

Item No. 5C1  
Pension Discussion  
Presentation  
June 28, 2018

# Unfunded Pension Liability

## Funding Goals & Challenges

# Unfunded Pension Liability Funding Goals

- Keep Amortization Schedules Under 20 Years
- Maximize Long-term Savings
- Unfunded Liability Contributions should be aggressive but mindful of current needs
- Maximize use of Additional Discretionary Payments (ADP)
- Keep contributions to CalPERS relatively level
- Don't increase risk
- Choose most cost effective path

\* New 20-year level-dollar amortization policies adopted by CalPERS are applied prospectively unless early implemented

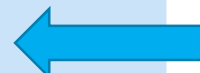
# Many Bases Form Unfunded Liability

## Where are ADPs Most Effective?

Base	Balance as of FY 2020	Remaining Year
1 Fresh Start Base \$305M	305,410,911	15
2 Experience - 2014 \$(76.9M)	(76,872,914)	27
3 Experience - 2015 \$31.9M	31,961,188	28
4 Assumption Change 2016 \$16.8M - 7.375%	16,873,600	19
5 Experience - 2016 \$21.5M	21,528,844	29
6 Assumption - 2017 \$16.4M - 7.25% Est.	16,338,103	20
7 Experience - 2017 (\$27.2M) Est.	(27,217,335)	30
8 Assumption - 2018 \$30.1M - 7.0% Est.	30,805,734	20
	318,828,130	

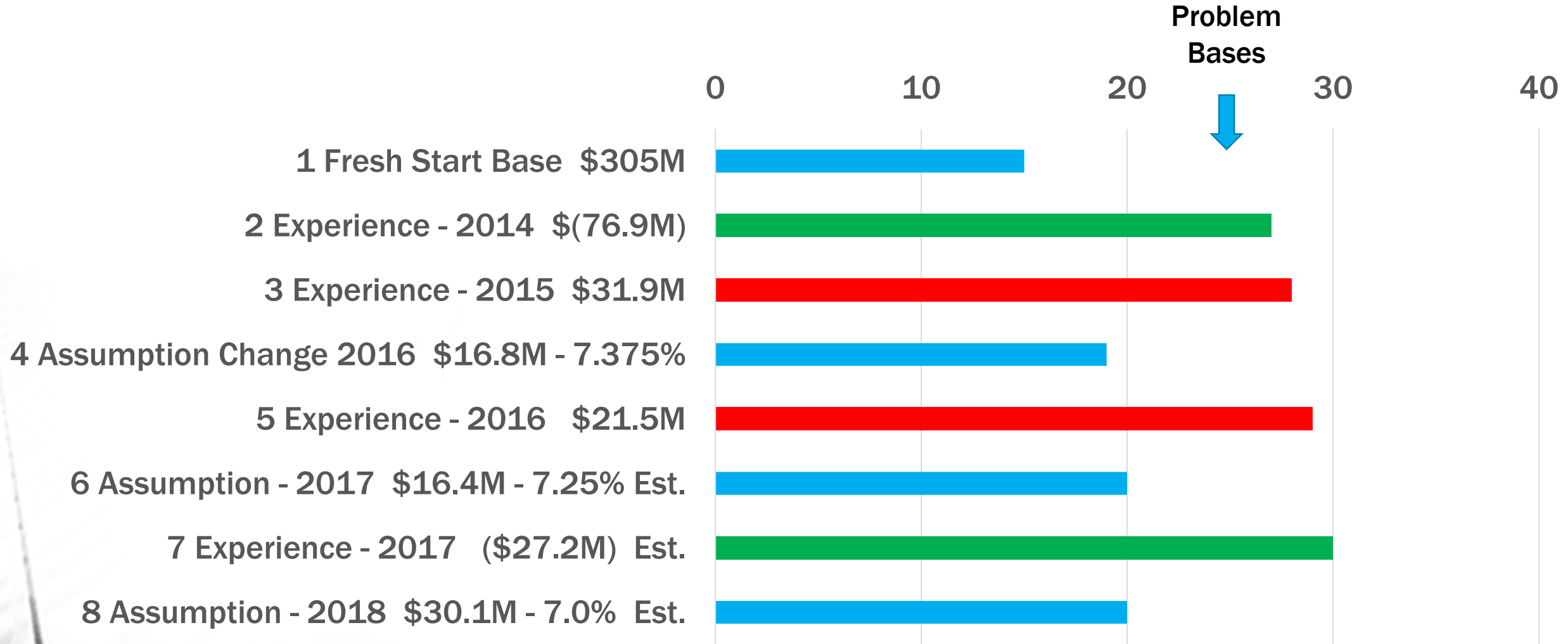


Apply here to achieve greatest short-term savings (e.g. lower min payment)



Apply here to longest base to achieve greatest L.T. savings

# Years to Final Maturity

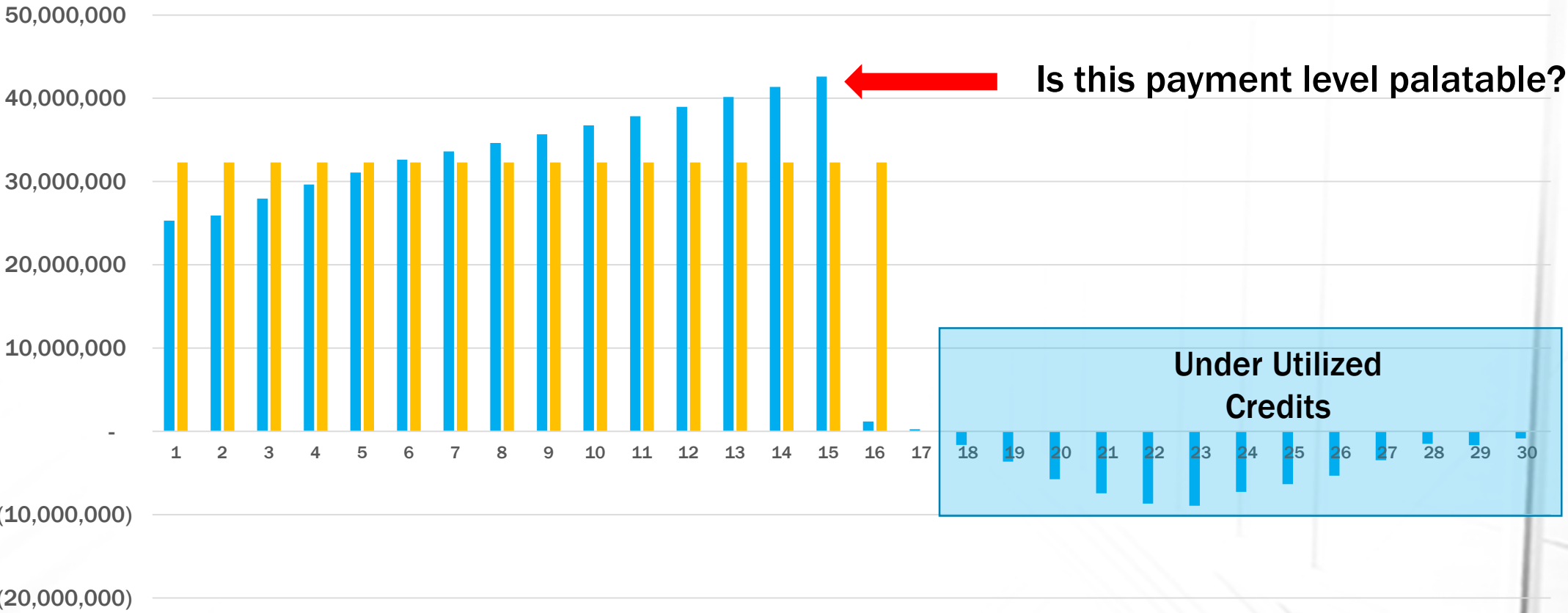


# Inclining Payment Schedules Make Level Payment Goal Challenging

Base	Balance FY 2020	Remaining Yrs	FY 2020 1	2021 2	2022 3	2023 4	2024 5	2025 6	2026 7	2027 8	2028 9	2029 10
1 Fresh Start Base	305,410,911	15	27,529,554	27,904,769	28,741,912	29,604,170	30,492,295	31,407,064	32,349,276	33,319,754	34,319,346	35,348,927
2 Experience - 2014	(76,872,914)	27	(4,021,557)	(5,044,363)	(5,195,694)	(5,351,565)	(5,512,112)	(5,677,475)	(5,847,800)	(6,023,233)	(6,203,930)	(6,390,048)
3 Experience - 2015	31,961,188	28	1,256,208	1,678,940	2,161,635	2,226,484	2,293,279	2,362,077	2,432,940	2,505,928	2,581,106	2,658,539
4 Assumption Chg. 2016 - 7.375%	16,873,600	19	615,563	932,262	1,280,307	1,648,395	1,697,847	1,748,782	1,801,246	1,855,283	1,910,942	1,968,270
5 Experience - 2016	21,528,844	29	572,314	859,363	1,180,191	1,519,496	1,565,081	1,612,034	1,660,395	1,710,206	1,761,513	1,814,358
6 Assumption - 2017 7.25% Est.	16,338,103	20	304,722	614,310	949,110	1,303,444	1,678,184	1,728,529	1,780,385	1,833,797	1,888,811	1,945,475
7 Experience - 2017 Est.	(27,217,335)	30	(371,727)	(743,016)	(1,147,960)	(1,576,532)	(2,029,784)	(2,090,678)	(2,153,398)	(2,218,000)	(2,284,540)	(2,353,076)
8 Assumption - 2018 - 7.0% Est.	30,805,734	20	-	574,557	1,158,291	1,789,560	2,457,662	3,164,240	3,259,168	3,356,943	3,457,651	3,561,380
	318,828,130	<b>Default</b>	<b>25,885,077</b>	<b>26,776,823</b>	<b>29,127,793</b>	<b>31,163,453</b>	<b>32,642,452</b>	<b>34,254,574</b>	<b>35,282,211</b>	<b>36,340,677</b>	<b>37,430,898</b>	<b>38,553,825</b>
		<b>Current Max.</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>	<b>35,000,000</b>
		<b>ADP</b>	<b>9,114,923</b>	<b>8,223,177</b>	<b>5,872,207</b>	<b>3,836,547</b>	<b>2,357,548</b>	<b>745,426</b>	<b>(282,211)</b>	<b>(1,340,677)</b>	<b>(2,430,898)</b>	<b>(3,553,825)</b>

\*Disclaimer - Payment schedules have not been adjusted to reflect the lower payroll growth assumption of 2.75% vs 3.00%

# Default Payment vs Full Fresh Start



■ Default    ■ Full Fresh Start Level \$ 16 Years



# **Potential Merits and Limitations of Section 115 Pension Prefunding Trusts**

# Potential Benefits of Using a Section 115 Trust

- Trust assets can be theoretically accessed to pay CalPERS at anytime to reduce volatility and offset unexpected rate increases (rate stabilization).
- Provides access to a broader universe of investments that the City can undertake on its own, including stocks and longer-term bonds.
- Allows the City to maintain control and investment oversight of assets.
- Rainy Day Fund - Emergency source of funds when Employer revenues are impaired based on economic or other conditions
- Diversifies investment assets and strategies.



# Potential Limitations of Using a Section 115 Trust

- Does not directly reduce Net Pension Liability
- Assets not recognized when CalPERS sets contribution rates
- More expensive to administer
- Added complexities for reporting & administration
- May introduce additional risks
  - Potentially short investment horizon
  - Difficult to diversify a small portfolio
  - Headline risk
- Assets can't be simply transferred to CalPERS. They must be sold at current market value
- In the event of an economic downturn, when the reserve funds might need to be accessed, the market value of the trust portfolio is also likely to be negatively impacted by the downturn.
- The Trust would not likely have a material impact on overall pension asset diversification or investment return relative to the \$550 million of pension assets already at CalPERS.

# Comments From Major Provider of 115 Trusts

- There are approximately 124 public agencies in California that have adopted a 115 trust.
- Of those, we have 60 cities that have adopted our program.
- The types of city clients run the gamut from perceived wealthy cities to those not considered as well off.
- The average deposit is probably under \$1 million
- Our program has no minimum fees nor monthly minimum, so those Cities that may not be able to contribute substantial sums can still participate.
- We simply charge a percentage of assets in the program to administer the program (which starts at 0.6%) so those making smaller deposits would pay smaller fees.
- The smallest deposit we have from a city is \$50,000.

# Future Pension Funding Policy Decision

- 1) Continue with Additional Discretionary Payments (ADP)
- 2) Fresh Start two or more bases to bring future credits forward
- 3) Divert ADP contributions to Section 115 Pension Prefunding Trust