City of Palo Alto (ID # 6144)

Finance Committee Staff Report

Report Type: Action Items **Meeting Date: 10/20/2015**

Council Priority: City Finances

Summary Title: GASB68

Title: New Pension Reporting Standards Government Accounting Standards Board Statement Number 68 (GASB 68)

From: City Manager

Lead Department: Administrative Services

Motion
Staff recommends that the Finance Committee review and discuss the new Government Accounting Standards Board pension reporting standards known as GASB 68.

Background
In June 2012, the Government Accounting Standards Board (GASB) approved a new reporting statement, GASB Statement No. 68 (GASB 68), that improved the financial reporting of pensions by local governments. GASB 68, formally titled *Accounting and Financial Reporting for Pensions*, establishes new accounting and financial reporting standards for local governments that provide their employees with pensions. The new standard requires government agencies to report pension information to increase transparency about pension costs to help decision makers factor in the financial impact of total pension obligations. GASB 68 must be implemented by June 30, 2015 and the City of Palo Alto will comply with this requirement with the upcoming FY2015 Comprehensive Annual Financial Report (CAFR), which is scheduled to be presented to the Finance Committee in November, 2015.

Discussion
Local governments with pensions have a total pension liability, which is the obligation to pay deferred pension benefits in the future. When the total pension liability is greater than the pension plan's assets there is a net pension liability, also known as unfunded pension liability. GASB 68 now requires governments to report their net pension liability on their government-wide financial statements, as well as in the proprietary fund statements, in the CAFR. Prior to GASB 68 the net pension liability was reported in the notes section of the CAFR.

Palo Alto's pension liability is calculated as follows:

	FY15 CAFR	
	Pension Liability	**% Funded**
Safety	$ 102.8 M	72.01%
Miscellaneous	187.1 M	71.80%
Total Pension Liability	**$ 289.9 M**	

The above figures are obtained from the CalPERS actuarial reports dated June 30, 2014 (Attached).

As discussed above, instead of discussing the City's pension liability in the Notes section of the CAFR, the pension liability figures will be presented for the first time in the FY2015 CAFR in the entity wide and separate proprietary fund schedules. The allocated net pension liability is presented below:

	General Fund	Electric Fund	Water Fund	Gas Fund	All Other Funds	Total
Net Pension Liability	$197.2	$26.1	$11.0	$11.8	$43.8	$289.9
Percentage	68.0%	9.0%	4.0%	4.1%	14.9%	100.0%

The pension liability will be allocated based on the employer contributions for FY2014 for the employees serving in each fund.

The new GASB 68 reporting requirements will impact the CAFR on an annual go forward basis. As with past practice, the city will continue to pay the annual required contribution for the pension liabilities as identified in the annual CalPERS actuarial reports. The next set of reports, which inform the City of its FY 2017 pension payments and rates, are scheduled to be released late October/early November 2015. There will be a small discrepancy between the reports since the GASB 68 reports are based on actuarial analysis using employee census data that is two years in arrears while the October actuarial reports are based on current calendar year employee census data.

The City's outside financial auditing firm, MGO, provided staff with guidance on how to conform to the GASB 68 requirements. MGO will provide a final opinion on the appropriateness of the GASB 68 allocation that will be presented in the FY2015 CAFR.

Next Steps
Starting with the FY2015 CAFR the GASB 68 pension liability figures will be presented in the CAFR on an annual basis.

Council referred the unfunded pension liability issue to the Finance Committee to explore potential action steps to reduce it and stabilize the annual employer contribution (Report ID # 6074).

Resource Impact
The pension liability reported in the CAFR for GASB 68 purposes does not impact the budget. The City's annual budget process will continue to use the pension liability figures that are provided by CalPERS in the actuarial valuation reports for the safety and miscellaneous plans in the October timeframe each year. The reports provide the employer contribution rate that is used to determine the annual pension cost for the City.

Attachments:
- Attachment A: GASB 68 Miscellaneous Plan Valuation Report (PDF)
- Attachment B: GASB 68 Safety Plan Valuation Report (PDF)

Attachment A

CalPERS

GASB 68 ACCOUNTING VALUATION REPORT

(CalPERS ID: 6373437857)
Rate Plan Identifier: 8

Prepared for the CITY OF PALO ALTO MISCELLANEOUS PLAN, an Agent Multiple-Employer Defined Benefit Pension Plan

Measurement Date of June 30, 2014

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ACTUARIAL CERTIFICATION

This report provides disclosure and reporting information as required under Governmental Accounting Standards Board Statement 68 (GASB 68) for the MISCELLANEOUS PLAN of the CITY OF PALO ALTO (the "Plan"), an Agent Multiple-Employer Defined Benefit Pension Plan participating in the California Public Employees' Retirement System (CalPERS), for the measurement period ended June 30, 2014. This information should be used for the fiscal year beginning after June 15, 2014 but ending on or before June 30, 2015.

Determinations for purposes other than financial accounting requirements may be significantly different from the results in this report. Thus, the use of this report for purposes other than those expressed here may not be appropriate.

This accounting valuation report relies on liabilities and related validation work performed by the CalPERS Actuarial Office as part of the June 30, 2013 annual funding valuation for the Plan. The census data and benefit provisions underlying the liabilities were prepared as of June 30, 2013 and certified as part of the annual funding valuation by the CalPERS Actuarial Office. The June 30, 2013 liabilities used for this accounting valuation are based on the actuarial assumptions recommended by the CalPERS Chief Actuary and adopted by the CalPERS Board in February 2014 as laid out in the 2014 report titled "CalPERS Experience Study and Review of Actuarial Assumptions." These liabilities were validated as part of the June 30, 2013 funding valuation that included the estimated impact of the change in actuarial assumptions on contribution requirements. The undersigned is relying upon these prescribed assumptions and methods and is not able to render an opinion on their reasonability, as this would require a substantial amount of additional work beyond the scope of this report. This report also relies on asset information for the measurement period as supplied by the CalPERS Financial Office. The fiduciary net position as of June 30, 2014, and the changes in net position for the year then ended were audited by CalPERS' independent auditors, Macias Gini & O'Connell LLP, as part of the audit of the Schedule of Changes in Fiduciary Net Position by Employer Rate Plan of CalPERS Agent Multiple-Employer Pension Plan.

With the provided liability and asset information, the total pension liability, net pension liability and pension expense were developed for the measurement period using standard actuarial techniques. In addition, the results are based on CalPERS' understanding of the financial accounting and reporting requirements under U.S. Generally Accepted Accounting Principles as set forth in GASB 68. The information in this report is not intended to supersede the advice and interpretations of the employer's auditor. This report may not provide all the information necessary to complete the required disclosures under GASB 68. The employer should supplement and update the information in this report with its own financial data as necessary to complete the disclosure information required by GASB 68.

The undersigned is familiar with the near-term and long-term aspects of pension valuations and meets the Qualification Standards of the American Academy of Actuaries necessary to render the actuarial opinions contained herein. The information provided in this report is dependent upon various factors as documented throughout this report, which may be subject to change. Each section of this report is considered to be an integral part of the actuarial opinions.

Henry Neeb

HENRY NEEB, ASA, MAAA

Introduction

This is the GASB 68 Accounting Valuation Report to be used for your fiscal year beginning after June 15, 2014 and ending on or before June 30, 2015 for your MISCELLANEOUS PLAN (Plan). GASB Statement No. 68 replaced the requirements of GASB 27 effective for fiscal years beginning after June 15, 2014.

Statement 68 was issued by GASB in June 2012, requiring public employers to comply with new accounting and financial reporting standards. Statement 68 outlines a different approach to the recognition and calculation of pension obligations. Under the new GASB standards, employers that participate in a defined benefit pension plan administered as a trust or equivalent arrangement are required to record the net pension liability, pension expense, and deferred outflows/deferred inflows of resources related to pensions in their financial statements as part of their financial position.

Net pension liability is the plan's total pension liability based on entry age normal actuarial cost method less the plan's fiduciary net position. This may be a negative liability (net pension asset).

Pension expense is the change in net pension liability from the previous fiscal year to the current fiscal year less adjustments. This may be a negative expense (pension income).

Deferred outflows and deferred inflows of resources related to pensions are certain changes in total pension liability and fiduciary net position that are to be recognized in future pension expense.

This report may not provide all the information necessary to complete the required disclosures under GASB 68. **The employer should supplement and update the information in this report with its own financial data as necessary to complete the disclosure information required by GASB 68.** For example, no adjustments have been made for contributions subsequent to the measurement date. Appropriate accounting treatment of any contributions made after the measurement date is the responsibility of the employer. CalPERS recommends that the employer consult with its auditor regarding any such adjustments.

Purpose of the Report

The Plan participates in the CalPERS agent multiple-employer defined benefit pension plan. This GASB 68 report provides accounting and financial reporting for pensions, to be used in the employer's financial reports. The pension expense is for the measurement period of 2013-14 and the net pension liability is measured as of June 30, 2014. Liabilities are based on the results of the actuarial calculations performed as of June 30, 2013 and were rolled forward to June 30, 2014. Fiduciary net position is based on fair value of investments as of June 30, 2014. Since GASB 68 allows a measurement date of up to 12 months before the employer's fiscal year-end, this report can be used for fiscal years beginning after June 15, 2014 and ending on or before June 30, 2015.

The following pension information is disclosed in this report:

- Summary of Significant Accounting Policies
- General Information about the Pension Plan
    - Plan Description, Benefits Provided and Employees Covered
    - Contribution Description
    - Actuarial Methods and Assumptions
    - Discount Rate
    - Pension Plan Fiduciary Net Position
- Changes in the Net Pension Liability
    - Sensitivity of the Net Pension Liability
    - Subsequent Events
    - Recognition of Gains and Losses
- Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions
- Schedules of Required Supplementary Information (10-Year History[1]):
    - Schedule of Changes in Net Pension Liability and Related Ratios
    - Schedule of Plan Contributions

The use of this report for other purposes may be inappropriate.

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

Summary of Significant Accounting Policies

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Plan and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the CalPERS Financial Office. For this purpose, benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

GASB 68 requires that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used.

Valuation Date (VD)	June 30, 2013
Measurement Date (MD)	June 30, 2014
Measurement Period (MP)	July 1, 2013 to June 30, 2014

General Information about the Pension Plan

Plan Description, Benefits Provided and Employees Covered

The Plan is an agent multiple-employer defined benefit pension plan administered by the California Public Employees' Retirement System (CalPERS). A full description of the pension plan regarding number of employees covered, benefit provisions, assumptions (for funding, but not accounting purposes), and membership information are listed in the June 30, 2013 Annual Actuarial Valuation Report. Details of the benefits provided can be obtained in Appendix B of the actuarial valuation report. This report and CalPERS' audited financial statements are publicly available reports that can be obtained at CalPERS' website under Forms and Publications.

Contribution Description

Section 20814(c) of the California Public Employees' Retirement Law (PERL) requires that the employer contribution rates for all public employers be determined on an annual basis by the actuary and shall be effective on the July 1 following notice of a change in the rate. The total plan contributions are determined through CalPERS' annual actuarial valuation process. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The employer is required to contribute the difference between the actuarially determined rate and the contribution rate of employees. For the measurement period ended June 30, 2014 (the measurement date), the average active employee contribution rate is 7.796 percent of annual pay, and the employer's contribution rate is 25.536 percent of annual payroll. Employer contribution rates may change if plan contracts are amended. It is the responsibility of the employer to make necessary accounting adjustments to reflect the impact due to any Employer Paid Member Contributions or situations where members are paying a portion of the employer contribution.

Actuarial Methods and Assumptions Used to Determine Total Pension Liability

For the measurement period ended June 30, 2014 (the measurement date), the total pension liability was determined by rolling forward the June 30, 2013 total pension liability. The June 30, 2013 and the June 30, 2014 total pension liabilities were based on the following actuarial methods and assumptions:

Actuarial Cost Method	Entry Age Normal in accordance with the requirements of GASB Statement No. 68
Actuarial Assumptions	
Discount Rate	7.50%
Inflation	2.75%
Salary Increases	Varies by Entry Age and Service
Investment Rate of Return	7.50% Net of Pension Plan Investment and Administrative Expenses; includes Inflation
Mortality Rate Table[1]	Derived using CalPERS' Membership Data for all Funds
Post Retirement Benefit Increase	Contract COLA up to 2.75% until Purchasing Power Protection Allowance Floor on Purchasing Power applies, 2.75% thereafter

[1] The mortality table used was developed based on CalPERS' specific data. The table includes 20 years of mortality improvements using Society of Actuaries Scale BB. For more details on this table, please refer to the 2014 experience study report.

All other actuarial assumptions used in the June 30, 2013 valuation were based on the results of an actuarial experience study for the period from 1997 to 2011, including updates to salary increase, mortality and retirement rates. The Experience Study report can be obtained at CalPERS' website under Forms and Publications.

Discount Rate

The discount rate used to measure the total pension liability was 7.50 percent. To determine whether the municipal bond rate should be used in the calculation of a discount rate for each plan, CalPERS stress tested plans that would most likely result in a discount rate that would be different from the actuarially assumed discount rate. Based on the testing, none of the tested plans run out of assets. Therefore, the current 7.50 percent discount rate is adequate and the use of the municipal bond rate calculation is not necessary. The long-term expected discount rate of 7.50 percent is applied to all plans in the Public Employees Retirement Fund. The stress test results are presented in a detailed report called "GASB Crossover Testing Report" that can be obtained at CalPERS' website under the GASB 68 section.

According to Paragraph 30 of Statement 68, the long-term discount rate should be determined without reduction for pension plan administrative expense. The 7.50 percent investment return assumption used in this accounting valuation is net of administrative expenses. Administrative expenses are assumed to be 15 basis points. An investment return excluding administrative expenses would have been 7.65 percent. Using this lower discount rate has resulted in a slightly higher total pension liability and net pension liability. This difference was deemed immaterial to the agent multiple-employer plan. However, employers may determine the impact at the rate plan level for their own financial reporting purposes. Refer to page 8 of this report, which provides information on the sensitivity of the net pension liability to changes in the discount rate.

CalPERS is scheduled to review all actuarial assumptions as part of its regular Asset Liability Management review cycle that is scheduled to be completed in February 2018. Any changes to the discount rate will require Board action and proper stakeholder outreach. For these reasons, CalPERS expects to continue using a discount rate net of administrative expenses for GASB 67 and 68 calculations through at least the 2017-18 fiscal year. CalPERS will continue to check the materiality of the difference in calculation until such time as we have changed our methodology.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class.

In determining the long-term expected rate of return, staff took into account both short-term and long-term market return expectations as well as the expected pension fund cash flows. Such cash flows were developed assuming that both members and employers will make their required contributions on time and as scheduled in all future years. Using historical returns of all the funds' asset classes, expected compound (geometric) returns were calculated over the short-term (first 10 years) and the long-term (11-60 years) using a building-block approach. Using the expected nominal returns for both short-term and long-term, the present value of benefits was calculated for each fund. The expected rate of return was set by calculating the single equivalent expected return that arrived at the same present value of benefits for cash flows as the one calculated using both short-term and long-term returns. The expected rate of return was then set equivalent to the single equivalent rate calculated above and rounded down to the nearest one quarter of one percent.

The table below reflects long-term expected real rate of return by asset class. The rate of return was calculated using the capital market assumptions applied to determine the discount rate and asset allocation. These geometric rates of return are net of administrative expenses.

Asset Class	New Strategic Allocation	Real Return Years 1 - 10[1]	Real Return Years 11+[2]
Global Equity	47.0%	5.25%	5.71%
Global Fixed Income	19.0	0.99	2.43
Inflation Sensitive	6.0	0.45	3.36
Private Equity	12.0	6.83	6.95
Real Estate	11.0	4.50	5.13
Infrastructure and Forestland	3.0	4.50	5.09
Liquidity	2.0	(0.55)	(1.05)

[1]An expected inflation of 2.5% used for this period
[2]An expected inflation of 3.0% used for this period

Pension Plan Fiduciary Net Position

The plan fiduciary net position disclosed in your GASB 68 accounting valuation report may differ from the plan assets reported in your funding actuarial valuation report due to several reasons. First, for the accounting valuations, CalPERS must keep items such as deficiency reserves, fiduciary self-insurance and OPEB expense included as assets. These amounts are excluded for rate setting purposes in your funding actuarial valuation. In addition, differences may result from early Comprehensive Annual Financial Report closing and final reconciled reserves.

Changes in the Net Pension Liability

The following table shows the changes in net pension liability recognized over the measurement period.

	Increase (Decrease)		
	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability/(Asset) (c) = (a) - (b)
Balance at: 6/30/2013 (VD)[1]	**$ 635,847,037**	**$ 413,410,472**	**$ 222,436,565**
Changes Recognized for the Measurement Period:			
• Service Cost	12,441,595		12,441,595
• Interest on the Total Pension Liability	46,963,318		46,963,318
• Changes of Benefit Terms	0		0
• Differences between Expected and Actual Experience	0		0
• Changes of Assumptions	0		0
• Contributions from the Employer		17,399,732	(17,399,732)
• Contributions from Employees		6,344,660	(6,344,660)
• Net Investment Income[2]		70,988,848	(70,988,848)
• Benefit Payments, including Refunds of Employee Contributions	(31,780,533)	(31,780,533)	0
Net Changes during 2013-14	**$ 27,624,380**	**$ 62,952,707**	**$ (35,328,327)**
Balance at: 6/30/2014 (MD)[1]	**$ 663,471,417**	**$ 476,363,179**	**$ 187,108,238**

[1] The fiduciary net position includes receivables for employee service buybacks, deficiency reserves, fiduciary self-insurance and OPEB expense. As described on Page 6, this may differ from the plan assets reported in the funding actuarial valuation report.

[2] Net of administrative expenses. For details, see note in Appendix B-2.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the Plan as of the measurement date, calculated using the discount rate of 7.50 percent, as well as what the net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower (6.50 percent) or 1 percentage-point higher (8.50 percent) than the current rate:

	Discount Rate - 1% (6.50%)	Current Discount Rate (7.50%)	Discount Rate + 1% (8.50%)
Plan's Net Pension Liability/(Asset)	$ 269,622,616	$ 187,108,238	$ 118,202,943

Subsequent Events

There were no subsequent events that would materially affect the results presented in this disclosure.

Recognition of Gains and Losses

Under GASB 68, gains and losses related to changes in total pension liability and fiduciary net position are recognized in pension expense systematically over time.

The first amortized amounts are recognized in pension expense for the year the gain or loss occurs. The remaining amounts are categorized as deferred outflows and deferred inflows of resources related to pensions and are to be recognized in future pension expense.

The amortization period differs depending on the source of the gain or loss:

Difference between projected and actual earnings	5 year straight-line amortization
All other amounts	Straight-line amortization over the average expected remaining service lives of all members that are provided with benefits (active, inactive, and retired) as of the beginning of the measurement period

The expected average remaining service lifetime (EARSL) is calculated by dividing the total future service years by the total number of plan participants (active, inactive, and retired).

The EARSL for the Plan for the 2013-14 measurement period is 3.1 years, which was obtained by dividing the total service years of 7,375 (the sum of remaining service lifetimes of the active employees) by 2,407 (the total number of participants: active, inactive, and retired). Note that inactive employees and retirees have remaining service lifetimes equal to 0. Also note that total future service is based on the members' probability of decrementing due to an event other than receiving a cash refund.

Pension Expense and Deferred Outflows and Deferred Inflows of Resources Related to Pensions

Paragraph 137 of GASB 68 and Questions 267 and 268 of the GASB 68 Implementation Guide set forth guidance on implementing the standard. The employer should use this guidance for the adjusting entries concerning the net pension obligation and the initial net pension liability/(asset). As of the start of the measurement period (July 1, 2013), the net pension liability/(asset) is $222,436,565.

For the measurement period ending June 30, 2014 (the measurement date), the CITY OF PALO ALTO incurred a pension expense/(income) of $14,484,819 for the Plan (see Appendix B-2 for the complete breakdown of the pension expense).

Note that no adjustments have been made for contributions subsequent to the measurement date. Adequate treatment of any contributions made after the measurement date is the responsibility of the employer.

As of June 30, 2014, the CITY OF PALO ALTO has deferred outflows and deferred inflows of resources related to pensions as follows:

	Deferred Outflows of Resources	**Deferred Inflows of Resources**
Differences between Expected and Actual Experience	$ 0	$ 0
Changes of Assumptions	0	0
Net Difference between Projected and Actual Earnings on Pension Plan Investments	0	(32,413,414)
Total	**$ 0**	**$ (32,413,414)**

The amounts above are net of outflows and inflows recognized in the 2013-14 measurement period expense.

Amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in future pension expense as follows:

Measurement Period Ended June 30:	Deferred Outflows/(Inflows) of Resources
2015	$ (8,103,353)
2016	(8,103,353)
2017	(8,103,353)
2018	(8,103,355)
2019	0
Thereafter	0

Schedules of Required Supplementary Information

Schedule of Changes in Net Pension Liability and Related Ratios During the Measurement Period

Measurement Period		2013-14[1]
TOTAL PENSION LIABILITY		
Service Cost	$	12,441,595
Interest		46,963,318
Changes of Benefit Terms		0
Difference Between Expected and Actual Experience		0
Changes of Assumptions		0
Benefit Payments, Including Refunds of Employee Contributions		(31,780,533)
Net Change in Total Pension Liability		**27,624,380**
Total Pension Liability – Beginning		**635,847,037**
Total Pension Liability – Ending (a)	**$**	**663,471,417**
PLAN FIDUCIARY NET POSITION		
Contributions – Employer	$	17,399,732
Contributions – Employee		6,344,660
Net Investment Income[2]		70,988,848
Benefit Payments, Including Refunds of Employee Contributions		(31,780,533)
Other Changes in Fiduciary Net Position		0
Net Change in Fiduciary Net Position		**62,952,707**
Plan Fiduciary Net Position – Beginning		**413,410,472**
Plan Fiduciary Net Position – Ending (b)	**$**	**476,363,179**
Plan Net Pension Liability/(Asset) – Ending (a) - (b)	**$**	**187,108,238**
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability		**71.80%**
Covered-Employee Payroll	**$**	**66,372,870**
Plan Net Pension Liability/(Asset) as a Percentage of Covered-Employee Payroll		**281.90%**

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

[2] Net of administrative expenses. For details, see note in Appendix B-2.

Notes to Schedule:

Benefit Changes: The figures above do not include any liability impact that may have resulted from plan changes which occurred after June 30, 2013. This applies for voluntary benefit changes as well as any offers of Two Years Additional Service Credit (a.k.a. Golden Handshakes).

Changes of Assumptions: There were no changes in assumptions.

Schedule of Plan Contributions[1]

		Fiscal Year 2013-14
Actuarially Determined Contribution[2]	$	17,399,732
Contributions in Relation to the Actuarially Determined Contribution[2]		(17,399,732)
Contribution Deficiency (Excess)	$	0
Covered-Employee Payroll[3, 4]	$	66,372,870
Contributions as a Percentage of Covered-Employee Payroll[3]		26.22%

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

[2] Employers are assumed to make contributions equal to the actuarially determined contributions. However, some employers may choose to make additional contributions towards their unfunded liability. Employer contributions for such plans exceed the actuarially determined contributions.

[3] Covered-Employee Payroll represented above is based on pensionable earnings provided by the employer. However, GASB 68 defines covered-employee payroll as the total payroll of employees that are provided pensions through the pension plan. Accordingly, if pensionable earnings are different than total earnings for covered-employees, the employer should display in the disclosure footnotes the payroll based on total earnings for the covered group and recalculate the required payroll-related ratios.

[4] Payroll from prior year $64,439,680 was assumed to increase by the 3.00 percent payroll growth assumption.

Notes to Schedule:

The actuarial methods and assumptions used to set the actuarially determined contributions for Fiscal Year 2013-14 were from the June 30, 2011 public agency valuations.

Actuarial Cost Method	Entry Age Normal
Amortization Method/Period	For details, see June 30, 2011 Funding Valuation Report.
Asset Valuation Method	Actuarial Value of Assets. For details, see June 30, 2011 Funding Valuation Report.
Inflation	2.75%
Salary Increases	Varies by Entry Age and Service
Payroll Growth	3.00%
Investment Rate of Return	7.50% Net of Pension Plan Investment and Administrative Expenses; includes Inflation.
Retirement Age	The probabilities of Retirement are based on the 2010 CalPERS Experience Study for the period from 1997 to 2007.
Mortality	The probabilities of mortality are based on the 2010 CalPERS Experience Study for the period from 1997 to 2007. Pre-retirement and Post-retirement mortality rates include 5 years of projected mortality improvement using Scale AA published by the Society of Actuaries.

APPENDICES

- **APPENDIX A – DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES RELATED TO PENSIONS**
- **APPENDIX B – INTEREST, TOTAL PROJECTED EARNINGS AND PENSION EXPENSE/(INCOME)**

APPENDIX A

DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES RELATED TO PENSIONS

- **SCHEDULE OF DIFFERENCES BETWEEN EXPECTED AND ACTUAL EXPERIENCE**
- **DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES FOR DIFFERENCES BETWEEN EXPECTED AND ACTUAL EXPERIENCE**
- **SCHEDULE OF CHANGES OF ASSUMPTIONS**
- **DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES FOR CHANGES OF ASSUMPTIONS**
- **SCHEDULE OF DIFFERENCES BETWEEN PROJECTED AND ACTUAL EARNINGS ON PENSION PLAN INVESTMENTS**
- **DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES FOR DIFFERENCES BETWEEN PROJECTED AND ACTUAL EARNINGS ON PENSION PLAN INVESTMENTS**
- **SUMMARY OF RECOGNIZED DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES**

Schedule of differences between expected and actual experience

			Increase (Decrease) in Pension Expense Arising from the Recognition of the Effects of Differences between Expected and Actual Experience (Measurement Periods)						
Measurement Period	**Differences between Expected and Actual Experience**	**Recognition Period (Years)**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
2013-14	$0	3.1	$0	$0	$0	$0	$0	$0	$0
Net Increase (Decrease) in Pension Expense			$0	$0	$0	$0	$0	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from differences between expected and actual experience

				Balances at June 30, 2014	
Measurement Period	**Experience Losses (a)**	**Experience Gains (b)**	**Amounts Recognized in Pension Expense through June 30, 2014 (c)**	**Deferred Outflows of Resources (a) - (c)**	**Deferred Inflows of Resources (b) - (c)**
2013-14			$0		
				$0	$0

Schedule of changes of assumptions

			Increase (Decrease) in Pension Expense Arising from the Recognition of the Effects of Changes of Assumptions (Measurement Periods)						
Measurement Period	**Changes of Assumptions**	**Recognition Period (Years)**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
2013-14	$0	3.1	$0	$0	$0	$0	$0	$0	$0
Net Increase (Decrease) in Pension Expense			$0	$0	$0	$0	$0	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from changes of assumptions

Measurement Period	Increase in Total Pension Liability (a)	Decrease in Total Pension Liability (b)	Amounts Recognized in Pension Expense through June 30, 2014 (c)	Balances at June 30, 2014: Deferred Outflows of Resources (a) - (c)	Balances at June 30, 2014: Deferred Inflows of Resources (b) - (c)
2013-14			$0		
				$0	$0

Schedule of differences between projected and actual earnings on pension plan investments

			Increase (Decrease) in Pension Expense Arising from the Recognition of Differences between Projected and Actual Earnings on Pension Plan Investments (Measurement Periods)						
Measurement Period	**Differences between Projected and Actual Earnings on Pension Plan Investments**	**Recognition Period (Years)**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
2013-14	$(40,516,767)	5.0	$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,355)	$0	$0
Net Increase (Decrease) in Pension Expense			$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,355)	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from differences between projected and actual earnings on pension plan investments

				Balances at June 30, 2014	
Measurement Period	Investment Earnings less than Projected (a)	Investment Earnings greater than Projected (b)	Amounts Recognized in Pension Expense through June 30, 2014 (c)	Deferred Outflows of Resources (a) - (c)	Deferred Inflows of Resources (b) - (c)
2013-14		$(40,516,767)	$(8,103,353)		$(32,413,414)
				$0	$(32,413,414)

Summary of recognized deferred outflows of resources and deferred inflows of resources

	Net Increase (Decrease) in Pension Expense (Measurement Periods)						
	2013-14	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
Differences between Expected and Actual Experience	$0	$0	$0	$0	$0	$0	$0
Changes of Assumptions	0	0	0	0	0	0	0
Differences between Projected and Actual Earnings on Pension Plan Investments	(8,103,353)	(8,103,353)	(8,103,353)	(8,103,353)	(8,103,355)	0	0
Grand Total	$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,353)	$(8,103,355)	$0	$0

APPENDIX B

INTEREST, TOTAL PROJECTED EARNINGS AND PENSION EXPENSE/(INCOME)

- **INTEREST ON TOTAL PENSION LIABILITY AND TOTAL PROJECTED EARNINGS**
- **PENSION EXPENSE/(INCOME)**

Interest on Total Pension Liability and Total Projected Earnings

Interest on the Total Pension Liability	Amount for Period (a)	Portion of Period (b)	Interest Rate (c)	Interest on the Total Pension Liability (a) X (b) X (c)
Beginning Total Pension Liability	$ 635,847,037	100%	7.5%	$ 47,688,528
Service Cost	12,441,595	50%	7.5%	466,560
Benefit Payments, including Refunds of Employee Contributions	(31,780,533)	50%	7.5%	(1,191,770)
Total Interest on the Total Pension Liability				**$ 46,963,318**

Projected Earnings on Pension Plan Investments	Amount for Period (a)	Portion of Period (b)	Projected Rate of Return (c)	Projected Earnings (a) X (b) X (c)
Beginning Plan Fiduciary Net Position excluding Receivables[1]	$ 410,312,475	100%	7.5%	$ 30,773,436
Employer Contributions	17,399,732	50%	7.5%	652,490
Employee Contributions	6,344,660	50%	7.5%	237,925
Benefit Payments, including Refunds of Employee Contributions	(31,780,533)	50%	7.5%	(1,191,770)
Total Projected Earnings				**$ 30,472,081**

[1] Contributions receivable for employee service buybacks, totaling $3,097,997 as of June 30, 2013, are excluded for purposes of calculating projected earnings on pension plan investments.

Pension Expense/(Income) for Measurement Period Ended June 30, 2014

Description		Amount
Service Cost	$	12,441,595
Interest on the Total Pension Liability		46,963,318
Changes of Benefit Terms		0
Recognized Differences between Expected and Actual Experience		0
Recognized Changes of Assumptions		0
Employee Contributions		(6,344,660)
Projected Earnings on Pension Plan Investments		(30,472,081)
Recognized Differences between Projected and Actual Earnings on Plan Investments		(8,103,353)
Other Changes in Fiduciary Net Position		0
Total Pension Expense/(Income)	**$**	**14,484,819**

Note: Plan administrative expenses are not displayed in the above pension expense table. Since the expected investment return of 7.50 percent is net of administrative expenses, administrative expenses are excluded from the above table, but implicitly included as part of investment earnings.

GASB 68 ACCOUNTING VALUATION REPORT

(CalPERS ID: 6373437857)
Rate Plan Identifier: 5080

Prepared for the
CITY OF PALO ALTO
SAFETY PLAN,
an Agent Multiple-Employer Defined Benefit Pension Plan

Measurement Date of June 30, 2014

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ACTUARIAL CERTIFICATION

This report provides disclosure and reporting information as required under Governmental Accounting Standards Board Statement 68 (GASB 68) for the SAFETY PLAN of the CITY OF PALO ALTO (the "Plan"), an Agent Multiple-Employer Defined Benefit Pension Plan participating in the California Public Employees' Retirement System (CalPERS), for the measurement period ended June 30, 2014. This information should be used for the fiscal year beginning after June 15, 2014 but ending on or before June 30, 2015.

Determinations for purposes other than financial accounting requirements may be significantly different from the results in this report. Thus, the use of this report for purposes other than those expressed here may not be appropriate.

This accounting valuation report relies on liabilities and related validation work performed by the CalPERS Actuarial Office as part of the June 30, 2013 annual funding valuation for the Plan. The census data and benefit provisions underlying the liabilities were prepared as of June 30, 2013 and certified as part of the annual funding valuation by the CalPERS Actuarial Office. The June 30, 2013 liabilities used for this accounting valuation are based on the actuarial assumptions recommended by the CalPERS Chief Actuary and adopted by the CalPERS Board in February 2014 as laid out in the 2014 report titled "CalPERS Experience Study and Review of Actuarial Assumptions." These liabilities were validated as part of the June 30, 2013 funding valuation that included the estimated impact of the change in actuarial assumptions on contribution requirements. The undersigned is relying upon these prescribed assumptions and methods and is not able to render an opinion on their reasonability, as this would require a substantial amount of additional work beyond the scope of this report. This report also relies on asset information for the measurement period as supplied by the CalPERS Financial Office. The fiduciary net position as of June 30, 2014, and the changes in net position for the year then ended were audited by CalPERS' independent auditors, Macias Gini & O'Connell LLP, as part of the audit of the Schedule of Changes in Fiduciary Net Position by Employer Rate Plan of CalPERS Agent Multiple-Employer Pension Plan.

With the provided liability and asset information, the total pension liability, net pension liability and pension expense were developed for the measurement period using standard actuarial techniques. In addition, the results are based on CalPERS' understanding of the financial accounting and reporting requirements under U.S. Generally Accepted Accounting Principles as set forth in GASB 68. The information in this report is not intended to supersede the advice and interpretations of the employer's auditor. This report may not provide all the information necessary to complete the required disclosures under GASB 68. The employer should supplement and update the information in this report with its own financial data as necessary to complete the disclosure information required by GASB 68.

The undersigned is familiar with the near-term and long-term aspects of pension valuations and meets the Qualification Standards of the American Academy of Actuaries necessary to render the actuarial opinions contained herein. The information provided in this report is dependent upon various factors as documented throughout this report, which may be subject to change. Each section of this report is considered to be an integral part of the actuarial opinions.

David Clement

DAVID CLEMENT, ASA, MAAA, EA
Senior Pension Actuary, CalPERS

Introduction

This is the GASB 68 Accounting Valuation Report to be used for your fiscal year beginning after June 15, 2014 and ending on or before June 30, 2015 for your SAFETY PLAN (Plan). GASB Statement No. 68 replaced the requirements of GASB 27 effective for fiscal years beginning after June 15, 2014.

Statement 68 was issued by GASB in June 2012, requiring public employers to comply with new accounting and financial reporting standards. Statement 68 outlines a different approach to the recognition and calculation of pension obligations. Under the new GASB standards, employers that participate in a defined benefit pension plan administered as a trust or equivalent arrangement are required to record the net pension liability, pension expense, and deferred outflows/deferred inflows of resources related to pensions in their financial statements as part of their financial position.

Net pension liability is the plan's total pension liability based on entry age normal actuarial cost method less the plan's fiduciary net position. This may be a negative liability (net pension asset).

Pension expense is the change in net pension liability from the previous fiscal year to the current fiscal year less adjustments. This may be a negative expense (pension income).

Deferred outflows and deferred inflows of resources related to pensions are certain changes in total pension liability and fiduciary net position that are to be recognized in future pension expense.

This report may not provide all the information necessary to complete the required disclosures under GASB 68. **The employer should supplement and update the information in this report with its own financial data as necessary to complete the disclosure information required by GASB 68.** For example, no adjustments have been made for contributions subsequent to the measurement date. Appropriate accounting treatment of any contributions made after the measurement date is the responsibility of the employer. CalPERS recommends that the employer consult with its auditor regarding any such adjustments.

Purpose of the Report

The Plan participates in the CalPERS agent multiple-employer defined benefit pension plan. This GASB 68 report provides accounting and financial reporting for pensions, to be used in the employer's financial reports. The pension expense is for the measurement period of 2013-14 and the net pension liability is measured as of June 30, 2014. Liabilities are based on the results of the actuarial calculations performed as of June 30, 2013 and were rolled forward to June 30, 2014. Fiduciary net position is based on fair value of investments as of June 30, 2014. Since GASB 68 allows a measurement date of up to 12 months before the employer's fiscal year-end, this report can be used for fiscal years beginning after June 15, 2014 and ending on or before June 30, 2015.

The following pension information is disclosed in this report:

- Summary of Significant Accounting Policies
- General Information about the Pension Plan
    - Plan Description, Benefits Provided and Employees Covered
    - Contribution Description
    - Actuarial Methods and Assumptions
    - Discount Rate
    - Pension Plan Fiduciary Net Position
- Changes in the Net Pension Liability
    - Sensitivity of the Net Pension Liability
    - Subsequent Events
    - Recognition of Gains and Losses
- Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions
- Schedules of Required Supplementary Information (10-Year History[1]):
    - Schedule of Changes in Net Pension Liability and Related Ratios
    - Schedule of Plan Contributions

The use of this report for other purposes may be inappropriate.

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

Summary of Significant Accounting Policies

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Plan and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the CalPERS Financial Office. For this purpose, benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

GASB 68 requires that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used.

Valuation Date (VD)	June 30, 2013
Measurement Date (MD)	June 30, 2014
Measurement Period (MP)	July 1, 2013 to June 30, 2014

General Information about the Pension Plan

Plan Description, Benefits Provided and Employees Covered

The Plan is an agent multiple-employer defined benefit pension plan administered by the California Public Employees' Retirement System (CalPERS). A full description of the pension plan regarding number of employees covered, benefit provisions, assumptions (for funding, but not accounting purposes), and membership information are listed in the June 30, 2013 Annual Actuarial Valuation Report. Details of the benefits provided can be obtained in Appendix B of the actuarial valuation report. This report and CalPERS' audited financial statements are publicly available reports that can be obtained at CalPERS' website under Forms and Publications.

Contribution Description

Section 20814(c) of the California Public Employees' Retirement Law (PERL) requires that the employer contribution rates for all public employers be determined on an annual basis by the actuary and shall be effective on the July 1 following notice of a change in the rate. The total plan contributions are determined through CalPERS' annual actuarial valuation process. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The employer is required to contribute the difference between the actuarially determined rate and the contribution rate of employees. For the measurement period ended June 30, 2014 (the measurement date), the average active employee contribution rate is 9.029 percent of annual pay, and the employer's contribution rate is 34.716 percent of annual payroll. Employer contribution rates may change if plan contracts are amended. It is the responsibility of the employer to make necessary accounting adjustments to reflect the impact due to any Employer Paid Member Contributions or situations where members are paying a portion of the employer contribution.

Actuarial Methods and Assumptions Used to Determine Total Pension Liability

For the measurement period ended June 30, 2014 (the measurement date), the total pension liability was determined by rolling forward the June 30, 2013 total pension liability. The June 30, 2013 and the June 30, 2014 total pension liabilities were based on the following actuarial methods and assumptions:

Actuarial Cost Method	Entry Age Normal in accordance with the requirements of GASB Statement No. 68
Actuarial Assumptions	
Discount Rate	7.50%
Inflation	2.75%
Salary Increases	Varies by Entry Age and Service
Investment Rate of Return	7.50% Net of Pension Plan Investment and Administrative Expenses; includes Inflation
Mortality Rate Table[1]	Derived using CalPERS' Membership Data for all Funds
Post Retirement Benefit Increase	Contract COLA up to 2.75% until Purchasing Power Protection Allowance Floor on Purchasing Power applies, 2.75% thereafter

[1] The mortality table used was developed based on CalPERS' specific data. The table includes 20 years of mortality improvements using Society of Actuaries Scale BB. For more details on this table, please refer to the 2014 experience study report.

All other actuarial assumptions used in the June 30, 2013 valuation were based on the results of an actuarial experience study for the period from 1997 to 2011, including updates to salary increase, mortality and retirement rates. The Experience Study report can be obtained at CalPERS' website under Forms and Publications.

Discount Rate

The discount rate used to measure the total pension liability was 7.50 percent. To determine whether the municipal bond rate should be used in the calculation of a discount rate for each plan, CalPERS stress tested plans that would most likely result in a discount rate that would be different from the actuarially assumed discount rate. Based on the testing, none of the tested plans run out of assets. Therefore, the current 7.50 percent discount rate is adequate and the use of the municipal bond rate calculation is not necessary. The long-term expected discount rate of 7.50 percent is applied to all plans in the Public Employees Retirement Fund. The stress test results are presented in a detailed report called "GASB Crossover Testing Report" that can be obtained at CalPERS' website under the GASB 68 section.

According to Paragraph 30 of Statement 68, the long-term discount rate should be determined without reduction for pension plan administrative expense. The 7.50 percent investment return assumption used in this accounting valuation is net of administrative expenses. Administrative expenses are assumed to be 15 basis points. An investment return excluding administrative expenses would have been 7.65 percent. Using this lower discount rate has resulted in a slightly higher total pension liability and net pension liability. This difference was deemed immaterial to the agent multiple-employer plan. However, employers may determine the impact at the rate plan level for their own financial reporting purposes. Refer to page 8 of this report, which provides information on the sensitivity of the net pension liability to changes in the discount rate.

CalPERS is scheduled to review all actuarial assumptions as part of its regular Asset Liability Management review cycle that is scheduled to be completed in February 2018. Any changes to the discount rate will require Board action and proper stakeholder outreach. For these reasons, CalPERS expects to continue using a discount rate net of administrative expenses for GASB 67 and 68 calculations through at least the 2017-18 fiscal year. CalPERS will continue to check the materiality of the difference in calculation until such time as we have changed our methodology.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class.

In determining the long-term expected rate of return, staff took into account both short-term and long-term market return expectations as well as the expected pension fund cash flows. Such cash flows were developed assuming that both members and employers will make their required contributions on time and as scheduled in all future years. Using historical returns of all the funds' asset classes, expected compound (geometric) returns were calculated over the short-term (first 10 years) and the long-term (11-60 years) using a building-block approach. Using the expected nominal returns for both short-term and long-term, the present value of benefits was calculated for each fund. The expected rate of return was set by calculating the single equivalent expected return that arrived at the same present value of benefits for cash flows as the one calculated using both short-term and long-term returns. The expected rate of return was then set equivalent to the single equivalent rate calculated above and rounded down to the nearest one quarter of one percent.

The table below reflects long-term expected real rate of return by asset class. The rate of return was calculated using the capital market assumptions applied to determine the discount rate and asset allocation. These geometric rates of return are net of administrative expenses.

Asset Class	New Strategic Allocation	Real Return Years 1 - 10[1]	Real Return Years 11+[2]
Global Equity	47.0%	5.25%	5.71%
Global Fixed Income	19.0	0.99	2.43
Inflation Sensitive	6.0	0.45	3.36
Private Equity	12.0	6.83	6.95
Real Estate	11.0	4.50	5.13
Infrastructure and Forestland	3.0	4.50	5.09
Liquidity	2.0	(0.55)	(1.05)

[1]An expected inflation of 2.5% used for this period
[2]An expected inflation of 3.0% used for this period

Pension Plan Fiduciary Net Position

The plan fiduciary net position disclosed in your GASB 68 accounting valuation report may differ from the plan assets reported in your funding actuarial valuation report due to several reasons. First, for the accounting valuations, CalPERS must keep items such as deficiency reserves, fiduciary self-insurance and OPEB expense included as assets. These amounts are excluded for rate setting purposes in your funding actuarial valuation. In addition, differences may result from early Comprehensive Annual Financial Report closing and final reconciled reserves.

Changes in the Net Pension Liability

The following table shows the changes in net pension liability recognized over the measurement period.

	Increase (Decrease)		
	Total Pension Liability (a)	**Plan Fiduciary Net Position (b)**	**Net Pension Liability/(Asset) (c) = (a) - (b)**
Balance at: 6/30/2013 (VD)[1]	**$ 355,054,289**	**$ 234,152,906**	**$ 120,901,383**
Changes Recognized for the Measurement Period:			
• Service Cost	6,221,042		6,221,042
• Interest on the Total Pension Liability	26,112,921		26,112,921
• Changes of Benefit Terms	0		0
• Differences between Expected and Actual Experience	0		0
• Changes of Assumptions	0		0
• Contributions from the Employer		7,615,779	(7,615,779)
• Contributions from Employees		2,762,215	(2,762,215)
• Net Investment Income[2]		40,033,488	(40,033,488)
• Benefit Payments, including Refunds of Employee Contributions	(19,985,106)	(19,985,106)	0
Net Changes during 2013-14	**$ 12,348,857**	**$ 30,426,376**	**$ (18,077,519)**
Balance at: 6/30/2014 (MD)[1]	**$ 367,403,146**	**$ 264,579,282**	**$ 102,823,864**

[1] The fiduciary net position includes receivables for employee service buybacks, deficiency reserves, fiduciary self-insurance and OPEB expense. As described on Page 6, this may differ from the plan assets reported in the funding actuarial valuation report.

[2] Net of administrative expenses. For details, see note in Appendix B-2.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the Plan as of the measurement date, calculated using the discount rate of 7.50 percent, as well as what the net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower (6.50 percent) or 1 percentage-point higher (8.50 percent) than the current rate:

	Discount Rate - 1% (6.50%)	Current Discount Rate (7.50%)	Discount Rate + 1% (8.50%)
Plan's Net Pension Liability/(Asset)	$ 148,419,847	$ 102,823,864	$ 64,946,625

Subsequent Events

There were no subsequent events that would materially affect the results presented in this disclosure.

Recognition of Gains and Losses

Under GASB 68, gains and losses related to changes in total pension liability and fiduciary net position are recognized in pension expense systematically over time.

The first amortized amounts are recognized in pension expense for the year the gain or loss occurs. The remaining amounts are categorized as deferred outflows and deferred inflows of resources related to pensions and are to be recognized in future pension expense.

The amortization period differs depending on the source of the gain or loss:

Difference between projected and actual earnings	5 year straight-line amortization
All other amounts	Straight-line amortization over the average expected remaining service lives of all members that are provided with benefits (active, inactive, and retired) as of the beginning of the measurement period

The expected average remaining service lifetime (EARSL) is calculated by dividing the total future service years by the total number of plan participants (active, inactive, and retired).

The EARSL for the Plan for the 2013-14 measurement period is 3.3 years, which was obtained by dividing the total service years of 2,232 (the sum of remaining service lifetimes of the active employees) by 676 (the total number of participants: active, inactive, and retired). Note that inactive employees and retirees have remaining service lifetimes equal to 0. Also note that total future service is based on the members' probability of decrementing due to an event other than receiving a cash refund.

Pension Expense and Deferred Outflows and Deferred Inflows of Resources Related to Pensions

Paragraph 137 of GASB 68 and Questions 267 and 268 of the GASB 68 Implementation Guide set forth guidance on implementing the standard. The employer should use this guidance for the adjusting entries concerning the net pension obligation and the initial net pension liability/(asset). As of the start of the measurement period (July 1, 2013), the net pension liability/(asset) is $120,901,383.

For the measurement period ending June 30, 2014 (the measurement date), the CITY OF PALO ALTO incurred a pension expense/(income) of $7,861,040 for the Plan (see Appendix B-2 for the complete breakdown of the pension expense).

Note that no adjustments have been made for contributions subsequent to the measurement date. Adequate treatment of any contributions made after the measurement date is the responsibility of the employer.

As of June 30, 2014, the CITY OF PALO ALTO has deferred outflows and deferred inflows of resources related to pensions as follows:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between Expected and Actual Experience	$ 0	$ 0
Changes of Assumptions	0	0
Net Difference between Projected and Actual Earnings on Pension Plan Investments	0	(18,322,780)
Total	**$ 0**	**$ (18,322,780)**

The amounts above are net of outflows and inflows recognized in the 2013-14 measurement period expense.

Amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in future pension expense as follows:

Measurement Period Ended June 30:	**Deferred Outflows/(Inflows) of Resources**
2015	$ (4,580,695)
2016	(4,580,695)
2017	(4,580,695)
2018	(4,580,695)
2019	0
Thereafter	0

Schedules of Required Supplementary Information

Schedule of Changes in Net Pension Liability and Related Ratios During the Measurement Period

Measurement Period		2013-14[1]
TOTAL PENSION LIABILITY		
Service Cost	$	6,221,042
Interest		26,112,921
Changes of Benefit Terms		0
Difference Between Expected and Actual Experience		0
Changes of Assumptions		0
Benefit Payments, Including Refunds of Employee Contributions		(19,985,106)
Net Change in Total Pension Liability		**12,348,857**
Total Pension Liability – Beginning		**355,054,289**
Total Pension Liability – Ending (a)	**$**	**367,403,146**
PLAN FIDUCIARY NET POSITION		
Contributions – Employer	$	7,615,779
Contributions – Employee		2,762,215
Net Investment Income[2]		40,033,488
Benefit Payments, Including Refunds of Employee Contributions		(19,985,106)
Other Changes in Fiduciary Net Position		0
Net Change in Fiduciary Net Position		**30,426,376**
Plan Fiduciary Net Position – Beginning		**234,152,906**
Plan Fiduciary Net Position – Ending (b)	**$**	**264,579,282**
Plan Net Pension Liability/(Asset) – Ending (a) - (b)	**$**	**102,823,864**
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability		**72.01%**
Covered-Employee Payroll	**$**	**21,895,824**
Plan Net Pension Liability/(Asset) as a Percentage of Covered-Employee Payroll		**469.60%**

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

[2] Net of administrative expenses. For details, see note in Appendix B-2.

Notes to Schedule:

Benefit Changes: The figures above do not include any liability impact that may have resulted from plan changes which occurred after June 30, 2013. This applies for voluntary benefit changes as well as any offers of Two Years Additional Service Credit (a.k.a. Golden Handshakes).

Changes of Assumptions: There were no changes in assumptions.

Schedule of Plan Contributions[1]

		Fiscal Year 2013-14
Actuarially Determined Contribution[2]	$	7,615,779
Contributions in Relation to the Actuarially Determined Contribution[2]		(7,615,779)
Contribution Deficiency (Excess)	$	0
Covered-Employee Payroll[3, 4]	$	21,895,824
Contributions as a Percentage of Covered-Employee Payroll[3]		34.78%

[1] Historical information is required only for measurement periods for which GASB 68 is applicable.

[2] Employers are assumed to make contributions equal to the actuarially determined contributions. However, some employers may choose to make additional contributions towards their unfunded liability. Employer contributions for such plans exceed the actuarially determined contributions.

[3] Covered-Employee Payroll represented above is based on pensionable earnings provided by the employer. However, GASB 68 defines covered-employee payroll as the total payroll of employees that are provided pensions through the pension plan. Accordingly, if pensionable earnings are different than total earnings for covered-employees, the employer should display in the disclosure footnotes the payroll based on total earnings for the covered group and recalculate the required payroll-related ratios.

[4] Payroll from prior year $21,258,082 was assumed to increase by the 3.00 percent payroll growth assumption.

Notes to Schedule:

The actuarial methods and assumptions used to set the actuarially determined contributions for Fiscal Year 2013-14 were from the June 30, 2011 public agency valuations.

Actuarial Cost Method	Entry Age Normal
Amortization Method/Period	For details, see June 30, 2011 Funding Valuation Report.
Asset Valuation Method	Actuarial Value of Assets. For details, see June 30, 2011 Funding Valuation Report.
Inflation	2.75%
Salary Increases	Varies by Entry Age and Service
Payroll Growth	3.00%
Investment Rate of Return	7.50% Net of Pension Plan Investment and Administrative Expenses; includes Inflation.
Retirement Age	The probabilities of Retirement are based on the 2010 CalPERS Experience Study for the period from 1997 to 2007.
Mortality	The probabilities of mortality are based on the 2010 CalPERS Experience Study for the period from 1997 to 2007. Pre-retirement and Post-retirement mortality rates include 5 years of projected mortality improvement using Scale AA published by the Society of Actuaries.

APPENDICES

- **APPENDIX A – DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES RELATED TO PENSIONS**
- **APPENDIX B – INTEREST, TOTAL PROJECTED EARNINGS AND PENSION EXPENSE/(INCOME)**

APPENDIX A

DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES RELATED TO PENSIONS

- **SCHEDULE OF DIFFERENCES BETWEEN EXPECTED AND ACTUAL EXPERIENCE**
- **DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES FOR DIFFERENCES BETWEEN EXPECTED AND ACTUAL EXPERIENCE**
- **SCHEDULE OF CHANGES OF ASSUMPTIONS**
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- **SCHEDULE OF DIFFERENCES BETWEEN PROJECTED AND ACTUAL EARNINGS ON PENSION PLAN INVESTMENTS**
- **DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES FOR DIFFERENCES BETWEEN PROJECTED AND ACTUAL EARNINGS ON PENSION PLAN INVESTMENTS**
- **SUMMARY OF RECOGNIZED DEFERRED OUTFLOWS OF RESOURCES AND DEFERRED INFLOWS OF RESOURCES**

Schedule of differences between expected and actual experience

Measurement Period	Differences between Expected and Actual Experience	Recognition Period (Years)	Increase (Decrease) in Pension Expense Arising from the Recognition of the Effects of Differences between Expected and Actual Experience (Measurement Periods)						
			2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	Thereafter
2013-14	$0	3.3	$0	$0	$0	$0	$0	$0	$0
Net Increase (Decrease) in Pension Expense			$0	$0	$0	$0	$0	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from differences between expected and actual experience

				Balances at June 30, 2014	
Measurement Period	Experience Losses (a)	Experience Gains (b)	Amounts Recognized in Pension Expense through June 30, 2014 (c)	Deferred Outflows of Resources (a) - (c)	Deferred Inflows of Resources (b) - (c)
2013-14			$0		
				$0	$0

Schedule of changes of assumptions

			Increase (Decrease) in Pension Expense Arising from the Recognition of the Effects of Changes of Assumptions (Measurement Periods)						
Measurement Period	**Changes of Assumptions**	**Recognition Period (Years)**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
2013-14	$0	3.3	$0	$0	$0	$0	$0	$0	$0
Net Increase (Decrease) in Pension Expense			$0	$0	$0	$0	$0	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from changes of assumptions

				Balances at June 30, 2014	
Measurement Period	**Increase in Total Pension Liability (a)**	**Decrease in Total Pension Liability (b)**	**Amounts Recognized in Pension Expense through June 30, 2014 (c)**	**Deferred Outflows of Resources (a) - (c)**	**Deferred Inflows of Resources (b) - (c)**
2013-14			$0		
				$0	$0

Schedule of differences between projected and actual earnings on pension plan investments

			Increase (Decrease) in Pension Expense Arising from the Recognition of Differences between Projected and Actual Earnings on Pension Plan Investments (Measurement Periods)						
Measurement Period	**Differences between Projected and Actual Earnings on Pension Plan Investments**	**Recognition Period (Years)**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
2013-14	$(22,903,475)	5.0	$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$0	$0
Net Increase (Decrease) in Pension Expense			$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$0	$0

Deferred outflows of resources and deferred inflows of resources arising from differences between projected and actual earnings on pension plan investments

				Balances at June 30, 2014	
Measurement Period	Investment Earnings less than Projected (a)	Investment Earnings greater than Projected (b)	Amounts Recognized in Pension Expense through June 30, 2014 (c)	Deferred Outflows of Resources (a) - (c)	Deferred Inflows of Resources (b) - (c)
2013-14		$(22,903,475)	$(4,580,695)		$(18,322,780)
				$0	$(18,322,780)

Summary of recognized deferred outflows of resources and deferred inflows of resources

	Net Increase (Decrease) in Pension Expense (Measurement Periods)						
	2013-14	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**Thereafter**
Differences between Expected and Actual Experience	$0	$0	$0	$0	$0	$0	$0
Changes of Assumptions	0	0	0	0	0	0	0
Differences between Projected and Actual Earnings on Pension Plan Investments	(4,580,695)	(4,580,695)	(4,580,695)	(4,580,695)	(4,580,695)	0	0
Grand Total	$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$(4,580,695)	$0	$0

APPENDIX B

INTEREST, TOTAL PROJECTED EARNINGS AND PENSION EXPENSE/(INCOME)

- **INTEREST ON TOTAL PENSION LIABILITY AND TOTAL PROJECTED EARNINGS**
- **PENSION EXPENSE/(INCOME)**

Interest on Total Pension Liability and Total Projected Earnings

Interest on the Total Pension Liability	Amount for Period (a)	Portion of Period (b)	Interest Rate (c)	Interest on the Total Pension Liability (a) X (b) X (c)
Beginning Total Pension Liability	$ 355,054,289	100%	7.5%	$ 26,629,072
Service Cost	6,221,042	50%	7.5%	233,290
Benefit Payments, including Refunds of Employee Contributions	(19,985,106)	50%	7.5%	(749,441)
Total Interest on the Total Pension Liability				**$ 26,112,921**

Projected Earnings on Pension Plan Investments	Amount for Period (a)	Portion of Period (b)	Projected Rate of Return (c)	Projected Earnings (a) X (b) X (c)
Beginning Plan Fiduciary Net Position excluding Receivables[1]	$ 233,203,719	100%	7.5%	$ 17,490,279
Employer Contributions	7,615,779	50%	7.5%	285,592
Employee Contributions	2,762,215	50%	7.5%	103,583
Benefit Payments, including Refunds of Employee Contributions	(19,985,106)	50%	7.5%	(749,441)
Total Projected Earnings				**$ 17,130,013**

[1] Contributions receivable for employee service buybacks, totaling $949,187 as of June 30, 2013, are excluded for purposes of calculating projected earnings on pension plan investments.

Pension Expense/(Income) for Measurement Period Ended June 30, 2014

Description		Amount
Service Cost	$	6,221,042
Interest on the Total Pension Liability		26,112,921
Changes of Benefit Terms		0
Recognized Differences between Expected and Actual Experience		0
Recognized Changes of Assumptions		0
Employee Contributions		(2,762,215)
Projected Earnings on Pension Plan Investments		(17,130,013)
Recognized Differences between Projected and Actual Earnings on Plan Investments		(4,580,695)
Other Changes in Fiduciary Net Position		0
Total Pension Expense/(Income)	**$**	**7,861,040**

Note: Plan administrative expenses are not displayed in the above pension expense table. Since the expected investment return of 7.50 percent is net of administrative expenses, administrative expenses are excluded from the above table, but implicitly included as part of investment earnings.