CALSTRS

Regular Meeting

Item Number 7 – Open Session

Subject: Chief Executive Officer Report

Presenter(s): Jack Ehnes

Item Type: Information

Date & Time: March 5, 2021 – 20 minutes

Attachment(s): None

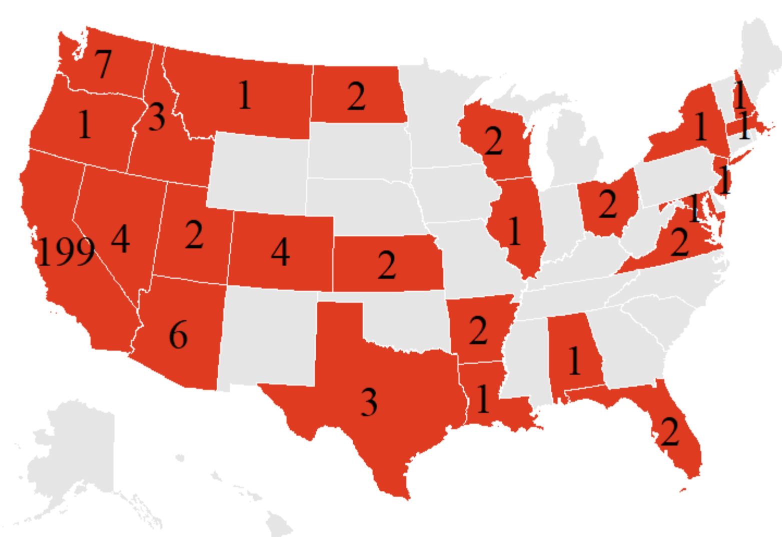
PowerPoint(s): None

COVID Related Member Deaths Rise Significantly in Recent Months

CalSTRS staff continue to monitor COVID related member deaths each month. Sadly, we witnessed statewide spikes in December and January rising to 253 cumulative deaths through January 21. The map below shows the distribution across states. Approximately 85% of retired CalSTRS members live in California, whereas California retired member deaths represent about 77% of total retired member deaths in the United States.

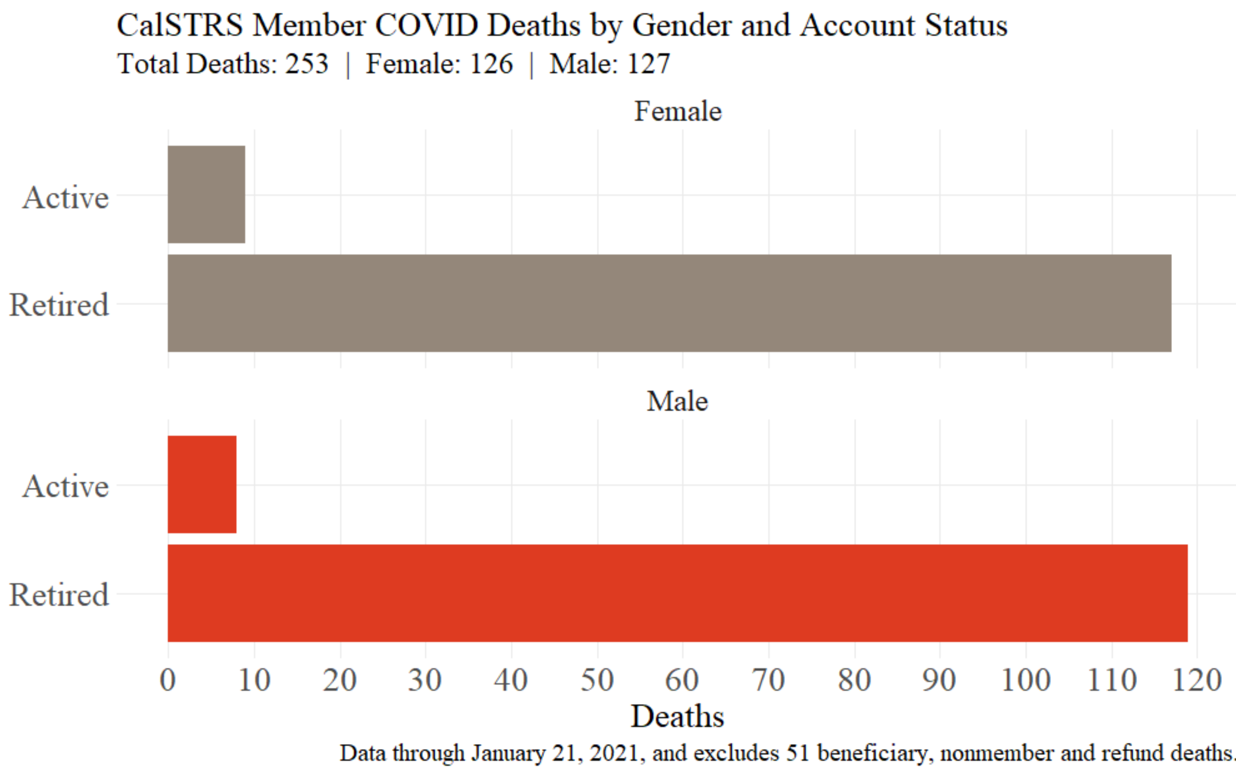
CalSTRS Member COVID Deaths through January 21, 2021

Total Deaths: 253 | International: 1 | Female: 126 | Male: 127



Counts exclude 51 beneficiary, nonmember and refund deaths.

Retired member deaths represent 93% of CalSTRS member deaths—236 retired deaths compared to 17 active deaths. The CalSTRS member population is split approximately 70% female and 30% male, while the proportion of deaths is split 50% female and 50% male. The California Department of Public Health reports the proportion of death in the general state population is 42% female and 58% male. The average age of death due to COVID-19 is 85 for retired females and 84 for retired males. The average age of death is 57 for active females (9 deaths) and 62 for active males (8 deaths).



Finalization of Benefits / Benefit Stabilization Update

During the 2020 calendar year, CalSTRS staff worked with stakeholder partners to develop legislative changes that would address varying interpretations of the statute of limitations currently contained within law. The effort also extended the time in which CalSTRS could recover overpayments with some responsibility borne by employers if errors were due to misreporting of information. At the December meeting, the board heard input from several stakeholder entities who expressed significant concern about the content contained within the proposal as drafted. As a result, the board directed staff to conduct additional research on the issues raised by stakeholders and requested more detail on the multiple complex issues that contribute to the overpayment of benefits.

At the board's January meeting, the CEO report provided an update on the approach CalSTRS is taking to perform the work necessary to resolve a number of impediments and/or inefficiencies that contribute to benefit adjustments. At that meeting, board members expressed a desire to understand the current process of when a benefit is finalized and the fundamental steps that are a regular part of initiating benefits. This update provides a somewhat detailed, but not all inclusive, summary of the varying events under which a benefit is calculated, adjusted and deemed final absent circumstances that change it.

When a member retires, statute requires CalSTRS to pay the benefit within 45 days of the benefit effective date or receipt of the application, whichever is later.[1] If the benefit is delayed beyond the 45 days, regular interest must be paid to the member.[2] One of Service Retirement's Customer Service Performance Measures is to pay retirement benefits within 30 days of the benefit effective date or receipt of the application, whichever is later, and on average, we consistently pay 98% of benefits within those 30 days. This ensures there is no gap in income when a member stops working and begins retirement.

When CalSTRS calculates a benefit, it is based on the data available at the initiation of the benefit. In a variety of circumstances, CalSTRS receives new information that may result in a difference to the benefit calculation. Benefits can increase or decrease, resulting in either an underpayment or an overpayment. Most of the time these changes are a regular part of establishing a benefit.

For example, if a member's retirement date is right after they stop working for their employer, there will likely be additional data submitted that could affect the benefit calculation. Employers are required to submit reports with compensation and contribution information on a monthly basis. The reports are due 30 calendar days after the pay period and are delinquent on the 45th calendar day.[3] This means that if a member's last day of work is on June 30, the employer's monthly report for the June pay period would be due by mid-August. If the member's retirement effective date is July 1, they will receive their first benefit payment before the data for the June pay period is received by CalSTRS. Therefore, their initial benefit would not include compensation or service credit for the month of June. When the employer submits the final month of payroll information, the benefit is adjusted to include the additional month of compensation and service credit.

Other common adjustments shortly after the initiation of a member's benefit can occur with the additional information provided in the Express Benefit Report, submitted by the employer upon a member's retirement. Employers report several pieces of information on the form, including last day of work, a reduction in school funds that may allow nonconsecutive three-year final compensation, and unused sick leave that can be converted to additional service credit at retirement. Statute requires employers to certify the number of unused sick leave days within 30 days of the member's retirement date or the date CalSTRS received the application, whichever is later.[4] On average, over the last five calendar years, we have received Express Benefit Report forms 60 days after the benefit effective date.

[1] Education Code section 22319.
[2] Education Code section 22321.
[3] Education Code sections 23004 and 23005.
[4] Education Code section 22717.

These two steps in the retirement process cause the most common benefit adjustments, meaning that even if no other issue triggers follow-on adjustments, a member's benefit is likely to have at least two adjustments before being considered stable.

Less frequently, there may be further adjustments to a member's benefit as result of multiple factors that can occur at any given point after the reports noted above are received by CalSTRS and the benefit was initially considered stable. Employers may rereport data when there is an audit or Compensation Review Unit finding that uncovers an inaccuracy in the information used to calculate a benefit. It is also possible that employers may retroactively submit data when they identify something on their own that needs to be changed, such as a retroactive pay increase. In both cases, the adjusted information is appended to a member's account and could affect the benefit calculation.

An examination of year-over-year changes from the Benefit Valuation File[5] shows that most retirees do not experience any changes to their retirement benefit. For example, only 4.5% of those members that were retired for the full 2018-19 school year experienced a change in their unmodified benefit, most of which were increases. Only approximately 0.5% of 2018-19 retirees experienced decreases. For those members, the median reduction in benefits was $12 per month. Additionally, most of the changes take place in the early years of retirement. Over 71% of the 2018-19 retirees that experienced a change in unmodified benefits had been retired less than three years.

Adjustments to members' and beneficiaries' monthly benefits may also result from various other changes, outside of employer-reported information, resulting from life and career events that may or may not affect the unmodified benefit. For example, a retired member may make a postretirement option change due to divorce, marriage or death of the option beneficiary, which can alter the option factor that was applied to the original benefit calculation. Additionally, adjustments may occur because of system-generated data fixes, court orders, community property splits, the death of an option beneficiary, data received from a concurrent retirement system and part-time community college comparison calculations. These are all examples of benefit adjustments made during the normal course of business. While the CalSTRS system does not capture the detail regarding the causes of benefit adjustments, a sample analysis of adjustments regularly completed by Financial Services indicates that, during the most recent quarter, approximately 38% of the benefit adjustments occur for reasons *not* related to employer-reported information.[6]

As noted above, there are a number of events and processes that transpire in the initiation and finalization of a benefit and elucidate an inventory of focus points that will help us shape a solution moving forward. Staff have already begun initial work embarking on internal analysis of law,

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[5] The Benefit Valuation File is an annual snapshot of benefits. Changes that occur within the year are not captured. Similarly, because this analysis isolated service retirement benefits without modification for joint and survivor options, changes that occur as a result of retiree or beneficiary death are also not captured.
[6] Customer Service Performance Review: Q2, Fiscal Year 2020-21.

processes and peer comparisons to evaluate where changes should be made and will continue with ongoing updates to the board as information and proposed resolutions are shaped.

Update on Regulations – Administrative Remedy Process for Employer Audits

At the March 2020 meeting, the board directed staff to begin drafting proposed regulations to allow all similarly affected members to appeal final employer audit findings. Under the current regulations and practice, only members that are included in the audit's sampled population are known to CalSTRS in time to inform them of their right to an administrative hearing. Any other affected members that may otherwise be a part of the systemic population unknown to CalSTRS but also subject to an audit finding cannot, in practice, be notified in time to be provided the same rights. As directed, staff have formed an internal drafting team and engaged with stakeholders.

Staff have shared two versions of the draft text with member and employer stakeholders and are making additional changes based on the feedback. As a result, staff are exploring ways to narrow the approach to focus more on the appeals process and less on the audit resolution process. For example, staff are re-evaluating whether to impose employer penalties and exploring additional methods to inform the membership of completed audits. Staff will be sharing the new draft language with stakeholders once it is available to continue to engage prior to any board action.

Path Forward: Staff Survey Shows Strong Positive Levels of Satisfaction and Engagement

At the January board meeting, staff discussed various approaches under consideration for shaping work in the future once the pandemic has stabilized and schools have reopened. We have continued to survey staff using one-day turnaround Pulse Surveys to help us understand various aspects of telework, perceptions of health safety, and future work design considerations. Pulse Survey #10 was completed on January 21st with 691 survey responses and a strong 55% response rate.

Just prior to the onset of the pandemic in February 2020, staff participated in the biannual engagement survey which includes questions on satisfaction and engagement. At the time, both areas of query indicted high levels of satisfaction and engagement. The satisfaction question was then included on Pulse Survey #4 in August 2020 to assess the impact of the pandemic and near universal teleworking of staff. With this recent survey, the same questions were again repeated to determine if this extraordinarily lengthy period of working from home had impacted the staff on these dimensions. The positive results are as follows for the whole organization:

- Job satisfaction changed from 73% satisfied in Feb 2020, to 87% in August 2020, to 82% in January 2021.
- Employee engagement significantly moved upward from 56% engaged in Feb 2020 to 67% in January 2021.

(Note: Employees are provided a 7-point scale and the "top two" responses are used to measure a positive response to ensure we are tapping into the strongest measure of feelings).

Year End Tax Filings Completed

CalSTRS is required to submit various tax filings to our members, their beneficiaries, vendors, the Internal Revenue Service and the State of California by the end of January each year, for certain expenditures paid during the previous calendar year. For calendar year 2020 the following tax filings were completed:

- 440,643 Forms 1099-R reporting $16,250,287,904.08 in benefit payments, $1,663,852,086.53 in federal tax withholding, and $477,162,145.21 in state tax withholding
- 103 Forms 1099-NEC reporting $94,449,517.46 in payments to vendors
- 26 Forms 1099-MISC reporting $335,477.15 in payments for non-member benefit payments from the Replacement Benefits Program and one legal settlement.
- 326 Forms W-2 reporting $10,719,217.10 in Replacement Benefits Program payments, $1,152,139.47 in federal income tax withholding, and $303,839.66 in state income tax withholding
- IRS Form 945 for Calendar Year 2020, which reconciles federal tax withholding and deposits related to Forms 1099-R, 1099-NEC, and 1099-MISC
- IRS Form 941 for the 4th Quarter of 2020, which reconciles the federal tax withholding reported on Forms W-2
- EDD Form DE-9 for the 4th Quarter of 2020, reporting $123,868,902.76 in state tax withholding

Headquarters Expansion (HQE) Construction Progress Update

As of January 31, 2021, the construction of the project is approximately 32% complete. However, due to the delay in the issuance of the Phase IV Architectural MEP/TI permit, the Substantial Completion Date (SCD) has been moved out another four weeks to September 16, 2022. This is a total impact to the original schedule of twelve weeks. Both the integrated project team and the Executive Steering Committee continue to evaluate all major project decisions at bi-weekly meetings and continue to monitor the status of the plan review with the Office of the State Fire Marshal very closely.

The detail below outlines the status of the construction activities, schedule, budget and associated risks.

Construction Activities

The installation of an underground fire pump conduit and waterproofing at the elevator pit was completed and all shoring has been removed at the lobby level. All zones of the concrete deck for office level four was completed and column groups and rebar is in process. The concrete deck pour for Zone A of office level five has begun.

Schedule Status

As mentioned, the schedule included in the GMP document projected a SCD of July 6, 2022 but due to permit delays, has been pushed out to September 16, 2022. There was one weather day used since the last report, and the remaining 21 weather impact days are included in the SCD that may or may not be needed. Below are upcoming substantial project milestones:

Project Milestones	**Start Date**	**Completion Date**
Phase IV Architectural/MEP/TI Permit/OSFM	03/31/20	Estimated completion date was 11/5/20- current assumption is 4/23/21
P-2 Structure	05/19/20	07/01/21
P-3 Structure	06/23/20	07/01/21
P-4 Structure	07/29/20	07/04/21
P-5 Structure	08/26/20	07/08/21
Exterior Envelope	04/27/21	11/15/21
Lobby Level Interior Improvements	03/01/21	12/01/21
Roof/Skylight Construction	07/28/21	11/10/21
Bridge Construction including interiors	10/26/21	04/08/22
Office Level 03 Interior Improvements	07/22/21	03/03/22
Office level O3 Owner Furniture Installation	03/11/22	04/21/22
Office Level 04 Interior Improvements	06/15/21	03/23/22
Office Level 04 Owner furniture Installation	03/18/22	04/27/22
Office Level 05 Interior Improvements	09/24/21	04/18/22
Office Level 05 Owner Furniture Installation	04/26/22	06/07/22
Office Level 06 Interior Improvements	10/22/21	05/16/22
Office Level 06 Owner Furniture Installation	05/24/22	07/06/22
Office Level 07 Interior Improvements	11/19/21	06/14/22

Office Level 07 Owner Furniture installation	07/14/22	08/24/22
Start-Up and Commissioning	03/01/22	07/11/22
FINAL AHJ Inspections	07/07/22	08/17/22
Estimated Project Completion Date	10/21/19 start	**09/16/22**

Budget Status

We continue to remain within budget for the overall project. However, continued safety protocols due to COVID-19 and the delay of the Phase IV permit, will have a significant impact on the project contingency. Based on the additional schedule delay, we anticipate having a shortfall of approximately $800K in the project contingency line item.

The expected shortfall is based on the following assumptions below:

COVID-19 costs: It is anticipated that the CDC requirements for COVID-19 will continue until the vaccine is widely available and governmental restrictions are lifted. Currently, there is $1.206M of forecasted costs included in the project contingency for costs anticipated in the next year. COVID related costs are approximately $55K to $70K per month depending upon the number of crafts people onsite. In the worst- case scenario where the COVID restrictions are not lifted for the remainder of the project schedule, (18-20 months), it seems likely that the entire forecasted cost will be exhausted. If restrictions are lifted by the end of 2021, the COVID costs earmarked in the project contingency would be reduced by $500K.

Schedule Delay costs: Currently there is a recognized schedule delay caused by the extended OSFM plan review timeline. Based upon the latest schedule completion date of September 16, 2022, additional hard and soft costs will be incurred. Currently there is $4.53M of forecasted costs included in the Project Contingency for the days added to the project schedule. The schedule delay costs are based upon conservatively estimated hard and soft costs incurred due to the 51 added workdays. It should be noted that included within the additional schedule delay are 21 weather days and 30 days of AHJ inspections and approvals. It seems unlikely that all of these days would be utilized. The team is continuously reviewing activity sequencing to identify ways to compress tasks; overlap tasks; and/or work overtime where it makes sense; to shorten the overall project schedule and decrease the added costs associated with the schedule delays. The schedule refinement will continue, although cannot truly be completed, until OSFM issues the Phase IV permit.

In addition, there are other costs that could potentially impact the Project Contingency. These include OSFM plan checking and inspection fees and well as City plan review fees. These costs are being monitored closely but will not be completely known until all of the permits are issued.

The team continues to explore possible cost savings opportunities in other project item categories such as furniture and AV that could offset the added costs described above.

The budget status for the month ending January 31, 2021 is summarized below:

Budget Categories	Total Project Budget	Costs to Date	Balance to Complete
Hard Costs	$ 244,392,717	$ 80,600,410	$ 163,792,307
Hard Cost Contingency	$ 5,965,190	$	$ 5,965,190
Soft Costs	$ 44,698,669	$ 19,553,988	$ 25,144,681
Project Contingency	$ 4,943,424		$ 4,943,424
Totals	**$ 300,000,000**	**$ 100,154,398**	**$ 199,845,602**

The hard cost contingency was reduced since the last board report by $109,406. These costs include a plan review by a 3rd party consultant to begin addressing issues prior to submitting the Phase IV permit package to the OSFM, and minor construction modifications.

The project contingency was reduced since the last board report by $132,543 due to monthly costs for COVID-19 safety protocols, and a small amendment for the architect, ZGF.

Risk Status

On-going risks associated with the project are:

1) Public Agency Plan review timeframes - This report's schedule reflects a further delay in the completion date from the original date of July 6, 2022, to August 18, 2022 and now to September 16, 2022. This is in response to not receiving OSFM Phase IV approval as originally planned due to OSFM management staff being deployed to support front line crews during the record-breaking NorCal wildfires last summer. The Phase IV plans were submitted for approval on April 1, and comments were not received until July 22. Based on the Phase IV review, the OSFM staff rejected previously approved plans included with the Phase I permit and required those plans to be amended and re-approved which caused further delays. Due to the timeframe of having Phase I, II, and III plans re-reviewed and approved (Phase I approval was granted February 8, and Phase II and III were submitted on February 9, with approvals anticipated by the end of February, if not sooner) the schedule has been updated with a Phase IV approval date of April 23, 2021. The team continues to work through the permitting issues with OSFM staff to make sure the Phase IV plan check process proceeds as expeditiously as possible, and the construction team is continuously analyzing alternate strategies to reducing the cost impacts once the permit is issued. Further delays in permit issuance could impact the projected completion date on a day for day basis. The risk level associated with public agency review comments and timeline remains is high.

2) COVID-19 - Although there have been additional costs related to COVID-19 due to health and safety, we are not experiencing any loss in productivity due to site outbreaks. The current risk level associated with COVID-19 remains low.

3) Timely delivery of utilities from PG&E - The permanent power connection date has been set for March 13, 2021. The current risk level associated with PG&E remains low but will continue to be tracked until permanent power is delivered.