

CalPERS Pension Cost Management Update

City Manager's Office

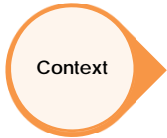
City Council
January 14, 2020

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OVERVIEW OF PRESENTATION



THE CALPERS CHALLENGE



Given Unfunded Pension Obligations, Our Collective Challenge (aka The CalPERS Challenge) is:

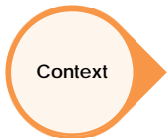
How to Effectively Secure the Solvent Financial Future of the City, Its Employees, & Its Retirees While Ensuring the Delivery of Public Services & Stewardship of Public Resources



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CALPERS PENSION FUNDING



As of 6/30/2019



Source: <https://www.calpers.ca.gov/page/about/organization/facts-at-a-glance/pension-buck>

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CALPERS FUTURE BENEFIT ESTIMATIONS



When a new member enrolls into the retirement plan, the CalPERS actuary estimates the individual's pension benefit making assumptions for:

1. Life expectancy*
2. Wage Increases
3. Inflation
4. Investment returns of the plan
5. Years of life after retirement
6. Other factors

The result is today's assumed cost of the employee's total future pension payout during retirement.



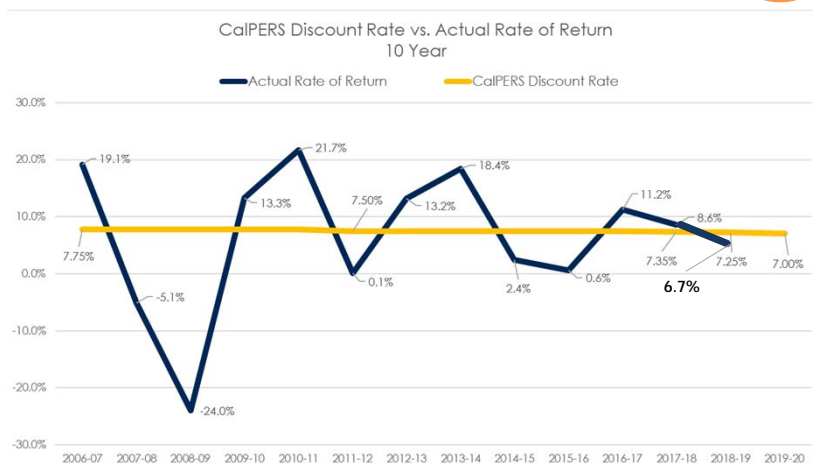
* Source: report attachment "CalPERS Experience Study 2017" 5

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CALPERS DISCOUNT RATE VS. ACTUAL RATE OF RETURN – 10 YEAR



- CalPERS' actual rate of investment return is subject to market volatility and CalPERS' investment policy.
- The discount rate is the assumed long-term interest rate used in CalPERS actuarials for defining current costs of future pension obligations.



Source: <https://www.calpers.ca.gov/docs/forms-publications/facts-investment-pension-funding.pdf> 6

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CALPERS CONTRIBUTION CATEGORIES



Each year, the City makes two types of payments to PERS:

1. **Normal Cost (NC):** Annual cost for current employees
2. **Unfunded Accrued Liability (UAL):** Actuarial Liability MINUS Actuarial Value of Assets
 - a. "How much we currently have vs. how much we need to have in the future when people actually retire"
 - b. Shortfall not repaid all at once; amortized over a longer period of time with the City paying down a portion each year (principal and interest at 7% annually)



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RIVERSIDE'S DEFINED BENEFIT PENSION PLANS



- A. City has 2 primary plans with CalPERS
 1. Miscellaneous: 5,166 covered members including 1,607 active
 2. Safety: 1,514 covered members including 568 active
- B. Multiple tiers and PEPRA plans within Miscellaneous and Safety

| BEFORE JANUARY 2013 | | | AFTER JANUARY 2013 (PEPRA) | |
|--|--|--------------------------|--|-------------------------------------|
| 3% @ 50 | 2.7% @ 55 | 3% @ 55 | 2% @ 62 | 2.7% @ 57 |
| Safety (Fire Tier 1, Police Tier 1, 2) | Miscellaneous (All Non-Sworn Tier 1 & 2) | Safety (Fire Tier 2) | Miscellaneous (All Non-Sworn Tier 3) | Safety (Fire & Police Tier 3) |



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RIVERSIDE FUNDED RATIOS



The City's CalPERS Funded Ratios represent the percentage of assets available today to pay all of the pension benefits promised to City employees.



Source: CalPERS Actuarial Valuation Reports dated July 2019 for the City of Riverside, as of June 30, 2018

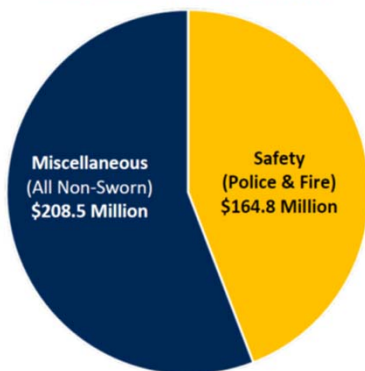
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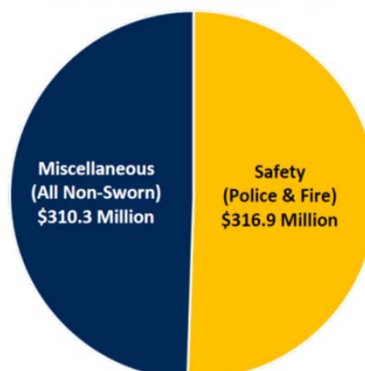
CITYWIDE UNFUNDED PENSION LIABILITY



Total UAL: \$373.3 Million
CalPERS Actuarial Report as of June 30, 2014



Total UAL: \$627.2 Million
CalPERS Actuarial Report as of June 30, 2018



Increased \$253.9 Million (68%)

Primarily due to change in discount rate



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UNFUNDED ACCRUED LIABILITY (UAL)

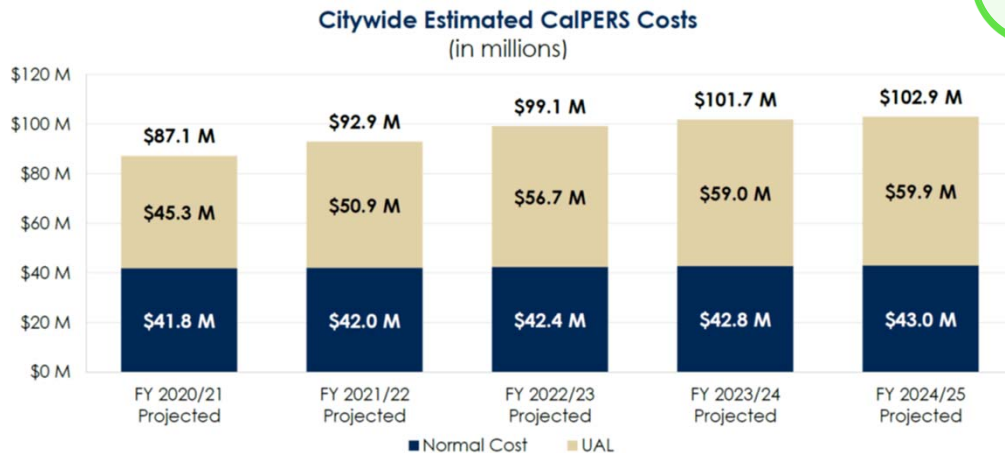


1. UAL is an actuarial term that refers to the difference between the values of assets and the estimated accrued liabilities of the plan.
2. UAL is the result of the actuarial assumptions that were not met.
3. It is not an absolute number - it is adjusted annually based upon the five most recent years of experience.
4. The amount is based on an actuarial valuation at a particular point in time.



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CITYWIDE ESTIMATED CALPERS COSTS



Sources: UAL - The UAL projections are based on an actuarial report prepared for the City by Bartel Associates, LLC., and provided to City Council on December 17, 2019. Normal Cost projections are based on the FY20/21 and 21/22 budget forecast modeling.

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GENERAL FUND ESTIMATED CALPERS COSTS*

General Fund Estimated CalPERS Costs by CalPERS Group
(in millions)



* Includes Measure Z



Sources: UAL - The UAL projections are based on an actuarial report prepared for the City by Bartel Associates, LLC., and provided to City Council on December 17, 2019. Normal Cost projections are based on the FY20/21 and 21/22 budget forecast modeling.

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UNFUNDED ACCRUED LIABILITY



- The amount of the UAL today is impactful to member agencies' financial health and financial planning strategies.
- The most important objective is to ensure the contributions the City is making are expected to eliminate the UAL over a reasonable period of time.

Example: Home mortgages are outstanding obligations and are managed through affordable, timely payments.



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RIVERSIDE'S CALPERS CHALLENGE INVESTMENT



Built & Implemented the infrastructure to address the CalPERS Challenge

| Description | Staff | 2019 Hours |
|---|-------|--------------|
| Weekly Team meetings | 7 | 364 |
| Monthly City Manager Brown Bag Lunches | 4 | 80 |
| Monthly Executive Leadership Team Meetings | 21 | 504 |
| Managed Hiring Review | 5 | 250 |
| Community Meetings as requested | 3 | 20 |
| League of California Cities Governance, Transparency & Labor Relations Committee | 1 | 24 |
| CalPERS Executive Team, including CEO Marcie Frost, to discuss concerns and investment activities. | 11 | 44 |
| Several staff members have attended professional conferences including ICMA, CalPERS, League of California Cities, CALPELRA and LCW | 10 | 276 |
| Contracts with external firms for labor negotiations, actuarial modeling, budget modeling, and investment strategies | 10 | 206 |
| Estimated hours not inclusive of analysis, report preparation, and approvals | | 1,768 |

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RIVERSIDE'S CALPERS CHALLENGE INVESTMENT



More infrastructure to address the CalPERS Challenge

1. CalPERS Challenge webpage with FAQs, documents, videos & a feedback email
2. Included CalPERS Challenge in the Legislative platform initiatives to stay engaged with State policy makers
3. City Council meeting standing agenda item to provide an update for CalPERS Challenge/Fiscal Solvency
4. Monthly CalPERS topics to the Finance Committee

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RIVERSIDE'S CALPERS CHALLENGE INVESTMENT



City Council's Finance Committee Discussions:

| Date | Topics |
|--------------------|--|
| October 10, 2018 | Update on the CalPERS Challenge |
| January 9, 2019 | Fresh Start Program |
| February 13, 2019 | CalPERS Challenge Update |
| March 13, 2019 | Priority Based Budgeting; Measure Z Reserve Policy; Partnership Compensation Model Estimated Fiscal Impact |
| April 10, 2019 | Section 115 Trust |
| June 12, 2019 | CalPERS Replacement Benefit Plan; Pension Funding Policy |
| July 10, 2019 | Sale of High Value Assets |
| August 14, 2019 | Financial Health Indicators |
| September 11, 2019 | Review of CalPERS Cost Sharing Measures |
| October 30, 2019 | General Fund Restructuring |

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RIVERSIDE'S CALPERS CHALLENGE INVESTMENT



Budget Engagement Commission Discussions:

| Date | Topics |
|-------------------|--|
| February 28, 2019 | Update on the Long Term Fiscal Management of CalPERS |
| May 20, 2019 | Formation of the CalPERS Ad Hoc Committee |
| July 11, 2019 | Pension Funding Policy |
| August 15, 2019 | CalPERS Ad Hoc Committee update |

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RIVERSIDE'S CALPERS CHALLENGE ACTIONS



Fiscal Solvency Measures Accomplished within Management Purview:

1. Pre-payment of the UAL at beginning of each fiscal year saves 3.5% or \$1.2M to \$1.5M annually
2. Discontinued a long practice of using left over funds from one budget year to fund expenses in the next year (Carry Over funds) freeing up- \$4.5M from FY 17/18 and \$4.M from FY 18/19
3. Established a Section 115 Trust – Current balance \$4.5M
4. Instituted Managed Hiring to generate savings - \$2.1M in FY 18/19
5. Pension Funding Policy - \$400K use of one-time revenues
6. Cost sharing provision in the Crossing Guard contract resulting in \$1.9M savings to the City over the 5 year agreement, all savings directed to the Section 115 Trust



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REVISED ASSUMPTIONS FROM THE FY 2018/19 YEAR END



Presented to City Council on June 18, 2019:

GENERAL FUND 5 YEAR FORECAST

| General Fund | Year 1 FY 2018/19 Projected | Year 2 FY 2019/20 Amended | Year 3 FY 2020/21 Projected | Year 4 FY 2021/22 Projected | Year 5 FY 2022/23 Projected |
|--------------------------|-----------------------------------|---------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
| Beginning Reserve | \$ 59,197,900 | \$ 60,433,966 | \$ 59,197,954 | \$ 42,040,754 | \$ 19,930,354 |
| Revenues | 271,170,217 | 279,136,415 | 276,758,200 | 279,967,100 | 284,677,000 |
| Expenditures | 269,934,151 | 280,372,427 | 293,915,400 | 302,077,500 | 312,094,900 |
| Surplus/(Deficit) | 1,236,066 | (1,236,012) | (17,157,200) | (22,110,400) | (27,417,900) |
| Ending Reserve | \$ 60,433,966 | \$ 59,197,954 | \$ 42,040,754 | \$ 19,930,354 | \$ (7,487,546) |
| % Reserve* | 21.9% | 21.6% | 20.1% | 13.9% | 6.4% |

* Beginning Reserve/Expenditures

This Forecast includes updated figures from the June 2018 Five Year Forecast based on actual costs, City Council approved supplemental amounts and adjustments throughout FY 2018/2019. It **does not include** any additional funding allocations from Measure Z outside of the adopted budget and approved spending plan which includes planned, but not encumbered expenses.



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REVISED ASSUMPTIONS FROM THE FY 2018/19 YEAR END

Here
&
Now

1. The FY 2018-2020 General Fund Budget, as developed by prior City Management in 2017/18, included a conservative approach that assumed a slowing of the economy with declining growth rates for the General Fund's major revenue sources.
2. As reported to City Council on December 17, 2019, the General Fund ended FY 2018/19 in better condition than projected, with revenues outperforming projections, and savings in nearly all expenditure categories. As a result, the City was able to achieve the aspirational 20% General Fund reserve goal and end the year with \$4.4M in surplus reserves.



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REVISED ASSUMPTIONS FROM THE FY 2018/19 YEAR END

Here
&
Now

1. Since closing FY2018/19, Finance has worked with their financial advisors to closely review the past 10 years of all actual transactional history and trends to update the methodology for budget assumptions to prepare for the FY 2020/21 and FY 2021/22 budget cycle.
2. The updated General Fund budget forecast assumptions include additional revenue growth of approximately \$4.7M and a decrease of approximately \$5.3M of expenditures.
3. The Finance Department has right sized the General Fund by removing transactions that are not General Fund activity (such as grants and special projects) which reduce the funding required to meet the General Fund's aspirational reserve amount of 20%.
4. The revised budget assumptions that utilize actual transactional history, combined with the corrections made to the General Fund, have resulted in an estimated General Fund **shortfall of approximately \$7M for both FY 2020/21 and FY 2021/22 – which is a significant difference from the \$18M (20/21) and \$22M (21/22) deficits projected as part of the 2-year budget, 5-year plan adopted in June 2018.**



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POTENTIAL GENERAL FUND IMPACTS



Forecast Revenue and expenses are estimates. There are unknown factors that may significantly impact the estimates, for example:

1. Legal Challenges to the General Fund transfers
2. Uncertain state and federal economic conditions or legislation
3. Ballot measures (i.e. Prop 13 split rolls)
4. CalPERS investment performance
5. Expiring labor agreements with pending negotiations
6. Climate change impacts to operations and investments
7. Unrealized forecast assumptions and
8. Other unforeseen changes



RIVERSIDE'S CALPERS CHALLENGE OPPORTUNITES



City Council's Finance Committee PENDING Potential Discussions:

| CalPERS Cost Management Options | Description |
|----------------------------------|---|
| Use of Cash Reserves | Establish a policy that may lower cash reserves requirements and utilize more cash to pay down the UAL. |
| Review the City's Fees & Charges | Many of the City's existing fees are established at a rate less than 100% of the cost to provide the related service. The City can offset some costs by increasing the current recovery rate. |
| Subsidy programs | The City provides significant support to community programs, organizations, and events. As we enter a new era of financial constraints, these subsidies may be reviewed for conformity to the City's strategic priorities and potential opportunities for cost savings. |



RIVERSIDE'S CALPERS CHALLENGE OPPORTUNITIES



City Council's Finance Committee PENDING Potential Discussions:

| CaIPERS Cost Management Options | Description |
|--|--|
| Reduce Operational Budget | The City could require departments to review their budgets to re-allocate budgeted funds towards an account to pay down the UAL. |
| Cash Pool Borrowing or Interfund Loans | Utilizing available cash on hand from different funds to help pay down the UAL and repay the funds overtime at a reasonable interest rate. |
| Measure Z – Strategic Use | Measure Z was passed by the City's voters in November 2016 to reduce cuts, repair infrastructure, and provide general services |

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NEXT STEPS FOR THE CALPERS CHALLENGE



Unless otherwise directed, these options are planned for Finance Committee for discussion and recommendation to the City Council:

| Date | Description |
|--------------|--|
| January 2020 | Pension Obligation Bond Workshop |
| March 2020 | 10-year forecast tool be available for all to use |
| March 2020 | Review of the Measure Z 5 Year Spending Plan |
| April 2020 | Corporate Sponsorship Decision Package |
| April 2020 | Decision Package on City Owned Real Estate Disposition |
| October 2020 | Revenue Generation Decision Package |

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RECOMMENDATIONS

That the City Council receive updated information and have a discussion on the long-term fiscal management of the City's California Public Employees Retirement System unfunded pension obligations.

