Finance Committee

City of Arts & Innovation

TO: FINANCE COMMITTEE **DATE: JANUARY 9, 2019**

FROM: FINANCE DEPARTMENT **WARDS: ALL**

SUBJECT: LONG TERM FISCAL MANAGEMENT OF THE CITY'S CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM FRESH START OPTION TO REDUCE IMPACTS ON CITY SERVICES

ISSUE:

Receive and provide feedback on a report about the CalPers Fresh Start savings for long-term fiscal management of the City's California Public Employees Retirement System unfunded pension obligations.

RECOMMENDATIONS:

That the Finance Committee:

1. Receive a monthly update on the Long-Term Management of California Public Employees Retirement System costs; and

2. Provide direction to staff regarding the CalPERS Fresh Start Program Option.

BACKGROUND:

On October 10, 2018, the Finance Committee requested monthly updates to the City Council Finance Committee regarding CalPERS cost management options.

On December 12, 2018, the Finance Committee received an update on CalPERS Cost Management options for consideration. This report includes additional information on one of those options – CalPERS Fresh Start Program.

DISCUSSION:

Collective Bargaining and Representation of Employees

The City maintains a strict commitment to collective bargaining which includes the requirement to meet and confer on any changes affecting wages, hours, promotions, benefits, and other employment terms. The City will not engage in activity that may be seen to run counter to the ability of the City and the Unions to communicate openly and honestly during the collective bargaining process, to find solutions that will ultimately benefit the City of Riverside. For simplicity, the City colloquially refers to this commitment as performing in “good faith” with the Unions and unrepresented employees alike.

Staff from the Finance Department, Human Resources Department, and the City Manager’s Office meet weekly to discuss the CalPERS Challenge. These meetings generate innumerable ideas, including those to address cost management dimensions of the CalPERS Challenge. One such option currently available to the City as noted in the previous Finance Committee discussion is the CalPERS Fresh Start Program.

Fresh Start Amortization Schedule and Alternatives

The amortization schedule on Attachment 1 shows the minimum contributions required for the Safety Plan only to pay off the UAL according to CalPERS amortization policy. This same scenario is similar for the Miscellaneous Plan as shown on Attachment 2. As the City looks to address CalPERS cost management strategies one of the options available to us is a Fresh Start or alternative amortization schedule. The benefit of a fresh start or alternative amortization schedule is the ability to pay off the UAL sooner and the potential savings in doing so. As a result, we have provided alternate amortization schedules to help analyze the current amortization schedule and illustrate the advantages of accelerating unfunded liability payments.

Shown on Table 1 are future year amortization payments for the Safety Plan only based on 1) the current amortization schedule reflecting the individual bases and remaining periods shown on Attachment 1; and 2) alternate “fresh start” amortization schedules using two sample periods that would both result in interest savings relative to the current amortization schedule. Note that the payments under each alternate scenario increase by 2.875% per year. The schedules do not reflect the impact of adopted discount rate changes that will become effective beyond June 30, 2017. The same things can be said for the Miscellaneous Plan as shown in Table 2.

TABLE 1 – Safety Plan

Amortization Schedule and Alternatives

	Current Amortization Schedule*		Alternate Schedules: 20 Year Amortization		Alternate Schedules: 15 Year Amortization	
Date	**Balance**	**Payment**	**Balance**	**Payment**	**Balance**	**Payment**
6/30/2019	289,862,686	19,134,466	289,862,686	21,664,062	289,862,686	26,357,478
6/30/2020	291,061,774	21,263,755	288,442,087	22,286,903	283,581,511	27,115,256
6/30/2021	290,142,672	23,662,129	286,273,470	22,927,652	276,060,184	27,894,819
6/30/2022	286,673,142	25,556,809	283,284,059	23,586,822	267,186,233	28,696,795
6/30/2023	280,989,909	26,269,436	279,395,269	24,264,943	256,838,381	29,521,828
6/30/2024	274,156,638	25,229,999	274,522,268	24,962,560	244,885,893	30,370,581
6/30/2025	267,904,408	27,431,835	268,573,512	25,680,234	231,187,868	31,243,735
6/30/2026	258,918,639	27,477,863	261,450,237	26,418,540	215,592,484	32,141,992
6/30/2027	249,233,734	28,267,851	253,045,922	27,178,074	197,936,185	33,066,075
6/30/2028	238,028,549	29,080,549	243,245,711	27,959,443	178,042,811	34,016,724
6/30/2029	225,169,345	29,916,616	231,925,785	28,763,277	155,722,659	34,994,705
6/30/2030	210,512,003	30,776,722	218,952,701	29,590,221	130,771,483	36,000,803
6/30/2031	193,901,266	29,541,019	204,182,672	30,440,940	102,969,417	37,035,826
6/30/2032	177,365,962	28,954,366	187,460,799	31,316,117	72,079,814	38,100,606
6/30/2033	160,239,398	26,193,617	168,620,242	32,216,456	37,848,013	39,195,999
6/30/2034	144,730,231	24,882,948	147,481,341	33,142,679		
6/30/2035	129,454,001	22,851,323	123,850,657	34,095,531		
6/30/2036	115,174,227	20,682,312	97,519,961	35,075,777		
6/30/2037	102,105,430	20,024,290	68,265,131	36,084,206		
6/30/2038	88,770,601	19,311,338	35,844,981	37,121,627		
6/30/2039	75,207,344	19,167,689				
6/30/2040	60,809,515	19,718,762				
6/30/2041	44,797,144	14,920,081				
6/30/2042	32,593,466	15,398,127				
6/30/2043	19,009,947	13,832,935				
6/30/2044	6,062,563	4,125,838				
6/30/2045	2,229,316	1,406,794				
6/30/2046	934,044	967,311				
6/30/2047						
6/30/2048						
Totals		**596,046,780**		**574,776,064**		**485,753,222**
Interest Paid		**306,184,094**		**284,913,378**		**195,890,536**
Estimated Savings				**21,270,716**		**110,293,558**

* This schedule does not reflect the impact of adopted discount rate changes that will become effective beyond June 30, 2017. For Projected Employer Contributions, please see Page 5.

Table 2 – Miscellaneous Plan

Amortization Schedule and Alternatives

	Current Amortization Schedule*		Alternate Schedules			
			15 Year Amortization		10 Year Amortization	
Date	**Balance**	**Payment**	**Balance**	**Payment**	**Balance**	**Payment**
6/30/2019	296,700,934	22,752,102	296,700,934	26,979,286	296,700,934	36,796,647
6/30/2020	294,649,314	24,206,204	290,271,578	27,754,941	280,104,564	37,854,550
6/30/2021	290,943,064	26,059,482	282,572,813	28,552,895	261,209,376	38,942,869
6/30/2022	285,048,823	27,199,226	273,489,513	29,373,791	239,817,208	40,062,476
6/30/2023	277,546,913	27,125,313	262,897,542	30,218,288	215,714,624	41,214,272
6/30/2024	269,577,664	27,905,163	250,663,079	31,087,063	188,671,784	42,399,183
6/30/2025	260,223,016	28,707,438	236,641,899	31,980,817	158,441,226	43,618,159
6/30/2026	249,359,310	29,532,774	220,678,599	32,900,265	124,756,562	44,872,181
6/30/2027	236,853,253	30,381,842	202,605,765	33,846,148	87,331,075	46,162,257
6/30/2028	222,561,200	31,255,321	182,243,079	34,819,224	45,856,217	47,489,421
6/30/2029	206,328,385	32,153,914	159,396,364	35,820,277		
6/30/2030	187,988,093	33,078,337	133,856,557	36,850,110		
6/30/2031	167,360,785	27,881,786	105,398,603	37,909,551		
6/30/2032	150,619,624	26,568,843	73,780,274	38,999,450		
6/30/2033	134,024,432	24,928,873	38,740,898	40,120,685		
6/30/2034	117,924,468	22,695,295				
6/30/2035	102,970,387	20,168,239				
6/30/2036	89,549,194	17,477,118				
6/30/2037	77,941,931	17,051,081				
6/30/2038	65,934,353	16,586,098				
6/30/2039	53,537,771	16,901,162				
6/30/2040	39,916,148	17,807,885				
6/30/2041	24,367,942	11,263,799				
6/30/2042	14,469,652	12,735,275				
6/30/2043	2,329,852	2,412,831				
6/30/2044						
6/30/2045						
6/30/2046						
6/30/2047						
6/30/2048						
Totals		**574,835,401**		**497,212,791**		**419,412,015**
Interest Paid		**278,134,467**		**200,511,857**		**122,711,081**
Estimated Savings				**77,622,610**		**155,423,386**

* This schedule does not reflect the impact of adopted discount rate changes that will become effective beyond June 30, 2017. For Projected Employer Contributions, please see Page 5.

The Current Amortization Schedule typically contains individual bases that are both positive and negative (See Attachment 1 for the Safety Plan and Attachment 2 for the Miscellaneous Plan). Positive bases result from plan changes, assumption changes, or plan experience that result in increases to the unfunded liability. Negative bases result from plan changes, assumption changes, or plan experience that result in decreases to the unfunded liability. The combination of positive and negative bases within an amortization schedule can result in unusual or problematic circumstances in future years such as:

- A positive total unfunded liability with a negative total payment,
- A negative total unfunded liability with a positive total payment, or
- Total payments that completely amortize the unfunded liability over a very short period of time

In any year where one of the above scenarios occurs, the CalPERS actuary will consider corrective action such as replacing the existing unfunded liability bases with a single “fresh start” base and amortizing it over a reasonable period.

The Current Amortization Schedule on Tables 1 and 2 above may appear to show that, based on the current amortization bases, one of the above scenarios will occur at some point in the future. It is impossible to know today whether such a scenario will in fact arise since there will be additional bases added to the amortization schedule in each future year. Should such a scenario arise in any future year, the actuary will take appropriate action based on guidelines in the CalPERS amortization policy.

CalPERS provided Fresh Start scenarios in the City’s June 30, 2017 CalPERS actuarial reports. Attachment 1 presents amortization schedules for a period of 20 years versus 15 years for the Safety Plan, while Attachment 2 presents an amortization period of 15 years versus 10 years for the Miscellaneous Plan. The longer amortization periods of 20 years and 15 years for the Safety and Miscellaneous plans respectively result in combined interest savings of approximately $21.3 million and $77.5 million. Selecting a the aggressive and shorter amortization periods or “fresh start” of 15 years (Safety) and 10 years (Miscellaneous) results in total interest savings of $110.3 million and $155.4 million, respectively. The longer-period options result in payments that in some instances are higher than the current amortization or lower, depending on the year of payment. This is due to the ramping up and ramping down of the UAL using the current method.

Commencing with the June 30, 2013 CalPERS actuarial valuation, all new gains or losses are amortized over a fixed 30-year period with a 5-year ramp up at the beginning and a 5-year ramp down at the end of the amortization period. All changes in liability due to plan amendments (other than golden handshakes) are amortized over a 20-year period with no ramp up. Changes in actuarial assumptions or changes in actuarial methodology are amortized over a 20-year period with a 5-year ramp up at the beginning and a 5-year ramp down at the end of the amortization period.

Staff do not recommend the CalPERS “fresh start” option because once the City requests this option from CalPERS it is a permanent fiscal commitment. This would lock the City into the new payment structure and will not allow for flexibility during unexpected economic slowdowns. It is expected that the City will reach critical budget deficits beginning in fiscal 2020-21 and beyond of approximately $15 - $20 million a year, and locking in higher annual UAL payments will exacerbate the budget deficit issue. Alternatively, the City can choose to mimic, rather than formerly commit to, one of the fresh start options now and pay more than the minimum allocation until it is no longer feasible for the City to continue to make extra payments modeled from a “fresh start” schedule.

<u>FISCAL IMPACT</u>:

There is no direct fiscal impact associated with presentation of this report. Upon direction from City Council to move forward with this CalPERS Cost Management Option, the costs and the associated long-term savings of the options will be provided as part of the recommendation to the report. The City's five-year projections on CalPERS costs have been included in the City's Adopted FY 2018-2020 Two-Year Budget and FY 2018-2023 Five-Year Plan assumptions.

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Attachments:

1. CalPERS Fresh Start Amortization Schedule – Safety Unit
2. CalPERS Fresh Start Amortization Schedule – Miscellaneous Unit
3. Presentation