Staff Report 20-391
Item 4.E.

AC Transit Retirement System

To: AC Transit Board of Directors September 2020

From: Jeffrey Lewis - Chair, AC Transit Retirement Board

Re: 2020 Semi-Annual Report (#2)

Like the rest of the world and at the rest of the District, the Retirement Board and staff have spent a lot of time and effort reacting to the pandemic. Our thoughts are with the many District employees, and their families, who are working on the frontlines during these times. This report will focus on:

- The recently completed Actuarial Valuation.
- Investment performance for 2020.
- The response of the Retirement System to the pandemic.
- A thank you to retiring board members Yvonne Williams, Joyce Willis, and Claudia Allen

Recently Approved Actuarial Valuation

At its August 27th meeting, the Retirement Board approved the 2020 Actuarial Valuation, completing a process that began in the spring. As in prior years, the General Manager, CFO, and Finance staff were involved in providing feedback to the Retirement Board. The Retirement Board approved a projected District contribution of $60.7 million for the District's 2020/21 fiscal year, an increase of $700,000 from last year. This contribution is based on the assumption that the District's pensionable payroll will be $185 million during the current fiscal year. The District's contribution can be broken down into two components: 1) the normal cost (plus expenses); and 2) the amortization of the unfunded liability. The normal cost is the cost allocated to fund the benefits earned for the current year of service for the current workforce; the amortization of the unfunded liability is the payment required to close the gap between the current funding level and the funding target over a specific period of years. For the current fiscal year, the normal cost is projected at $24.5 million (13.4% of pensionable payroll), while the amortization of the unfunded liability plus expenses will be $36.2 million. Roughly 57% of the District's contribution is a result of amortizing the unfunded liability. The projected District contribution in the current valuation was $60.7 million, while in last year's valuation it was $60.1 million.

In comparing last year's results to this year's, our actuary highlighted the reduction in projected payroll from $194 million to $185 million and the increase in the amortization of the unfunded liability from $32.7 million to $34.7 million.

At its August meeting, the Retirement Board, along with District staff, reviewed the projected District contribution and the projected funded ratio of the Plan for the next 20 years. These are discussed below. As always, we welcome the opportunity to answer any questions from District Board members pertaining to the Actuarial Valuation.

This year is the third year in which the actuary computed the District's contribution on the PEPRA plan for unrepresented employees hired after 12/31/15. The estimated savings for the District's current fiscal year, as a result of the implementation of PEPRA, is roughly $300,000.

Funded Ratio

The funded ratio of the Plan increased slightly on the Actuarial Value of Assets, from 69.8% to 70.9%, while it increased substantially on a Market Value of Assets from 65.2% to 73.1%. The dramatic increase in the funded ratio on a Market Value of Assets basis was a result of the strong investment performance in 2019 (see below). The slight increase in the funded ratio on the Actuarial Value of Assets was a result of the smoothing methodology employed by the Plan, which limited the impact of the current year investment gains, as well as the significant contributions being made by the District. As you will recall, smoothing spreads over five years each year's gains or losses, compared to our assumptions, and minimizes changes to the District's contributions for the following year.

Projections

The 2020 Actuarial Valuation includes projections for the District's expected contributions and the funded ratio of the Plan over the next 20 years. These projections assume that all the assumptions made by our actuary are met. We all know that not all assumptions will be met; however, the projections on pages 8 and 9 (these pages are attached to this report) of the Actuarial Valuation are the best forecast of where the District contribution and the Funded Ratio of the Plan are headed.

The Retirement Board is happy to provide the District with projected results under any scenario requested. If you would like to discuss these projections, please contact Hugo Wildmann.

Investment Results

To say that investment performance in 2020 has been volatile would be an understatement. The Plan ended 2019 with $746.9 million in assets. At the end of March (2020), as the markets reacted to COVID-19, Plan assets had declined to roughly $642 million. At the end of August, Plan assets had climbed to over $750 million. The District's contribution for Fiscal Year 21/22 will be set based on Plan assets at the end of this calendar year.

As of the writing of this report, few market pundits would have predicted that U.S. equity markets would be up by more than 4% while the world was in the midst of the most severe pandemic in 100 years. U.S. equity markets were down over 25% near the end of March. Of course, we have no way of knowing how the market will perform for the rest of the year or in the upcoming years.

When writing about investment results in these reports, I have consistently mentioned that the focus of the Retirement Board is on the long-term. We all know that in the short-term, markets will go up and down, but over the long-term, we expect equity markets, in which over half of the Plan's assets are invested, to go up.

Through the end of August, the investment return for calendar year 2020 for the Plan is over 3.0%. As I have mentioned often, it is reasonable to expect that roughly one year out of every three or four years will produce a negative return for the Plan and that close to 40% of years will produce a return below our actuarially assumed rate. The fact that the Plan will have a year (or several years in a row) of returns below the actuarially assumed rate is not a reason for alarm or a time to implement changes to the investment portfolio. It is usually a time to take a long-term view and wait out the cyclical nature of the markets.

As part of our long-term asset allocation strategy, the Board purchased $7 million in equities in March and April after the market had declined and sold $7 million in equities in early September. In order to keep our equity allocation close to our 51% long-term target, the Board needs to sell equities after a period of strong performance and purchase equities when they have performed poorly. In 2020, these transactions resulted in investment gains of approximately $2 million. In this particular case, we managed to "buy low and sell high".

Department Activity

Like many other departments at AC Transit, the Retirement Department has successfully transitioned to working from home with occasional trips to the office. With technology – Zoom, Facetime and email -- the department has been able to meet the requests of employees and retirees.

Thank You

This is the last Semi-Annual report I will write with Yvonne and Joyce on the Retirement Board. I would like to thank them for their long and dedicated service. I speak for the other board members when I say what a pleasure it has been to have Yvonne and Joyce as fellow board members. Yvonne and Joyce have shared their extensive knowledge of District operations with the Retirement Board which has been helpful on countless occasions. Even though Claudia Allen is not retiring until next year, I would also like to thank Claudia for her dedicated service on the Board. Her knowledge of District finances and operations has been a valuable resource in our decision making.

Please feel free to call me, Jeffrey Lewis (510-463-3900), or Hugo Wildmann (510-891-4889), if you would like to discuss this report or request additional information.