12/11/18

5:00pm
Study Session
Item #3

Presentation and Discussion on City Retirement Costs

December 11, 2018

Total Compensation Overview

Total Compensation generally consists of four primary elements:

1. Salary – compensation paid to an employee
2. Insurance – Medical, Dental, Vision, VEBA, Life Insurance
3. Retirement – CalPERs and Social Security
4. Other Benefits – Medicare, Employee Assistance Program (EAP), Long-term Disability

Note: May differ based on negotiated MOU

2

POST MEETING MATERIAL

Components of CalPERs Pension Costs

The minimum required employer contribution includes the sum of two components:

1. **Employer Normal Rate** – the annual cost for the fiscal year for active employees' pension. This is shown as a percentage of payroll and is paid as part of the payroll reporting process
   - FY 19/20 Safety Rate – 20.877%
   - FY 19/20 Miscellaneous Rate – 10.667%
2. **Employer Amortization of Unfunded Accrued Liability (UAL)** – a fixed dollar amount needed to fully fund past service credit earned by current and former employees. The UAL is billed monthly to the City or can be paid in a lump sum.
   - FY 19/20 Safety Cost – $16.6 million
   - FY 19/20 Miscellaneous Cost - $20.2 million

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Components of CalPERs Pension Costs

- **Employee Rate** – employee's share of pension costs
  - Safety Rate – 9%
    - Police Safety Classic members pay an additional cost sharing rate of 2.25%
  - Miscellaneous Rate – 8%
- **PEPRA** – California Public Employees' Pension Reform Act of 2013
  - FY 19/20 Safety Rate – 10.50%
  - FY 19/20 Miscellaneous Rate – 6.50%

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The Center of What's Possible

PERSable Wages

- Normal rate of pay
- Not all compensation is "PERSable" - generally excludes:
  - Overtime
  - Bonuses or one-time payments
  - Leave payouts

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City of Santa Clara
The Center of What's Possible

Pension Trends

- Significant year over year increases of contribution rates both in the past and future
- Unfunded liability increasing
- Pension costs rising due to actuarial methodology changes, demographic assumption changes, de-risking policies
- CalPERS investment returns have large fluctuations

6

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Unfunded Accrued Liability (UAL)

- Cost of benefits provided by employer but not yet fully funded
- Current unfunded liability totals more than $500 million
- Changes each year dependent on investment returns and CalPERS Board changes to actuarial methodology changes, demographic assumption, de-risking policies

7

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Fiscal Planning

- As a current practice, City contracts with Bartel to do an analysis of the CalPERS actuarial report to advise on the fiscal impact
- CalPERS reports come out each year and provide two years of projections
- Bartel projects long term rates
- City incorporates Bartel projections into the 10 year financial forecast

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City of Santa Clara
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Pension Cost – Forecasted Impacts

- Large increases in projected contributions
- With FY 2019/20 Preliminary Forecast
  - Change in methodology funding of UAL from percentage to fixed dollar to create budgetary savings
  - UAL Dollar increase $2.4m Safety, $2.6 Misc from 18/19
- 10-Year Impact - FY 2029/30 UAL contribution
  - Safety UAL $32.2m up 94% from 19/20
  - Misc UAL $31.7m up 57% from 19/20

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City of Santa Clara
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Bartel Associates, LLC Presentation

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CITY OF SANTA CLARA
MISCELLANEOUS & SAFETY PLANS

BARTEL ASSOCIATES, LLC

CalPERS Actuarial Issues – 6/30/17 Valuation
Final Results

John Bartel, President
Bianca Lin, Assistant Vice President
Kevin Yang, Actuarial Analyst
Bartel Associates, LLC

December 11, 2018

Agenda

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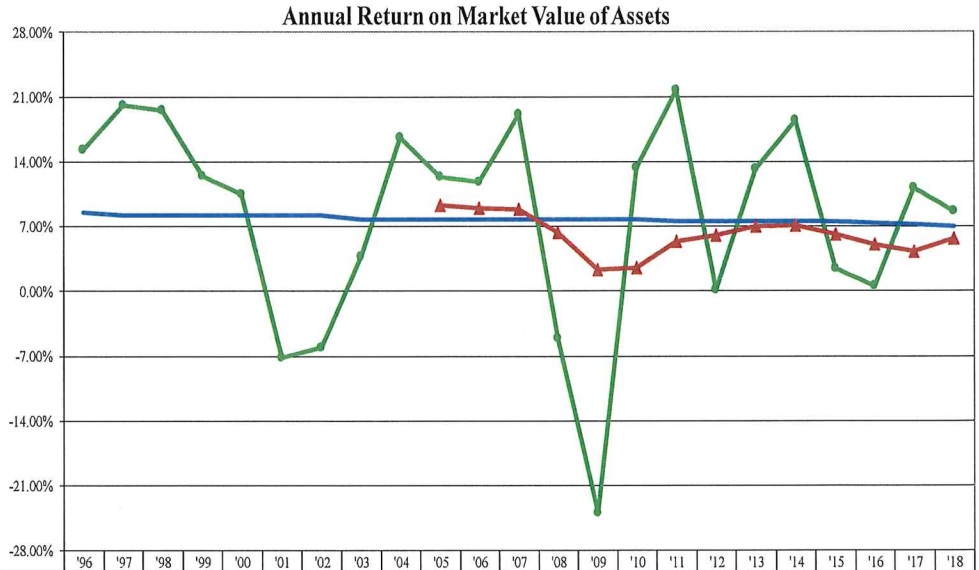
How We Got Here

- Investment Losses
- CalPERS Contribution Policy
- Enhanced Benefits
- Demographics

How We Got Here – Investment Return



	'96	'97	'98	'99	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11	'12	'13	'14	'15	'16	'17	'18
MVA	15.3%	20.1%	19.5%	12.3%	10.5%	-7.2%	-6.1%	3.7%	16.6%	12.3%	11.8%	19.1%	-5.1%	-24.0%	13.3%	21.7%	0.1%	13.2%	18.4%	2.4%	0.6%	11.2%	8.6%
Discount Rate	8.50%	8.25%	8.25%	8.25%	8.25%	8.25%	8.25%	7.75%	7.75%	7.75%	7.75%	7.75%	7.75%	7.75%	7.75%	7.50%	7.50%	7.50%	7.50%	7.50%	7.375%	7.25%	7.00%
10-Year Rolling Average										9.3%	9.0%	8.9%	6.4%	2.3%	2.6%	5.4%	6.1%	7.0%	7.2%	6.2%	5.1%	4.3%	5.8%

Above assumes contributions, payments, etc. received evenly throughout year.

How We Got Here – Old Contribution Policy

- Effective with 2003 valuations:
  - Slow (15 year) recognition of investment losses into funded status
  - Rolling 30 year amortization of all (primarily investment) losses

- Designed to:
  - First smooth rates and
  - Second pay off UAL

- Mitigated contribution volatility

How We Got Here – Enhanced Benefits

- At CalPERS, Enhanced Benefits implemented using all (future & prior) service

- Typically not negotiated with cost sharing

City of Santa Clara	Tier 1	Tier 2	PEPRA
Miscellaneous	2.7%@55 FAE1	N/A	2%@62 FAE3
Safety Police	3%@50 FAE1	N/A	2.7%@57 FAE3
Safety Fire	3%@50 FAE3	N/A	2.7%@57 FAE3

- Note:
  - FAE1 is highest one year (typically final) average earnings
  - FAE3 is highest three years (typically final three) average earnings

How We Got Here – Demographic

- Around the State
  - Large retiree liability compared to actives
    - State average: 55% for Miscellaneous, 65% for Safety
  - Declining active population and increasing number of retirees
  - Higher percentage of retiree liability increases contribution volatility

- City of Santa Clara percentage of liability belonging to retirees:
  - Miscellaneous 64%
  - Safety 71%

How We Got Here – Demographic

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CalPERS Changes

- Contribution policy changes:
  - No asset smoothing
  - No rolling amortization
  - 5-year ramp up
  - Included in 6/30/13 valuation (first impact 15/16 rates; full impact 19/20)
- Assumption changes:
  - Anticipate future mortality improvement
  - Other, less significant, changes
  - Included in 6/30/14 valuation (first impact 16/17 rates; full impact 20/21)
- CalPERS Board changed their discount rate:

	Rate	Initial	Full
6/30/16 valuation	7.375%	18/19	22/23
6/30/17 valuation	7.25%	19/20	23/24
6/30/18 valuation	7.00%	20/21	24/25

- December 2018: CalPERS Board selected asset allocation similar to current portfolio. No change to the discount rate.

CalPERS Changes

- Risk Mitigation Strategy
  - Move to more conservative investments over time
  - Only when investment return is better than expected
  - Lower discount rate in concert
  - Essentially use ≈50% of investment gains to pay for cost increases
  - Likely get to 6.0% over 20+ years
  - Risk mitigation suspended until 6/30/18 valuation
- February 2018 CalPERS adopted new amortization policy
  - Applies only to newly established amortization bases
    - Fixed dollar amortization rather than % pay
    - Amortize gains/losses over 20 rather than 30 years
    - 5-year ramp up (not down) for investment gains and losses
    - No ramp up/down for other amortization bases
  - Minimizes total interest paid over time and pays off UAL faster
  - Effective June 30, 2019 valuation for 2021/22 contributions

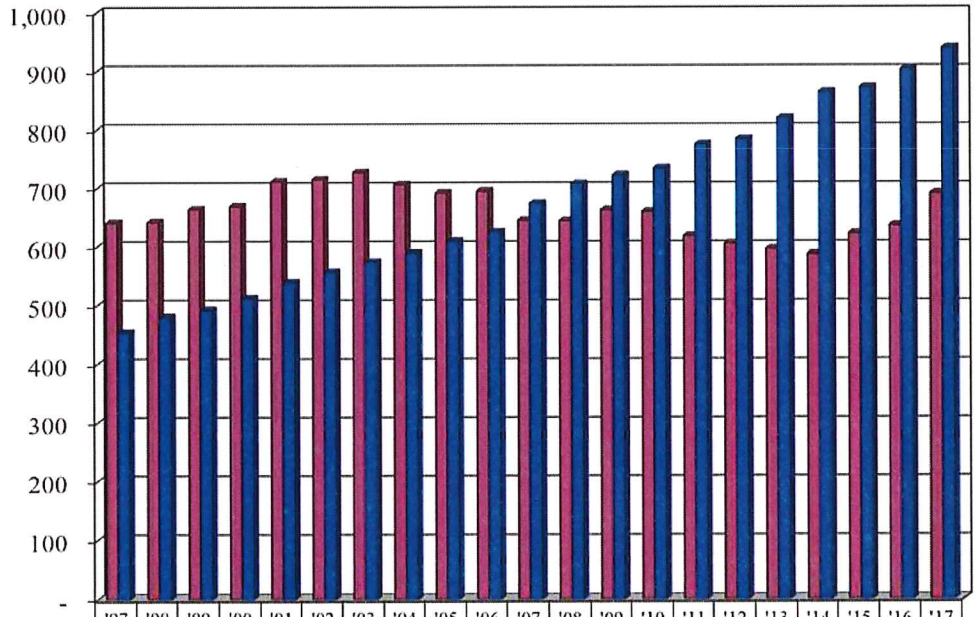
  Included in this study

SUMMARY OF DEMOGRAPHIC INFORMATION - MISCELLANEOUS

	1997	2007	2016	2017
Actives				
■ Counts	641	645	636	691
■ Average				
• Age	45	47	46	45
• City Service	11	13	12	10
• PERSable Wages	$ 55,500	$ 79,300	$ 98,400	$ 102,100
■ Total PERSable Wages	39,700,000	56,300,000	68,400,000	76,800,000
Inactive Members				
■ Counts				
• Transferred	118	204	223	217
• Separated	66	147	185	205
• Retired				
□ Service		517	737	771
□ Disability		61	63	62
□ Beneficiaries		96	103	106
□ Total	454	674	903	939
■ Average Annual City Provided Benefit for Service Retirees[1]	N/A	$ 26,400	$ 42,100	$ 43,100
■ Active / Retiree Ratio (City)	1.5	1.0	0.7	0.7
■ Active / Retiree Ratio (All CalPERS)	N/A	1.7	1.3	1.3

[1] Average City-provided pensions are based on City service & City benefit formula, and are not representative of benefits for long-service employees.

SUMMARY OF DEMOGRAPHIC INFORMATION - MISCELLANEOUS

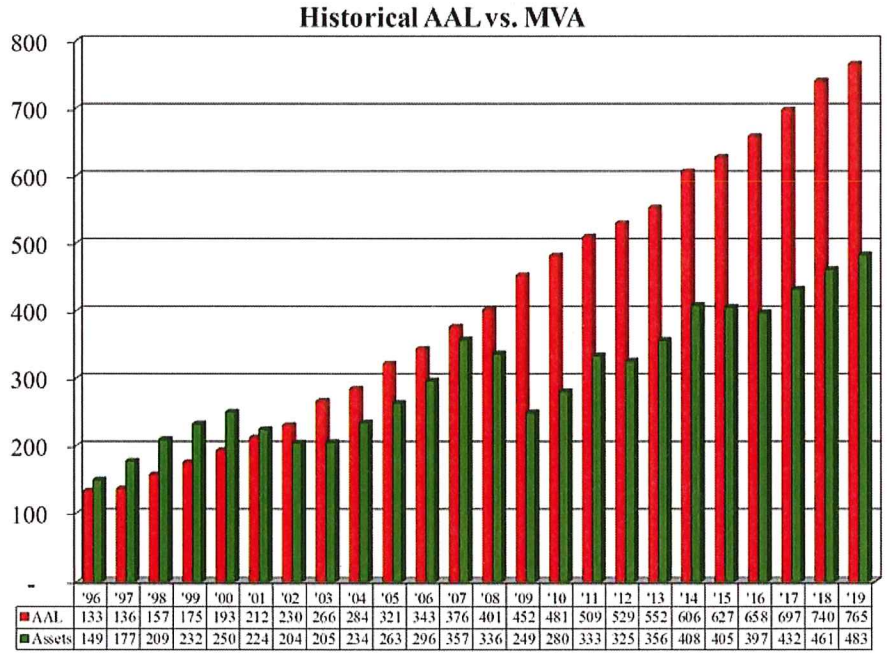


	'97	'98	'99	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11	'12	'13	'14	'15	'16	'17
Active	641	642	664	669	711	715	727	706	692	695	645	644	663	660	618	605	596	587	622	636	691
Receiving Payments	454	480	492	512	539	557	574	589	609	625	674	707	722	734	775	784	819	864	872	903	939

PLAN FUNDED STATUS - MISCELLANEOUS

	June 30, 2016	June 30, 2017
Active AAL	$ 216,100,000	$ 222,300,000
Retiree AAL	417,800,000	449,600,000
Inactive AAL	23,600,000	25,300,000
Total AAL	657,500,000	697,200,000
Assets	396,900,000	432,100,000
Unfunded Liability	260,600,000	265,100,000
Funded Ratio	60.4%	62.0%

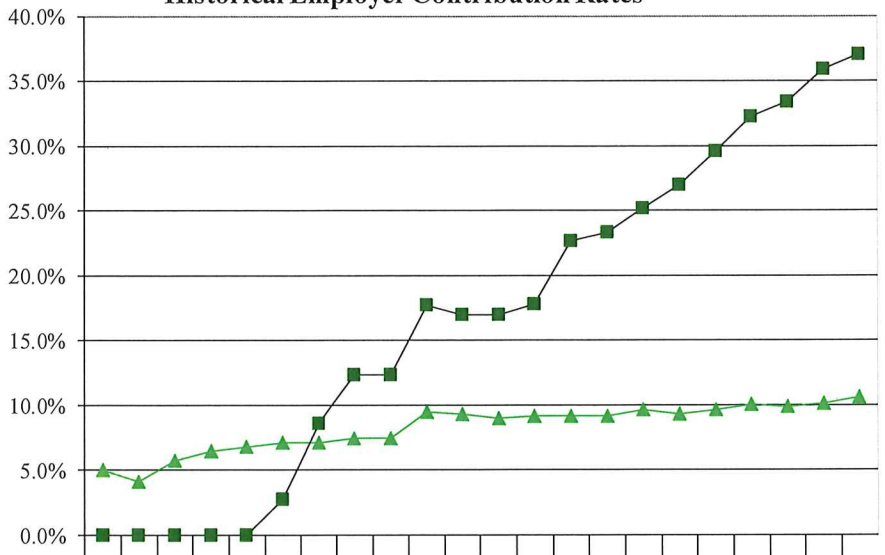
FUNDED STATUS (MILLIONS) - MISCELLANEOUS



6/30/18 & 6/30/19 funded status estimated

CONTRIBUTION RATES - MISCELLANEOUS

Historical Employer Contribution Rates



	98/99	99/00	00/01	01/02	02/03	03/04	04/05	05/06	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14	14/15	15/16	16/17	17/18	18/19	19/20
Normal Cost	5.0	4.2	5.7	6.5	6.8	7.2	7.2	7.5	7.5	9.5	9.4	9.0	9.2	9.2	9.2	9.6	9.3	9.7	10.1	9.9	10.2	10.7
Total Rate	0.0	0.0	0.0	0.0	0.0	2.8	8.6	12.3	12.3	17.7	17.0	17.0	17.8	22.7	23.3	25.2	27.0	29.6	32.3	33.4	35.9	37.0

CONTRIBUTION RATES - MISCELLANEOUS

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CONTRIBUTION PROJECTIONS - MISCELLANEOUS

- Investment Return:
  - June 30, 2018 8.6%[2]
  - Future returns based on stochastic analysis using 1,000 trials[3]

	25th Percentile	50th Percentile	75th Percentile
Current Investment Mix	**0.1%**	**7.0%**	**14.8%**
Ultimate Investment Mix	**0.8%**	**6.0%**	**11.4%**

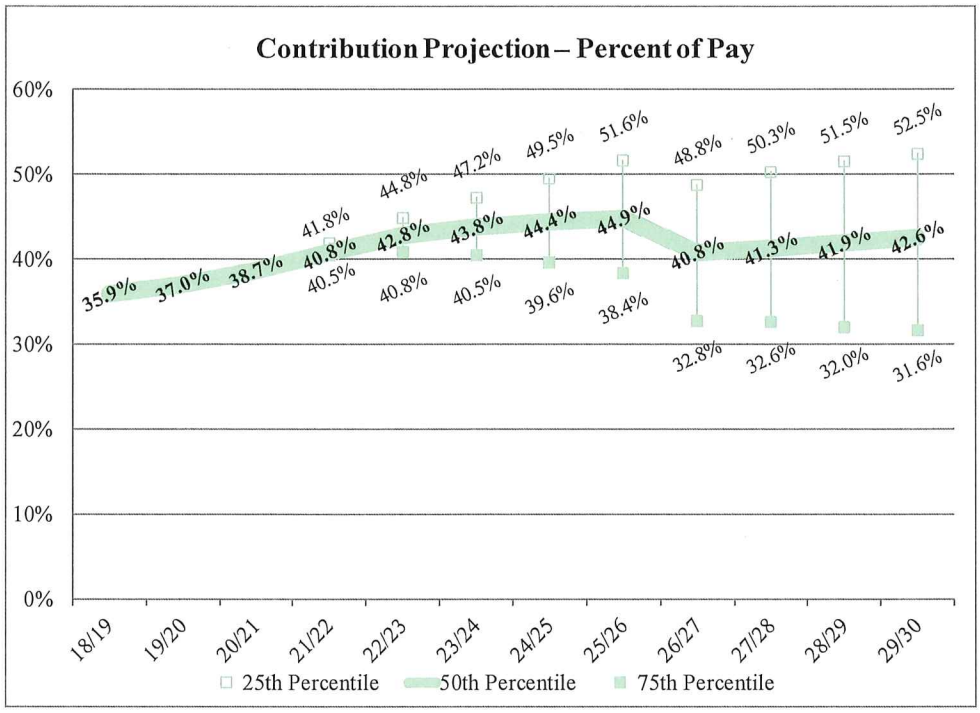
  - Assumes investment returns will generally be 6.5% (as compared to 7.0%) over the next 10 years and higher beyond that.
- Assumption Changes – Discount Rate
  - Decrease to 7.0% by June 30, 2018 valuation
  - Additional Discount Rate decreases due to Risk Mitigation policy.
- No Other: Gains/Losses, Method/Assumption Changes, Benefit Improvements
- Different from CalPERS projection

[2] based July 2018 CalPERS press release
[3] Nth percentile means N percentage of our trials result in returns lower than the indicated rates.

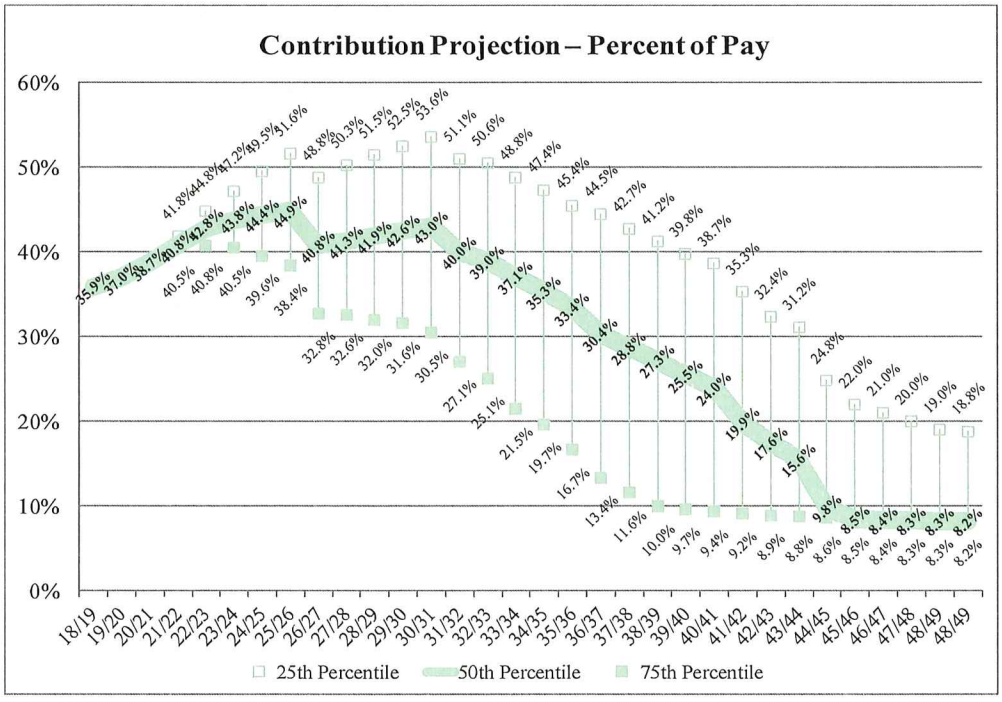
CONTRIBUTION PROJECTIONS - MISCELLANEOUS

- New hire assumptions:
  - 62.5% of 2018/19 hires are PEPRA members and 37.5% are Classic members
  - Percentage of PEPRA member future hires to increase from 62.5% to 100% over 15 years

CONTRIBUTION PROJECTIONS - MISCELLANEOUS



CONTRIBUTION PROJECTIONS - MISCELLANEOUS



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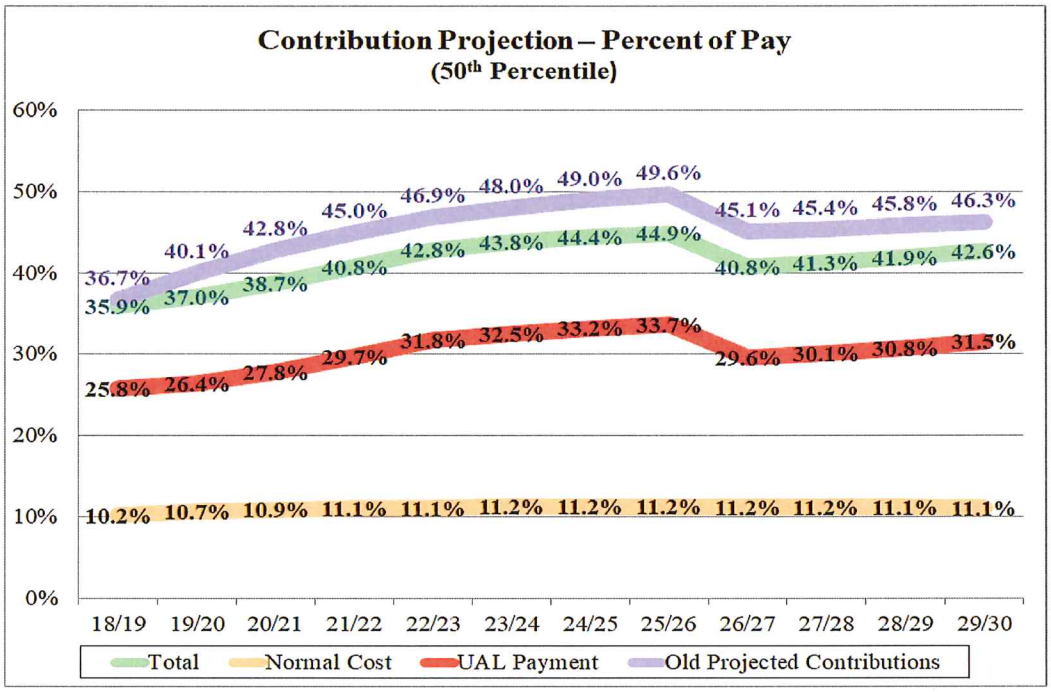
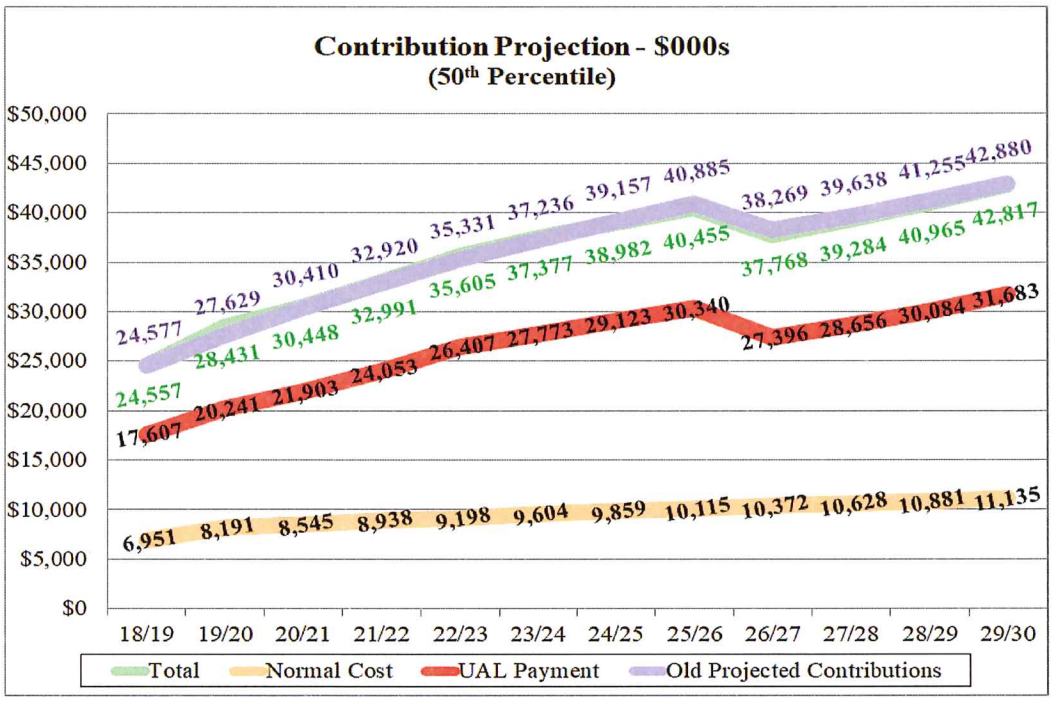


CONTRIBUTION PROJECTIONS - MISCELLANEOUS

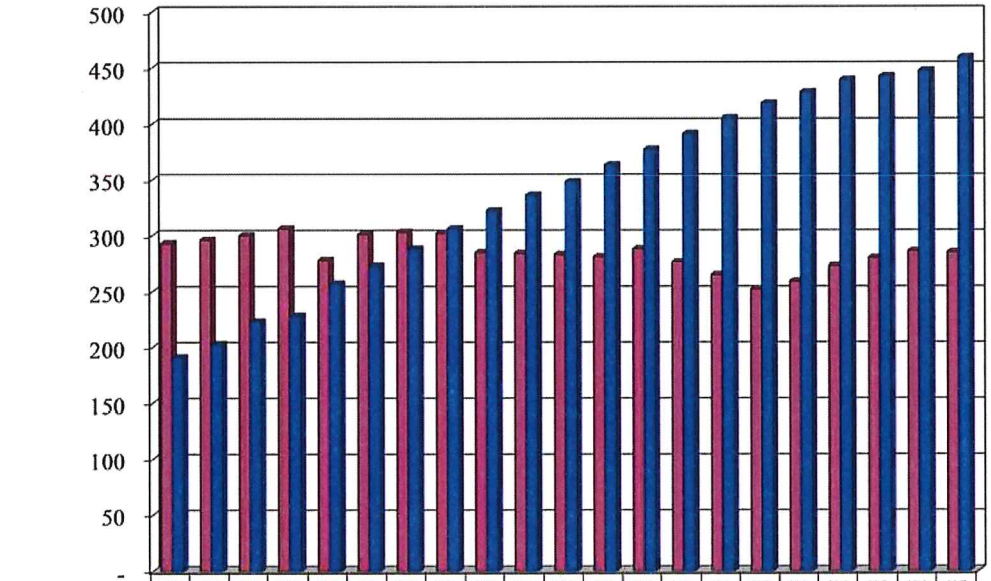


SUMMARY OF DEMOGRAPHIC INFORMATION - SAFETY

	1997	2007	2016	2017
Actives				
■ Counts	293	283	286	285
■ Average				
• Age	42	41	41	41
• City Service	14	13	11	12
• PERSable Wages	$ 82,400	$ 126,200	$ 144,800	$ 157,800
■ Total PERSable Wages	27,000,000	39,300,000	45,300,000	49,000,000
Inactive Members				
■ Counts				
• Transferred	11	31	28	30
• Separated	13	16	29	29
• Retired				
□ Service		183	253	259
□ Disability		123	139	141
□ Beneficiaries		42	55	59
□ Total	191	348	447	459
■ Average Annual City Provided Benefit for Service Retirees[4]	N/A	40,500	94,600	95,400
■ Active / Retiree Ratio (City)	1.5	0.8	0.6	0.6
■ Active / Retiree Ratio (All CalPERS)	N/A	1.7	1.3	1.3

[4] Average City-provided pensions are based on City service & City benefit formula, and are not representative of benefits for long-service employees.

SUMMARY OF DEMOGRAPHIC INFORMATION - SAFETY

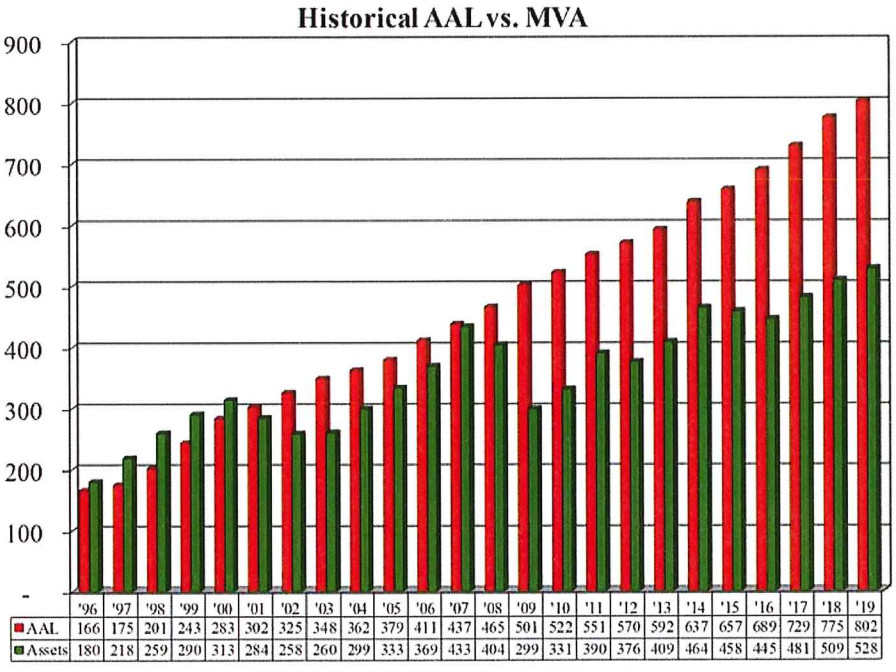


	'97	'98	'99	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11	'12	'13	'14	'15	'16	'17
■ Active	293	296	300	306	278	301	303	302	285	284	283	281	288	276	265	252	259	273	280	286	285
■ Receiving Payments	191	203	223	228	257	273	288	306	322	336	348	363	377	391	405	418	428	439	442	447	459

PLAN FUNDED STATUS - SAFETY

	June 30, 2016	June 30, 2017
Active AAL	$ 187,100,000	$ 206,400,000
Retiree AAL	495,000,000	516,600,000
Inactive AAL	6,800,000	5,600,000
Total AAL	688,900,000	728,600,000
Assets	445,000,000	481,000,000
Unfunded Liability	243,900,000	247,600,000
Funded Ratio	64.6%	66.0%

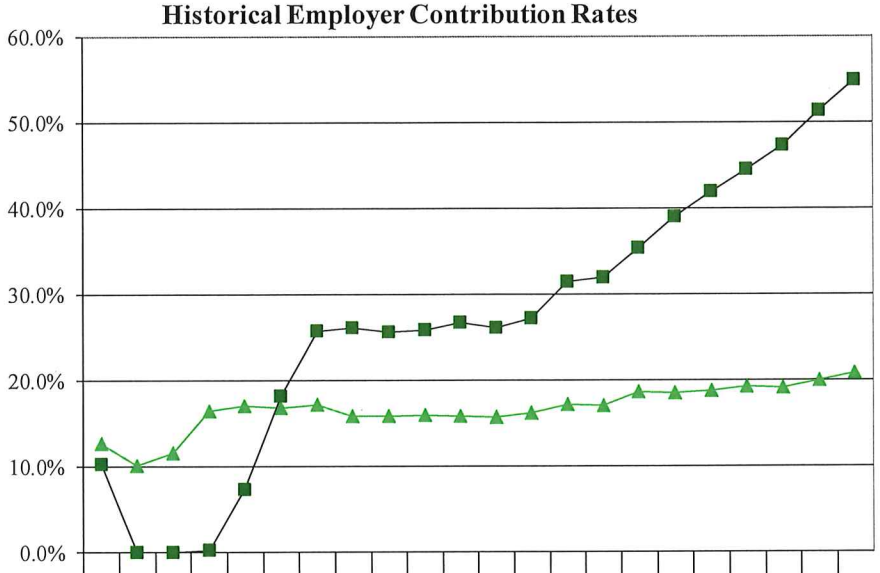
FUNDED STATUS (MILLIONS) - SAFETY



6/30/18 & 6/30/19 funded status estimated

CONTRIBUTION RATES - SAFETY

Historical Employer Contribution Rates



	98/99	99/00	00/01	01/02	02/03	03/04	04/05	05/06	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14	14/15	15/16	16/17	17/18	18/19	19/20
Normal Cost	12.7	10.1	11.6	16.4	17.1	16.8	17.2	15.8	15.9	15.9	15.9	15.8	16.1	17.2	17.0	18.7	18.6	18.8	19.2	19.2	20.0	20.9
Total Rate	10.2	0.0	0.0	0.2	7.3	18.1	25.7	26.1	25.6	25.8	26.7	26.1	27.2	31.5	31.9	35.3	39.0	41.9	44.4	47.3	51.3	54.8

CONTRIBUTION RATES - SAFETY

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CONTRIBUTION PROJECTIONS - SAFETY

- Investment Return:
  - June 30, 2018 8.6%[5]
  - Future returns based on stochastic analysis using 1,000 trials[6]

	25th Percentile	50th Percentile	75th Percentile
Current Investment Mix	**0.1%**	**7.0%**	**14.8%**
Ultimate Investment Mix	**0.8%**	**6.0%**	**11.4%**

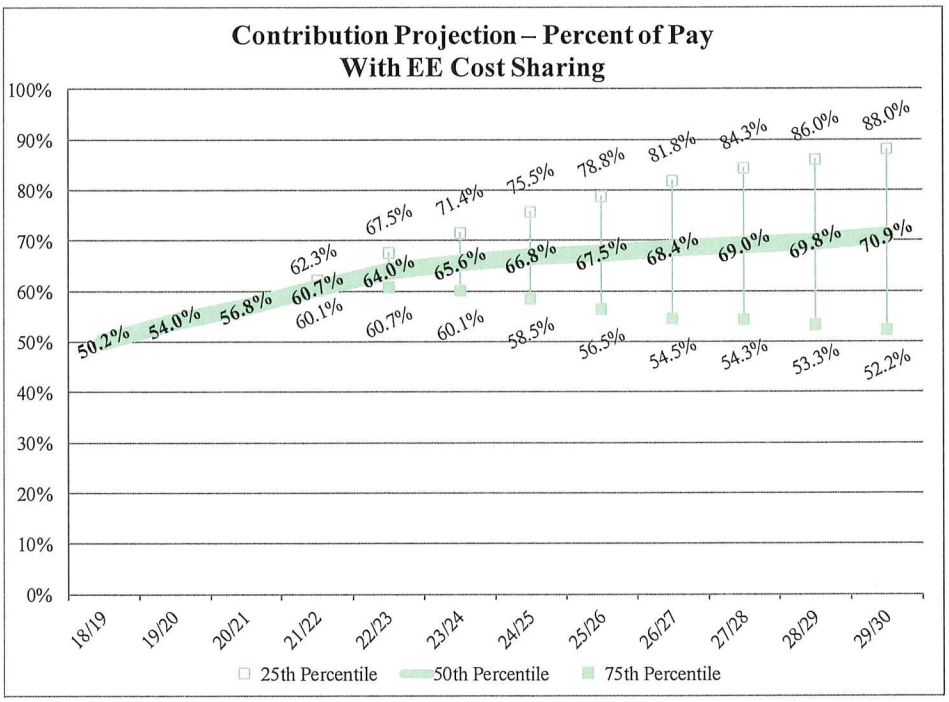
  - Assumes investment returns will generally be 6.5% (as compared to 7.0%) over the next 10 years and higher beyond that.
- Assumption Changes – Discount Rate
  - Decrease to 7.0% by June 30, 2018 valuation
  - Additional Discount Rate decreases due to Risk Mitigation policy.
- No Other: Gains/Losses, Method/Assumption Changes, Benefit Improvements
- Different from CalPERS projection

[5] based July 2018 CalPERS press release
[6] Nth percentile means N percentage of our trials result in returns lower than the indicated rates.

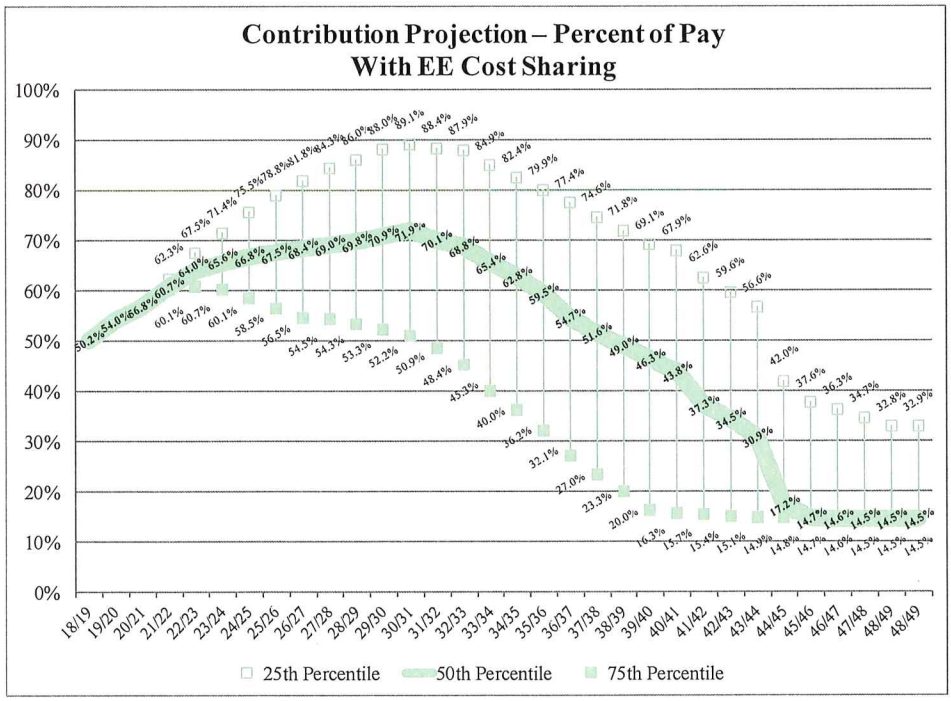
CONTRIBUTION PROJECTIONS - SAFETY

- New hire assumptions:
  - 75.0% of 2018/19 hires are PEPRA members and 25.0% are Classic members
  - Percentage of PEPRA member future hires to increase from 75.0% to 100% over 5 years
- Employee Cost Sharing
  - Police Safety Classic employees pay 2.25% toward employer rates

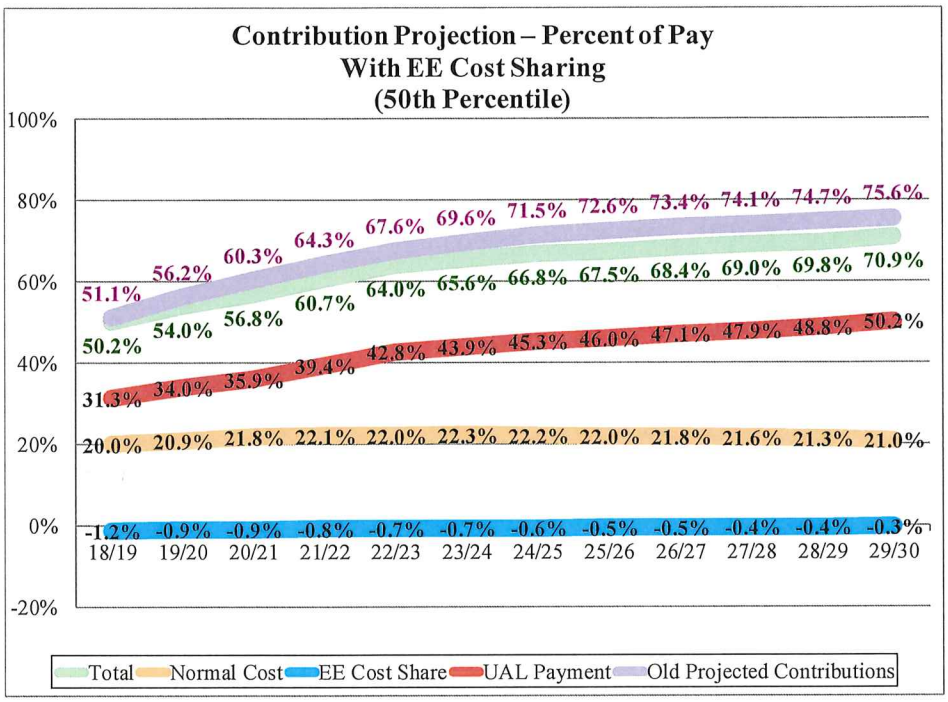
CONTRIBUTION PROJECTIONS - SAFETY



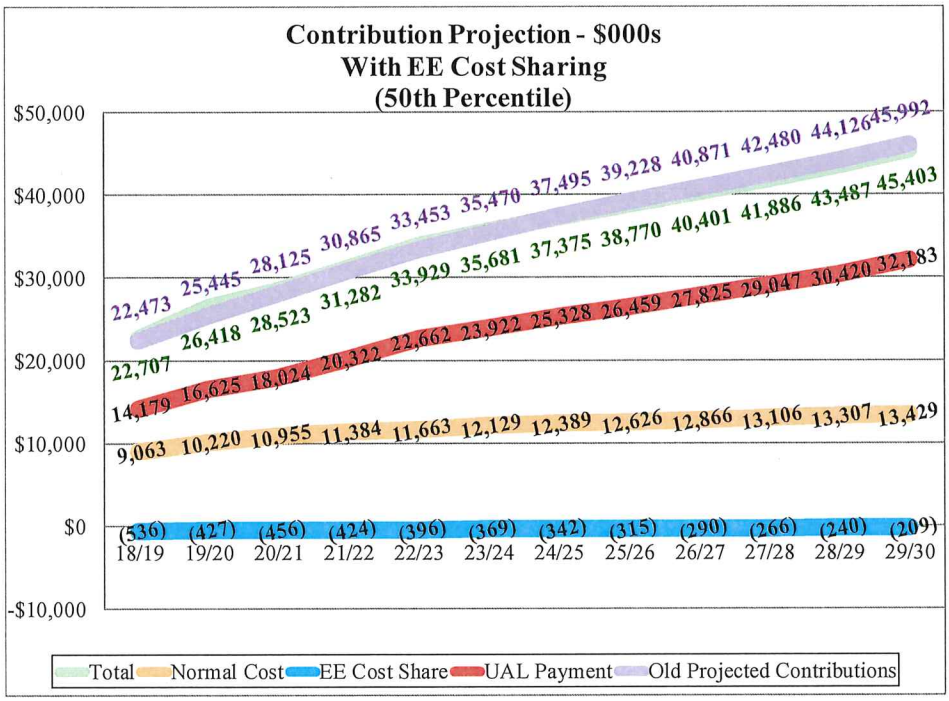
CONTRIBUTION PROJECTIONS - SAFETY



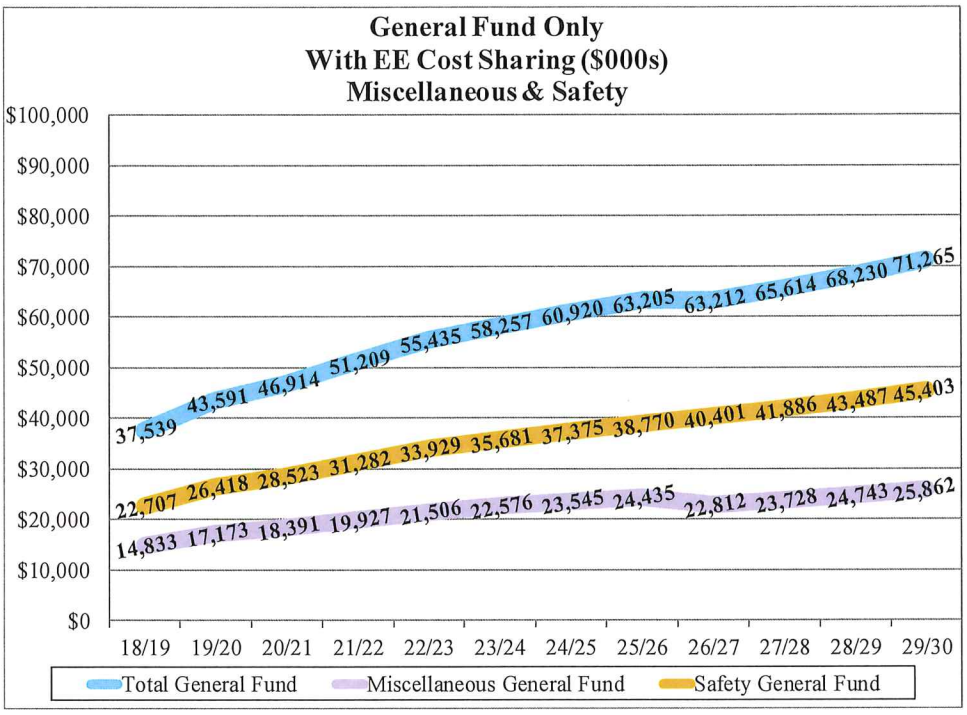
CONTRIBUTION PROJECTIONS - SAFETY



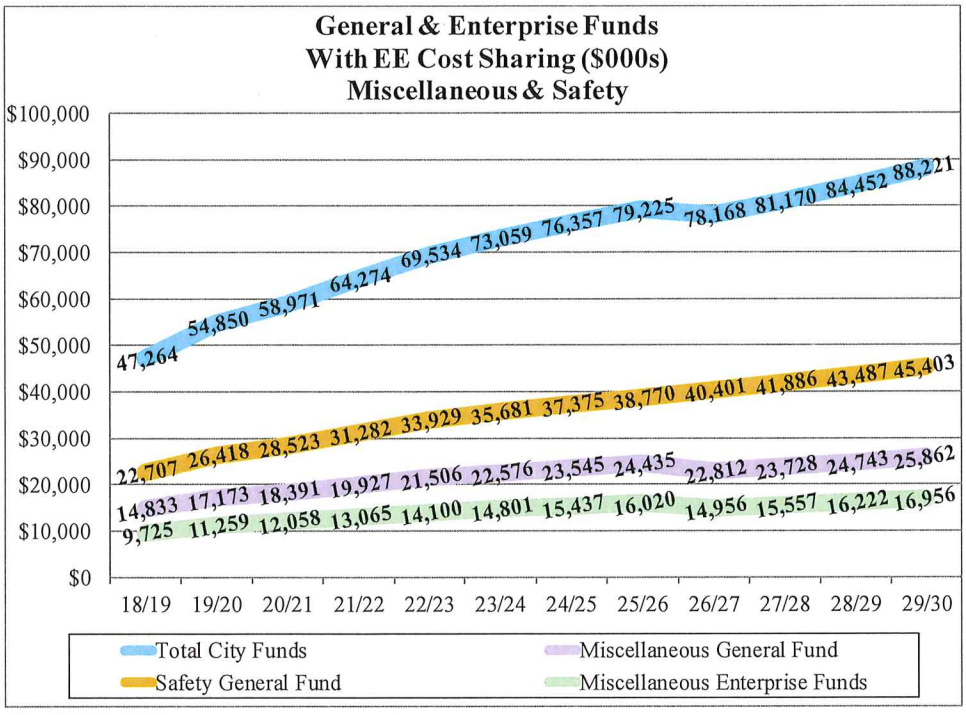
COMBINED MISCELLANEOUS AND SAFETY



COMBINED MISCELLANEOUS AND SAFETY



COMBINED MISCELLANEOUS AND SAFETY



COMBINED MISCELLANEOUS AND SAFETY

Funded Status Summary on June 30, 2017
(Amounts in $Millions)

	Miscellaneous	Safety	Total
■ AAL	$ 697	$ 729	$ 1,426
■ Assets	432	481	913
■ Unfunded AAL	265	248	513
■ Funded Ratio	62.0%	66.0%	64.0%

COMBINED MISCELLANEOUS AND SAFETY

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PAYING DOWN THE UNFUNDED LIABILITY & RATE STABILIZATION

- Where do you get the money from?
- How do you use the money?

WHERE DO YOU GET THE MONEY FROM?

- POB
- Borrow from General Fund similar to State
- One time payments

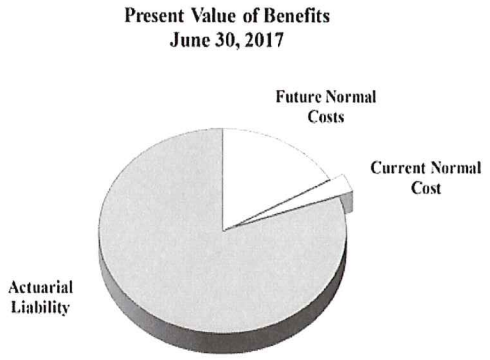
How Do You Use the Money?

- Internal Service Fund
- Make payments directly to CalPERS
- Irrevocable Supplemental (§115) Trust

Irrevocable Supplemental (§115) Pension Trust

- Consider:
  - How much can you put into Trust?
    - ☐ Initial seed money?
    - ☐ Additional amounts in future years?
  - When do you take money out?
    - ☐ Target budget rate?
    - ☐ Year target budget rate kicks in?
      - ○ Before or after CalPERS rate exceeds budgeted rate?

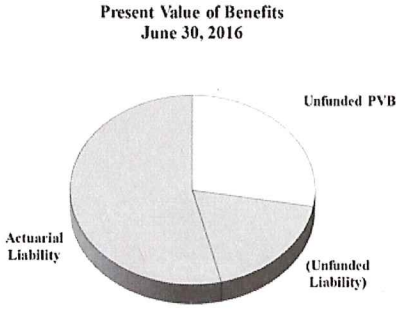
APPENDIX – DEFINITIONS

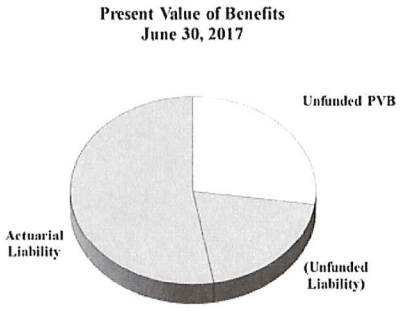


- **Present Value of all Projected Benefits:**
  - The value now of amounts due to be paid in the future
- **PVB - Present Value of all Projected Benefits:**
  - Discounted value (at valuation date - 6/30/17), of all future expected benefit payments based on various (actuarial) assumptions

- **Current Normal Cost:**
  - Portion of PVB allocated to (or "earned" during) current year
  - Value of employee and employer current service benefit
- **Actuarial Liability:**
  - Discounted value (at valuation date) of benefits earned through valuation date [value of past service benefit]
  - Portion of PVB "earned" at measurement

APPENDIX – DEFINITIONS





- **Target-** Have money in the bank to cover Actuarial Liability (past service)
- **Unfunded Liability -** Money short of target <u>at valuation date</u>
- **Unfunded Liability -** Money short of target <u>at valuation date</u>
  - If all actuarial assumptions were always exactly met, then the plan assets would always equal AAL
  - Any difference is the unfunded (or overfunded) AAL
  - Every year, the actuary calculates the difference between the expected UAAL and Actual UAAL. This is a new layer or amortization base
  - Each new layer gets amortized (paid off) over a period of time as part of the contribution [rate].

City of Santa Clara
The Center of What's Possible

Key Takeaways

- Pension costs are a significant component of total compensation
- Further adjustments and increases are likely – will be difficult to absorb without additional revenue or cost savings
- Pension costs continue to increase but will eventually decrease as more employees enroll in PEPRA
- Staying disciplined in long term planning will continue to serve the City's residents and businesses well
- Using the 10-year financial forecast provides us with the time to make adjustments

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