1.0 Pension System Governance

The Sonoma County Employees' Retirement Association (SCERA) was established in 1946 pursuant to the County Employees Retirement Law of 1937 to administer the County's defined-benefit public pension plan. SCERA is not part of the statewide California Public Employees' Retirement System ("CalPERS"). From 1946 to 1998, SCERA was administered through the County of Sonoma's Treasurer's Office, and the Treasurer was the Retirement Administrator. In 1998, governance of the plan was shifted out of the Treasurer's office and into a separate agency. SCERA now operates independently of the County and is governed by a 9-member Board of Retirement. SCERA currently administers defined-benefit pension plans for multiple employers, including non-County entities; however, employees and retirees from the County and affiliated special districts governed by the Board of Supervisors/Directors still comprise roughly 90% of total plan members.

Governed by Board of Supervisors/Directors	Non-County Entities
• County of Sonoma • Sonoma County Water Agency • Community Development Commission	• Sonoma Valley Fire District • Superior Court • Sonoma County Transportation Authority

SCERA's Board of Retirement responsible for establishing policies to administer the pension plan, making benefit determinations, and managing the investment of assets. The day-to-day management of SCERA is delegated to the Chief Executive Officer appointed by the Board of Retirement. While SCERA makes benefits determinations for individual retirees, the Board of Supervisors/Directors is responsible for approving the formulas used to calculate members' pension benefits, which is handled through collective bargaining:

SCERA Board of Retirement	County Board of Supervisors/Directors
• Responsible for plan administration • Makes benefits determinations • Manages investment of assets • Recommends Ad hoc COLAs to the BOS for consideration	• Approves pension benefit formulas through collective bargaining • Approves COLA benefits for its employees and retirees (CERL Articles 16.5 and 16.6)

1.1. County Employees Retirement Law of 1937

The County of Sonoma is one of 20 counties in the State of California covered by the County Employees Retirement Law of 1937 (also known as CERL or '37 Act), as contained in Government Code Title 3, Division 4, Part 3, Articles 1 through 18. This is a statutory system that is separate and distinct from CalPERS, which is governed under a different section of the Government Code.

1.2. Public Employees' Pension Reform Act of 2013

The California Public Employees' Pension Reform Act (PEPRA) was signed by Governor Jerry Brown in 2012 and went into effect on January 1, 2013 (AB 340 and AB 197); PEPRA applies to all public retirement systems in California. PEPRA made several changes to the pension benefits for new employees hired on or after the effective date, including setting new maximum benefits, adopting a lower-cost pension formula for safety and non-safety employees, with requirements to work longer to reach full retirement age, and a cap on the amount of compensation used to calculate a pension. PEPRA also reformed pension spiking, required a three-year averaging of final compensation for new employees to calculate

pension benefits, removed certain elements of pay from being counted in the retirement calculation, and provided counties with new authority to negotiate cost sharing agreements with current employees.

2.0 County Employee Retirement Plan Benefits and Tiers

All permanent County employees working at least 50% of a full-time position are members of the SCERA retirement system. Participation and member contributions are mandatory for all eligible employees, expect for certain elected officials and newly hired employees aged 60 or over, for which participation is optional.

SCERA members are separated into different retirement plans or tiers depending on their job classification and when they first joined the SCERA retirement system upon being hired by the County, and each tier has specific benefits formulas and minimum retirement ages. SCERA members fall into two main categories, either General or Safety, depending on their job classification during their working career. Most County job classifications fall under the General category, which includes approximately 80% of all active and retired members. The Safety category primarily includes job classifications providing fire and public safety services.

Within the over-arching General and Safety categories, SCERA members fall under distinct retirement plan tiers depending on their hire date and eligibility. Members who entered the retirement system before PEPRA was enacted January 1, 2013, are in the Plan A Legacy tier. Most members who entered the retirement system after that date are in the Plan B PEPRA tier; however, some members joining after this date are eligible for the Plan A Legacy tier due to having reciprocity with another qualified California retirement system. All Legacy Plan A active members are eligible for the same benefit formula, but a cohort of pre-Legacy retirees who retired prior to 2003 have a different benefit formula.

2.1 Calculation of Pension Benefits

Upon retirement or separation, pension benefits for SCERA members are calculated using established formulas that depend on the members' specific retirement plan and tier. Members' benefit calculation relies on multiplying three main factors together, and increasing any of these factors results in a higher lifetime pension benefit:

1. Age Factor, or members' age when they start receiving benefits. Pension formulas specify the optimal retirement age for maximizing benefits, expressed as a percentage. For example, the PEPRA Plan B "2.5% at 67" Age Factor means members can achieve a maximum age factor of 2.5% at age 67, but the factor is reduced proportionally depending on age, as low as 1.0% at age 52.
2. Compensation Factor, or members' highest average compensation. Benefits for Plan A Legacy members are calculated using the member's highest average monthly compensation over a consecutive 12-month period; benefits for Plan B PEPRA members are calculated using the member's highest average monthly compensation over a consecutive 3-year period. Higher average compensation
3. Members' total years of service. Service credit measures the amount of time members have been participating in the SCERA Plan, plus any purchases of eligible service credit completed. Service credit is earned for the time members are in paid status, including time on paid vacation, holiday, or sick leave.

The two hypothetical examples below illustrate how pension benefit calculations utilize these three factors:

Age Factor (a)	Avg. Monthly Compensation (b)	Years of Service (c)	Monthly Pension Benefit (a) *(b) * (c)
3.0%	$5,000	30	$4,500
2.0%	$4,000	20	$1,600

The table below summarizes the pension formulas for the various retirement tiers:

Plan Tier Description	Member Eligibility	Age Factor	Compensation Factor
Pre-Legacy General	Retired prior to 2003	2.6% @ Age 62	Highest 12-month average
Pre-Legacy Safety	Retired prior to 2003	2.0% @ Age 50	Highest 12-month average
Plan A Legacy General	Hired prior to 1/1/2013, or after w/ reciprocity	3.0% @ Age 60	Highest 12-month average
Plan A Legacy Safety	Hired prior to 1/1/2013, or after w/ reciprocity	3.0% @ Age 50	Highest 12-month average
Plan B PEPRA General	Hired after 1/1/2013	2.5% @ Age 67	Highest 3-year average
Plan B PEPRA Safety	Hired after 1/1/2013	2.7% @ Age 57	Highest 3-year average

Refer to SCERA's website for additional information, including tables showing how these factors affect determination of benefits: https://scretire.org/active-deferred/calculating-your-benefit

2.2 Pension Cost-of-Living Adjustments

SCERA operates under an Ad-hoc cost-of-living-adjustment (COLA) design with no automatic, ongoing COLA benefit pre-funded by employer and employee contributions. As a result, pension benefits paid to members do not receive automatic annual COLAs, like recipients of Social Security benefits. The Retirement Board can recommend Ad-hoc COLAs be granted within the parameters of existing COLA statutes, but the Board of Supervisors as the governing body of the County must approve implementation the COLA. Current County Employment Retirement Law (CERL) statutes allow for two types of COLAs:

1) Purchasing Power COLAs, which implement a one-time benefit increase for retirees to restore purchasing power lost over time due to inflation up to a target level, typically 80% of lost purchasing power. Application of a purchasing power COLA results in earlier retirees receiving larger relative benefits increases compared to recent retirees, and it would not apply to retirees who have lost less than 20% of purchasing power since their retirement date.
2) Flat percentage COLAs, which provide the same one-time across-the-board percent increase to all retirees.

From 1946 through 2008, Ad hoc COLAs were approved ~75% of the time, funded by excess earnings, amortized unfunded liability, realized investment gains, or increased employer contributions. Great Recession investment losses negatively impacted SCERA's excess earnings, which prevented further COLA recommendations after 2008.

2.3 Limits on Pension Benefits

Retirement law and Internal Revenue Code (IRC) Section 415(b) limit the annual benefit amount that can be paid to a retiree from retirement systems, which applies to SCERA. This limit is based on an individual's age at retirement and their retirement plan (General/Safety). The County has an excess benefits plan which pays the difference between a member's calculated benefit and the IRC allowable limit. Internal Revenue Code Section 401(a) (17) also imposes limits on pensionable compensation that may be used to calculate retirement benefits for individuals who first became members of SCERA on or after January 1, 1996. These limits may be adjusted annually by the Internal Revenue Service; refer to the IRS website for current limits: https://www.irs.gov/retirement-plans/cola-increases-for-dollar-limitations-on-benefits-and-contributions.

The retirement benefit for Plan A Legacy members below the IRS limit is capped at 100% of their highest average monthly compensation. Pensionable compensation used to calculate the retirement benefit for a Plan B PEPRA member is also capped; refer to the California State Controller's Office website for annual limits: https://www.sco.ca.gov/PEPRA_Compensation_Limits.html. Pension benefits for Plan B PEPRA members who participate in Social Security, like County employees, are capped at 100% of the PEPRA limit.

3.0 Funding the Pension Plan

The SCERA pension plan is funded by a combination of contributions from participating employers, contributions from active employees, and earnings on those invested funds over time. All participating members contribute to the Plan through regular biweekly payroll deductions. Because SCERA is a tax-qualified plan, contributions into the SCERA fund are not taxed when they are made, but benefits based on the contributions will be taxed as benefits are paid. Contribution rates vary according to plan tiers.

The annual contribution rates paid by the County and its employees are determined every year as part of SCERA's annual actuarial valuation and review conducted by an independent actuary. If all actuarial assumptions in the valuations occurred exactly as predicted, the Plan would be funded at 100%. However, in practice, the Plan's actual experience each year varies from the demographic and economic assumptions used to set contribution rates. When earnings or other assumptions do not meet expectations, it results in creation of unfunded liabilities for the retirement system. The Plan will always experience some years that exceed earnings and some years when the earnings assumptions are not met. The ideal is to create a well-funded plan over time by having more overfunding than underfunding through refining of actuarial methodology and prudent investment of assets. Both the County as employer and its employees pay annual contributions to fund the expected normal cost of the Plan based on the actuarially determined rates. Adverse actuarial assumption changes, other experience losses, or investment return shortfalls result in creation of unfunded liabilities for the pension system, and the County as employer is responsible for paying for the unfunded liabilities via higher annual employer contribution rates. SCERA's annual valuations can be viewed on its website: https://scretire.org/financial/actuarial-reports

3.1 Unfunded Liability Cost Sharing with Employees

Starting in Fiscal Year 2003-04, the County negotiated with General and Safety employee groups to have all County employees contribute supplemental contributions toward the pension system's unfunded

liability over a set 20-year period, ending in Fiscal Year 2023-24. All County employees paid supplemental contributions towards UAAL, equal to 3.03% of pensionable payroll for General members and 3.00% for Safety members. Supplemental contributions expired June 2023 for all Plan B PEPRA Safety members, and expired June 2024 for all Plan B General members and a subset of Plan A Legacy members. The cost sharing arrangement has been maintained for approximately 1,000 Plan A Legacy employees (including Salary Resolution and four bargaining units) who continue to pay supplemental contributions towards unfunded liability equal to 3.00%/3.03% of pensionable pay.

3.2 Normal Cost Sharing with Legacy Plan A Employees

Employees' annual contribution rates as a percentage of pensionable compensation vary according to their plan tier. Plan A Legacy employees pay normal cost contribution rates based on their age of entry into the system, and whether they are General or Safety members, with individuals hired at a younger age paying a lower rate than older individuals, because their invested contributions have more time to benefit from compounding returns. Plan B PEPRA employees pay a flat normal cost contribution rate irrespective of age, but the rate varies depending on if they are General or Safety. The Plan B PEPRA employee contribution rate calculated to be equal to a 50/50 normal cost share with the County as employer (excludes unfunded liabilities borne by the County).

As an outcome of collective bargaining negotiations in 2016, the County reached agreement with employee labor groups to implement normal cost sharing arrangements for all Plan A Legacy employees, which was an incremental move towards 50/50 sharing of normal cost, which Plan B PEPRA members already pay. As part of this cost sharing arrangement, the increased cost sharing by Legacy employees is partially offset by receiving a taxable reimbursement in their biweekly paychecks.

4.0 Accelerated Payment of Unfunded Liabilities

The SCERA Plan's unfunded liability is calculated as the amount by which future obligations to pay retired members' benefits exceeds the present value of the Plan's available fund assets. The pension system pays for retirees' pension benefits through a combination of employer and employee contributions, plus investment income earned on those contributions. The contribution rates are adjusted annually based on an analysis of the estimated costs to meet all future retiree benefit obligations based on current economic (i.e., wage inflation and assumed investment returns) and non-economic (i.e., member demographic and mortality rate) assumptions. New unfunded liabilities are created each year whenever actual experience does not meet actuarial assumptions. When unfunded liability is created each year, it is amortized over a fixed 20-year period from the year created, and the County's annual employer contribution rates are in turn increased to pay the annual cost for the unfunded liability over the 20-year period.

To help reduce the County's total unfunded pension liability, the Board of Supervisors adopted a financial policy in June 2019 that authorized annual prepayments towards unfunded liabilities, equal to 0.5% of pensionable payroll, plus the option for one-time payments. The recurring prepayments equal to 0.5% of pensionable payroll are made every year on top of the required annual employer contributions paid by the County, and they are applied directly to the unfunded liability. The Board has also authorized several one-time payments using General Fund savings at fiscal year-end close. Prepaying unfunded liability helps avoid future interest costs calculated at SCERA's assumed discount rate; as a rule of thumb, future interest cost avoided over a 20-year period is equal to approximately 80% of the prepayment amount (i.e., a $5,000,000 prepayment avoids another $4,000,000 of costs over time). Refer to Section I of the Annual Pension Report for more information.

5. Pension Obligation Bonds

Pension Obligation Bonds ("POB") are issued by government entities to help cover its obligations to the pension system in which its employees are members. In addition to paying its proportional share of the pension system's unfunded liability, the County also pays for unfunded pension liabilities indirectly via its debt service on several outstanding Pension Obligation Bonds, which were issued in the past to help pay unfunded liability obligations to SCERA. The bonds were issued by the County on three separate occasions—1993, 2003, and 2010—when the interest rate difference, or spread, between SCERA's assumed discount rate (8.00% - 8.25% at the time of issuance) and the bond market, afforded an opportunity for significant savings over the 20-year payment period used both by the system and the bond market.

The POB proceeds were deposited in the SCERA pension fund upon issuance and invested to continually earn a return over time. In turn, the County pays POB principal and interest debt service payments to bondholders in accordance with the respective 20-year payment schedules for each issuance. The 1993 Pension Obligation Bond issuance was fully paid in 2013, and the 2003 bond issuance was fully paid in 2023. Refer to Section II of the Annual Pension Report for more information.