INTEREST CREDITING POLICY

I. PURPOSE

The purpose of this policy is to establish the process used to credit semi-annual interest to reserves. This policy defines the reserves maintained by Mendocino County Employees Retirement Association (MCERA) and determines the priorities and sequence by which interest will be credited to the reserves.

II. POLICY OBJECTIVES

The objective of this policy is to provide reasonable and prudent allocation of earnings.

III. DEFINITIONS

Actuarially Assumed Investment Rate of Return: The expected investment earnings rate of return used in the annual actuarial valuation of the Plan, recommended to the MCERA Board by the Plan's third-party actuary in an experience study and set by the MCERA Board.

Actuarial Value of Assets: The Market Value of Assets less deferred investment gains or losses as calculated under the Plan's five-year actuarial asset smoothing method. If necessary, the Actuarial Value of Assets is adjusted to be within 75% - 125% of the Market Value of Assets.

Available Earnings: Represent the actual earnings of the Plan as determined based on the smoothed Actuarial Value of Assets.

Valuation Reserves: Include the Employee Reserve, Employer Reserve, Retiree Reserve, Death Benefit Reserve, Transition Reserve, and the Negative Contingency Reserve.

Other Valuation Reserves: Includes Employer Reserve, Retiree Reserve, Death Benefit Reserve, Transition Reserve, and the Negative Contingency Reserve.

IV. RESERVES

MCERA maintains the following reserves:

VALUATION RESERVES:

A. Employee Regular Contributions Reserve and Employee COLA Contributions Reserve:

The reserves to which member contributions are credited. (known as Employee Reserves.) These contributions may be refunded to the member upon separation from service or left on deposit by the member upon separation from service (deferred retirement). Upon the retirement of a member an amount equal to the member's contributions plus credited interest will be transferred to the Retiree Annuity Reserve and Retiree COLA Reserve.

B. County Advance Reserve and County Advance COLA Reserve:

The reserves to which regular and cost-of-living employer contributions are credited. (known as Employer Reserves.) Upon retirement of a member, a transfer is made to the Retiree Current Service Reserve and Retiree COLA Reserve.

C. Retiree Annuity Reserve, Retiree Current Service Reserve, and Retiree COLA Reserve:

The reserves to which transfers are made from Employee Regular Contributions Reserve, Employee COLA Contributions Reserve, County Advance Reserve, and County Advance COLA Reserve at the time of a member's retirement. (known as Retiree Reserves.) The transfer to these reserves equals the present value of the total benefits due the retiree and eligible beneficiaries at the time of retirement.

D. Survivor Death Benefit Reserve

The reserve is credited with the present value of death and survivor benefits expected to be paid upon the death of an active member.

E. Actuarial Value Transition Reserve

This reserve represents the accumulated difference between the Actuarial Value of Assets and the book or cost value of reserves on July 1, 2023. This is a one-time adjustment to align the reserve balances with the Actuarial Value of Assets.

F. Negative Interest Reserve

This reserve tracks the amount of interest credited to the reserve accounts that has not been paid for out of earnings of the fund.

NON-VALUATION RESERVES:

G. Deferred Return Reserve:

This reserve represents the unrecognized return after smoothing of investment gains and losses. This reserve is not credited with interest.

III. CREDITING RATES

A. Regular Interest Rate

By statute, this rate is interest at 2.5% a year until otherwise determined by the Board, compounded semiannually on June 30th and December 31st to all contributions in the retirement fund which have been on deposit for six months immediately prior to that date (Government Code section 31591).

With respect to the rates of interest to be credited to members and Valuation Reserves, the Board may, in its sound discretion recommend a rate that is higher or lower than the actuarial interest rate assumption.

The Regular Interest Rate is the target rate to be credited to all valuation reserves except the Employee Reserves. By this policy, the Board sets the Regular Interest Rate equal to the current Actuarially Assumed Investment Rate of Return adopted by the Board. The Actuarially Assumed Investment Rate of Return is the rate in effect for the June 30 valuation that immediately precedes the following December 31 and June 30 interest crediting dates.

B. Employee Crediting Rate

Employee accounts shall be credited each December 31 and June 30. The Employee Crediting Rate is 2.5% per year, credited semiannually.

IV. INTEREST CREDITING

1. Upon determining Available Earnings for the interest crediting period, MCERA shall credit interest semiannually as set forth below:

2. Credit the Employee Reserves at the semi-annual Employee Crediting Rate. The semiannual interest crediting rate for Employee Reserves is 1.25% each semi-annual period. Deduct this amount from Available Earnings. If this amount of interest is more than Available Earnings, credit the reserve and charge the shortfall to the Negative Interest Reserve.

3. Credit the Employer Reserve with the dollar difference between one-half of the Actuarially Assumed Investment Rate of Return on the Employee Reserve and one-half of the Employee Reserve Interest Crediting Rate. If this amount of interest

is more than Available Earnings, credit the reserve and charge the shortfall to the Negative Interest Reserve.

4. Semiannual interest will be credited to the Other Valuation Reserves. The Semiannual interest crediting rate is one-half of the Actuarially Assumed Investment Rate of Return. If Available Earnings are not sufficient after step 2 and step 3, credit the reserve and charge the shortfall to the Negative Interest Reserve.

5. If Available Earnings exceed the amount required to credit interest to the Other Valuation Reserves, the balance of the Available Earnings after interest crediting shall be applied first to the Negative Interest Reserve, until such reserve reaches zero, then pro-rata to the Employer Reserves until the plan achieves 100% funded status.

V. POLICY REVIEW

The Board of Retirement shall review this policy at least every three (3) years and may amend the policy as deemed necessary.

VI. POLICY HISTORY

The Board adopted this policy on November 15, 2023.