



Regular Meeting

Item number 15b – Open session

Subject: Actuarial Valuation of the Defined Benefit Supplement Program and Consideration for the Adoption of an Additional Earnings Credit

Presenter(s): David Lamoureux, CalSTRS; Nick Collier and Scott Preppernau, Milliman

Item type: Action

Date and time: May 28, 2026– 10 minutes

Attachment(s):

Attachment 1 – June 30, 2025 Actuarial Valuation for the Defined Benefit Supplement Program

Attachment 2 – Proposed Resolution for the Adoption of an Additional Earnings Credit

PowerPoint presentation(s):

Summary of Valuation Results for the Defined Benefit Supplement Program

Item purpose

The purpose of this item is to present the results of the June 30, 2025 actuarial valuation of the Defined Benefit Supplement Program and to consider the adoption of an additional earnings credit of 4.53%.

Recommendation

Staff recommends that an additional earnings credit of 4.53% of the June 30, 2025 account balance be awarded to members of the Defined Benefit Supplement Program who were not retired as of June 30, 2025. Considering that the accounts for the members of the Defined Benefit Supplement Program have already been credited with a minimum interest rate of 4.61% for fiscal year 2024-25, granting the recommended additional earnings credit of 4.53% would result in a total return of 9.14% for the 2024-25 fiscal year.

Executive Summary

The attached report is the annual actuarial valuation of the Defined Benefit Supplement Program required as per Section 22311.5 of the Education Code. The actuarial valuation provides a snapshot of the funds assets and liabilities as of June 30, 2025.

Funded Ratio

The funded ratio of a pension plan is the ratio of a plan’s assets to its actuarial obligation. The following table compares key information about the funded ratio of the Defined Benefit Supplement Program between June 30, 2025 and June 30, 2024 actuarial valuations.

Summary of key results for Defined Benefit Supplement Program

	June 30, 2025 Valuation	June 30, 2024 Valuation
Actuarial obligation	\$16.07 billion	\$15.03 billion
Actuarial value of assets	\$20.82 billion	\$19.38 billion
Unfunded actuarial obligation / (Actuarial surplus)	(\$4.75 billion)	(\$4.35 billion)
Proposed additional earnings credit (estimated dollar value / percent of account balance awarded)	\$0.61 billion ¹ / 4.53%	\$0.61 billion ² / 4.81%
Final unfunded actuarial obligation / (Actuarial surplus)	(\$4.14 billion)	(\$3.74 billion)
Funded ratio		
- Before additional earnings credit	129.6%	129.0%
- After additional earnings credit	124.8%	123.9%

The funded status and the actuarial surplus have both increased since the 2024 valuation. Note that the final funded status and actuarial surplus from the 2024 valuation are those which reflect the additional earnings credit awarded by the board in May 2025. As shown above, the funded status increased by 5.7% from 123.9% on June 30, 2024 (after the additional earnings credit) to 129.6% on June 30, 2025 (before the additional earnings credit). The actuarial surplus increased by about \$1.01 billion, from a \$3.74 billion surplus on June 30, 2024 (after the additional earnings credit) to a \$4.75 billion surplus on June 30, 2025 (before the additional earnings credit).

These increases were primarily the result of the investment return for fiscal year 2024-25, which was greater than both the assumed investment return of 7.0% and the minimum interest rate credited to the member’s account of 4.61%. As shown on page 1 of the attached report, the investment return for the Defined Benefit Supplement Program was calculated to be 9.2% for

¹ Subject to approval by the board at the May 2026 meeting.

² Approved by the board in May 2025.

fiscal year 2024-25. For additional details on the changes in the surplus, please refer to Table 4, *Actuarial Gains and Losses*, on page 12 of the attached report.

The funded status for the Defined Benefit Supplement Program is based on the market value of assets. This differs from the Defined Benefit Program which uses an actuarial value of assets which smooths the volatility in the investment markets by reflecting only one-third of the net accumulated investment gains and losses in a year. For the Defined Benefit Supplement Program the volatility of the investment market is managed by establishing a gain and loss reserve, which, if positive, includes investment earnings in excess of the amount needed to fund the program liabilities and, if negative, reflect an unfunded actuarial obligation of the program. If, in any year, investment earnings are less than necessary, any positive balance in the gain and loss reserve is used to fund the minimum interest rate. If the balance in the gain and loss reserve is sufficient to properly protect the program against investment losses, any remaining actuarial surplus can be used to fund an additional earnings credit.

Additional Earnings Credit

Section 25006 of the Education Code allows the board to declare an additional earnings credit for members of the Defined Benefit Supplement Program. The board adopted a policy on granting additional earnings credits with the purpose of providing Defined Benefit Supplement members earnings on their accounts equal to the assumed rate of return, currently 7%, over the long term. The board's policy is designed to balance the need to ensure the long-term sustainability of the program with the goal of providing robust returns to members. The board policy states that additional earnings credits may be awarded if the funded ratio of the program surpasses certain thresholds. The thresholds are determined using a two-step allocation process.

1. The first step in the process allocates the excess of the actuarial surplus over the standard deviation of the expected long-term rate of return on the investment portfolio, limited to the difference between the minimum interest rate from the previous valuation and the long-term assumed rate of earnings.
2. The second step in the process allocates 50% of the remaining actuarial surplus over two times the standard deviation of the expected long-term rate of return on the investment portfolio.

The additional earnings credit awarded would be the sum of the allocation from the two steps.

The standard deviation for the Defined Benefit Supplement Program was set at 11.3% when the board adopted the most recent experience study in January 2024. This means that the board is asked to consider an additional earnings credit only when the program has a funded status greater than 111.3%. For the second threshold, the funded ratio would have to exceed 122.6% following the first threshold allocation.

As of June 30, 2025, the Defined Benefit Supplement Program had a funded ratio of 129.6%, which exceeds the first threshold. After the first allocation, the funded status is 127.0% which

exceeds the second threshold. Based on board policy, an additional earnings credit of 4.53% has been calculated as the sum of 2.39% under the first allocation step and 2.14% under the second allocation step. Awarding a 4.53% additional earnings credit will reduce the funded status of the program from 129.6% down to 124.8% and reduce the actuarial surplus by \$614 million, from \$4.75 billion down to about \$4.14 billion. For more details on the calculation of the recommended additional earnings credit refer to Table 6, *Additional Earnings Credit Based on Board Policy*, on page 14 of the attached report.

As shown on page 2 of the attached report, granting the recommended additional earnings credit of 4.53% would be the 8th time in the last 10 years that an additional earnings credit is granted to the members of the Defined Benefit Supplement Program.

Considering that the accounts for the members of the Defined Benefit Supplement Program have already been credited with a minimum interest rate of 4.61% for fiscal year 2024-25, granting the recommended additional earnings credit of 4.53% would result in a total return of 9.1% credited to members' accounts for fiscal year 2024-25. The table below shows the average compounded return credited to members' accounts over the last five, 10 and 20 years for the Defined Benefit Supplement Program, reflecting all previously granted additional earnings credit and the 4.53% under consideration in this item.

Average compounded return credited to members' accounts

Last 5 years	Last 10 years	Last 20 years
9.6%	7.5%	6.8%

If awarded, the additional earnings credit of 4.53% will be applied to the June 30, 2025, account balance for members who were not retired as of June 30, 2025.

Strategic Plan linkage: Goal 1: Trusted stewards – Ensure a well-governed, financially sound trust fund.

Board Policy linkage: Board Governance Manual: Section 7G – Benefits and Services Policy – Actuarial Valuations of the Defined Benefit Supplement Program and the Cash Balance Benefit Program.
