typically this charge will be between 0.25% and 2% of salaries.
    c. Charges will be transferred to the County's Internal Pension Management Trust Fund prior to transfer to the Section 115 Pension Trust.

6. **Investments**

   The purpose of investing funds is to accumulate sufficient assets to implement this pension funding policy. Assets that are in the irrevocable External Pension Trust are not subject to the County Investment Policy for internal reserves and laws governing County treasury investments. A primary advantage of placing funds into the trust account rather than holding them in fund balances for subsequent contribution to the California Public Employees Retirement System (CalPERS) is that investments in the trust can be made under the more flexible rules of California Government Code Section 53216.1 rather than the more restrictive rules of Government Code Section 53601. An investment in the Section 115 Pension Trust has the potential of yielding a larger rate of return than those funds held in the County's pooled investments.

    a. At least annually the Section 115 Pension Trust Administrators shall assess the investment strategies for the Trust. The Section 115 Pension Trust Administrators shall have authority to adjust investment strategies at any time. Any adjustment to the investment strategy shall be reported to the Board of Supervisors.
    b. Pension trust assets should be invested to achieve an objective of capital preservation prior to the Minimum Balance Target being achieved.
    c. After the MBT target balance has been achieved, the trust asset allocation should be reviewed with the additional goal of achieving a return that more closely matches or exceeds the discount rate used by CalPERS actuaries to determine the actuarial liability while maintaining a reasonable level of capital preservation.

d. The Section 115 Pension Trust Administrators should regularly review and monitor the investment results.

7. Withdrawing Assets

Assets contributed to the Section 115 Pension Trust can only be withdrawn to pay pension costs, or OPEB costs for the corresponding Section 115 OPEB Trust. The County's stated intention is to specifically reserve these assets to:

- Support the funding of the ADC. This might occur when the Actuarially Determined Contribution required by CalPERS is greater than the Target Contribution Rate, or when the County is under significant fiscal distress and finds it difficult to pay the Actuarially Determined Contribution from that year's revenues.
- Support funding of the Target Contribution Rate.
- Reduce the Unfunded Accrued Liability. This might be done to lower the peak projected contribution rate down toward the Target Contribution Rate, or to achieve future budget savings in excess of the contributions being made.

The steps for making such a withdrawal will be as follows:

a. The CAO shall request Board approval prior to the withdrawal of assets from the trust.
b. The CAO shall evaluate the withdrawals needed to maintain the stated Target Contribution Rate.
c. If assets are being withdrawn due to fiscal distress, some of the factors that should be considered in determining whether the County is in a period of fiscal distress are as follows:
    - Uncertainty regarding ability to pay short-term obligations on time.
    - Ability to meet long-term obligations including those from debt issuances, pension plans or other postemployment benefits is uncertain given the extent of obligations in comparison to available resources.
    - Ability to maintain financial stability is impaired including reductions to credit rating, reliance on declining or unstable sources of revenue, and inability to raise revenues to support commitments.
    - Ability to maintain services is not possible based on fiscal condition and the County is required to layoff personnel.

8. Restoration of Trust Balance

a. If withdrawals cause the External Pension Trust to fall below the Minimum Balance Target (MBT), the External Pension Trust shall be funded or replenished to the MBT within 5 fiscal years.

F. Accounting for Pension Costs

1. **Internal Service Fund**
   a. The CAO shall maintain the Internal Pension Management Account to record the following:
      - Pension contributions deducted from Payroll
      - Contributions paid to CalPERS and to the External Pension Trust.
      - Transactions related to prepayment of UAL contributions.
      - UAL contributions from other plan participants (e.g. Humboldt Superior Court).

   b. Beside the normal transactions that are authorized by the Board of Supervisors or the CAO, the Internal Pension Management Account will hold any savings realized through prepayment until recommendation by the CAO through the budget process.
   c. The Internal Pension Management Account shall be maintained in the County's accounting and financial reporting system.

2. **External Pension Trust (Section 115 Pension Trust)**
   a. The Section 115 Pension Trust Fund will be held externally from the County treasury and shall track the assets, investment gains, and losses and other activities of the trust.
   b. All assets of the Section 115 Pension Trust shall be properly and accurately accounted for on the County's annual financial statements.
   c. The CAO shall report annually to the Board of Supervisors on the financial condition and performance of the Section 115 Pension Trust Fund, within 6 months of fiscal year end. Such report shall include appropriate recommendations regarding the investment and use of assets to achieve the purpose of the trust.

G. Responsibilities

Departmental Contribution Amounts for costs related to the Pension Funding Policy will be established by the CAO and adopted by the Board. Payroll and the Auditor-Controller, as specified below, shall carry out the following actions to ensure proper implementation of the Pension Funding Policy.

1. **Contributions, Collections and Reconciliation**
   a. Payroll shall apply the stated County-wide Contribution Amounts based on the salary expense per full-time equivalent allocations for each fiscal year.
   b. The Auditor-Controller shall every payroll cycle collect the necessary funds from departments to meet Board-adopted Contribution

Amounts.

c. The Auditor-Controller shall deposit the required portion of departmental contributions into the Pension Management Trust Fund and transfer to the Section 115 Pension Trust on, at least, a monthly basis.
d. The Auditor-Controller shall reconcile the Contribution Amounts at midyear to determine if any adjustments to the Contribution Amount in conjunction with revenue forecasts need to be made to the upcoming budget cycle.

2. Other Payments

a. The Auditor-Controller shall only direct additional funding to the Pension Management Trust Fund pursuant to official Board actions. Such actions typically occur during the budget process or when unanticipated or one-time funding is available during the fiscal year.

H. Review of Funding Policy

Funding a defined benefit pension plan requires a long-term horizon. As such, the County will review this policy at least every 5 years to determine if changes to this policy are needed to ensure adequate resources are being accumulated.

Board Approved:

____ ____________________

Appropriate Board Chair Name, Board Chairperson Date

Pursuant to Board Order ___________ Dated ______________