

# CITY OF RIVERSIDE, CALIFORNIA

## CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM (CaPERS) OVERVIEW AND UPDATE

AS OF JANUARY 26, 2018

### CaPERS 101: HOW DOES IT WORK?

#### DEFINED BENEFIT PLAN PENSION FORMULAS

Defined Benefit Plans (DBPs) are pension plans in which an employee receives fixed benefits that are based on length of service and salary earned at the time of retirement. The City's relationship with CalPERS to provide a DBP to its employees dates back to 1945 when the initial plan was approved by Riverside voters by Special Election on June 5. Further, the City's Charter (Article X – Retirement), requires a CalPERS retirement for City employees.

A defined contribution plan (DCP), such as a 401K, is a dollar contribution to a retirement fund. The total retirement in a DCP is generally based on the amount of assets and growth of the money.

The City has several employee groups with different CalPERS DPB formulas (see below). The formula represents the percent of salary for each year employed with the City that a plan member will receive at or after the specified age.

For example, for a plan member that receives a pension of 2.7% @ 55 with a 3-year highest salary average of \$65,000 and 20 years of service will:

- Be eligible to retire at 55 years of age
- Receive an annual pension based on the following formula:
  - Years of service x pension rate x 3-year highest salary average = annual pension
  - $20 \times 2.7\% \times \$65,000 = \$35,100$  annual pension

#### CITY'S DEFINED BENEFIT PLAN PENSION FORMULAS

The City has five CalPERS DBP formulas depending on hire date and employee group. How costs are shared between the City and employees is explained in the next section of this handout.

##### BEFORE JANUARY 2013

**3%**  
**@ 50**

Safety  
(Fire Tier 1,  
Police Tier 1, 2)

**2.7%**  
**@ 55**

Miscellaneous  
(All Non-Sworn  
Tier 1 & 2)

**3%**  
**@ 55**

Safety  
(Fire Tier 2)

##### AFTER JANUARY 2013 (PEPRA)

**2%**  
**@ 62**

Miscellaneous  
(All Non-Sworn  
Tier 3)

**2.7%**  
**@ 57**

Safety  
(Fire & Police  
Tier 3)

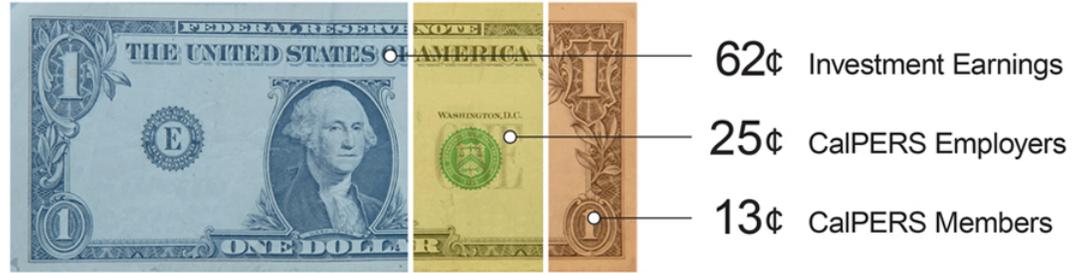
(SEE THE LAST PAGE FOR INVESTMENT AND CaPERS TERMINOLOGY DEFINITIONS)

# HOW ARE CaIPERS BENEFITS FUNDED?

## TWO-THIRDS OF FUNDS COME FROM INVESTMENTS

Historically, more than 60% of all funds paid to CalPERS retirees comes from investment earnings. When CalPERS does not meet its investment return goals, the City will pay more.

Every dollar paid to CalPERS retirees comes from three sources:

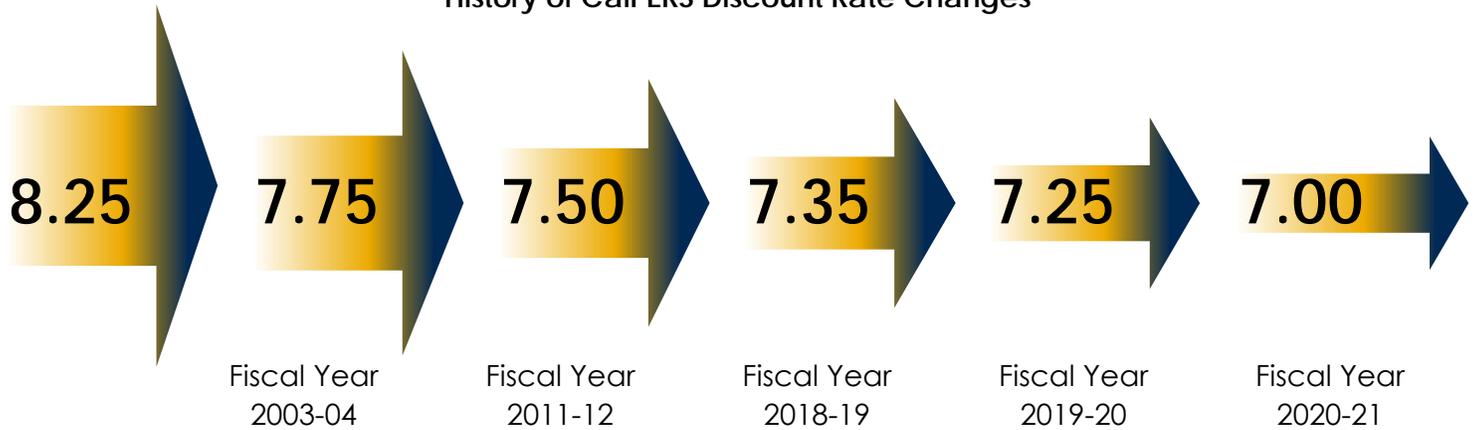


## LOWER CaIPERS DISCOUNT RATES INCREASE CITY PENSION COSTS

A discount rate, also known as expected or assumed rate of return, is the estimated long-term average return expected to be earned on investments. The more gains made from a CalPERS plan investment, the less the City will need to contribute.

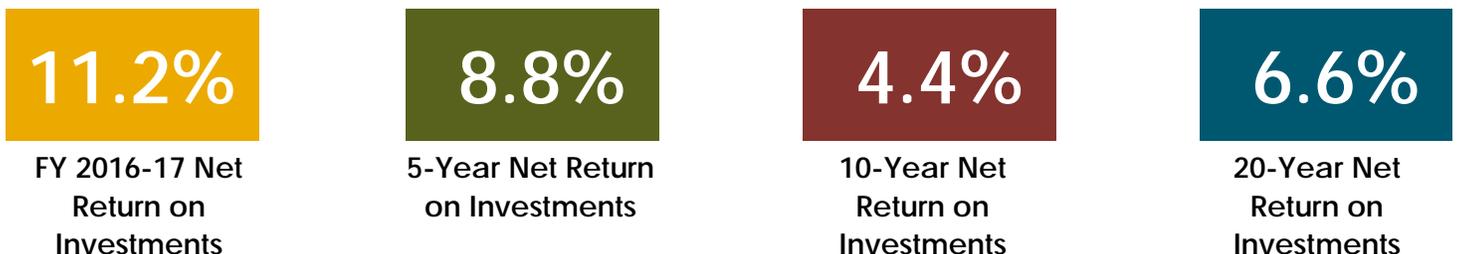
CalPERS recently (December 2016) reduced the discount rate to be more consistent with long-term market expectations. As a result, the City will need to contribute more each year.

History of CalPERS Discount Rate Changes



## SHORT AND LONG-TERM VIEW OF RETURN ON INVESTMENTS

In FY 2016-17, CalPERS had its best investment return at 11.2% when compared to the previous two years (FY 2014-15 was 2.4% and FY 2015-16 was 0.61%). Although this is movement in the right direction, the investment return did not eliminate unfunded pension liabilities (32% of total liability – CalPERS pension plans are funded at 71-74%). CalPERS' investment strategy focuses on long-term performance instead of the more volatile short-term performance. Therefore, the current strategy to increase the employer contribution to the plan remains unchanged.



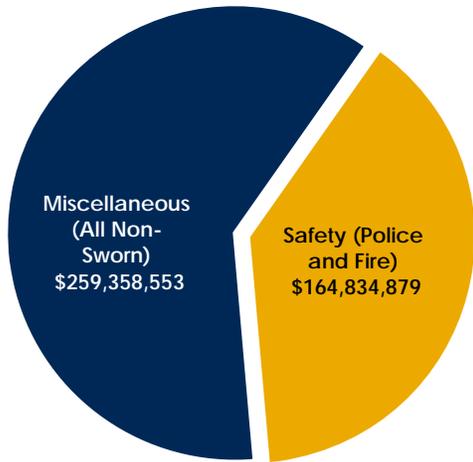
# ARE THE CITY'S PENSIONS SUFFICIENTLY FUNDED?

## CITYWIDE UNFUNDED PENSION LIABILITY

The difference between the City's retirement plan assets and the amount that will be needed to be paid as a pension to employees in the future is known as the unfunded accrued liability (UAL). It is based on calculations provided by the CalPERS Actuarial Office that take into consideration various factors including expected long-term returns on investments and the life expectancy of retirees. UAL is not paid in one year, it is amortized over a period of 20-30 years.

### August 2016 for FY 2017-18

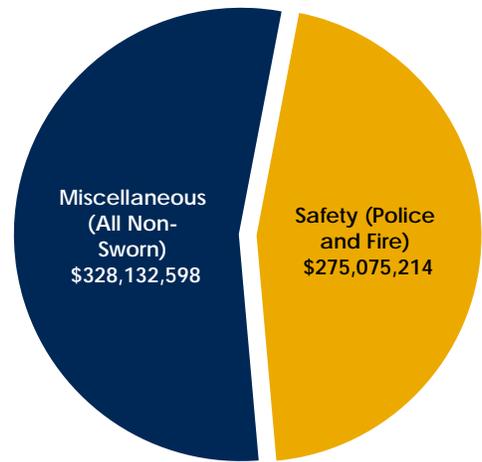
Based on Actuarial Report as of June 30, 2015



**Total UAL**  
**\$424.2 Million**

### July 2017 for FY 2018-19

Based on Actuarial Report as of June 30, 2016



**Total UAL**  
**\$603.2 Million**



**Increased**  
**\$179.0 Million (42%)**

Primarily due to change in discount rate



MISCELLANEOUS  
EMPLOYEES

**74.3%**

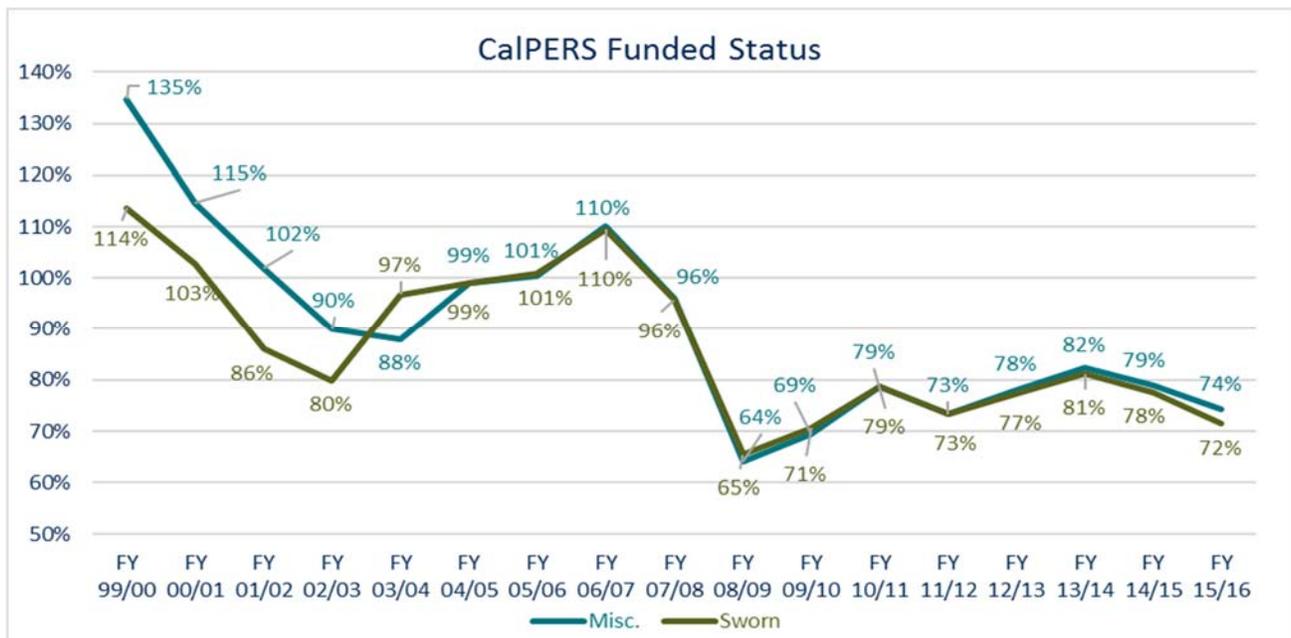
## CITY CalPERS FUNDED RATIOS

Represents the percentage of assets available today to pay all of the pension benefits promised to City employees.



SAFETY  
EMPLOYEES

**71.6%**



# HOW ARE CaIPERS COSTS PAID?

## COST SHARING BETWEEN CITY AND EMPLOYEES

CalPERS establishes an employer rate, which the City must pay for each participating employee, and an employee rate, which either the City or the employee may pay.

The employer rate is an actuarial calculation provided to the City by CalPERS each year. The total amount is comprised of two factors. The first is an estimated percentage of salary based on the employee pool (age, salary, investment returns, etc.). The second, if applicable, is an annual lump sum payment due to pay down an unfunded accrued liability (UAL).

Depending on the pension formula, CalPERS statutorily sets the employee rate at 7-11.5% of the employee's salary. Until recently, the City paid the employee rate for most City employees. This practice was discontinued in 2011-2012 for new employees. In 2016, the City also required all existing employees to gradually transition to paying their share of pension costs over the next four to five years. The information below represents amounts paid by employees and the City for FY 2017-2018.

Miscellaneous	Tier 1	Tier 1	Tier 2	Tier 2	Tier 3
	Classic Members - Hired into CalPERS system prior to January 1, 2013				Public Employee Pension Reform Act (PEPRA) - All Misc. Employees
	<i>SEIU / SEIU Refuse</i>	<i>IBEW/IBEW Supervisors / Unrepresented</i>	<i>SEIU / SEIU Refuse</i>	<i>IBEW/IBEW Supervisors / Unrepresented</i>	
Hire Date	Prior to 6/7/2011	Prior to 10/19/2011	On or after 6/7/2011	On or after 10/19/2011	On or after 1/1/2013
DBP Formula	2.7%@55	2.7%@55	2.7%@55	2.7%@55	2.0%@62
Required Employee Contribution Rates	8.00%	8.00%	8.00%	8.00%	7.00%
Employee Contribution Paid By City	2.00%	6.00%	0.00%	0.00%	0.00%
Required Employer Contribution	12.14%	12.14%	12.14%	12.14%	12.14%
Employer Paid UAL Lump Sum Payment	\$15,683,043				

Safety	Tier 1	Tier 1	Tier 2	Tier 2	Tier 3
	Classic Members - Hired into CalPERS system prior to January 1, 2013				Public Employee Pension Reform Act (PEPRA) - All Safety Employees
	<i>Police (3 groups)</i>	<i>Fire (2 groups)</i>	<i>Police (3 groups)</i>	<i>Fire (2 groups)</i>	
Hire Date	Prior to 2/17/2012	Prior to 6/10/2011	On or after 2/17/2012	On or after 6/10/2011	On or after 1/1/2013
DBP Formula	3.0%@50	3.0%@50	3.0%@50	3.0%@55	2.7%@55
Required Employee Contribution Rates	9.00%	9.00%	9.00%	9.00%	11.50%
Employee Contribution Paid By City	7.50%	8.00%	0.00%	0.00%	0.00%
Required Employer Contribution	19.87%	19.87%	19.87%	19.87%	19.87%
Employer Paid UAL Lump Sum Payment	\$12,351,650				

# WHAT ARE THE PROJECTED CaIPERS COST INCREASES?

## CITYWIDE CaIPERS COST OVERVIEW

Over the next five years (FY 2018-19 to FY 2022-23), the City anticipates its annual retirement expenditures to increase by 45.5% from approximately \$74.5 million to \$108.3 million. These projections are based on the City's most recent CaIPERS actuarial reports dated July 2017. The information below provides a five-year look at the City's overall pension costs and pension costs in the City's major funds (General, Electric, Water, and Sewer).

Citywide Estimated CaIPERS Costs



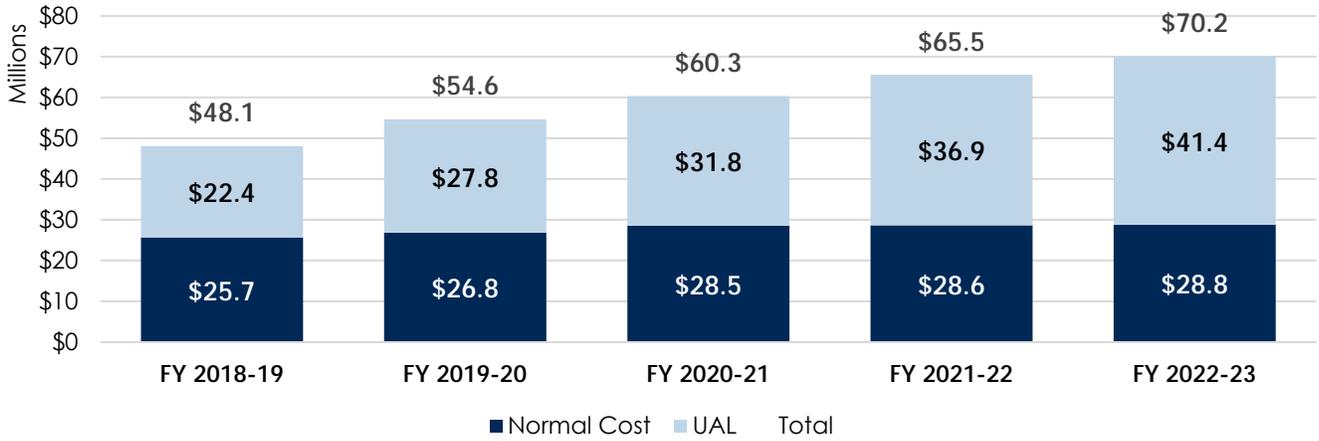
## GENERAL FUND CaIPERS COST OVERVIEW

General Fund CaIPERS costs are expected to increase more than \$22 million or 46%.

General Fund Estimated CaIPERS Costs by CaIPERS Group



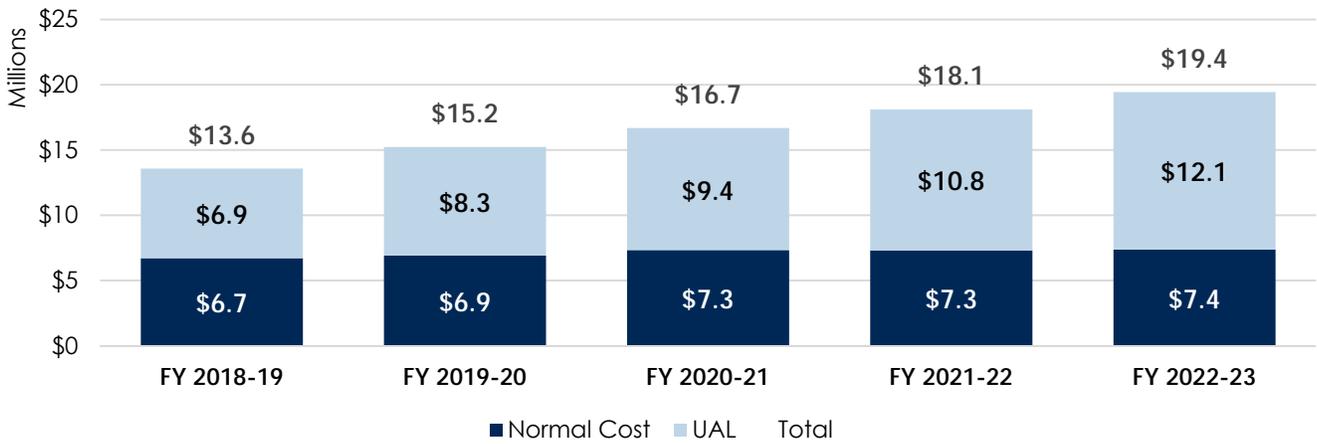
### General Fund Estimated CalPERS Costs



### ELECTRIC FUND CalPERS COST OVERVIEW

Electric Fund CalPERS costs are expected to increase more than \$5.9 million or 43%.

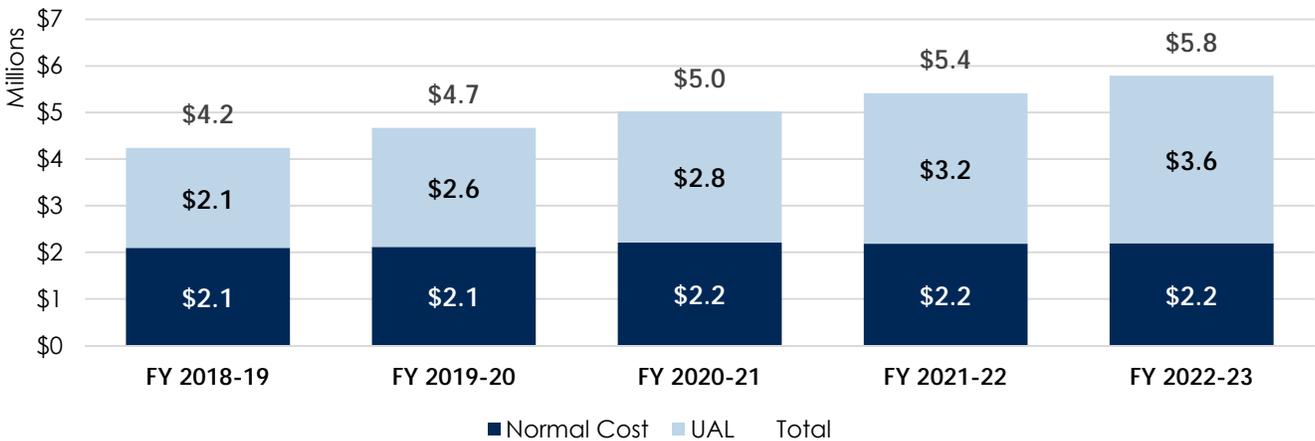
#### Electric Fund Estimated CalPERS Costs



### WATER FUND CalPERS COST OVERVIEW

Water Fund CalPERS costs are expected to increase more than \$1.6 million or 38%.

#### Water Fund Estimated CalPERS Costs



## SEWER FUND CalPERS COST OVERVIEW

Sewer Fund CalPERS costs are expected to increase more than \$1.2 million or 44%.

### Sewer Fund Estimated CalPERS Costs



## WHY ARE CALPERS COSTS INCREASING?

The City's retirement plans went from having an excess of cash (i.e. super-funded, or funded above 100%) to being under-funded. Currently, the City's CalPERS plans are funded at 74% (non-sworn) and 72% (sworn). This is mainly due to investment losses by CalPERS during the Great Recession, which impacted all of the California agencies' retirement plans managed by CalPERS. Additional factors have also contributed to increasing costs:

- Retroactive retirement benefit enhancements for City employees between 2001 and 2006;
- Long-term investment returns not meeting expectations (e.g. 8.8% over last five years, 4.4% over last 10 years, and 6.6% over last 20 years);
- The resulting changes in the CalPERS anticipated return-on-investment rate over the past 15 years, from 8.25% to 7%; and
- CalPERS retirees living longer.

As a result of the above factors, which contributed to the decline in overall retirement plan funding levels, California public entities such as the City of Riverside must increase their payments into the CalPERS system in future years. The payment levels are determined by CalPERS, and they are increasing exponentially.

## WHAT HAS THE CITY DONE TO ADDRESS PENSION COST INCREASES?

### THE CITY HAS TAKEN SEVERAL STEPS OVER THE YEARS TO REDUCE PENSION COSTS

- **2011-2012** – Required all new employees to pay the employee portion of the CalPERS pension costs.
- **2013** – Established lower pension benefits for new employees, resulting in lower pension costs.
- **2016** – Existing employees not currently paying the employee share of CalPERS retirement costs began doing so.
- **2017** – Refinanced \$30 million Bond Anticipation Note using Measure Z Funds. Allowed a fixed interest rate for the pension related debt and an accelerated payoff of the principal balance.
- **Every Year** – Implement operational efficiencies, where possible, to minimize costs and impact to service levels as CalPERS costs increase.

## INVESTMENT & CaIPERS TERMINOLOGY YOU SHOULD KNOW

**Actuarial Report** – An actuarial valuation is a type of appraisal which requires making economic and demographic assumptions in order to estimate future liabilities. The assumptions are typically based on a mix of statistical studies and experienced judgment.

**Bond Anticipation Note (BAN)** – A short-term obligation that is issued for temporary financing needs. The principal payoff may be covered by a future longer-term bond issue. These notes normally have maturities of one year or less and interest is payable at maturity rather than semi-annually.

**Defined Benefit Plan (DBP)** – A type of pension plan in which an employer/sponsor promises a specified monthly benefit upon retirement that is predetermined by a formula based on the employee's earnings history, tenure of service and age.

**Defined Contribution Plan (DCP)** – A type of retirement plan in which a certain amount or percentage of money is set aside each year by a company (or employee) for the benefit of each of its employees. Benefits directly depend upon individual investment returns.

**Discount Rate** – Also known as the expected rate of return or the assumed rate of return. It is the estimated long-term average return expected to be earned on investments.

**Funded Ratio** - Percentage of assets available today to pay all of the pension benefits promised to employees.

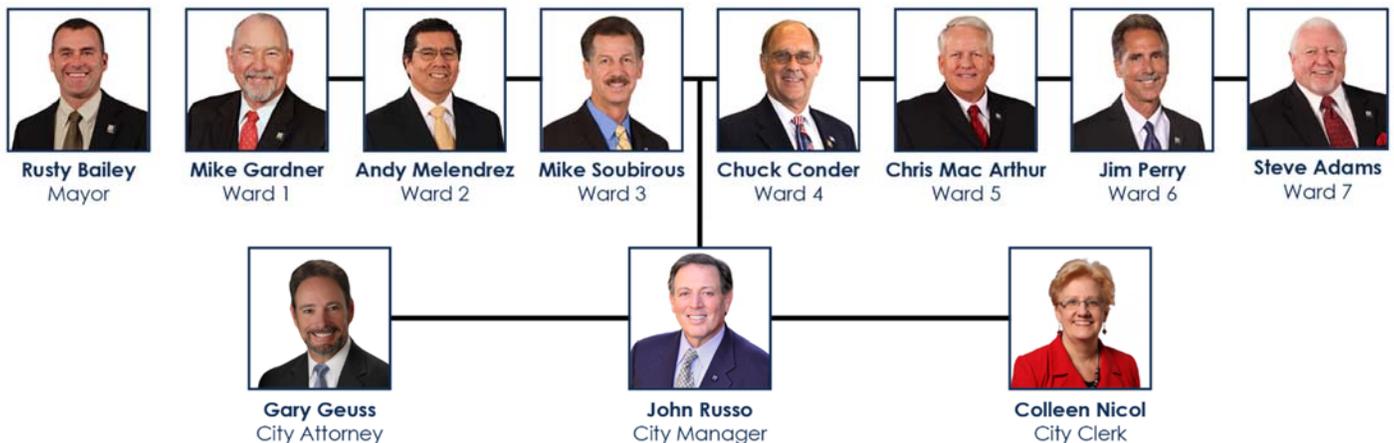
**Normal Costs** – The annual cost of service accrual for the upcoming fiscal year for active employees. The normal cost should be view as the long-term contribution rate for existing employees.

**Pension Obligation Bond (POB)** – Taxable bond that some state and local governments have issued as part of an overall strategy to fund the unfunded portion of their pension liabilities by creating debt.

**PEPRA - Public Employees' Pension Reform Act of 2013** – A pension reform bill that went into effect January 1, 2013. The bill impacts new public employees and establishes a limit on the amount of compensation that can be used to calculate a retirement benefit.

**Unfunded Accrued Liability (UAL)** – Portion of the plan's unfunded liability that is not funded by the plan's asset value.

## CITY LEADERSHIP



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