Valuation highlights

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1. The results of this valuation reflect (1) an increase in the cost-of-living adjustment (COLA) assumption from 2.50% to 2.75% per annum for General Tiers 1, 2 and 3 and Safety Tiers 1 and 2 members and (2) an increase in the interest crediting rate for member's account balance to reflect the higher COLA assumption. These changes were recommended by Segal in our Review of Economic Actuarial Assumptions and adopted by the Board for the June 30, 2023 valuation outlined in *Section 4, Exhibit 1* of this report. The assumption changes resulted in an increase of $124.9 million, or 1.7%, in the Actuarial Accrued Liability, an increase in the average employer contribution rate of 2.25% of payroll, and an increase in the average member rate of 0.20% of payroll. Of the 2.25% of payroll increase in the employer rate, 0.20% of payroll is due to an increase in the Normal Cost and 2.05% of payroll is due to an increase in the UAAL rate.

2. This valuation reflects one minor actuarial refinement of applying beginning of year timing of decrements for exiting from active membership status in calculating the normal cost rate. The refinement resulted in a net 0.13% of payroll decrease in the average employer contribution rate and a net 0.02% of payroll decrease in the average member contribution rate.

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3. The ratio of the Valuation Value of Assets to Actuarial Accrued Liabilities decreased from 88.66% to 85.06%. This ratio is one measure of funding status, and its history is a measure of funding progress. The ratio of the Market Value of Assets to the Actuarial Accrued Liability increased from 81.28% to 81.94%. These measurements are not necessarily appropriate for assessing the sufficiency of plan assets to cover the estimated cost of settling the plan's benefit obligation or the need for, or the amount of, future contributions.

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4. The Association's UAAL (which is based on the Valuation Value of Assets) has increased from $784.7 million to $1,111.7 million. The increase in UAAL is primarily due to change in the COLA assumption, investment return (after smoothing) less than the 6.50% assumed rate, COLA increases[1] greater than expected for retirees and beneficiaries with a 3% maximum COLA and individual salary increases greater than expected for active members. A complete reconciliation of the Association's UAAL is provided in *Section 2, Subsection E*.

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5. The UAAL amortization layers established as of the June 30, 2008 valuation have been fully amortized as of June 30, 2023 which resulted in a decrease in the UAAL contribution rate of about 2.31% of payroll for the plan in total. For illustration we have continued to show the 2008 layers in *Section 3, Exhibit H*, but with zero "Outstanding Balance" and "Years Remaining". Note that the UAAL contributions are expected to continue to decline in the next few valuations as other layers are fully amortized, as shown in the graphical projection found in *Section 3, Exhibit I* on page 79.

[1] The annual CPI for the West Region used by the Board to set April 1, 2023 COLA came in at 8.0%. For Tiers with a maximum 3.0% COLA, there will be an actuarial loss between the expected benefit increase (2.50% assumed annually starting April 1, 2023 in the June 30, 2022 valuation) and the actual benefit increase (3.0% granted on April 1, 2023 and on every April 1 thereafter until the COLA banks used to track the difference between the 8.0% actual CPI and the actual COLA granted are fully exhausted).

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6. The actuarial loss of $305.4 million, or 4.1% of the Actuarial Accrued Liability, is due to an investment loss of $138.0 million, a contribution gain of $14.6 million, and a net experience loss from sources other than investments and contributions of $182.0, prior to the reflection of COLA assumption change. This loss was primarily due to COLA increases greater than expected for retirees and beneficiaries with a 3% maximum COLA.

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7. The average employer contribution rate calculated in this valuation increased from 45.93% of payroll to 49.26% of payroll. This increase is primarily due to change in the COLA assumption, investment return (after smoothing) less than the 6.50% assumed rate, COLA increases greater than expected for retirees and beneficiaries with a 3% maximum COLA and individual salary increases greater than expected for active members offset to some extent by the effect of June 30, 2008 UAAL amortization layers becoming fully amortized and amortizing prior year's UAAL over a larger than expected projected total payroll. A complete reconciliation of the Association's average employer rate is provided in *Section 2, Subsection F*.

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8. The average member rate calculated in this valuation has increased from 9.45% of payroll to 9.58% of payroll. This change is primarily due to change in the COLA assumption. A complete reconciliation of the Association's average member rate is provided in *Section 2, Subsection F*.

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9. The rate of return on the Market Value of Assets was 9.61% for the 2022-2023 plan year. The return on the Valuation Value of Assets was 4.24% for the same period after considering the gradual recognition of current and prior years' investment gains and losses. This resulted in an actuarial loss when measured against the assumed rate of return of 6.50%. This actuarial investment loss increased the average employer contribution rate by 2.25% of payroll.

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10. The total unrecognized net investment loss as of June 30, 2023 is about $232.1 million as compared to an unrecognized net investment loss of $510.7 million in the previous valuation. This deferred investment loss of $232.1 million will be recognized in the determination of the Actuarial Value of Assets for funding purposes in the next few years as shown in *Section 2, Subsection B*.

    The net deferred losses of $232.1 million represent about 3.8% of the Market Value of Assets. Unless offset by future investment gains or other favorable experience, the recognition of the $232.1 million market losses is expected to have an impact on the Association's future funded ratio and contribution rate requirements. This potential impact may be illustrated as follows:

    a. If the net deferred losses in this year's valuation were recognized immediately and entirely in the Valuation Value of Assets, the funded ratio would decrease from 85.1% to 81.9%.

       For comparison purposes, if all the net deferred losses in the June 30, 2022 valuation had been recognized immediately in the June 30, 2022 valuation, the funded ratio in last year's valuation would have decreased from 88.7% to 81.3%.

    b. If the net deferred losses in this year's valuation were recognized immediately and entirely in the Valuation Value of Assets, the average employer contribution rate would increase from 49.26% to 53.04% of payroll.

For comparison purposes, if all the net deferred losses in the June 30, 2022 valuation had been recognized immediately in the June 30, 2022 valuation, the average employer contribution rate in last year's valuation would have increased from 46.49% to 55.45% of payroll.

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11. In preparing the breakdown of the total costs of the General Tier 1 plan into the cost to provide the "Regular" and the "Settlement" benefits, we have followed the FCERA practice of allocating the cost to provide a benefit under Section 31676.12 as the cost for the "Regular" benefit and allocating the difference between this "Regular" benefit cost and the cost to provide a benefit under Section 31676.14 plus Section 31627 as the "Settlement" benefit. In particular, this means that the difference between benefits under Sections 31676.12 and 31676.14 is considered "Settlement" and so under the Settlement Agreement could be funded out of future undistributed excess earnings. Based on discussions with Counsel, the Agreement might not be clear as to what should be considered the "Settlement" benefit. We will require guidance from the Board if and when the Board and Counsel consider the use of any future undistributed excess earnings to pay the cost of the "Settlement" benefit.

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12. The Actuarial Standards Board approved Actuarial Standard of Practice No. 51 (ASOP 51) regarding risk assessment, which was first effective with FCERA's June 30, 2019 actuarial valuation. ASOP 51 requires actuaries to identify and assess risks that "may reasonably be anticipated to significantly affect the plan's future financial condition". Examples of key risks listed that are particularly relevant to FCERA are asset/liability mismatch risk, investment risk, and longevity risk. The standard also requires an actuary to consider if there is any ongoing contribution risk to the plan, however it does not require the actuary to evaluate the particular ability or willingness of contributing entities to make contributions when due, nor does it require the actuary to assess the likelihood or consequences of future changes in applicable law.

    The actuary's initial assessment can be strictly a qualitative discussion about potential adverse experience and the possible effect on future results, but it may also include quantitative numerical demonstrations where informative. The actuary is also encouraged to consider a recommendation as to whether a more detailed assessment or risk report would be significantly beneficial for the intended user in order to examine particular financial risks. When making that recommendation, the actuary will take into account such factors as the plan's design, risk profile, maturity, size, funded status, asset allocation, cash flow, possible insolvency and current market conditions.

    Because the actuarial valuation results are dependent on a fixed set of assumptions and data as of a specific date, there is risk that emerging results may differ, perhaps significantly, as actual experience is fluid and will not exactly track current assumptions. This potential divergence may have a significant impact on the future financial condition of the plan. We have not been engaged to perform a detailed analysis of the potential range of the impact of risk relative to the Association's future financial condition, but have included a brief discussion of key risks that may affect the Association in *Section 2, Subsection J*. A more detailed assessment of the risks tailored to specific interests or concerns of the Board would provide the Board with a better understanding of the inherent risks. This assessment would further discuss and highlight information and risks particular to FCERA such as detailed historical experience and key events, growing plan maturity, heightened contribution sensitivity to asset and liability changes, and projected sensitivity to potential future investment returns through selected scenario or stress test projections.

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Note that this year the risk assessment section includes the disclosure of a "Low-Default-Risk Obligation Measure" (LDROM). This disclosure, along with commentary on the significance of the LDROM, is a new requirement under Actuarial Standard of Practice No. 4 (ASOP 4) for all pension funding actuarial valuation reports.

13. Segal strongly recommends an actuarial funding policy that targets 100% funding of the Actuarial Accrued Liability. Generally, this implies payments that are ultimately at least enough to cover Normal Cost, interest on the UAAL and the principal balance. The funding policy adopted by the Board as described in *Section 4, Exhibit 1* meets this standard.
14. This report constitutes an actuarial valuation for the purpose of determining the actuarially determined contribution (ADC) under the plan's funding policy and measuring the progress of that funding policy. The Net Pension Liability (NPL) and Pension Expense under Governmental Accounting Standards Board (GASB) Statements No. 67 and No. 68, for inclusion in the plan and employer's financial statements as of June 30, 2023, will be provided separately. The accounting disclosures will utilize different methodologies from those employed in the funding valuation, as required by the GASB. However, the ADC in this valuation is expected to be used as the ADC for GASB financial reporting.
15. It is important to note that this actuarial valuation is based on plan assets as of June 30, 2023. The plan's funded status does not reflect short-term fluctuations of the market, but rather is based on the market values on the last day of the plan year. Moreover, this actuarial valuation does not include any possible short-term or long-term impacts on mortality of the covered population that may emerge after June 30, 2023 due to COVID-19. Segal is available to prepare projections of potential outcomes of market conditions and other demographic experience upon request.

Summary of key valuation results

		June 30, 2023		June 30, 2022	
		Total Rate	Estimated Annual Dollar Amount[1] ($ in '000s)	Total Rate	Estimated Annual Dollar Amount[1] ($ in '000s)
Employer Contribution Rates:	• General Tier 1	54.17%	$78,161	50.81%	$73,313
	• General Tier 2	51.59%	3,651	48.34%	3,421
	• General Tier 3	51.80%	15,102	48.42%	14,117
	• General Tier 4	43.41%	6,749	39.90%	6,203
	• General Tier 5	41.44%	101,151	37.86%	92,413
	• Safety Tier 1	72.07%	24,674	69.28%	23,718
	• Safety Tier 2	72.15%	2,986	69.61%	2,881
	• Safety Tier 4	59.40%	3,289	56.86%	3,148
	• Safety Tier 5	55.08%	25,212	52.74%	24,140
	All Categories Combined	**49.26%**	**$260,975**	**45.93%**	**$243,354**
Average Member Contribution Rates:	• General Tier 1	10.56%	$15,237	10.26%	$14,804
	• General Tier 2	7.33%	519	7.17%	507
	• General Tier 3	8.58%	2,501	8.31%	2,423
	• General Tier 4	7.80%	1,213	7.89%	1,227
	• General Tier 5	7.95%	19,405	8.01%	19,552
	• Safety Tier 1	13.95%	4,776	12.90%	4,416
	• Safety Tier 2	12.25%	507	11.61%	480
	• Safety Tier 4	11.10%	615	11.06%	612
	• Safety Tier 5	13.09%	5,992	13.19%	6,037
	All Categories Combined	**9.58%**	**$50,765**	**9.45%**	**$50,058**

[1] Based on June 30, 2023 projected annual compensation of $529,841,000.

Summary of key valuation results (continued)

		June 30, 2023 ($ in '000s)	June 30, 2022 ($ in '000s)
Actuarial Accrued Liability as of June 30:	• Retired members and beneficiaries	$4,804,332	$4,427,231
	• Inactive vested members[1]	397,062	367,279
	• Active members	2,241,435	2,124,349
	• Total Actuarial Accrued Liability	7,442,829	6,918,859
	• Normal Cost for plan year beginning June 30[2]	126,672	120,722
Assets as of June 30:	• Market Value of Assets (MVA)[3]	$6,099,025	$5,623,399
	• Valuation Value of Assets (VVA)[3]	6,331,112	6,134,136
Funded status as of June 30:	• Unfunded Actuarial Accrued Liability on Market Value of Assets basis	$1,343,804	$1,295,460
	• Funded percentage on MVA basis	81.94%	81.28%
	• Unfunded Actuarial Accrued Liability on Valuation Value of Assets basis	$1,111,717	$784,723
	• Funded percentage on VVA basis	85.06%	88.66%
Key assumptions:	• Net investment return	6.50%	6.50%
	• Inflation	2.50%	2.50%
	• Payroll growth increase	3.00%	3.00%
	• Cost of living adjustments		
	– Tiers with 3.00% COLA	2.75%	2.50%
	– Tiers without COLA	0.00%	0.00%

1 Includes inactive members with member contributions on deposit with less than five years of service.
2 Includes administrative expense load.
3 Excludes non-valuation reserves (contingency reserve, if any).

Summary of key valuation results (continued)

		June 30, 2023	June 30, 2022	Change From Prior Year
Demographic data as of June 30:	**Active Members:**			
	• Number of members	7,650	7,466	2.5%
	• Average age	41.8	42.1	(0.3)
	• Average service	10.0	10.3	(0.3)
	• Total projected compensation	$529,840,359	$491,461,957	7.8%
	• Average projected compensation	$69,260	$65,827	5.2%
	Retired Members and Beneficiaries:			
	• Number of members:			
	– Service retired	6,756	6,610	2.2%
	– Disability retired	413	406	1.7%
	– Beneficiaries	1,205	1,159	4.0%
	– Total	8,374	8,175	2.4%
	• Average age	70.7	70.5	0.2
	• Average monthly benefit[1]	$3,489	$3,384	3.1%
	Inactive Vested Members:			
	• Number of members	5,187	4,848	7.0%
	• Average age	43.7	43.7	0.0
	Total Members:	21,211	20,489	3.5%

[1] Benefits include regular and settlement benefits but exclude non-vested supplemental benefits, if any.