



Orange County Sanitation District

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STEERING COMMITTEE

Agenda Report

File #: 2019-526

Agenda Date: 8/28/2019

Agenda Item No: 10.

FROM: James D. Herberg, General Manager
Originator: Lorenzo Tyner, Assistant General Manager

SUBJECT:

ELIMINATION OF UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL) AND NET PENSION LIABILITY (NPL) WITHIN THE ORANGE COUNTY EMPLOYEES' RETIREMENT SYSTEM

GENERAL MANAGER'S RECOMMENDATION

RECOMMENDATION: Recommend to the Board of Directors to:

Direct staff to pay off the following amounts in the Orange County Sanitation District's defined pension plan administered by the Orange County Employees' Retirement System (OCERS) in an amount not to exceed \$38 million:

- Unfunded Actuarial Accrued Liability (UAAL) in the amount of \$9 million for pension benefits
- Net Pension Liability (NPL) in the amount of \$29 million for deferred investment loss

BACKGROUND

As of July 1, 2014, the Orange County Sanitation District (Sanitation District) had an UAAL in its defined pension plan administered by OCERS of \$194 million. The Sanitation District made advanced payments to eliminate the UAAL and maintain a fully funded plan. In 2017, the Sanitation District had a credit with OCERS.

However, for the year ended December 31, 2018, OCERS' actuarial assumed rate of return was 7.00 percent, but actual investment returns were a loss of approximately two percent. The Sanitation District's allocated share of this shortfall resulted in a UAAL and NPL of \$9 million and \$29 million, respectively.

Over the last 20 years, OCERS' annual rate of return exceeded the Sanitation District's 70% of the time. Due to their ability to invest in the equity market, staff believes that, over the long-term, OCERS will consistently outperform the Sanitation District's return on investments. Therefore, staff recommends reducing its investment portfolio to fund its current total UAAL and NPL of approximately \$38 million.

RELEVANT STANDARDS

- Ensure the public's money is wisely spent
- Resolution No. OCSD 18-23 - Sanitation District's adopted Investment Policy - prudent

investor standard

PROBLEM

The return on investments by OCERS was less than planned within its actuarial assumptions, thereby creating a new Sanitation District UAAL (\$9 million) and NPL (\$29 million) for the OCERS year-ended December 31, 2018 of approximately \$38 million.

The Sanitation District could amortize the payment of this \$38 million UAAL and NPL over a long period of time, such as 10 to 20 years; however, in doing so, the Sanitation District would have to make up the anticipated returns these funds would be earning by OCERS over this repayment period. By paying these funds off now, the Sanitation District will forgo future anticipated interest expense of approximately 7.00% a year.

PROPOSED SOLUTION

Direct staff to pay off the Sanitation District's total UAAL and NPL estimated at \$38 million.

TIMING CONCERNS

As soon as the UAAL and NPL payoffs is made, the annual 7.00% interest rate applied against these funds will cease.

RAMIFICATIONS OF NOT TAKING ACTION

The Sanitation District will have to pay off its UAAL and NPL through a 10-to-20-year amortization scheduled at a rate of 7.00%, far below its ability to produce returns on its investment portfolio.

PRIOR COMMITTEE/BOARD ACTIONS

October 2016 - Board approved a \$40 million paydown of the UAAL with OCERS.

May 2015 - Board approved the FY 2015-16 Budget Update, which included a line item for the pay down of \$50 million in UAAL with OCERS.

July 2014 - Board action approved \$125 million pay down of UAAL with OCERS.

FINANCIAL CONSIDERATIONS

Payment of the Unfunded Actuarial Accrued Liability (UAAL) and Net Pension Liability (NPL) will result in the reduction of the Sanitation District reserves by \$38 million. It is anticipated that as OCERS' actual investment returns improve, most, if not all, of these funds will be recouped as a credit against future pension expenditures.

ATTACHMENT

The following attachment(s) may be viewed on-line at the OCSD website (www.ocsd.com) with the complete agenda package:

N/A