ATTACHMENT 3:

CALPERS DISCOUNT RATE CHANGE AND RELATED ARTICLES

THE PUBLIC EYE JANUARY 21, 2017 1:17 PM

Local governments grapple with increasing pension costs before higher tab comes in 2018

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BY BRAD BRANAN
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In South Lake Tahoe, roads are crumbling, and the city is struggling to find ways to repair years of damage caused by harsh weather and snowplows. Orangevale residents worry that fire crews won't arrive quickly enough in an emergency after their local fire station was closed during the recession.

Despite an economic recovery, local government leaders in California say rising pension costs have made it more difficult to restore some programs they cut during the recession.

The Sacramento Metropolitan Fire District, for instance, expects to pay $34 million in retirement costs this year, a 26 percent jump from 10 years ago, accounting for inflation and excluding a big increase in employee contributions.

Metro Fire's main retirement plan is one of the 10 most expensive plans in the capital region, based on a ratio of annual pension costs to payroll for current employees. Those plans will cost local governments an average of 42 cents for every dollar in current employee salary costs next year, a 25 percent increase over two years ago, The Sacramento Bee found in a review of records for 26 of the largest local governments in Sacramento, El Dorado, Placer and Yolo counties participating in CalPERS.

Local govern … tirement system to for … on contributions … local governments, but expect them to exceed the increases of recent years.

Municipal finance expert Michael Coleman said the higher payments will force governments to continue a pattern that started in the recession, cutting services to pay pensions..

“This is going to be significant for many cities and it’s going to mean some tough decisions,” he said. “You may have cities that will make cuts that go way below their standards for services.”

The most expensive pension plans are typically for police and fire employees. Of the 10 plans with the highest rates in the region, eight are for police officers and firefighters, who can retire earlier and with more money than other government employees.

Of pension plans with more than 15 active employees, Folsom’s safety plan is the most expensive in the region, with a rate of 47 cents for every dollar in current payroll costs. The city has lost about 150 employees since the recession, down to 150, and pension costs are one reason for the cuts, said Finance Director Jim Francis.

A Metro Fire safety employee with 30 years of experience can retire at age 50 and make 90 percent of salary for life. The average annual pension for a Metro Fire retiree in the last five years was about $90.000, according to CalPERS.

Highest pension rates

Pension costs are rising and are expected to get higher. One way to express this is by comparing pension costs to payroll for current employees; current payroll is separate from a government’s pension contributions. Here are the 10 local plans with the highest such ratio:

Employer	Plan	Pension costs as a percentage of payroll 2014-15	2017-18
City of Folsom	Safety	37%	47%
City of Galt	Safety	39%	46%
City of Davis	Safety Fire	n/a	45%
Sac. Metropolitan Fire Dist.	Safety	36%	45%
City of Woodland	Safety	35%	43%
City of Davis	Safety Police	n/a	40%
City of Roseville	Safety	36%	40%
City of Sacramento	Safety	31%	39%
City of West Sacramento	Safety Fire Tier 1	28%	37%
City of South Lake Tahoe	Miscellaneous	29%	34%

Source: CalPERS Note: Excludes plans with ten or fewer employees. The Sacramento Bee

Local governments increased pension benefits after the state did the same for its employees in 1999. Investment returns have not met the projections used to support those increases, forcing CalPERS to raise rates for local and state governments to make sure it has enough money to pay benefits promised to retirees.

The recession created a double whammy for local governments because it lowered property tax revenue, one of their main income sources, at the same time it caused huge losses in the stock market. When investment returns suffer, local governments have to pay CalPERS additional money to ensure the retirement system remains sustainable.

Metro Fire faced the double whammy in 2009, when the agency decided to shutter three fire stations. In 2011, Metro Fire closed a four

Increased pe ... cial officer. She did not k

Station 33 on Main Avenue in Orangevale remains closed. Residents fear what that will mean should they have a fire or a heart attack.

“I worry about it all the time,” said Curtis Beldi, who lives next door to the station. “How much longer will it take for them to get to me?”

Around the corner, Sandie Mixa has similar concerns. She said neighbors with medical problems got a quick response when the station was open. No one wants to be the first to test Metro Fire’s response now, she said.

In 2015, Metro Fire reopened three of the four closed stations. Eric Bridge, deputy chief for operations, said the station’s relatively low number of calls meant the agency couldn’t justify the cost of reopening. The station responded to about 250 calls in the first six months of 2009 before it was closed.

Of the three reopened stations, only one has been returned to full service, with the other two providing only medical service 12 hours a day and no fire protection. Staffing has risen but is still 12 percent below pre-recession levels. Bridge said Metro Fire is operating at pre-recession service levels, although he said that it has not conducted a study of emergency response times since a consultant concluded in 2009 that the cuts would slow the agency’s responses.

Steve Maviglio, a spokesman for a union coalition that advocates for pensions, acknowledged that costs have risen, but said that almost all public sector workers are contributing higher amounts toward their retirement than before. He added that many government workers did not receive pay raises during the recession in exchange for protecting their retirement benefits.

Pension costs remain a big burden in South Lake Tahoe, said City Manager Nancy Kerry.

When the city took a big hit in revenues during the recession, it searched for ways to cut costs. South Lake Tahoe legally had to continue funding pensions, but services like road maintenance are essentially optional, so South Lake Tahoe deferred needed repairs for years, Kerry said.

Now the roads are in bad shape, especially because snow and snow plows cause greater deterioration, she said. Voters recently rejected a sales tax increase that would have helped pay for road improvements.

Kerry said state law prevents cities from renegotiating past benefit levels. “The reason none of the cities can manage the pension costs is because they can’t negotiate,” she said.

West Sacramento cut about a fourth of its more than 400 employees during the recession of the last decade, and increases in pension costs prevented the city from rehiring many of them when the economy returned, said Phil Wright, assistant city manager.

“Our rates go up every year - up, up, up,” he said. “It’s hard.”

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MORE THE PUB

Pension costs may crush city budgets

By Dennis Wyatt
Executive Editor
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POSTED February 25, 2017 1:14 a.m.

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Pension payments for the City of Manteca's municipal workforce is project to go up $13.6 million through 2025 eclipsing projected salary increases by 81 percent.

The somber news was delivered to the Manteca City Council during the mid-year budget review on Friday afternoon during a workshop at the Manteca Transit Center.

The increase in city payments to the California Public Employment Retirement System fund will go from $11.6 million in 2018 to $25.2 million in 2025. To give you an idea of the magnitude of that 117 percent increase in CalPERS payment the 2025 city bill is $10 million shy of the entire general fund budget of $35 million that is now in place to run the city during the current fiscal year.

Mayor Steve DeBrum has pushed hard for the city to put more emphasis on the impact of the unfunded PERS liability will have on Manteca. In past years it has been given just a passing mention in budget reviews and municipal budget workshops.

Manteca is not alone. Virtually every city, school district, and county in California as well as the state itself is facing massive increases in CalPERS contributions as the system deals with unfunded liability.

CalPERS now has a $139 billion shortfall with assets on hand to cover only 68 percent of their retirement obligations. It covers 62 cents of every dollar in actual pensions that are paid out with returns from investments, 25 cents from employer contributions, and 13 cents from workers paying into the retirement plan.

The pension fund's board in December voted to lower the anticipated rate of returns from investments from 7.5 percent to 7.0 percent. At it is ratcheted down — 7.375 percent in 2018-2019, 7.25 percent in 2019-2020, and 7 percent in 2020-2021 — it will send the city's required contributions higher.

"Everyone knows they really should have dropped it down to 6 percent," Councilman Richard Silverman noted as he pointed out CalPERS investments yielded just over 2 percent last year and not the projected 7.5 percent. The CalPERS board has basically said as much as members have commented the projected rate of return may have to be reduced further to either 6.5 percent or 6 percent.

Silverman said there are cities in California that are in "serious trouble" trying to figure how they will be able to pay new rates based on just the 7.35 percent return for 2018-2019 let alone the ultimate 7 percent target without cutting municipal services.

"Manteca is not one of them," Silverman added.

But while Manteca may be fine for the next two fiscal years, DeBrum as well as Finance Director Susan Mallory have warned that may not be the case farther down the road hence the impacts being projected out to 2025.

The $13.6 million jump over the next eight years may just be the tipped of the ice berg.

Manteca's unfunded CalPERS liability is expected to go from $89.4 million to $95 million.

Retirement is just one of the cost factors that contributed to employee benefits constituting 26 percent of the general fund budget. The city faces increasing health care costs for existing and retired municipal workers. Post-employment benefits for workers already retired are coming in at $1 million this year, up $50,000 from last year. The costs are primarily attributed to negotiated retirement healthcare plans.

Overall 77 percent of the general fund budget or $26.8 million goes to salaries and benefits.

The current fiscal year payroll for all city employees — including sewer, water, golf, and solid waste employees working in those enterprise fund municipal divisions that are supported by users fees and not taxes — comes to $32.7 million and CalPERS payments to $11.6 million. The payroll is projected to reach $40.2 million in 2025 while the CalPERS payments will hit $25.2 million.

Employees contribute to the retirement fund as well. Their share this year is $1.6 million. Based on the current contract it will be almost $2.1 million in 2025.

Cutting jobs, street repairs, library books to keep up with pension costs

Generous retirement benefits for public safety employees could help push the Bay Area city of Richmond into bankruptcy

By JUDY LIN

REPORTING FROM RICHMOND, CALIF. | FEB. 6, 2017

Richmond, a working-class city of 110,000 on the east shore of San Francisco Bay, has been struggling with the cost of employee retirement benefits. Pension-related expenses have risen from $25 million to $44 million annually in the last five years and could reach $70 million by 2021. (Robert Durell / CALmatters)

When the state auditor gauged the fiscal health of California cities in 2015, this port community on the eastern shore of San Francisco Bay made a short list of six distressed municipalities at risk of bankruptcy.

Richmond has cut about 200 jobs — roughly 20% of its workforce — since 2008. Its credit rating is at junk status. And in November, voters rejected a tax increase that city leaders had hoped would help close a chronic budget deficit.

“I don’t think there’s any chance we can avoid it,” said former City Councilman Vinay Pimple, referring to bankruptcy.

A major cause of Richmond’s problems: relentless growth in pension costs.

Payments for employee pensions, pension-related debt and retiree healthcare have climbed from $25 million to $44 million in the last five years, outpacing all other expenses.

By 2021, retirement expenses could exceed $70 million — 41% of the city’s general fund.

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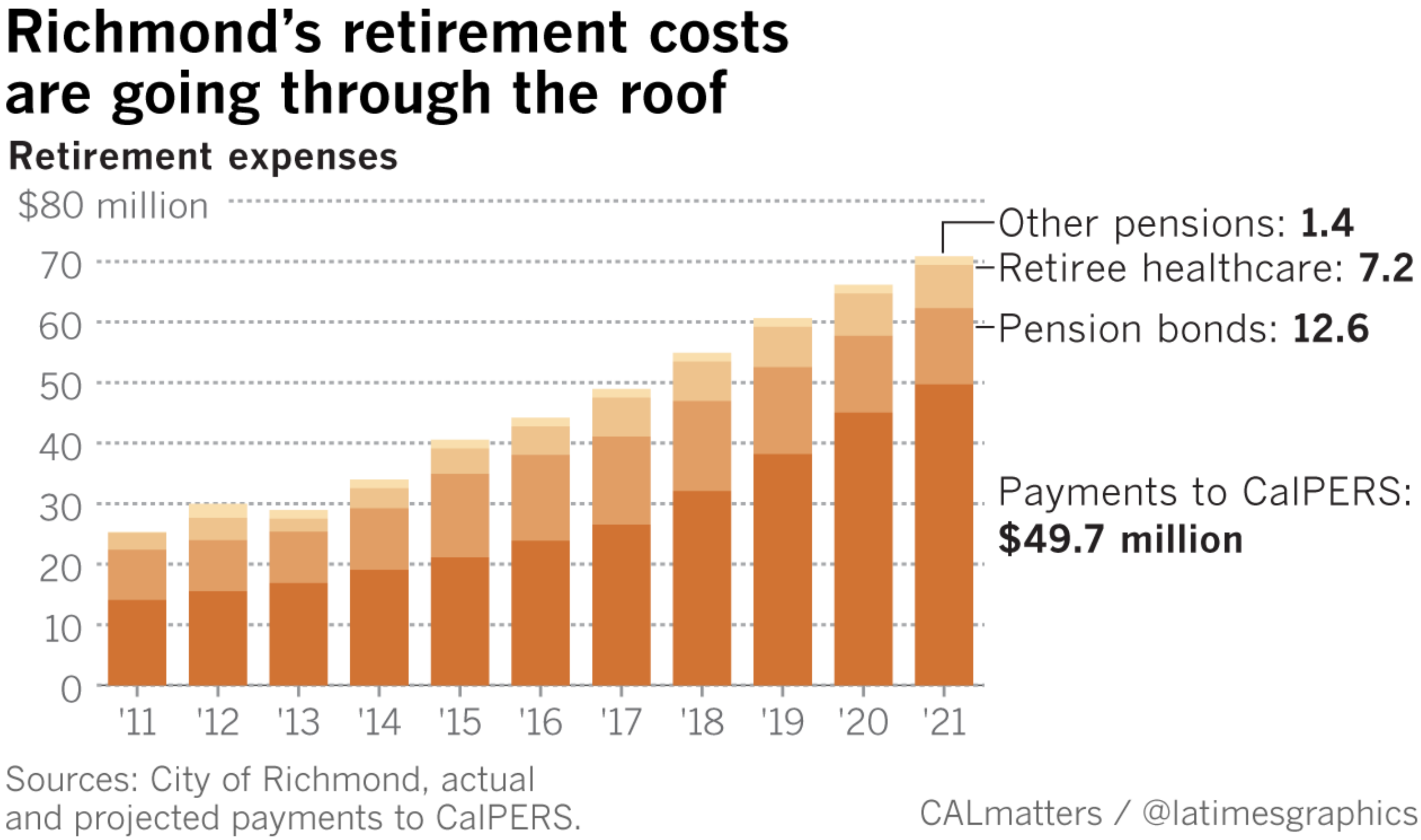
Richmond is a stark example of how pension costs are causing fiscal stress in cities across California. Four municipalities — Vallejo, Stockton, San Bernardino and Mammoth Lakes — have filed for bankruptcy (http://www.pbs.org/newshour/updates/municipalities-declared-bankruptcy/) protection since 2008. Others are on the brink.

“The truth is that there are cities all over the state that just aren’t owning up to all their problems,” said San Bernardino City Manager Mark Scott.

Increasingly, pension costs consume 15% or more (http://www.latimes.com/projects/la-me-pension-squeeze/) of big city budgets, crowding out basic services and leaving local governments more vulnerable than ever to the next economic downturn.



Richmond is a racially diverse, working-class city of 110,000 whose largest employer is a massive Chevron oil refinery. Like many California municipalities, Richmond dug a financial hole for itself by granting generous retirement benefits to police and firefighters on the assumption that pension fund investments would grow fast enough to cover the cost.

That optimism proved unfounded, and now the bill is coming due.

Richmond Makes Cuts To Services As Pension Costs For Public-Sector Workers Mount (http://www.capradio.org/articles/2017/02/06/richmond-makes-cuts-to-services-as-pension-costs-for-public-sector-workers-mount/)

Listen to a report by Capital Public Radio.

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Read the story (http://www.capradio.org/articles/2017/02/06/richmond-makes-cuts-to-services-as-pension-costs-for-public-sector-workers-mount/)

City Manager Bill Lindsay insists that Richmond can avoid going off a cliff. Last year, financial consultants mapped a path to stability for the city by 2021 — but at a considerable cost in public services.

The city cut 11 positions (http://www.mercurynews.com/2016/07/06/facing-prospect-of-further-credit-downgrade-richmond-passes-budget/), reduced after-school and senior classes, eliminated neighborhood clean-ups to tackle illegal trash dumping, and trimmed spending on new library books — saving $12 million total.

City officials also negotiated a four-year contract with firefighters that freezes salaries and requires firefighters to pay $4,800 a year each toward retirement healthcare. Until then, the benefit was fully funded by taxpayers.

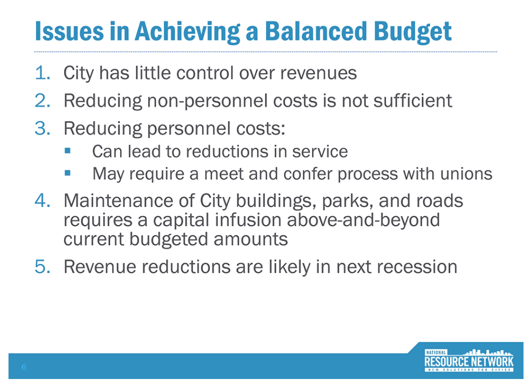
“I’ve seen some of my good friends go through it in Vallejo and Stockton, and what we found out during those [bankruptcies] is that your union contracts aren’t necessarily guaranteed,” said Jim Russey, president of Richmond Firefighters Local 188.

Richmond’s consultants said the city had to find $15 million (http://documents.latimes.com/richmond-five-year-budget-forecast-2016/) more in new revenue or budget cuts by 2021. Lindsay said the city has been looking hard for additional savings, and the police union recently agreed to have its members contribute toward retirement healthcare.

July 26, 2016

Tough sledding

Financial consultants with the National Resource Network spelled out the daunting challenges Richmond faces in righting its finances.



(http://documents.latimes.com/richmond-five-year-budget-forecast-2016/)

“If you look at the five-year forecast, with reasonable assumptions, even with the growth in pension cost, it does start to generate a surplus,” Lindsay said.

Joe Nation, a former Democratic state legislator who teaches public policy at Stanford’s Institute for Economic Policy Research, is not so sanguine. He reviewed Richmond’s retirement cost projections and said they leave little room to maneuver.

Over the next five years, every dollar the city collects in new revenue will go toward retirement costs, leaving little hope of restoring city services, Nation said.

“If there is an economic downturn of any kind, I can imagine that they could be pushed to the brink of bankruptcy, if not bankruptcy,” Nation said.

Last month, the California Public Employees' Retirement System (CalPERS), the state's main pension fund, lowered its projected rate of return on investments from 7.5% to 7% per year. That means Richmond and other communities will have to pay more (http://documents.latimes.com/calpers-circular-letter/) each year to fund current and future pension benefits.

Dec. 21, 2016

Lower returns, higher cost

CalPERS told local governments it was lowering its projected rate of return on investments. That means taxpayers will have to pay more to fund retirement benefits.

To: **All Public Agency Employers**

Subject: **Discount Rate Change**

The purpose of this Circular Letter is to inform you of recent changes to the CalPERS discount rate assumption and the impact these changes are expected to have on required employer and PEPRA member contributions. This Circular Letter will assist you in calculating projected pension cost increases in future years. The June 30, 2016, annual valuations will provide updated projections of expected future year pension contributions. These reports will be available this summer.

At the December 21, 2016, meeting, the CalPERS Board of Administration approved lowering the CalPERS discount rate assumption, the long-term rate of return, from 7.50 percent to 7.00 percent over the next three years. This will increase public agency employer contribution costs beginning in Fiscal Year 2018-19.

(http://documents.latimes.com/calpers-circular-letter/)

The change is expected to increase local government pension payments by at least 20% starting in 2018, according to CalPERS spokeswoman Amy Morgan.

An analysis by the nonprofit news organization CALmatters indicates that Richmond's retirement-related expenses could grow to more than $70 million per year by 2021. That represents 41% of a projected $174-million general fund budget.

Lindsay said the city's estimates of future pension costs are lower because of different assumptions about salary increases and other costs.

The city of Richmond's pension-related budget problems have taken a toll on public services, including street repair. (Robert Durell / CALmatters)

Voters approved a sales tax increase in 2014 to help stabilize the city's finances. But in November, voters rejected an increase in the property transfer tax (http://www.ci.richmond.ca.us/DocumentCenter/View/39147) that was expected to bring in an additional $4 million to $6 million annually.

Lindsay said the city was never counting on the property transfer tax in its 5-year plan. If the city needed more cash, he says Richmond has properties it can sell.

“Budget management is much more difficult in Richmond than in Beverly Hills, but you still manage it,” Lindsay said. “To say it’s spiraling out of control into bankruptcy does incredible damage to our community and it’s just not accurate.”

Richmond is especially hard hit by personnel costs because of high salaries for public employees. The city’s average salary of $92,000 (http://publicpay.ca.gov/Reports/Cities/Cities.aspx) for its 938 employees was fifth highest in California as of 2015, according to the state controller. The city’s median household income is $54,857.

Police officers and firefighters in Richmond make more than $137,000 (https://www.calpers.ca.gov/docs/actuarial-reports/2015/richmond-city-safety-2015.pdf) per year on average, compared with an average $128,000 per year for Berkeley police (https://www.calpers.ca.gov/docs/actuarial-reports/2015/berkeley-city-safety-police-2015.pdf) and firefighters (https://www.calpers.ca.gov/docs/actuarial-reports/2015/berkeley-city-safety-fire-2015.pdf), where housing prices are more than 60% higher than in Richmond.

Public safety salaries averaged $115,000 (https://www.calpers.ca.gov/docs/actuarial-reports/2015/oakland-city-safety-2015.pdf) in Oakland and $112,000 (https://www.calpers.ca.gov/docs/actuarial-reports/2015/vallejo-city-safety-2015.pdf) in Vallejo.

Mayor Tom Butt says of Richmond's pension-related financial problems: "It's a huge mess … One of these days, it's just going to come crashing down." (Robert Durell / CALmatters)

Richmond Mayor Tom Butt, an architect and general contractor who has served on the city council for two decades, says the city that was once among the state's most dangerous has little choice but to pay higher salaries to compete for employees with nearby communities that are safer and more affluent.

"You can't convince anyone here that they deserve less than anybody in any other city," Butt said.

Lindsay said the decision to offer higher salaries for public safety employees was strategic.

"The city council made a conscious decision to put a lot into public safety, in particular reducing violent crime. And largely, we've been successful," Lindsay said.

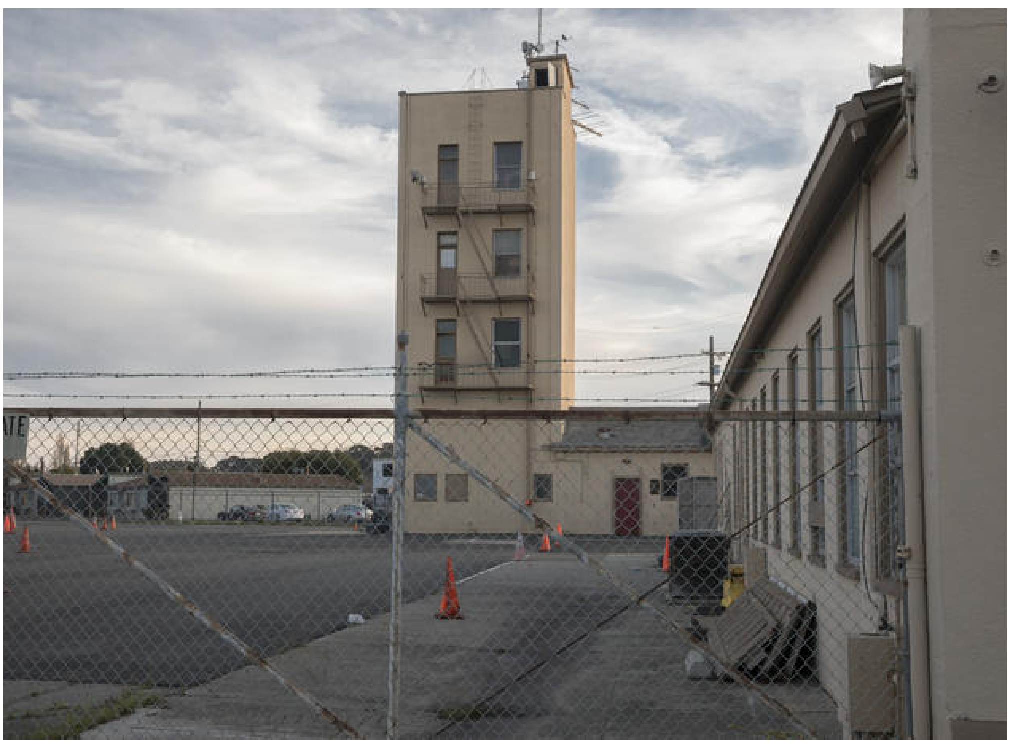
Violent crimes have been declining in the city over the past decade with homicides dropping to a low of 11 in 2014. But Richmond is experiencing an uptick, recording 24 homicides in 2016, according to the police department.

Part of the challenge with public safety costs dates to 1999, when Richmond, like many local governments, matched the state's decision to sweeten retirement benefits for California Highway Patrol Officers.

CHP officers could retire as early as 50 with 3% of salary for each year of service, providing up to 90% of their peak salaries in retirement. Other police departments soon demanded and got similar treatment.

Richmond firefighters are eligible to retire at age 55 with 3% of salary for each year of service. Recent hires will have to work longer to qualify for a less generous formula under legislation passed in 2013.

Richmond's actuarial pension report (https://www.calpers.ca.gov/docs/actuarial-reports/2015/richmond-city-safety-2015.pdf) shows there are nearly two retirees for every police officer or firefighter currently on the job.



To cope with severe budgetary pressures, the city of Richmond put this Fire Department training facility up for sale. (Robert Durell / CALmatters)

In a way, Richmond is a preview of what California cities face in the years ahead. According to CalPERS (https://www.calpers.ca.gov/docs/board-agendas/201609/financeadmin/item-8c-01.pdf), there were two active workers for every retiree in its system in 2001. Today, there are 1.3 workers for each retiree. In the next 10 or 20 years, there will be as few as 0.6 workers for each retiree collecting a pension.

Because benefits have already been promised to today's workers and retirees, cuts in pension benefits for new employees do little to ease the immediate burden. It "means decades before the full burden of this will be completely dealt with," said Phil Batchelor, former Contra Costa County administrator and former interim city manager for Richmond.

Today, Richmond's taxpayers are spending more to make up for underperforming pension investments. CalPERS projects that the city's payments for unfunded pension liabilities will more than double in the next five years, from $11.2 million to $26.8 million.

Now, the lower assumed rate of investment return is projected to add nearly $9 million to Richmond's costs by 2021.

"It's a huge mess," said Mayor Butt. "I don't know how it's going to get resolved. One of these days, it's just going to come crashing down."

Judy Lin is a reporter at CALmatters, a nonprofit journalism venture in Sacramento covering state policy and politics.

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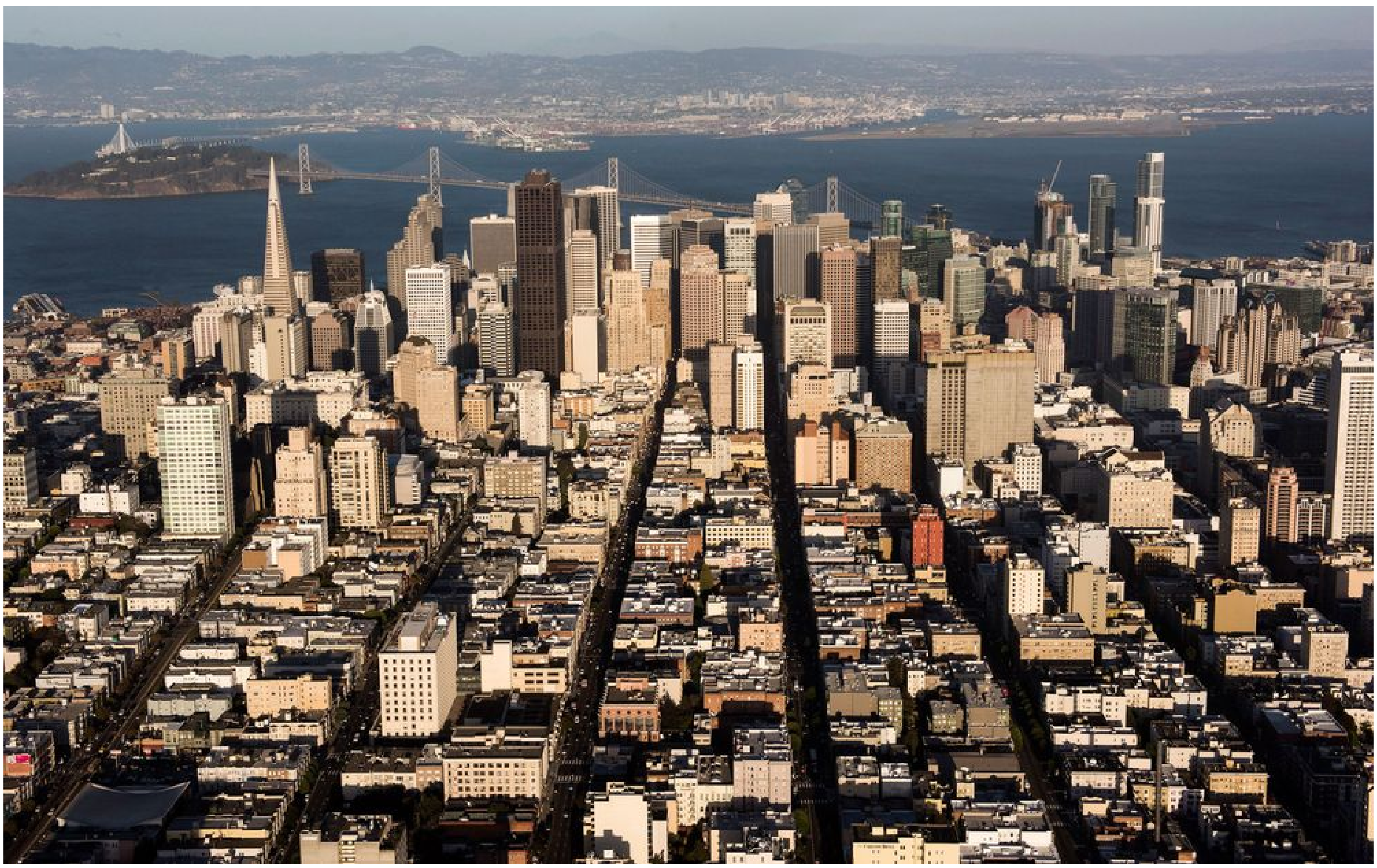
Additional credits: Sean Greene

Even San Francisco, Flush With Tech Wealth, Has Pension Problems

by **Romy Varghese**
March 20, 2017, 2:00 AM PDT

- Pension cost to rise more than three times faster than revenue
- With retirees living longer, pension shortfall has swelled



The skyline of downtown San Francisco. *Photographer: David Paul Morris/Bloomberg*

The technology industry has transformed San Francisco <https://www.bloomberg.com/quote/8785Z:US> with a boom other cities can only envy. But it hasn't eradicated a problem well known to industrial-era towns: the rising cost of pensions.

The city, where the unemployment rate is just 3.2 percent and the typical home sells for more than $1 million, is facing a budget shortfall that will reach $848 million in five years. Increases in pension payments and other payroll costs are driving the gap, according to a five-year financial plan <http://sfcontroller.org/sites/default/files/Documents/Budget/Five%20Year%20Financial%20Plan%20FY17-18%20through%20FY21-22%20%28Proposed%29%20FINAL.pdf> , despite a measure voters approved in 2011 that aimed to cut employee-retirement bills.

San Francisco officials, who will present an updated fiscal blueprint this week, say they can adjust spending to balance their books, as well as gird for cuts the federal government may implement. Yet the predicament, even in a city known for stratospheric wealth, underscores the financial challenge for states and cities around the country that have to make good on promises to police officers, teachers and other civil servants.

"I do think there will be another conversation in the not too distant future about what is affordable for the city and our employees for pensions," said Controller Ben Rosenfield. "I don’t think where we are is where we need to end up."

For some cities without San Francisco’s prodigious tax base, however, reforms alone aren’t enough. State and local governments have about $2 trillion less than what they need to cover retirement benefits because of investment losses, inadequate contributions and perks granted in boom times. And in California, over the next few years, there will be "a rash of local agencies unable to meet their pension obligations," said Dane Hutchings, a lobbyist for the League of California Cities.

San Francisco’s net pension liability -- a key measure of how much retirement benefits exceed the assets set aside to cover them -- more than doubled to $5.5 billion in the year ended in June due to lagging investment returns and an update to assumptions, including longer lifespans for retirees. In addition, the city lost a court case and must now pay some cost of living adjustments to retirees it was trying to limit because of the measure that voters approved.

Contributions to the San Francisco Employees’ Retirement System <https://www.bloomberg.com/quote/0617478D:US> will increase 36 percent by 2022, more than three times faster than the city’s revenue, according to the five-year plan. The general-fund budget this year is $4.9 billion.

"These costs will continue to be a significant budgetary challenge for the foreseeable future," wrote analysts in March at S&P Global Ratings, which grades the city at AA+, the second-highest rank.

This is occurring even after voters more than five years ago approved several measures that sought to curb the growth in retirement expenses, such as requiring employee contributions that go higher based on the city's share and limiting what's included in pension calculations to hold down the payouts.

The budget shortfalls are also a result of how city officials have decided to spend the money flooding in. With a burgeoning population, San Francisco turned to restoring and expanding programs. Voters weighed in through ballot measures to mandate spending for groups such as seniors and children. The city has hired 4,519 more workers since fiscal 2011, a 17 percent increase in its payrolls.

It's plowed more money into repairing its facilities and renovating streets, the controller said. Municipal workers responded to 97 percent of pothole repair requests in 72 hours last year, according to a city scorecard <http://sfgov.org/scorecards/livability> .

"We're definitely a service-rich government," Rosenfield said.

Mayor Ed Lee recognizes the need to address the rising retirement costs, said Melissa Whitehouse, budget director.

"It's very important to him to make sure our fiscal house is in order when he leaves office," she said.

Calpers May Cut Return Target Again, California's Brown Says

by **Romy Varghese**
March 2, 2017, 2:13 PM PST
Updated on March 2, 2017, 3:43 PM PST

- Pension lowered rate to 7 percent from 7.5 percent in Dec.
- Cities are hit harder by rising pension costs, Brown says

California Governor Jerry Brown said the state's retirement system is "probably" going to lower its investment-return goal again, a move that will further pressure local governments already straining under rising pension costs.

The California Public Employees' Retirement System <https://www.bloomberg.com/quote/3261Z:US> decided in December to lower its assumed rate of return to 7 percent from 7.50 percent over three years, which means higher contributions to make up the difference.

"All that imposes greater costs on local and state government," Brown said during an interview in his Sacramento office. "The pressure will mount."

Across the country, state and local governments have about $2 trillion less than what they need to cover retirement benefits -- the result of investment losses, inadequate contributions and perks granted in boom times. The problem is acute in California, where it helped bankrupt the cities of Stockton, San Bernardino and Vallejo.

In California, local governments are under more pressure than the state because a greater share of their budgets are consumed by payroll, Brown said. The contributions to Calpers by the state government alone have nearly doubled in five years.

"The pensions are squeezing local government more than state government," he said.

"We are focused on a comprehensive review of our assets and liabilities this year while concentrating on implementing the changes to the discount rate the Calpers board adopted in December," Calpers spokeswoman Amy Morgan said by email. "No decision has been made."