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Receive a presentation from Doug Pryor, Bartel and Associates, LLC, on the projected long-term Public Employees' Retirement System (CalPERS) costs for the County of Solano, including the projected financial impacts to the County resulting from the February 2018 CalPERS Board of Administration decision to amend the amortization policy; Receive financial scenarios to address the County's goal to reach a 90% funded status for pensions over time; Receive recommendations on alternative pension contribution scenarios from the Pension Advisory Committee; and Approve an Appropriation Transfer Request (ATR) increasing appropriations by $6.6 Million in the respective funds for an additional payment to the CalPERS Public Safety Plan unfunded liability account funded by the General Fund CalPERS Rate Reserve (4/5 vote required)

Published Notice Required? Yes ____ No _X_
Public Hearing Required? Yes ____ No _X_

DEPARTMENTAL RECOMMENDATIONS:

1) The Director of Human Resources recommends that the Board of Supervisors receive an update to the February 2017 presentation from Bartel Associates, LLC on the fiscal impacts of recent California Public Employees' Retirement System (CalPERS) changes, including scenarios which address the County's goal to reach a 90% funded status;

2) Receive recommendations on alternative pension contribution scenarios from Pension Advisory Committee; and

3) Approve an Appropriation Transfer Request (ATR) increasing appropriations by $6.6 Million in the respective funds for an additional payment to the CalPERS Public Safety Plan unfunded liability account funded by the General Fund CalPERS Rate Reserve (4/5 vote required).

SUMMARY:

The CalPERS Board of Administration, in April 2013 and in February 2014, approved significant changes to their actuarial assumptions effective FY2015/16 to improve the funded status of the retirement plan. These changes included new smoothing and amortization methods and an update to the mortality tables. CalPERS will use a fixed 25-year amortization period for unfunded gains and losses rather than a rolling 30-year amortization period. Additionally, CalPERS updated the mortality tables to increase the life expectancy since people are living longer and, therefore, this requires retirement benefits paid over a longer period of time. These changes increased the County's employer rates.

In December 2016, the CalPERS Board of Administration approved lowering the investment return discount rate assumption from 7.50% to 7.00% over the next three years. The phase-in of the discount rate was reduced to 7.375% for the actuarial valuations dated June 2016, reduced to 7.25% for the actuarial valuations dated June 2017, and reduced to 7.00% for the actuarial valuations dated June 2018. These changes will result in an increase to the County's employer rates.

In December 2017, the CalPERS Board of Administration affirmed the asset allocation model, which was similar to the existing asset portfolio. In February 2018, the CalPERS Board of Administration adopted a new amortization policy, which applies only to newly established amortization bases, reduces total interest paid over time and pays off unfunded actuarial liabilities quicker. This change becomes effective with the June 30, 2019 valuation (for FY2021/22 contributions).

FINANCIAL IMPACT

Bartel Associates, LLC will present detailed findings (Attachment A) as part of their oral presentation.

The total costs as a result of these changes are estimated to increase the County's retirement costs from $46.245 million in FY2016/17 to a projected $92.788 million in FY2023/24 as shown in Attachment B. The General Fund's estimated share of these costs is projected to increase from $13.822 million in FY2016/17 to an estimated $32.387 million in FY2023/24. Note that these projected costs are based on the current number of county employees in CalPERS and the current Federal and State revenues that reimburse the County for employee costs.

The staff report includes recommendations that proactively pay down the unfunded pension obligations of the County.

DISCUSSION:

CalPERS Retirement Plans

The County provides regular and limited-term employees retirement benefits offered through the California Public Employees' Retirement System (CalPERS). Retirement benefits are provided through one of two plans: safety plans for county sheriff officers and county peace officers, and "miscellaneous" plan for all non-safety employees. Retirement benefits are based on the retirement formula factor, employee's earnings, age at time of retirement, and the number of service years the employee worked.

County sheriff officers safety benefits are provided to Deputy Sheriffs (and higher ranks) under a 3% at age 50 retirement formula, or for employees hired after January 17, 2011 under a 3% at age 55 retirement formula. The county sheriff safety officers benefits for new members of the retirement system as of January 1, 2013 is 2.7% at age 57 as set by state legislation.

County peace officer safety benefits are provided to other safety employees (such as Correctional Officers or Probation Officers) under a 2% at age 50 retirement formula, or for employees hired after May 4, 2012 under a 2% at age 55 retirement formula. The county peace officer safety benefits for new members of the retirement system as of January 1, 2013 is 2% at age 57 as set by state legislation.

Non-safety employees receive retirement benefits under a "miscellaneous" formula of 2.7% at age 55, or for employees hired after May 4, 2012 under a 2% at age 60 retirement formula. The miscellaneous formula for new members of the retirement system as of January 1, 2013 is 2% at age 62 as set by state legislation.

A summary of the County's historical retirement costs are shown in Attachment C. Note, that these expenditures would have been much greater if the County had not negotiated collective bargaining terms with employees paying their own share of retirement and if the County had not negotiated and implemented the second (lower) tier of retirement benefits. (The retirement formulas effective as of January 1, 2013 are a result of statewide pension reform legislation.)

The CalPERS Board of Administration (governing board) approved in April 2013 and in February 2014 significant changes to their actuarial assumptions effective FY2015/16 to improve the funded status of the retirement plan. These changes include new smoothing and amortization methods. CalPERS will use a fixed 25-year amortization period for unfunded gains and losses rather than a rolling 30-year amortization period. Additionally, CalPERS updated the mortality tables to increase the life expectancy since people are living longer and, therefore, requires retirement benefits over a longer period of time. These changes increase the County's employer rates.

In December 2016, the CalPERS Board of Administration approved a reduction in the assumed investment return discount rate from 7.50% to 7.00%, over a three year phase in period. Lowering the discount rate will result in increases in both the normal costs (the cost of pension benefits accruing in one year for active members) and the accrued unfunded liabilities. These increases result in higher employer (County) contributions. Like the earlier changes, the CalPERS Board of Administration directed a multi-year phased-in approach to the change. The discount rate was lowered from 7.50% to 7.375% (increasing the County's FY2018/19 employer rates), then to 7.25% (increasing the County's FY2019/20 rates), and finally to 7.00% (increasing the County's FY2020/21 employer rates). As the impacts of each of these three reduced discount rates are phased-in, the County will not realize the full fiscal impact (increased costs) until FY2024/25.

The decision to reduce the discount rate was based on lower expected future asset returns. CalPERS also has a long-term goal to further reduce overall risk/volatility in the portfolio. CalPERS' risk mitigation strategy was adopted in 2015 to move to more conservative investments over time, using years with better than expected investment returns to achieve an expected 6.50% discount rate in approximately twenty years. In adopting the December 2016 reduced discount rate, CalPERS left unanswered how it will integrate the risk mitigation strategy into this new discount rate policy. Risk mitigation is expected to be clarified later this year, and may result in further reductions to the discount rate in years after June 30, 2018. Additionally, the CalPERS Board of Administration will review their capital market assumptions later this year, which may also result in additional reductions to the discount rate.

In December 2017, the CalPERS Board of Administration affirmed the asset allocation model, which was similar to the existing asset portfolio. There was no resulting discount rate change.

In February 2018, the CalPERS Board of Administration adopted a new amortization policy, which applies only to newly established amortization bases. The new amortization policy requires public agencies to pay a fixed dollar amortization rather than a percent of pay for unfunded liabilities. Actuarial gains/losses will be amortized over 20 years (a reduction from 30 years), the five year ramp up/down for investment gains and losses as amended by eliminating the ramp down (resulting in initially higher rates, but payments over a shorter duration), and eliminating the ramp up/down for other amortization bases. These changes reduce total interest paid over time and pays off unfunded actuarial liabilities quicker. These changes become effective with the June 30, 2019 valuation (for FY 2021/22 contributions).

Bartel Assocates, LLC, an actuarial firm, was contracted to calculate the fiscal impact. Bartel Associates previously made presentations to the Board of Supervisors in June 2013 and June 2014. This updated Bartel Associates, LLC report now incorporates the CalPERS approved 2017 and 2018 changes. The Bartel Associates, LLC report is included as Attachment A.

Pension Funding Policy

In June 2014 the Pension Advisory Committee (County Administrator, Assistant County Administrator, Treasurer-Tax Collector-County Clerk, Auditor-Controller, and Director of Human Resources) presented, and the Board approved, the County's Pension Funding Policy. On February 7, 2017, the Board approved an updated pension funding policy. The policy prescribes: maintain a stable, well-funded CalPERS pension account that provides the necessary assets to meet pension commitments to employees; ensure planning mechanisms are in place to ensure sufficient liquidity to pay substantially higher annual pension contributions in the future providing flexibility in maintaining a healthy funding level as CalPERS assumptions are adjusted. The goals of the policy are:

1) To achieve and maintain a funding ratio at or above 90% in the County's Safety and Miscellaneous

CalPERS Plans.
2) To reduce the County’s unfunded liability consistent with a 90% funding level.
3) To stabilize annual contributions.

The County annually reviews and forecasts future costs based on the annual CalPERS actuarial valuation so future costs can be anticipated and incorporated into strategies consistent with the pension funding policy. The following strategies are considered annually during the budget process to help achieve the County’s stated goals:

1) Fund a General Fund pension reserve for use in achieving the goals in this policy.
   a) As existing pension and other outstanding debt is retired, those payment streams may be redirected to fund the CalPERS Pension Reserve.
   b) Direct a portion of year-end fund balance to the CalPERS Pension Reserve.
   c) Use of one-time revenues.
   d) Board allocating assets to the CalPERS Pension Reserve as part of the annual Budget Hearings.
2) In consultation with Public Agency Retirement System (PARS), work to establish a 115(P) trust fund after the IRS private ruling is issued to PARS.
   a) Note: The Board established the 115(P) trust effective February 10, 2015 and appointed the Treasurer-Tax-Collector and the Auditor-Controller, or their successor or designee, as the County’s Plan Administrator.
3) Maximize cost sharing and cost recovery from state and federal programs.
4) Make additional ongoing contributions to CalPERS in excess of normal contribution if financially feasible.
5) Prepay CalPERS annual contribution early to achieve a discount if conditions permit, and place savings in the CalPERS reserve.
   a) Note: The County continues to prepay CalPERS annual contributions and plans to do so for FY2018/19.
6) Approve the filling of only mission critical positions.
7) Support legislative initiatives as necessary.
8) Issue debt (e.g., pension obligation bonds) when practical to achieve the stated goals when market conditions allow.

Alternative Contribution Scenarios

As part of the presentation to the Board, Doug Pryor will cover alternatives that the County may consider to utilize the County’s CalPERS reserve estimated balance of $20.9 million (at year-end) and use those funds to pay down the unfunded pension liability estimated at $414.5 million for Miscellaneous Employees and $130.8 million for Safety Employees as of June 30, 2016. This unfunded pension liability for the County covers 6,406 active and retired employees.

In light of the Pension costs for the County, the Pension Advisory Committee has recommended in the past, to establish a CalPERS reserve and to establish an IRS 115 Trust for Pension obligations.

The projected cash balances at June 30, 2018, for the General Fund CalPERS reserve are projected to be $20.9M and the IRS 115 Trust at $20.4M. The Pension Advisory Committee continues to be proactive in paying down the unfunded pension obligations (in addition to the annual payment to CalPERS).

On June 4, 2018, the Pension Advisory Committee discussed various alternative/scenarios and has the following recommendations for the Board to consider and approve during the Budget Hearings later in June 2018:

1) Delegate authority to the County Administrator to transfer an amount of $10 million from the CalPERS

reserve to the IRS 115Trust to ensure higher interest earnings and to build up assets for future payments to CalPERS. This action has the most impact and will be used to stabilize the employer rates/contributions in the peak years of FY23/24-FY33/34 for both Miscellaneous and Safety Employee Plans illustrated on page 55 of the Bartel Report. (Scenario 4 shows $15M transfer). (Consider this recommendation at Budget Hearings.)

2) Authorize a pre-payment of $1.59 million from the County's CalPERS reserve to CalPERS to pay off specific unfunded liabilities bases in the Safety Plan for the County of Solano CalPERS plan. (Scenario 1) and attachment. The Board is requested to consider this recommendation prior to Budget Hearings in order to meet the FY18/19 deadline of June 20, 2018 for payment to CalPERS. (Recommend to Approve ATR; requires 4/5 votes).

3) Authorize a pre-payment of $5 million from the County's CalPERS reserve to the CalPERS to pay off a portion of unfunded liabilities bases in the Safety Plan for the County of Solano CalPERS plan based on the input from the assigned CalPERS actuary. The Pension Advisory Committee wanted to make an ad hoc payment to CalPERS of $5M to the Safety Plan at this time, instead of transferring the full $15M to the IRS 115Trust; (results in a transfer of $10M to the IRS 115Trust.). The Board is requested to consider this recommendation prior to Budget Hearings in order to meet the FY18/19 deadline of June 20, 2018 for payment to CalPERS. (Recommend to Approve ATR; requires 4/5 votes).

The County's Miscellaneous Plan includes County, Court and Fair employees. A majority of the County Miscellaneous employee salary and benefits are eligible for some portion of federal and state reimbursement. It is recommended by the Pension Advisory Committee to first address the unfunded liabilities of the Safety Plan which only includes County employees. The increasing costs for providing public safety services to the county residents require that the County use more General Fund revenues as a funding source, due to the State of California realigning programs to the county level without a sufficient level of funding. Also, the cost of the safety personnel continues to increase in our county due to the additional staff required to provide services at this time and the cost per employee is higher. This prepayment of a few unfunded liabilities will bring down the annual employer rate by a small margin.

Future consideration that requires more budget analysis:

Given that the County's Miscellaneous Plan includes the County, Courts and the Solano County Fair employees, the calculations to apply any prepayment to the Miscellaneous Plan complicates the accounting of the application for the prepayment to the employer rates. The prepayment option would result in paying down the courts and Fair Association unfunded liability without their financial payments for these costs. However, the county could elect to reduce amortization period for one or several accrued liability bases with an amortization period longer and reduce it to 20 years. This option would irrevocable increase the employer rate for County, Courts and Solano County Fair and would increase employer contribution rate equitably to all. This option pays down the liability quicker and reduces the interest cost over the remaining term. The cost for this approach is still being evaluated internally for county departments and this option would require consultation with the Solano Courts and the Fair Association.

ALTERNATIVES:

The Board could choose not to accept the updated presentation on CalPERS funding status; however, this is not recommended as the enacted changes by CalPERS will have a considerable fiscal impact to the County.

OTHER AGENCY INVOLVEMENT:

CalPERS provided information that was used in evaluating the fiscal impacts. The County Pension Advisory

Committee met and discussed the Bartel Report and formulated recommendations for Board of Supervisors consideration and action.

CAO RECOMMENDATION:

APPROVE DEPARTMENTAL RECOMMENDATION