CITY OF BELVEDERE

FINANCE SUB-COMMITTEE:
Taskforce on Pensions & OPEBs

<u>AGENDA</u>

January 21, 2021
Via Zoom
10:00 a.m.

Join Zoom Meeting
https://us02web.zoom.us/j/4136417003?pwd=TXB1T1pERy8rcG5Hbkdjd1Y2NFVBUT09

Meeting ID: 413 641 7003
Passcode: Belvedere

Dial by your location
    833 548 0282 US Toll-free
    877 853 5247 US Toll-free
    888 788 0099 US Toll-free
    833 548 0276 US Toll-free

Meeting ID: 413 641 7003
Passcode: 310801

1. Welcome and Introductions/Comments from the Chair
2. Expectations and Timeline Discussion – Chair
3. Briefings/Discussion of the City's pension position and potential strategies for managing pension liabilities
4. Adjourn

Attachments:

1. Presentation on the City's financial trends
2. Pension White Paper
3. Change in UAL Paper
4. Where to find the City's valuation reports:
    a. CalPERS Valuations – Miscellaneous Classic
    b. CalPERS Valuations – Miscellaneous PEPRA
    c. CalPERS Valuations – Safety Classic
    d. CalPERS Valuations – Safety PEPRA
    e. PARS Valuations
5. Taskforce Timeline (draft-only)

Date posted: January 19, 2021.

Date posted: January 19, 2021.

City of Belvedere Finances

Trend Analysis Project
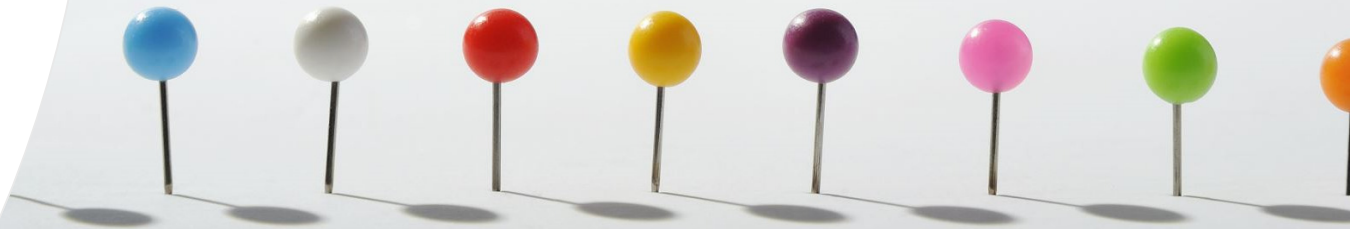
Project Objective

- Using 20 years of budget data this project seeks to identify trends in revenues and expenditures to:

- Assess the City's fiscal health.

- Identify areas of risk.

- Explore avenues for cost savings and/or revenue generation.

Data Cleaning Process

- The project draws on audited budget data from 2000-01 to 2018-19 and unaudited data for 2019-20.

- Data has been sorted and recategorized to provide a consistent timeseries.

- Data has been cleaned of capital projects financed by special assessments, as well as extraordinary paydowns of the City's unfunded pension liabilities to establish an "apples for apples" dataset of Recurring Expenditures and Recurring Revenues.

- Trends in aggregate and departmental budgets are then explored.

- [All errors are mine.]

Recurring & Extraordinary Revenues

Extraordinary Revenues Are Stripped From Trend Analysis

US$ millions

Legend: Recurring Revenues, Special Assessments*
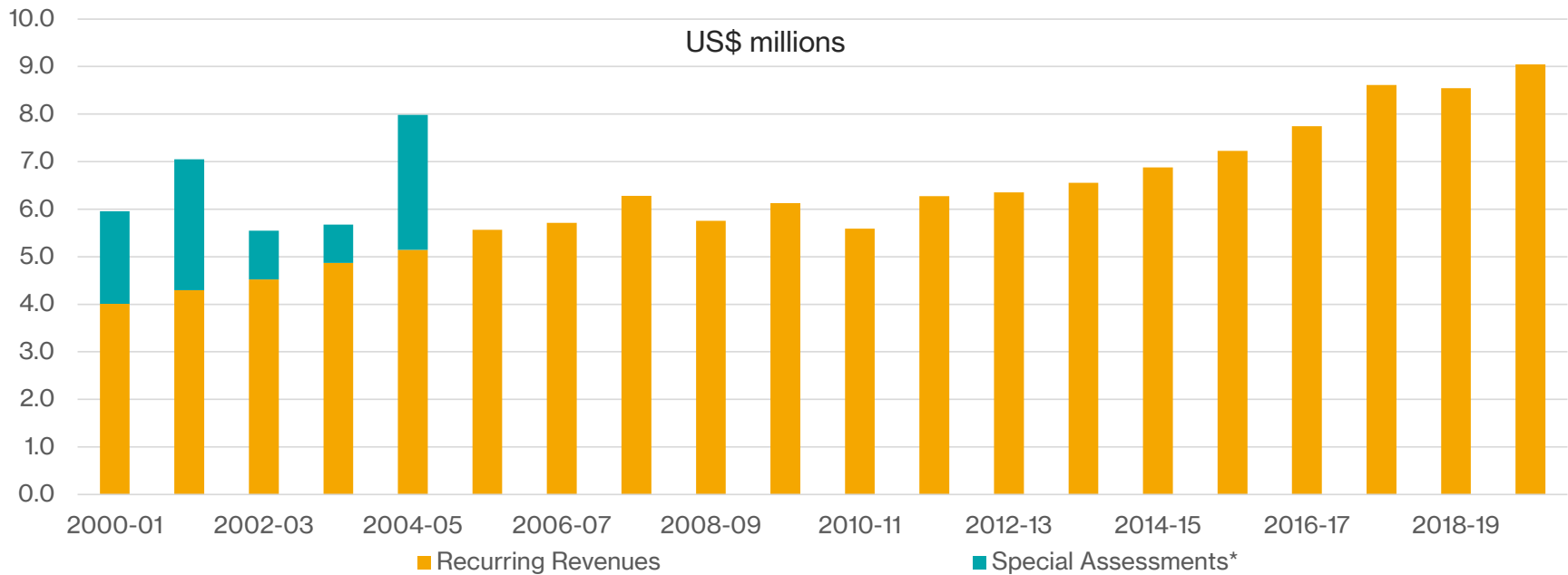
*Includes Corinthian Island, Upper Beach and Madrona Special Assessment Districts, Sewer Enterprise Fund and Reed Drainage Project.
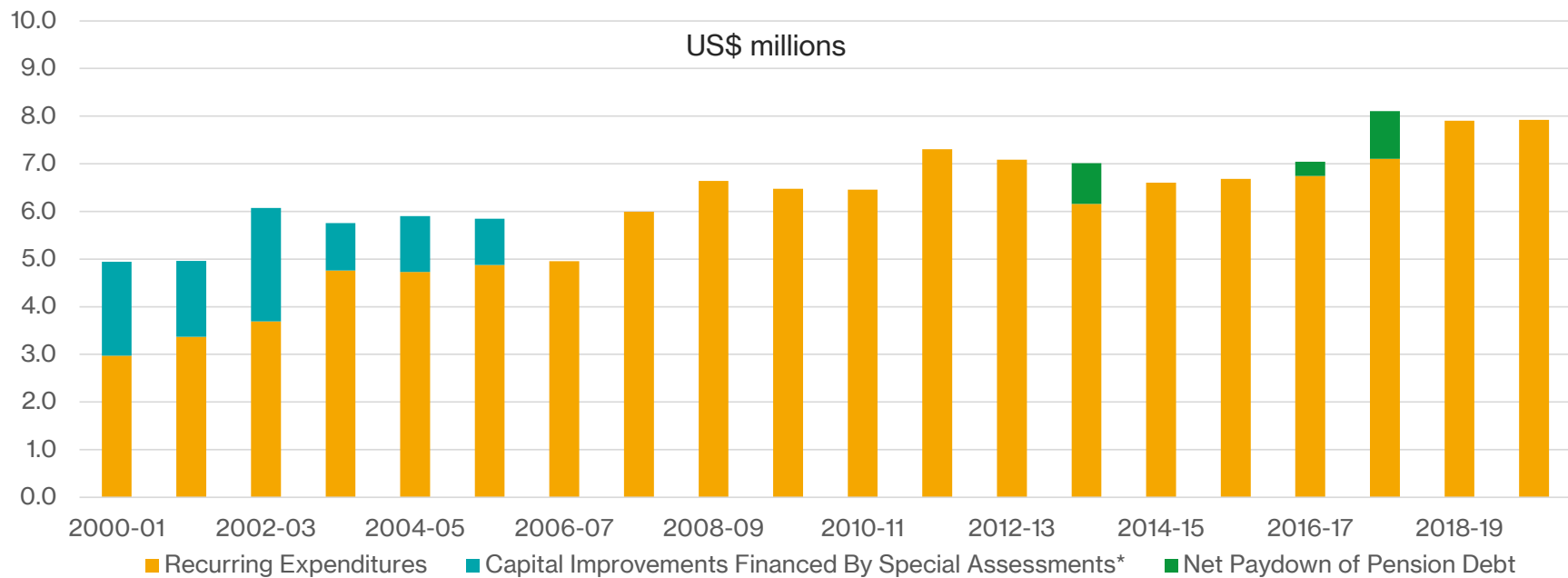
Recurring & Extraordinary Spending

Extraordinary Expenditures Are Stripped From Trend Analysis

*Comprises Corinthian Island and Upper Beach Special Assessment Districts, Sewer Enterprise Fund and Reed Drainage Project.
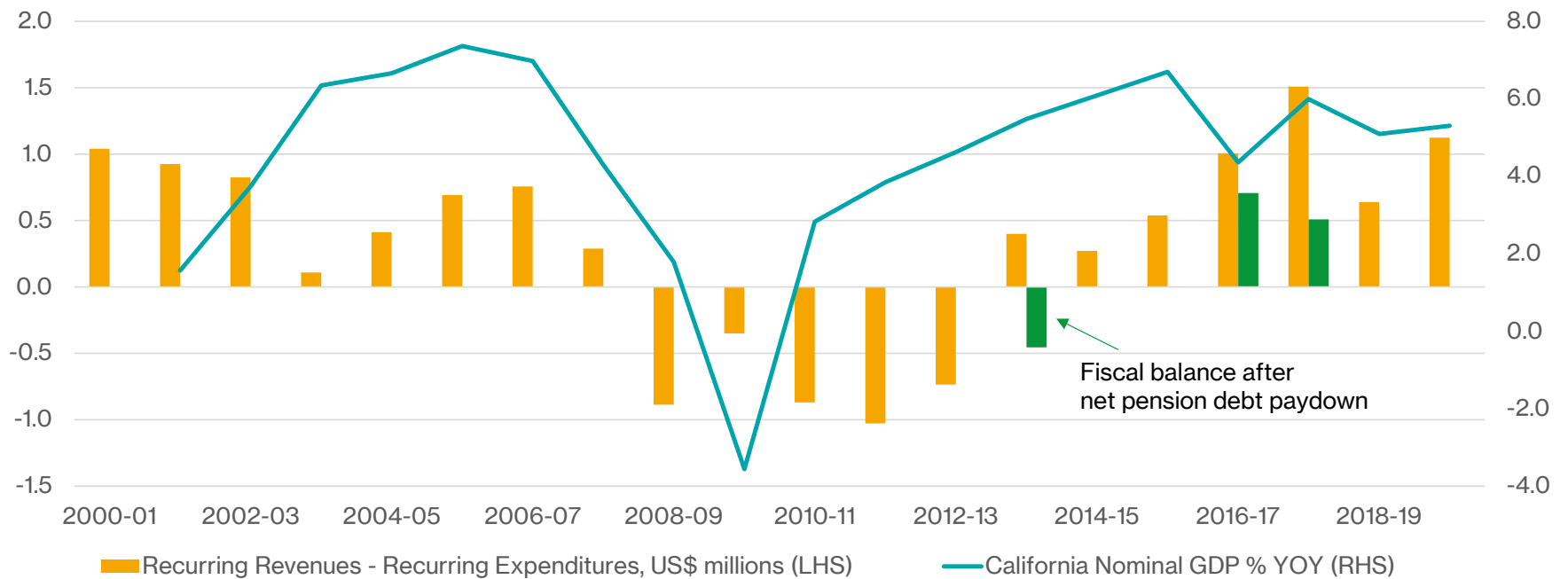
Budget Trends

Fiscal Balance & Economic Growth

Sustained Deficits During Early 2010s Despite Strong Economy

Fiscal balance after
net pension debt paydown

Recurring Revenues - Recurring Expenditures, US$ millions (LHS) ———California Nominal GDP % YOY (RHS)

Fiscal Balance

- The budget has ebbed and flowed between surplus and deficit over the past two decades.

- A strong economy during the 2010s should have delivered budget surpluses, but large capital improvements budgets from 2007-08 to 2011-12 kept the budget underwater.

- The City reined in spending growth in 2013-14 as it committed to close the unfunded pension gap. It has since worked hard to ensure long-term budget health.

- The economic fallout from COVID-19 and ongoing investment underperformance by CalPERS pose new challenges to the City's finances.

Revenue & Expenditure Growth

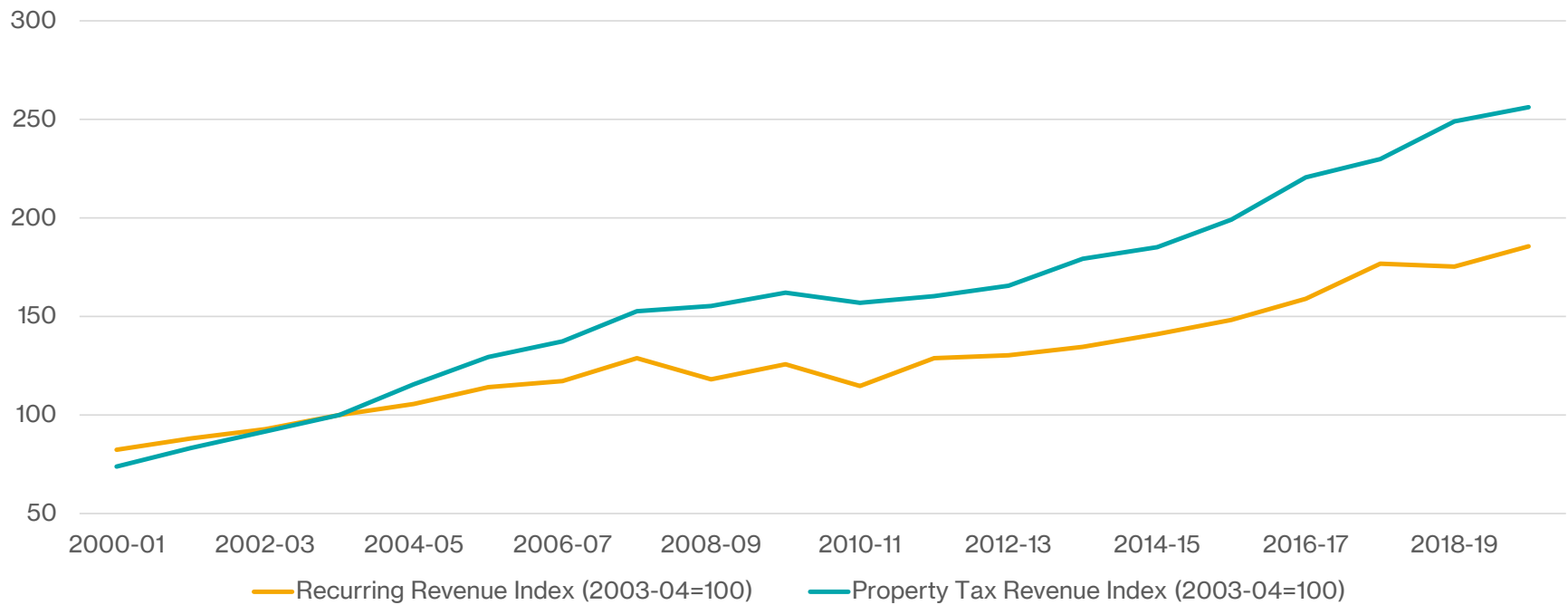Bumper Spending Is Reined In As City Prioritizes Pension Debt Paydown

9
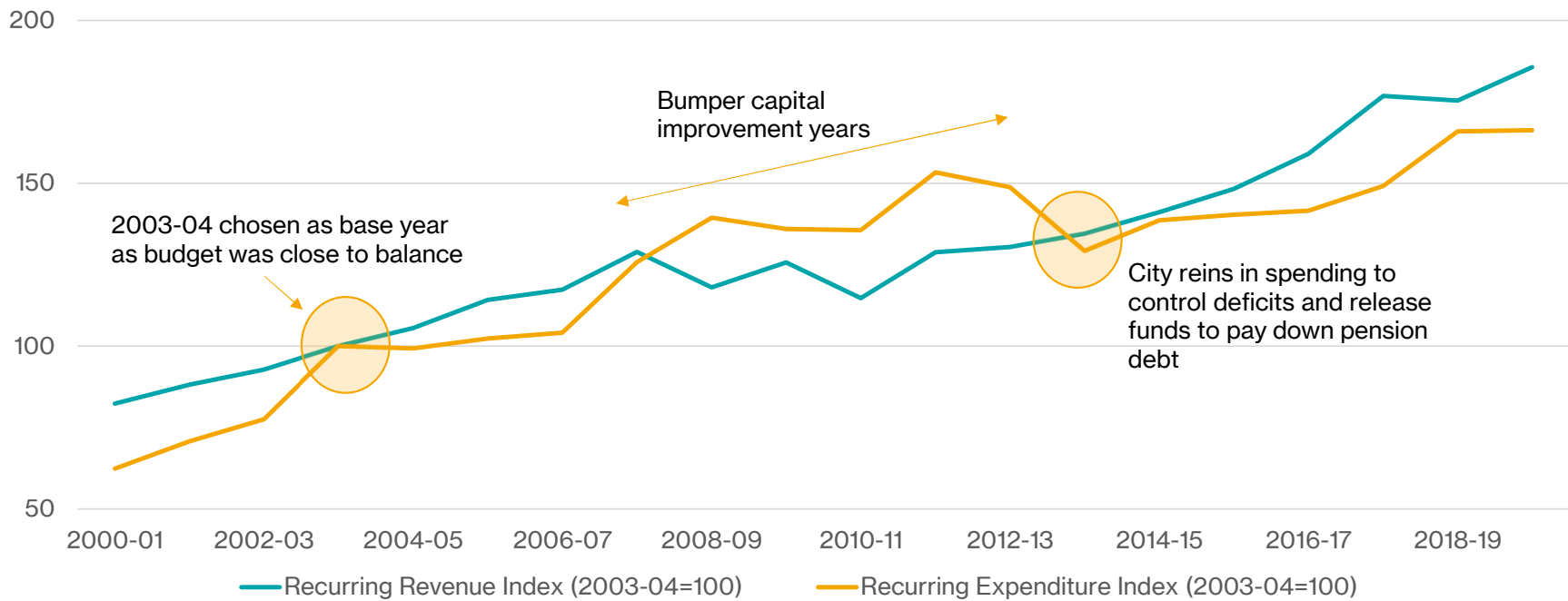
Revenue Trends

Property Tax Trends

Property Tax Growth Outpaced Total Revenue Growth from 2000-01 to 2010-11

Property Tax Trends

Property Taxes Now Steady At About Two-Thirds of Recurring Revenues

2000-01	42
	44
2002-03	47
	47
2004-05	52
	53
2006-07	55
	56
2008-09	62
	61
2010-11	64
	59
2012-13	60
	63
2014-15	62
	63
2016-17	65
	61
2018-19	67
	65

■ Property Taxes, % of Recurring Revenues

12
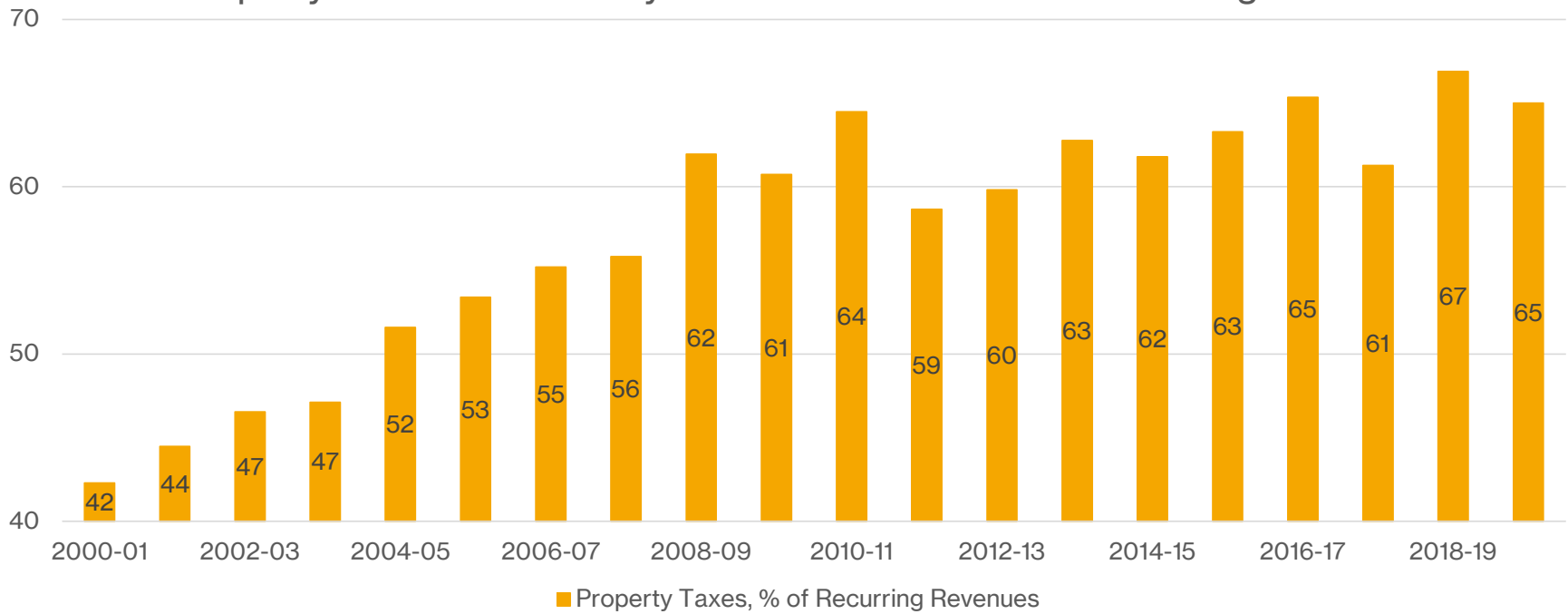
Property Tax Dependence

- The City's increased reliance on property tax revenues has advantages and disadvantages.

- Property tax revenues are *predictable* because they are based on assessed values. Assessed values rise annually by 2% or the rate of inflation, whichever is lower.

- Only if a property is remodeled or changes ownership does the assessed value get rebased to the current fair market value.

- But property taxes are *inflexible*, and they are subject to catastrophic downside in the event of a housing market collapse or disaster that impacts the housing stock.

- Note: Property tax revenues lag the economic/property market cycle by about 18 months, because assessed values are set in the January prior to the start of the fiscal year.

Sources of Revenue

% of Recurring Revenues	2000-01	2019-20	Change (% pts)
Property Taxes	42.3	65.0	+22.7
Local Non-Property Taxes	6.7	3.9	-2.8
Licenses & Permits	9.7	6.0	-3.7
Fines & Forfeitures	1.0	0.4	-0.6
Investment & Property	4.9	1.7	-3.2
Other Agencies	8.8	2.1	-6.7
Service Charges	6.1	3.6	-2.5
Fire Tax	10.9	10.2	-0.8
Other Revenues	9.6	7.2	-2.4
Total	**100.0**	**100.0**	**0.0**

Other Sources of Revenue

- The Fire Tax has remained steady as a share of revenue. Other revenue sources have declined in importance.

- Investment & property income has collapsed due to lower interest rates, as has revenue from other agencies due to cash-strapped county and state governments.

- Revenues from permitting, service charges, and fines – mostly related to local planning and building – have not increased in nominal terms despite steady residential construction volumes.

Planning & Building Revenues
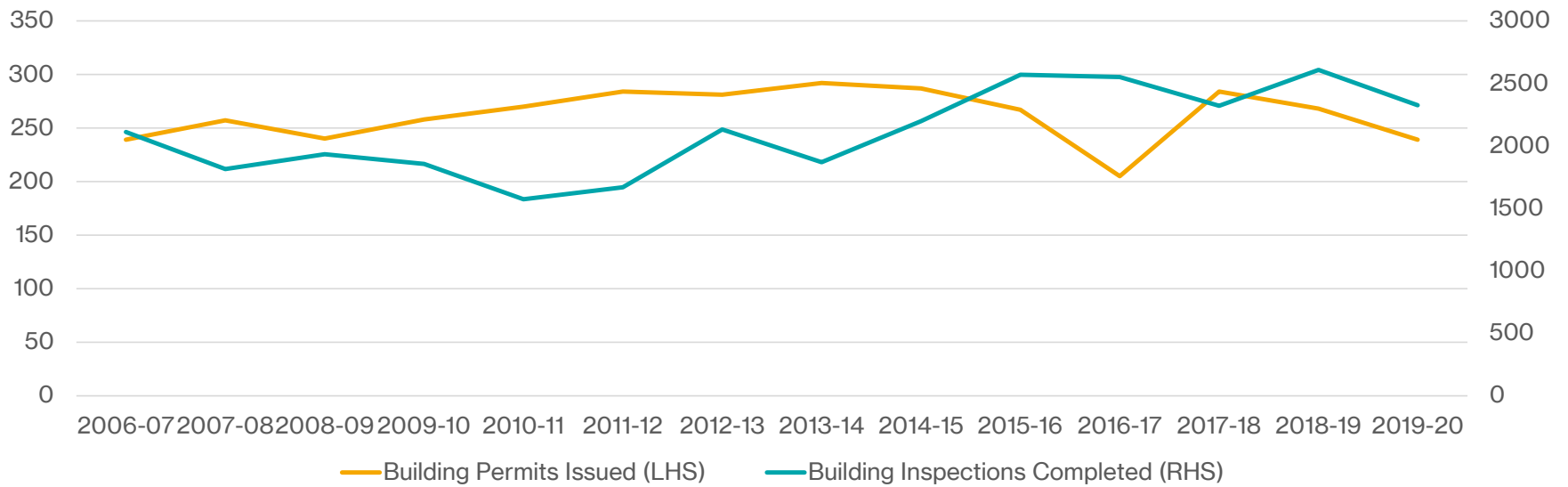

Planning & Building Revenues Have *Flatlined* For 20 Years
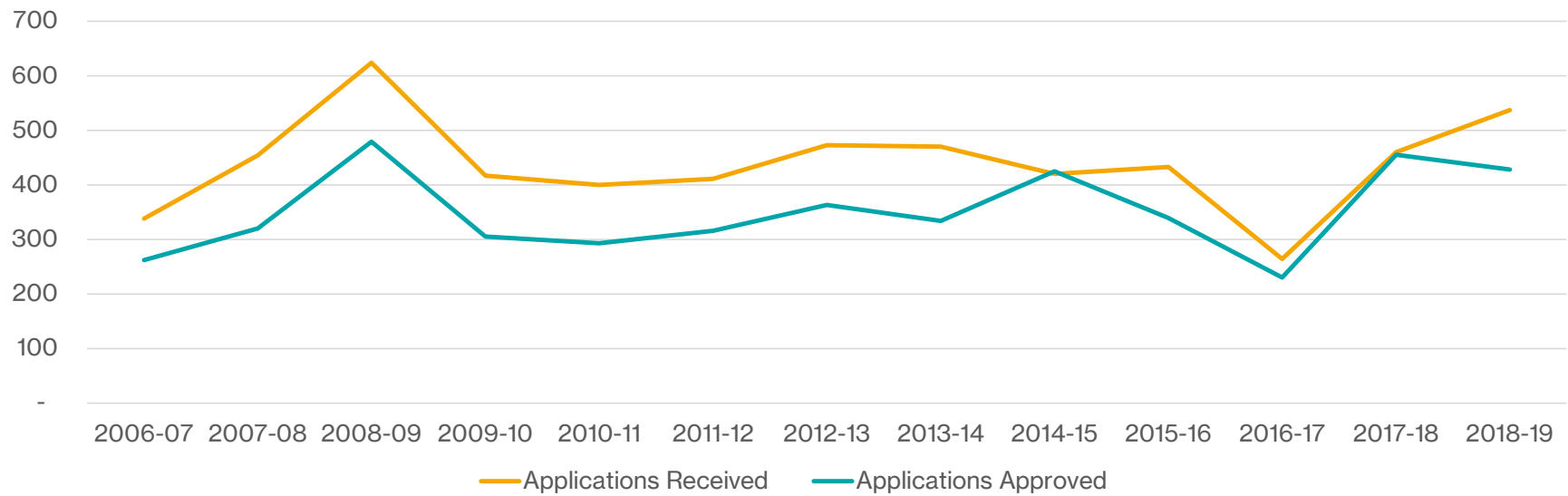Despite Steady Residential Construction Activity
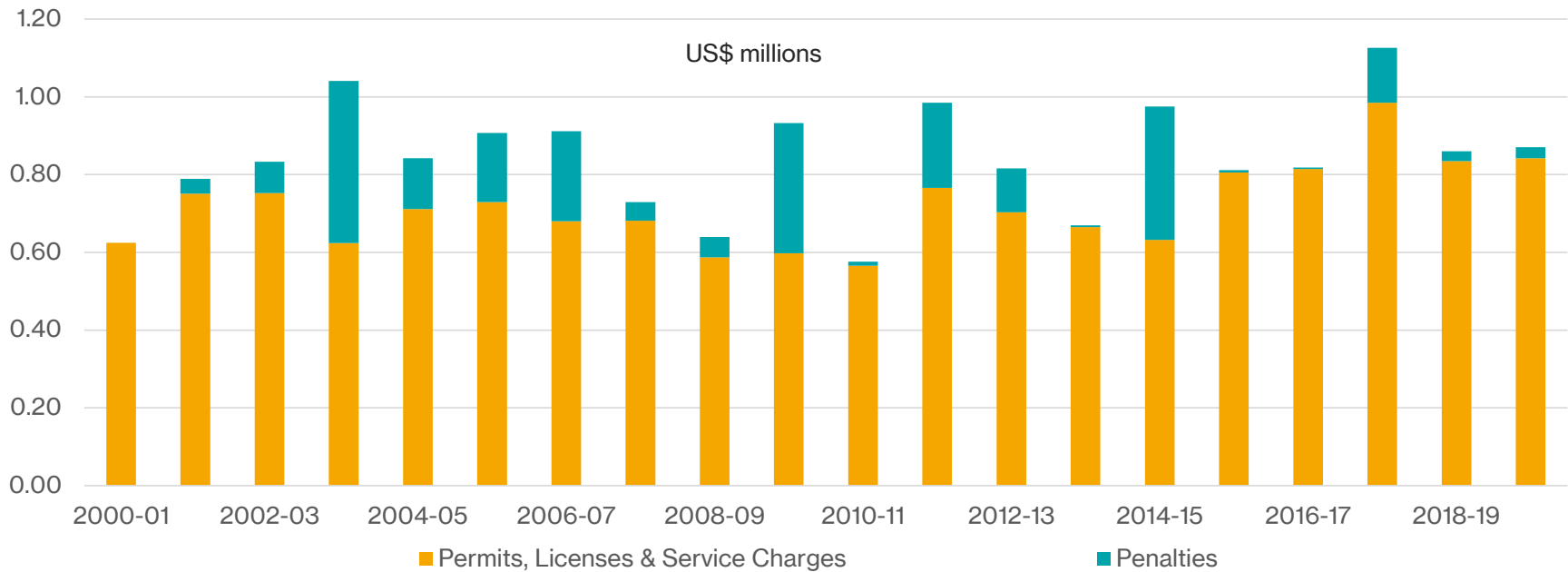
Building Department Activity

Building Department Activity Has Remained Very Stable

Planning Department Activity

The Overall Trend in Planning Department Activity Has Also Been Stable

Expenditure Trends

Personnel Costs

- Recurring personnel costs continue to account for around half of the budget.

- Salary & wage growth has been modest over recent years and headcounts are down.

- Benefits have risen because of rising pension & healthcare costs for current *and* former employees. The increase in cost is systemic and largely, but not entirely, outside of the City's control.

- New costs associated with pension-related debt (lease-leaseback) have added to personnel costs.

- The City has made several large paydowns of its unfunded pension liability since 2013-14. This is an additional workforce cost.
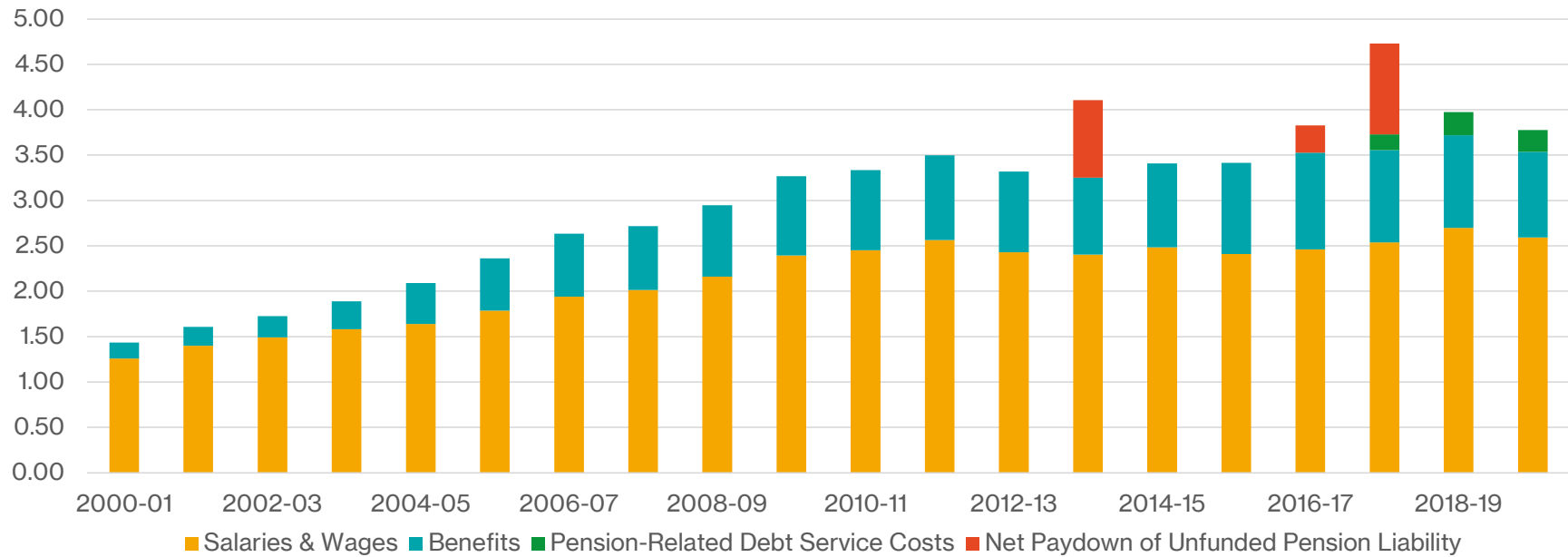
Recurring Personnel Costs

As a Percentage of Recurring Expenditures

Legend: ■ Salaries & Wages ■ Benefits ■ Pension-Related Debt Service Costs

Personnel Costs: Total

USD Millions

Pension Pressures

- Generous pensions, increased life expectancy and optimistic investment assumptions have created instability in the Californian public pension system.

- In 2013, pension reform reduced the generosity of benefits for new CalPERS members, but not existing ones (Classic members). The California Rule prohibits such adjustments.

- In 2015, new accounting standards required municipalities to bring unfunded pension liabilities on balance sheet.

- Between 2013-14 and 2017-18, the City paid down $4.75 million of unfunded pension liabilities ($2.6 million debt-financed), briefly delivering fully-funded status.

- By June 2019, the City's unfunded position had risen back to $1.58 million. Further deterioration is likely as CalPERS continues to undershoot its investment target.

Belvedere's Pension Position

As at June 2019	
Actuarial Liability[1]	$23.88 million
Market Value Of Assets	$22.30 million
Unfunded Actuarial Liability (a)	$1.58 million
CalPERS Funding Ratio	93.4%
Lease-Leaseback Debt (b)	$2.46 million
Total Pension Debt (a+b)	$4.04 million
All Debt Funding Ratio	83.1%
Active Members (Of Which Classic)	18 (11)
Retired Members (Of Which Classic)	53 (53)

[1] Present value of future benefits attributable to past service using CalPERS discount rate of 7.0%. Source: CalPERS

Pension Debt

USD Millions
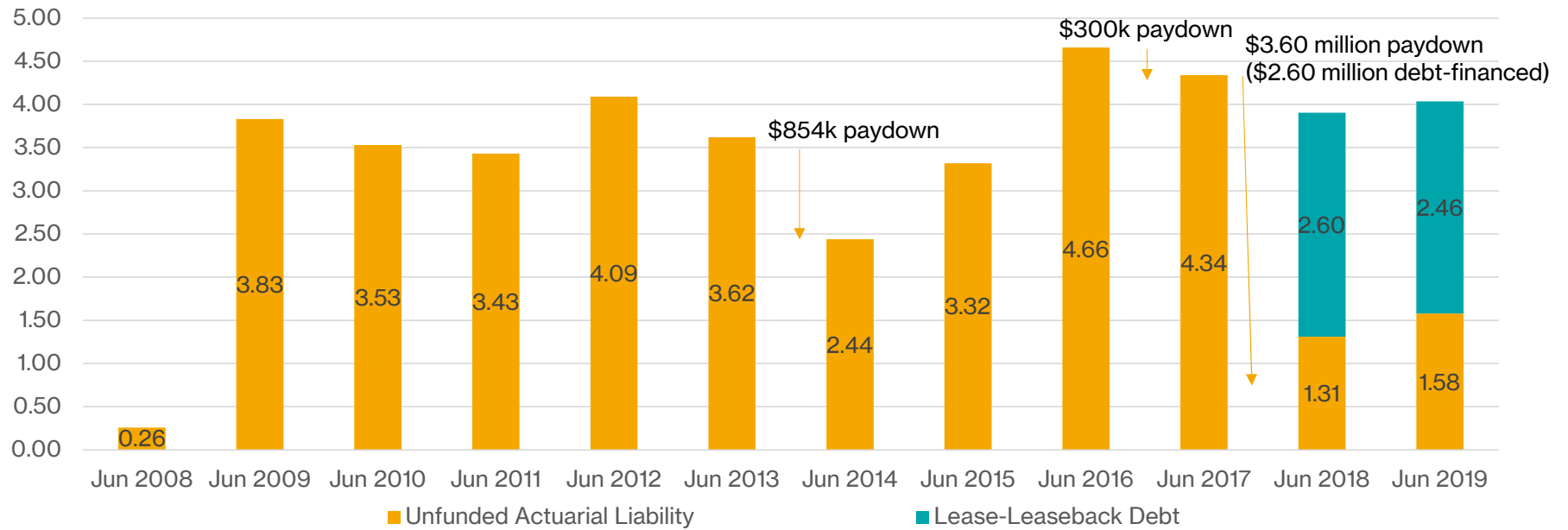
Healthcare Costs

- The City's healthcare expenses have risen fivefold since 2000-01. Healthcare benefits are offered to both active and retired employees, through a cost-sharing arrangement.

- High medical cost inflation, increased life expectancy, an aging pool, and generous healthcare benefits offered to retired City Managers have pushed costs higher.

- The City utilizes a "pay-go" approach to funding healthcare costs, paying the expense from the current operating budget.

- The City does not set aside funds to pay for healthcare benefits already promised both to retirees and to current employees when they retire. This funding gap is known as the net OPEB (Other Post-Employment Benefits) liability.

- The City's net OPEB liability stood at $1.31 million as at June 2019.

- Unlike pensions, healthcare benefits may be altered with fewer constraints.

Belvedere's OPEB Position

As of June 2019	
Total OPEB Liability[1]	$1.31 million
Market Value Of Assets	$0
Net OPEB Liability	$1.31 million
Discount Rate (Bond Buyers 20-Year Bond Index)	3.50%
Medical Inflation Assumption	6.30% for 2021, Decreasing To 4% In 2076
Active Members	18
Inactive Members (Of Which Receiving Benefits)	18 (11)
Eligibility	Retire Directly From City, Age 50+ & 5 Years CalPERS Service, Or Disability

[1] Present value of future benefits attributable to past service. Source: Bartel Associates

Departmental Trends

Departmental Spending

- The split of spending between departments has bumped around over the years, largely dependent on headcount. On average, shares have remained roughly the same.

- Fire costs have steadily pushed higher as a share of the budget.

- Capital improvements are the delta in the budget and fluctuate significantly.

Departmental Spending

% of Recurring Expenditures	2000-01	2019-20	Change (% pts)
General Administration	12.6	12.3	-0.4
Planning & Building	11.9	11.8	-0.1
Police	22.0	18.4	-3.7
Public Works	13.4	13.6	0.2
Community Center	0.5	0.9	0.5
Non-Departmental	4.4	5.6	1.1
Capital Improvements	12.5	11.0	-1.5
Fire	18.8	21.3	2.6
Other Restricted Funds	3.8	5.1	1.3
Total	**100.0**	**100.0**	**0.0**

Fire Spending

- Belvedere contracts with Tiburon Fire Protection District for fire and ambulatory services. TFPD contract costs have outpaced other departmental spending categories.

- Belvedere's Fire Tax escalator has not kept pace with contract costs. As a result, the Fire Tax covers a diminishing share of fire expenses. The General Fund picks up the remainder.

- TFPD had unfunded pension liabilities of $8.78 million as at June 2019. Increased required payments by CalPERS will affect contract costs going forward.

Fire Contract: Source of Funds

USD Millions
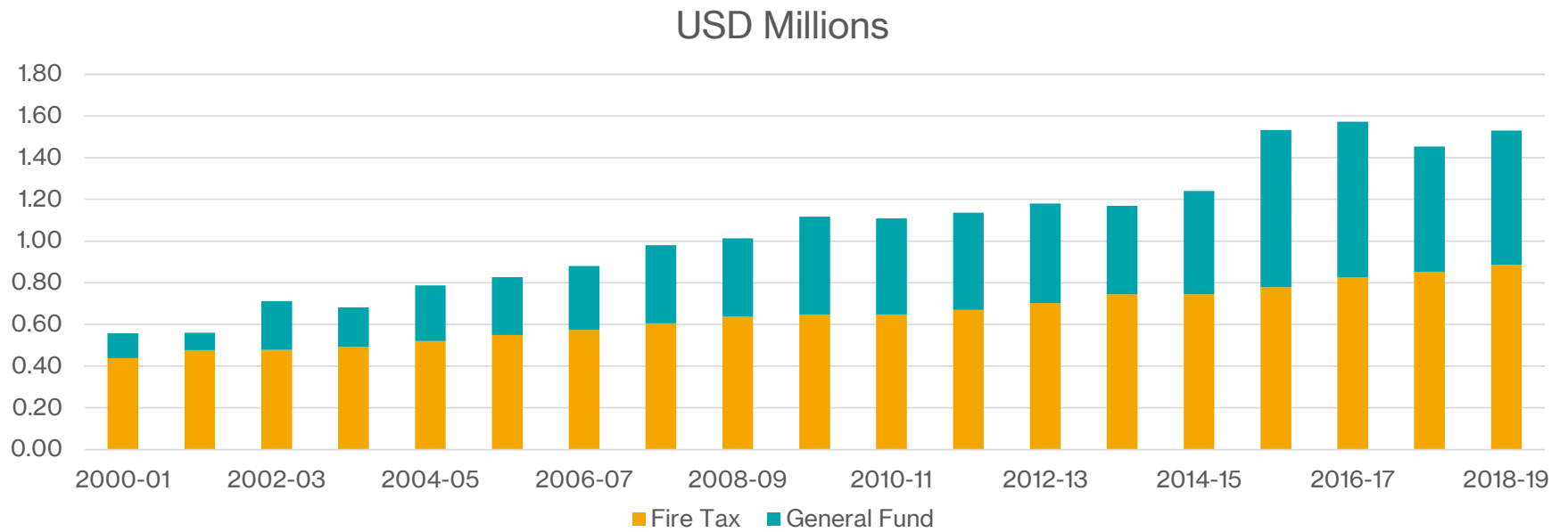
Building & Planning

- Building & planning department expenses have consistently edged higher in nominal terms, and, at times, as a share of the budget.

- License, permit and service fees have not kept pace with these higher costs.

- As a result, the department has become loss making.

Building & Planning Spending

As a Percentage of Recurring Expenditures
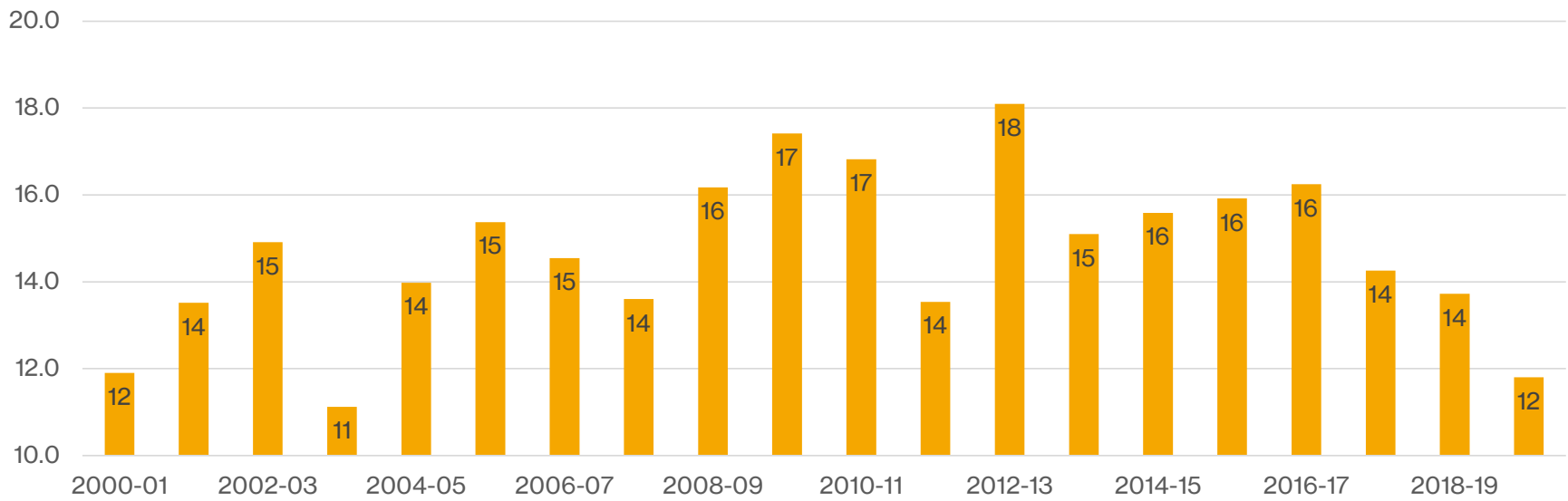
Building & Planning Net Balance

Department Revenues *Minus* Department Expenses[1] ($ Millions)
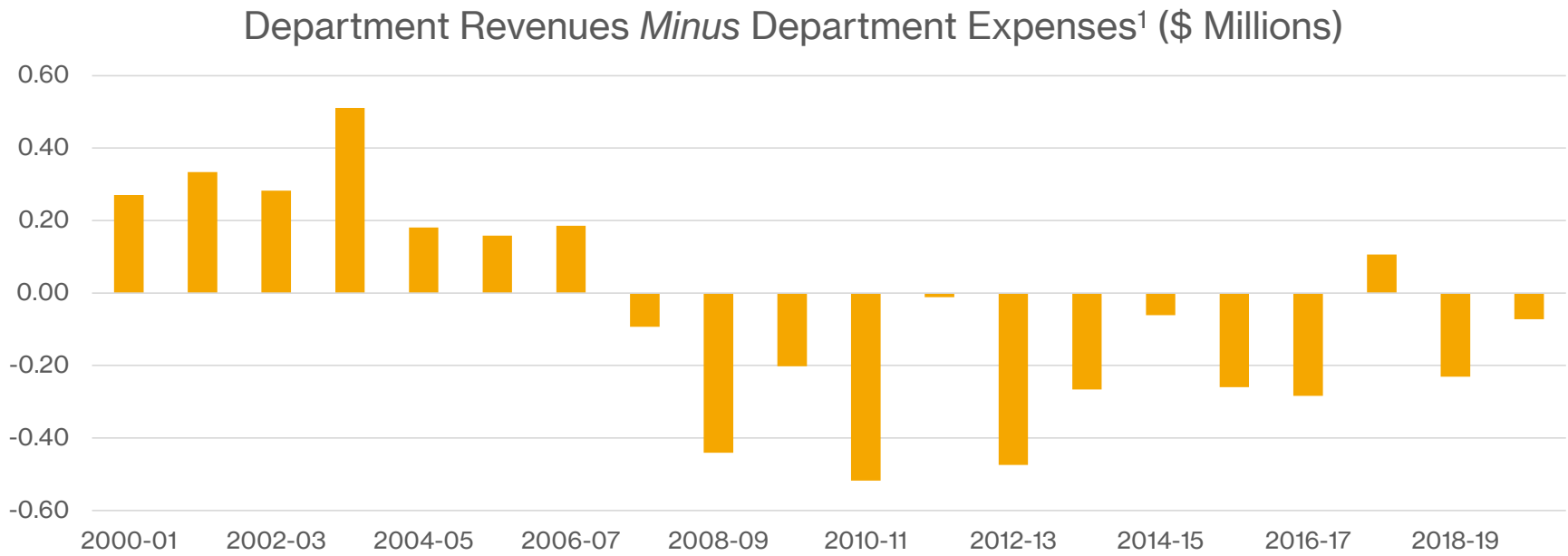
[1]Expenses exclude admin overhead assigned to Planning & Building Departments.

Capital Improvements

- As pension costs have accelerated, capital improvements have taken a back seat.

- Emergency repairs to a portion of the seawall and the publicly-privately financed Golden Gate Stairs boosted capital improvements in 2018-19 and 2019-20.

- The City's two seawalls need upgrading. The estimated project cost is $20.1 million. No source of funding has been identified.

Capital Improvements

As a Percentage of Recurring Expenditures
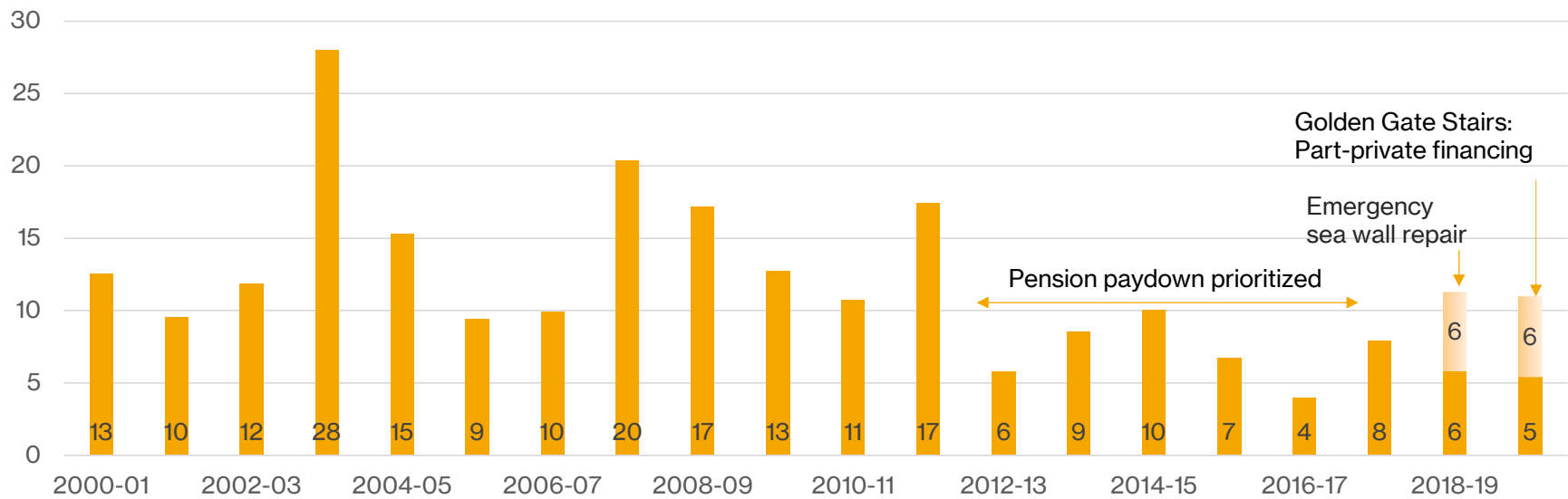
Conclusions & Recommendations

Conclusions: 1

- Belvedere has been working hard to maintain its good fiscal standing but rising pension and healthcare costs and the economic fallout of COVID create new challenges.

- It is important to fully understand the City's pension and OPEB risk through comprehensive review and scenario modeling, and adoption of a Pensions' and OPEB Strategy.

- Fire contract costs are burdensome and unlikely to ease up. Alternative options should be explored. An increase in the Fire Tax through a ballot initiative might also be considered.

- Building and planning departments are not covering their costs. Fee schedules should be reevaluated to ensure cost recovery.

Conclusions: 2

- The City's increasing dependence on property taxes provides revenue stability, but also revenue inflexibility.

- Efforts should be made to ensure new constructions are fully marked-to-market to optimize property tax revenues.

- Capital improvements are slowly being chipped away as the budget comes under pressure. Private fundraising for capital projects may become the norm.

- There is limited scope to fund the Sea Wall Project from the current budget. A new revenue stream should be identified.

Addendum

Pension Funding Status by City: June 2018

US$ million	Actuarial Liability (1)	Market Value of Assets (2)	Unfunded Actuarial Liability (3=1-2)	POBs/Other Pension Debt (4)	Funding Status (3+4/1)
Belvedere	22.1	20.8	1.3	2.6	82%
Corte Madera	69.8	49.3	20.5	0.0	71%
Fairfax	34.3	28.1	6.2	0.0	82%
Larkspur	63.6	45.9	17.7	0.0	72%
Mill Valley	158.8	112.8	46.0	3.2	69%
Novato	225.7	153.9	71.8	18.6	60%
Ross	25.6	21.4	4.2	0.0	84%
San Anselmo	54.2	36.0	18.2	1.4	64%
San Rafael	584.1	450.0	134.1	0.0	77%
Sausalito	103.5	72.9	30.6	0.0	70%
Tiburon	38.0	28.9	9.2	0.0	76%

[1] Present value of future benefits using **CalPERS' discount rate of 7.0%.** Source: California Pension Tracker, Stanford University

Pension Funding Status By City: June 2018 Market Discount Rate Scenario

US$ million	Market Liability (1)	Market Value of Assets (2)	Unfunded Market Liability (3=1-2)	Pension Obligation Bonds (4)	Funding Status (3+4/1)
Belvedere	37.0	20.8	16.3	2.6	49%
Corte Madera	115.9	49.3	66.6	0.0	43%
Fairfax	57.9	28.1	29.8	0.0	49%
Larkspur	105.6	45.9	59.7	0.0	43%
Mill Valley	258.6	112.8	145.8	3.2	42%
Novato	349.5	153.9	195.6	18.6	39%
Ross	42.5	21.4	21.1	0.0	50%
San Anselmo	85.3	36.0	49.3	1.4	41%
San Rafael	928.8	450.0	478.8	0.0	48%
Sausalito	167.6	72.9	94.7	0.0	43%
Tiburon	62.3	28.9	33.4	0.0	46%

[1] Present value of future benefits using **market discount rate of 3.25%.** Source: California Pension Tracker, Stanford University
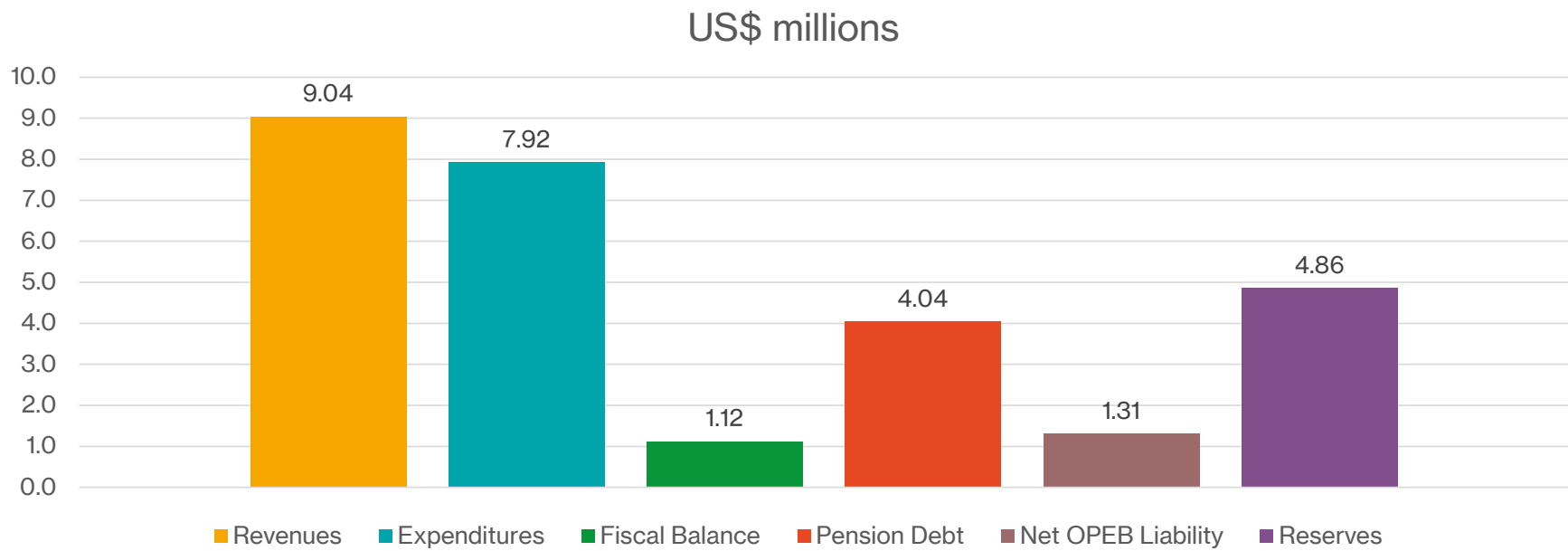
Fiscal Snapshot 2019-20

US$ millions

Pension debt and net OPEB liability as at June 2019. June 2020 data not available.

Reserve Policy

- In 2008-09, the City introduced a reserve policy that required the City to maintain a reserve balance equal to no less than six months of combined General Fund operating expenses and fire service contract costs.

- That policy was expanded in 2020-21 so that reserves must now equal no less than six months of combined General Fund operating expenses, fire service contract costs *and* pension-related debt service costs.

- The City has met its reserve target every year since inception.

- The reserve fund is intended as a rainy-day fund for catastrophic loss.

A Sustainable Pensions' Strategy for Belvedere

Introduction

The City of Belvedere maintains a robust fiscal standing but rising pension and OPEB costs pose concerns. It is important that the trajectory of these costs is understood, and that a strategy is developed to budget appropriately and proactively for them. This paper discusses the City's pension position and is intended as background for the *Taskforce on Pensions and OPEBs* to begin its work.

PART 1: CALPERS

What is CalPERS?

California Public Employees' Pension System (CalPERS) is a public pension fund that provides retirement benefits for California's state workers and employees of local public agencies. Of the 478 cities in California, 449 of them contract with CalPERS for employee retirement benefits. Larger cities like Los Angeles, San Francisco and San Jose maintain their own pension funds. In total, there are 85 public pension funds operating in California, of which CalPERS is the largest, with 2.0 million members. The other dominant ones include the California State Teachers Retirement System (CalSTRS), the University of California Retirement System, and the county systems that operate outside of CalPERS under the County Employees Retirement Law (CERL). There is reciprocity between the various California public pension systems.

Is it a defined-benefit system?

Yes, pensions offered through CalPERS are defined benefit plans. The amount pensioners receive each month is determined by their age at retirement, the number of years worked and highest annual salary. For example, a "2% at 55" plan provides a pension equal to 60% of final salary if the recipient retires at age 55 after 30 years of work. Payments are then indexed to inflation through an annual cost-of-living adjustment (COLA) and continue from retirement until death. Pension rights vest after five years of employment and the minimum retirement age is 50 in most cases. Contracting agencies choose what benefit formula to offer their employees from a set of options provided by CalPERS. Safety workers are typically offered more generous benefits than non-safety workers because of the nature of their work and shorter working lives. Contracting agencies also select their COLA, their highest annual salary formula (one year or three-year average), and various other optional benefits.

Is CalPERS in financial difficulty?

CalPERS was designed to be a prefunded system. Employees and employers make monthly contributions which are invested through CalPERS' investment arm. Assuming investment returns meet expectations, and barring other actuarial surprises, there should be sufficient funds, after expenses, to cover the pensions that contracting agencies will eventually owe.

For much of its existence, CalPERS worked as designed. Indeed, by 1999, CalPERS was significantly overfunded with assets equal to 128% of accrued liabilities, thanks to a booming stock market. As a result, unions pushed the state legislature to pass SB 400, which cut employer payments and increased the generosity of pensions for state employees (local agencies followed suit), both prospectively *and retrospectively*. Under the new "3% at 50" formula, for example, safety workers could retire at age 50 after 30 years of service and receive 90% of final pay for the rest of their lives. The new formulas were based on the premise that CalPERS would produce an 8.25% investment return in perpetuity, keeping the system fully funded. But returns did not live up to these lofty goals, with asset values falling sharply during the Great Recession of 2007-09. Coupled with increased life expectancy, CalPERS has moved from surplus into sustained deficit, with no obvious solutions for closing the gap. It is important to recognize that CalPERS itself is just a managing agency. Ultimately, it is the state and local agencies that contract with CalPERS that bear financial responsibility for the pension commitments they have made.

Chart 1: CalPERS Net Investment Return, % YOY

Fiscal Year End 6/30. Source: CalPERS
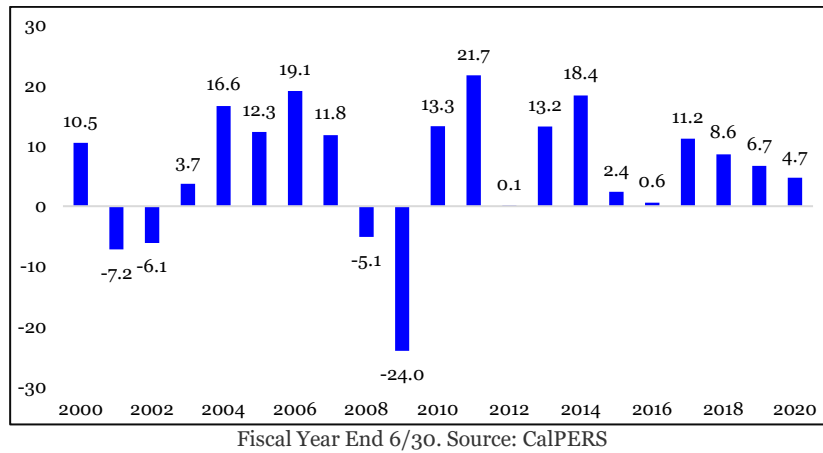
Chart 2: CalPERS Cumulative Investment Performance Index (1999=100)

Fiscal Year End 6/30. Source: Author's Calculations
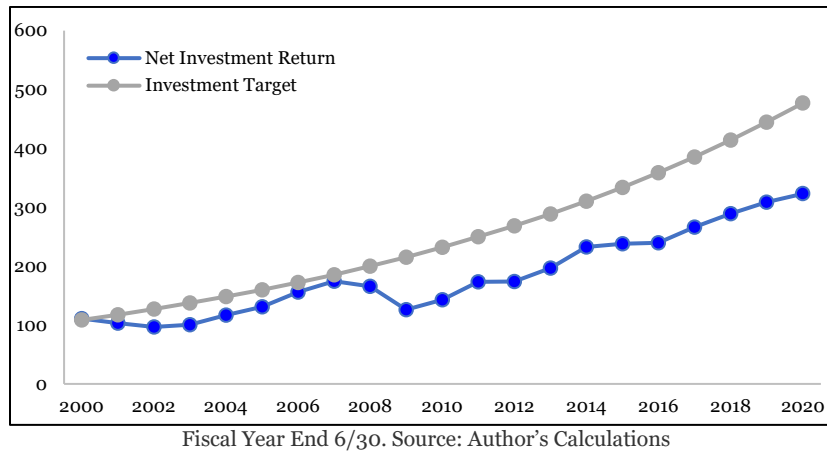
Can benefits be cut?

Yes and no. In 2012, the state legislature passed the California Public Employees' Pension Reform Act (PEPRA) which created a new class of employee for anyone new to the California public pensions system, with less generous benefits, a higher minimum retirement age (new non-safety workers only), and higher contributions. But pension conditions for existing CalPERS members ("classic members") were left untouched, except for a ban on certain forms of pension spiking. The reforms also provided scope for higher classic employee contribution rates. The act covered the state's two largest pension systems, CalPERS and CalSTRS, as well as 20 county systems.

Why are classic employees so protected?

One key reason PEPRA did not go further in targeting the pension rights of classic employees is the legal ruling known as the **California Rule**, which was established by a 1955 California Supreme Court ruling. This holds that public employees are guaranteed the pension they have accrued to date *and* are entitled to keep earning a pension according to rules that are at least as generous for the reminder of their service. Changes to pension benefits "must bear some material relation to the theory of a pension system and its successful operation" and if they result in disadvantages to employees, they should be accompanied by comparable new advantages. For all intents and purposes, this prevents any reduction in the generosity of pension formulas for existing employees.

In fact, unions sued in the aftermath of PEPRA arguing that the elimination of certain forms of pension spiking for classic members violated the California Rule. The issue was litigated, and in 2020 the California Supreme Court ruled that the changes were permissible and that no offsetting benefit was required because the changes were simply closing loopholes on pension spiking that distorted pension calculations. Nevertheless, the scope of the ruling was narrow, and the core tenets of the California Rule remain intact.

What happens to pension obligations if agencies file for bankruptcy?

Various cash-strapped agencies have filed for bankruptcy over the years, the largest ones being the City of Vallejo in 2008, and Stockton and San Bernardino in 2012. Fast-rising pension costs were a major contributing factor in all three cases. In the Stockton case, the bankruptcy judge opened the door for pension benefit cuts, arguing that under federal law such contract impairment was constitutional, despite the California Rule. Yet Stockton kept pension debt off the table, choosing instead to restructure other debts, cut retiree health insurance benefits, reduce services, cut staff, and impose new voter-approved taxes. It did this to avoid a "risk-free" termination valuation from CalPERS (see page 14) which would have revealed a level of debt so large that restructuring might have become impossible. Nevertheless, smaller, less-complex agencies have subsequently defaulted on their CalPERS obligations. In 2014, the City of Loyalton stopped paying its CalPERS' bills. Its retirees became the first in California to see their pensions cut by CalPERS, to just 40 cents on the dollar.

So how well funded is CalPERS today?

Despite the PEPRA reforms, and a healthy 8.5% investment performance in the 10 years to June 30, 2020, CalPERS has struggled to close the funding gap that emerged in the wake of the Great Recession. A low starting base, increased life expectancy and modest lowering of the discount rate (see next) have stifled the improvement in funded status. Provisional data for June 30, 2020 shows CalPERS' contracting agencies with an average funded ratio of 71%. This compares with a low of 61% in 2009 and a peak of 128% in 1999. This amounts to $160 billion in unfunded pension debt, equal to more than $12,000 per Californian household. CalPERS is just one of several underfunded public pension systems in California.

Table 1: CalPERS' Public Employees Retirement Fund (PERF)

Year	Total Fund Market Value (US$ bn)	Funded Status (%)
2011-12	233.4	69.6
2012-13	257.9	69.8
2013-14	300.3	76.3
2014-15	301.9	73.1
2015-16	302.0	68.3
2016-17	326.4	68.0
2017-18	354.0	70.2
2018-19	372.6	71.0*
2019-20	389.0	70.8*

*Using a 7.0% discount rate. Source: CalPERS

Is true funded status worse than officially reported?

Yes, this is likely true. Let's back up. Funded status is essentially the ratio of assets (market value of assets) to liabilities (actuarial accrued liability). The UAL (unfunded accrued liability) is the gap between liabilities and assets. Whilst it is easy enough to calculate the market value of assets, calculating the present value of future pension benefits – the accrued actuarial liability – is complicated and relies on a whole bunch of economic and demographic assumptions. At the crux of the calculation is the discount rate, used to discount these future cashflows. A higher discount rate means a lower present value liability. To be conservative and ensure pension commitments are covered, pension models typically use the yield on high investment-grade

municipal bonds as the discount rate i.e. what they are sure to earn by investing employer and employee contributions. But CalPERS uses its expected rate of return on investments as its discount rate. This would be fine if CalPERS met its investment goal, but it has fallen short on a sustained basis, with returns averaging 5.5% since 2000, short of the 8.5% return envisaged when the state legislature enhanced benefits in 1999. CalPERS discount rate currently stands at 7.0%, above what most analysts think it a reasonable long-term investment return. This means that accrued liabilities are understated, and the funding gap is likely wider than officially reported.

Table 2: CalPERS' Discount Rate

Year	Old Rate	New Rate
2004	8.25%	7.75%
2012	7.75%	7.50%
2018-19	7.50%	7.375%
2019-20	7.375%	7.25%
2020-21	7.25%	7.00%

Source: CalPERS

Table 3: CalPERS' Net Investment Returns (June 30, 2020)

| Year	Compounded Rate of Return
1 year	4.7%
5 years	6.3%
10 years	8.5%
20 years	5.5%
30 years	8.0%

Source: CalPERS

Do employers and employees have to pay more to fund the gap?

Yes, they do. Each year, CalPERS actuaries calculate a plan's annual required contribution, based on actuarial valuations from two years prior (i.e. 2020-21 contributions are based on actuarial valuations as of June 30, 2018), which is the minimum that must be paid. It comprises two elements: the normal cost rate, which is the annual cost of service accrual for current employees, and an annual payment towards the UAL. The former is shared between employer and employee. The latter is paid by the employer **i.e. the cost of *past* inaccuracies in assumptions is borne entirely by the employer.**

Annual Required Contribution = Normal Cost Rate + Annual Payment on UAL

Although CalPERS lets the UAL be amortized over 20-30 years, so as not to overwhelm agencies' finances, agencies do have the option of making additional extraordinary payments to pay down their UAL at a faster clip. Those that can afford to often do. All told, employer contributions have surged over the past decade, and are now three to four times as high as employee contributions.

Chart 3: CalPERS' Contributions History (US$ billion)
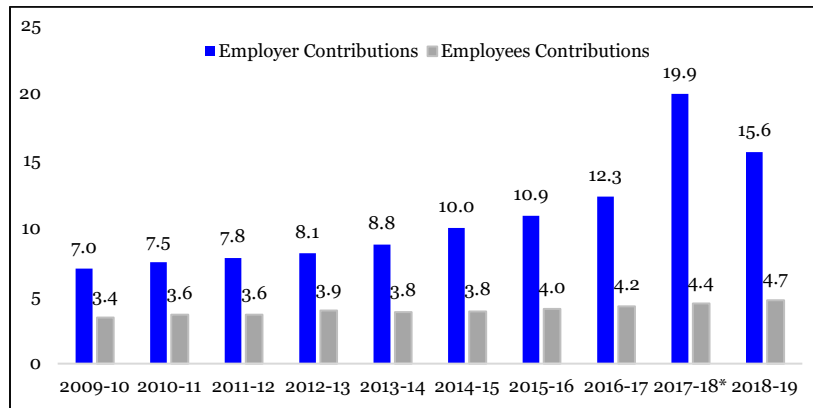
*2017-18 employer contribution includes $6 bn contribution from the state. Source: CalPERS

CalPERS produces a nice catch-all graphic to illustrate the sources of income that fund public employee pensions, and how these sources have evolved, known as *The CalPERS Pension Buck*. The 2020 version, based on the prior 20 years of data, shows the cost split between investment earnings, employer contributions and employee contributions as 55 cents, 32 cents and 13 cents, respectively. In 2015, the split was 65/22/13. The original intent of SB 400 was that investment earnings would contribute 75 cents and the remainder would be split between the employer and employee. The *Pension Buck* is a backward-looking indicator. The respective shares continue to work against employers.

Chart 4: The CalPERS' Pension Buck 2020

Based on CalPERS income over the last 20 years (as of June 2020) every dollar spent on public pensions comes from these three sources. Source: CalPERS

How do we fix the problem?

Simply put, there are no quick fixes to this complex problem. Optimists hope that a sustained increase in investment returns will make the problem disappear. Others think that Sacramento will eventually pass comprehensive pension reform that trims benefits for prospective service, to ensure the pension system's "successful operation", as permitted by the California Rule. Even if true, agencies will still carry the cost of unfunded pension benefits already accrued. Proactive agencies – cognizant that pension debt growth is a form of deficit spending – are pursuing various strategies to close the gap. Common elements include:

- More accurately valuing UALs using a lower discount rate.
- Imputing the true cost of pension accruals when budgeting for the year.
- Negotiating with staff to shift a greater share of pension costs onto employees.

- Making lump sum payments, accelerating amortization schedules, and funding special reserves to pay down pension debt at a faster rate.
- Slowing the pace at which new pension obligations accrue, through headcount cuts, trimming pensionable pay and shifting to contract workers.
- Pursuing other cost-cutting measures and/or tax increases to ensure long-term fiscal sustainability.

In truth, none of these are particularly palatable solutions, and the challenge is striking a good balance between responsible pension planning and ongoing delivery of essential public services.

PART 2: Belvedere's Pension Status

What does Belvedere's pension plan look like?

The City of Belvedere offers four defined-benefit plans administered by CalPERS, as follows:

- Non-Safety Classic Plan – 2% at 55
- Non-Safety PEPRA Plan – 2% at 62
- Safety Classic Plan – 2% at 50
- Safety PEPRA Plan – 2.7% at 57

It uses a 3-year average of highest compensation to calculate final salary, except for the classic non-safety plan, for which it uses a single-year high. It contracts for a 2% cost-of-living-adjustment for retirees. As of June 30, 2019 (latest available data), Belvedere had 18 active employees: 7 PEPRA members and 11 classic members. This compares with a retirement pool of 53 members, all of whom are classic members.

Table 4: Belvedere's CalPERS Pool: June 30, 2019

Membership Type	Active Members	Retired Members
Non-Safety Classic	8	26
Non-Safety PEPRA	5	0
Safety Classic	3	27
Safety PEPRA	2	0
Total	18	53

Data excludes survivors of retired members. Source: CalPERS

Because Belvedere's classic plans are not the most generous offered by CalPERS (see page 12), in 2006 it began offering a Retirement Enhancement Plan, operated by the Public Agency Retirement System (PARS), to long-term city workers to supplement CalPERS. The plan offers an additional benefit factor of up to 0.5% for non-safety workers (with the total benefit factor capped at 2.5%) and 0.3% for safety workers who complete at least 15 years of service for Belvedere, retire directly from the City and CalPERS, and are at least 55 years' old at retirement. The plan has been closed to new employees since January 1, 2012. There are currently 7 retirees collecting this benefit, with 6 active employees likely to meet the eligibility requirements. Contributions into the PARS plan are paid entirely by the employer.

The City also offers employees the option of participating in a 457(b) defined contribution plan. 457(b) plans are the equivalent of 401(k) plans for government employees. Employees can elect to defer compensation into the plan and the City will match up to $150 per month. Since this is a DC plan, there is no risk borne by the employer.

Does Belvedere have a UAL?

Yes, as with most agencies in California, Belvedere's net pension position moved into sharp deficit following the Great Recession and associated stock market collapse. The combined UAL of its four CalPERS' plans jumped to $3.8 million as of June 30, 2009. Over the next decade, the City worked hard to pay down its UAL, making a series of payments above and beyond the annual required contribution ($854,000 in 2013-14, $300,000 in 2016-17, and $3.6 million in 2017-18, of which $2.6 million was financed through a 30-year lease-leaseback of the City's Corporation Yard). Thanks to these extraordinary payments, Belvedere's UAL with CalPERS dropped to $1.6 million as of June 30, 2019 (latest available data). However, once the outstanding balance of lease-leaseback debt is added back, the UAL rises to $4.0 million, higher than a decade earlier. Concurrently, the UAL on the City's Retirement Enhancement Plan stood at $178,065 as of June 30, 2019, bringing total net pension debt to $4.2 million, an all-in funded ratio of 85%. For context, total City revenues were $9.0 million and expenditures were $8.2 million in 2018-19. Growth in the UAL is

expected in the year to June 30, 2020 given the poor investment environment. CalPERS posted a provisional return of 4.7% in 2019-20, against a target of 7%.

Chart 5: Belvedere's Net Pension Debt
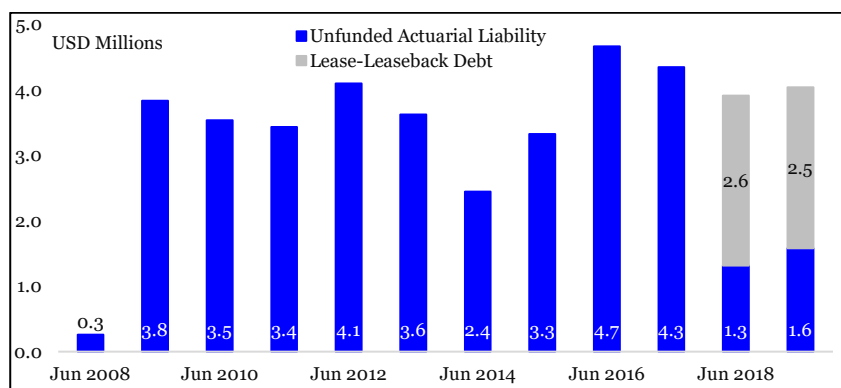
Excludes PARS UAL. Source: City of Belvedere Finance Department

Table 5: Belvedere's Net Pension Debt: June 30, 2019

US$ Millions	Actuarial Accrued Liability	Market Value of Assets	Unfunded Actuarial Accrued Liability	Funded Ratio
Non-Safety Classic	13.53	12.67	0.87	93.6%
Non-Safety PEPRA	0.23	0.20	0.36	84.7%
Safety Classic	10.01	9.36	0.65	93.5%
Safety PEPRA	0.94	0.73	0.21	77.4%
Total CalPERS	**23.88**	**22.30**	**1.58**	**93.4%**
PARS	0.85	0.68	0.18	79.2%
Lease leaseback debt	2.46	-	2.46	-
Total	**27.19**	**22.97**	**4.21**	84.5%

As of June 30, 2020, PARS' UAL stood at $199, 181 and the outstanding balance on the lease leaseback stood at $2,325,000.
Source: CalPERS & City of Belvedere Finance Department

How much are Belvedere's annual pension costs?

These costs can be broken down into two categories; those shared between the employee and employer, and those borne solely by the employer.

- The normal cost rate – the annual cost of service accrual for current employees – is shared between the employee and employer. The NCR has pushed steadily higher in recent years (see Table 6) because of changes to CalPERS' longevity and discount rate assumptions. Because Belvedere's classic employee contribution rates are fixed by negotiated agreement (7% for non-safety and 9% for safety), the City has picked up a disproportionate share of the growth in the NCR. PEPRA employees pay half of their normal cost rate by law.
- The employer-only costs comprise the annual payment towards the UAL, the cost of servicing the lease-leaseback debt and the cost of the City's PARS plan, plus any extraordinary payments towards the City's UAL.

Chart 6 plots the history of the City's annual employer pension costs, excluding the $2.15 million in net extraordinary UAL payments made since 2013-14. In 2020-21, these costs are estimated to be around 30% of payroll, nearly four times as high as the weighted-average employee contribution rate (8%). This is consistent with statewide trends, despite the City's large paydowns of pension debt. The maturity of

Belvedere's pension plan – i.e. a very low ratio of active employees to retirees – exposes the City to large shifts in employer contributions, measured as a percentage of payroll, from investment losses, assumption changes etc., (see page 14 on plan maturity for further explanation).

Table 6: CalPERS Normal Cost Contribution Rate

% of Salary	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Classic Safety							
Employee NCR, %	9.00	9.00	9.00	9.00	9.00	9.00	9.00
Employer NCR, %	13.81	14.78	14.97	15.72	16.64	18.15	18.19
Classic Non-Safety							
Employee NCR, %	7.00	7.00	7.00	7.00	7.00	7.00	7.00
Employer NCR, %	8.51	8.88	8.92	9.41	10.22	11.03	10.88
PEPRA Safety							
Employee NCR, %	11.00	12.00	12.00	12.00	12.00	13.00	13.00
Employer NCR, %	11.15	12.08	11.99	12.14	13.03	14.04	13.13
PEPRA Non-Safety							
Employee NCR, %	6.25	6.25	6.25	6.25	6.75	6.75	6.75
Employer NCR, %	6.24	6.56	6.53	6.84	6.98	7.73	7.59

PEPRA employees have an initial contribution rate of 50% of the total normal cost. If the total normal cost changes by more than 1% point, the employee rate must equal 50% of the new normal cost. Source: CalPERS & City of Belvedere Finance Department

Chart 6: City of Belvedere's Annual Pension Costs* (US$000s)
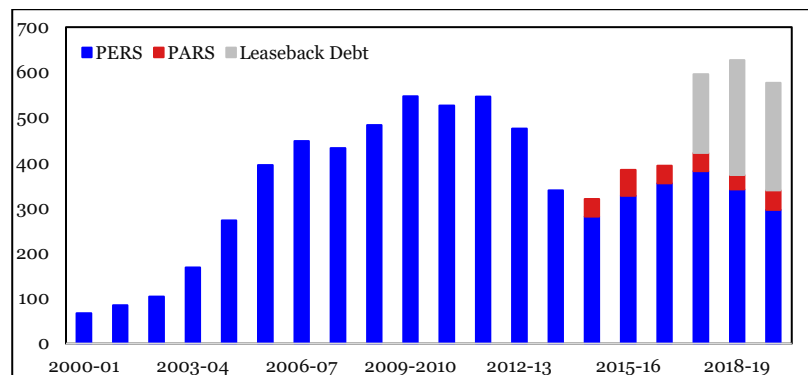
*Excludes $2.15 million in extraordinary net UAL payments made by the City to CalPERS since 2013-14.
Source: City of Belvedere Finance Department

Is Belvedere's funded position better than other cities in Marin?

In truth, it is difficult to make apples-for-apples comparisons of agencies' net pension debt by simply comparing agencies' funded status with CalPERS. That is because many agencies, like Belvedere, have Retirement Enhancement Plans outside of CalPERS, or have issued pension obligations bonds (see page 14), or other pension-type debt, adding to their liabilities. On the asset side, some agencies have established Section 115 trusts (see later discussion) or pension reserve funds, excluded from the CalPERS calculation. Moreover, many agencies have contracts with, or membership of, outside public agencies that carry their own unfunded pension obligations. The City of Belvedere, for example, contracts with Tiburon Fire Protection District (TFPD) for fire and emergency medical services and is part of the Belvedere-Tiburon Library Agency JPA. As of June 30, 2019, TFPD's UAL with CalPERS was $8.78 million (80% funded status) and the Library's UAL was $1.33 million (78% funded status). Although the City has no legal liability for these debts, TFPD will likely require the City to pay higher costs for service as its UAL is amortized, so unless the City can find an alternative provider, these higher costs are contractual. Likewise, the Library will probably ask the City to help subsidize its pension debt repayments, as it struggles with its own finances.

With these caveats in mind, Table 7 provides a comparison of Marin cities' UALs with CalPERS (or MCERA in the case of San Rafael) as of June 30, 2018, as compiled by Stanford's *California Pension Tracker*. The table shows each city's funded status with CalPERS and its funded status adjusted for pension obligation bond issuance or other pension-type debt. On either basis, Belvedere fares well compared to its neighbors.

Table 7: CalPERS' UAL by City: June 30, 2018

US$ million	Actuarial Liability	Market Value of Assets	UAL	Funded Status	POBs/Other Pension Debt	Adj. Funded Status
Belvedere	22.1	20.8	1.3	94%	2.6	82%
Corte Madera	69.8	49.3	20.5	71%	0.0	71%
Fairfax	34.3	28.1	6.2	82%	0.0	82%
Larkspur	63.6	45.9	17.7	72%	3.2	69%
Mill Valley	155.7	112.8	42.9	72%	0.0	72%
Novato	207.0	153.9	53.1	74%	18.6	60%
Ross	25.6	21.4	4.2	84%	0.0	84%
San Anselmo	52.8	36.0	16.8	68%	1.4	64%
San Rafael	584.1	450.0	134.1	77%	0.0	77%
Sausalito	103.5	72.9	30.6	70%	0.0	70%
Tiburon	38.0	28.9	9.1	76%	0.0	76%

Source: California Pension Tracker, Stanford University

Is there more that Belvedere can do?

Belvedere has worked hard to stay ahead of its pension obligations, but its annual pension costs continue to rise, with further growth expected in the years ahead. Proactive planning would allow the City to manage its unfunded pension obligations on a steady basis and avoid a sharp reduction in operations and personnel as minimum annual payments move higher. The following steps should be considered:

1. Adopt a lower discount rate

First, the City should consider adopting a more realistic discount rate for valuing its pension obligations and lay out a medium-term fiscal plan for systematically paying down the true value of its pension debt to a desired level of funding. This will be a dynamic process, as new growth/or shrinkage in the UAL is possible any year that CalPERS' investment performance undershoots/overshoots the City's adopted discount rate. The lower discount rate should also be used in budgeting for annual workforce costs. Headcounts and service levels might be impacted, and new revenues/taxes might be necessary to create sufficient room in the budget for these higher pension costs. The City's consulting PARS actuary (Milliman, Inc.) suggests a 30-year discount rate of 5.14%. Table 8 shows the size of Belvedere's UAL with CalPERS as of June 30, 2019 using different discount rates. This demonstrates the sizeable impact that a lower discount rate has on debt levels and the extent to which the City has de facto been deficit spending over the past decade.

The City would have to think carefully about if, and when, to recognize a new, lower discount rate on its financial statements (below that of other CalPERS' contracting agencies), as the higher recognized value of pension debt could negatively impact the City's perceived creditworthiness. This is an important consideration if the City decides to seek debt financing for its Seawall Project.

Table 8: Belvedere's UAL at Different Discount Rates

As of June 30, 2019	CalPERS' UAL	Funded Status
7.0%	$1.6 million	93.4%
6.0%	$4.5 million	83.5%
3.25%	$17.5 million	56.6%
1.75%	$26.4 million	46.3%

Refers to the City of Belvedere's UAL with CalPERS only. Source: CalPERS

2. Review its amortization schedule

Second, as part of its medium-term fiscal plan, the City should also decide if it can pay down its pension debt at a faster pace than required by CalPERS' amortization schedule. This does not mean the City should alter its contract with CalPERS to re-amortize its pension debt, as this would obligate the City to pay according to the new schedule, which could impact service delivery. An informal arrangement is probably preferred.

3. Establish a Section 115 trust

Third, the City should consider establishing a Section 115 trust as an alternative or adjunct to paying down debt (and thus investing) with CalPERS. A Section 115 trust creates ringfenced funds for pensions and allows those funds to be invested in higher risk instruments than general fund monies. The assets reduce reported net pension debt on agencies' financial statements, just as paying additional funds to CalPERS does. Section 115 trusts have various advantages. First, they provide investment diversification vis a vis CalPERS. Second, unlike funds invested with CalPERS, they can be used to assist in meeting annual required payments to CalPERS in bad years, providing rate smoothing. Third, they provide scope for better duration matching of plan liabilities. That said, there are fees associated with Section 115 trusts and investment returns do not necessarily outperform those generated by CalPERS, so this option needs to be carefully studied.

4. Increase employee cost sharing

Fourth, the City should consider increasing employee contributions for classic members. PEPRA employees already pay 50% of the normal cost rate, and by law the City can also require classic members to pay 50% of the normal cost, capped at 8% of pay for non-safety members and 12% of pay for safety members. Belvedere's current rates are 7% and 9% respectively. Note that the PEPRA reforms allow agencies to go further and negotiate with employees to pay part of the *employer's* normal cost rate, but this is often agreed in return for an enhanced benefit. This option should be carefully modeled as it does not necessarily generate savings for the employer. For example, employee groups often ask for a slightly higher COLA in exchange for a higher cost share. Whilst this may lower the employer NCR in the short term, it increases the employer contribution in the medium term, because of the compounding effect of higher salary bases and the additional investment risk.

5. Blue skies option

Finally, the City could consider more creative solutions. A key constraint to controlling the long-term trajectory of the City's UAL is the fact that new City employees automatically join the CalPERS class and enjoy the same generous defined-benefit pension plans. Hypothetically, new employees could be hired through a new entity outside of the City of Belvedere (perhaps a new JPA structure) and offered defined contribution plans. This would align City practices with the private sector and younger public agencies (e.g. Marin Clean Energy, the Ranch, Marin Transit). Existing employees would stay in the CalPERS class employed by the City of Belvedere. This option would not affect the pension commitments the City has made to past and present employees, but it would remove the pension risk associated with new hires. It is not clear what legal hurdles this option would face, or whether it would create problems attracting talent.

PART 3: Policy Wonk Stuff (Optional)

Explain how benefit formulas work

In simple terms, the benefit a retiree receives is equal to his "benefit factor" multiplied by his highest annual salary multiplied by his years of service. The benefit factor changes according to number of years worked and age at retirement. For example, using the City's "2% at 50" classic safety formula, if an employee retires at age 50 after 30 years of work, his benefit factor is 2.0, but if he retires at age 55 after 30 years of work, his benefit factor is 2.7 (statistically he has less years to live). Thus, if his final salary is $100,000, he will receive $60,000 per year if he retires at age 50, and $81,000 per year if he retires at age 55. His pension benefit is upgraded by 2% per year (COLA). Benefits are capped as a percentage of final compensation, albeit at a high level. CalPERS' various plans offer different benefit factors, escalators and caps, so it is not always easy to assess which offers the richest benefits. Typically, safety formulas are richer than non-safety formulas, as shown by comparing Belvedere's plans in the tables below. The table on the following page summarizes all plans offered by CalPERS.

Table 9: Belvedere Classic Safety Benefit Formula: 2% at 50

Age at Retirement	Benefit Factor	Benefit After 30 Years' Service
50	**2.00%**	**60.0**
51	2.14%	64.2
52	2.28%	68.4
53	2.42%	72.6
54	2.56%	76.8
55 or older	2.70%	81.0

Formula capped at 90% of final compensation. Source: CalPERS

Table 10: Belvedere Classic Non-Safety Benefit Formula: 2% at 55

Age at Retirement	Benefit Factor	Benefit After 30 Years' Service
50	1.426	42.78
51	1.522	45.66
52	1.628	48.84
53	1.742	52.26
54	1.866	55.98
55	**2.00**	**60.00**
56	2.052	61.56
57	2.104	63.12
58	2.156	64.68
59	2.210	66.30
60	2.262	67.86
61	2.314	69.42
62	2.366	70.98
63 or older	2.418	72.54

Formula capped at 96.72% of final compensation. Source: CalPERS

Table 11: Benefit Formulas: Classic and PEPRA Members

Formula	Min. Retirement Age	Pension @ 30 Yrs' Service[1]	Maximum Pension[2]
Non-Safety/Miscellaneous Employees			
PEPRA Members			
2% at 62	52	60%	100%
Classic Members			
2% at 55	50	60%	96.72%
2.5% at 55	50	75%	95%
2.7% at 55	50	81%	102.6%
2% at 60	50	60%	96.72%
3% at 60	50	90%	120%
Safety Workers			
PEPRA Members			
2% at 57	50	60%	80%
2.5% at 57	50	75%	100%
2.7% at 57	50	81%	108%
Classic Members			
2% at 50	50	60%	90%
3% at 50	50	90%	90%
2% at 55	50	60%	90%
2.5% at 55	50	75%	90%
3% at 55	50	90%	90%

[1.]Pension as a % of final compensation assuming retirement takes place after 30 years of service at full retirement age of plan.
[2.]Benefit factors are different for each plan and change according to the number of years worked and age at retirement.
Plans are capped at different levels as a percentage of final compensation. Please refer to CalPERS' benefit tables for more details.
Source: CalPERS

How does CalPERS amortize agencies' pension debt?

Each year, CalPERS requires agencies to pay down a portion of their UAL as part of their annual required contribution. The amount that needs to be paid is determined by CalPERS' amortization policy. CalPERS divides the UAL into what it calls amortization bases. Each year's base is essentially the increase/decrease in a plan's UAL and is broke down by source e.g. investment gains/losses. Different portions of the base are amortized according to different rules, including the number of repayment periods, how the payments are spread over time (dollar flat or rising), and whether there is a ramp up/ramp down in payments. CalPERS recently revised its amortization policy to be more stringent (see Table 13). The rule change takes effect in 2021-22 and applies to new UAL bases created on or after June 30, 2019. UALs established prior to that date will continue to be amortized according to the prior policy.

Table 12: CalPERS Old Amortization Policy

Source of UAL	Investment Gain/Loss	Non-Investment Gain/Loss	Assumption/ Method Change	Benefit Change
Amortization Period	30 Years	30 Years	20 Years	20 Years
Escalation Rate	Payroll	Payroll	Payroll	Payroll
Ramp Up	5 Years	5 Years	5 Years	0
Ramp Down	5 Years	5 Years	5 Years	0

Source: CalPERS

Table 13: CalPERS New Amortization Policy

Source of UAL	Investment Gain/Loss	Non-Investment Gain/Loss	Assumption/ Method Change	Benefit Change
Amortization Period	20 Years	20 Years	20 Years	20 Years
Escalation Rate	0%	0%	0%	0%
Ramp Up	5 Years	0	0	0
Ramp Down	0	0	0	0

Source: CalPERS

What is risk pooling and how does this work at CalPERS?

Risk pooling refers to the spreading of financial risk evenly among contributors. CalPERS uses risk pooling to reduce fluctuations in employer contribution rates caused by unexpected demographic events i.e. shorter or longer post-retirement longevity. CalPERS requires all employers with 100 or fewer active employees to participate in risk pools, pooling their assets and liabilities. Participation in risk pools for employers with more than 100 active employees is optional. CalPERS operates two risk pools, one for non-safety groups and one for safety groups.

Why does plan maturity matter?

Pension plan maturity is an important consideration in gauging a plan's sensitivity to risk. As a plan's population ages, and more members reach retirement, its obligations become large relative to its source of contributions. The ratio of assets to payroll (leverage ratio) increases as the plan matures and, as a result, investment losses become more costly to the plan. For example, with a leverage ratio of 3.0, a 10% investment loss would be equivalent to 30% of payroll. A 6.0 leverage ratio would mean that the same investment loss would cost 60% of payroll. Thus, agencies with mature plans are exposed to higher volatility in employer contributions, measured as a percentage of payroll. On all measures, Belvedere's two classic pension plans are very mature compared with the CalPERS average.

Table 14: Maturity Measures for Belvedere's Classic Plans

As of June 30, 2019	Assets to Payroll Ratio	Active Employee to Retiree Ratio	Retiree Liabilities/Total Liabilities, %
Non-Safety Classic	15.1	0.31	67%
Safety Classic	25.2	0.11	66%

Source: CalPERS

What are pension obligation bonds?

Pension Obligation Bonds (POBs) are a tool used by public agencies to "pay down" their unfunded pension liabilities, by replacing one form of debt (the existing UAL) with another (the POB). Agencies often believe that such issuance locks in a lower cost of funding. It does not. Only if the rate of return that CalPERS earns over the life of the bond exceeds the cost of POB funding, does the POB save the agency money. The idea that POBs guarantee a fixed saving assumes that CalPERS consistently and exactly meets its investment target, which it does not. The economics of the City's 2017 lease-leaseback are the same as those of a POB, but the City was able to secure a lower cost of funding (4.46% interest rate, subsequently refinanced at 2.55%) because of the securitized nature of the transaction.

Why don't agencies just quit CalPERS?

The California Rule forbids agencies from reducing the generosity of pension benefits for existing employees for past *or prospective service.* Exiting CalPERS would not change this calculus, but it would allow employers to launch new defined-contribution pension schemes for new employees (no longer

constrained by the CalPERS class system), offering significant potential cost savings. However, to exit CalPERS, agencies must pay a termination fee to relieve themselves of their accrued pension obligations. This termination fee represents the UAL calculated using a "risk-free" discount rate. CalPERS places the liabilities of exited agencies into its Terminated Agency Pool and because no future employer contributions are made into the pool, CalPERS secures these liabilities with risk-free assets, typically high-quality municipal bonds. The lower discount rate significantly increases the UAL of terminated plans, which must be paid on exit, making it prohibitively expensive for most employers to exit CalPERS. As of June 30, 2019, the City of Belvedere's hypothetical termination liability stood at $17.5 million using a 3.25% discount rate, or $26.4 million using a 1.75% discount rate. CalPERS provides two estimates based on the lowest and highest rates available over the surrounding 19-month period.

What accounting rules govern public pensions?

Accounting rules for public agencies are set by the Government Accounting Standards Board (GASB). In 2012, GASB issued two statements, GASB 67 and 68, setting new rules for the measurement and reporting of public pensions data to be used in agencies' Comprehensive Financial Annual Reports (CAFRs). The new standards, which took effect in FY 2013-14 and 2014-15 respectively, attempted to address concerns about the valuation of pension assets, the use of the expected rate of return as the discount rate to measure pension liabilities, and the fact that agencies did not report unfunded pension liabilities on their balance sheets, but instead reported the cumulative deficiency in their annual required contributions (ARC) since 1997. Going forward, agencies were required to report the market value of their pension assets, use a blended discount rate to measure their pension liabilities (albeit with discretion), and report the full value of their unfunded pension liabilities on balance sheet. Because of pension fund reporting delays, agencies can report pension liability data from the end of the prior fiscal year in their annual statements. Although the new standards improved transparency, agencies have relied on workarounds to avoid (almost entirely) using a lower blended discount rate, thus continue to understate their liabilities.

It is important to note that there is little in common between agencies' Annual Valuation Reports (AVRs) provided by CalPERS and the pension data included in agencies' CAFRs. The rules governing, and objectives of, the two reports are different. AVRs detail agencies' funded status, debt amortization schedules, and changes in minimum annual required contributions, to help in agencies' budgetary planning. CAFRs are designed for investors to assess trends in agencies' financial health and solvency. They report agencies' net financial position on an accrual basis. One confusing element of CAFRs relates to "deferred outflows and inflows of pension resources" which are essentially components of net pension debt that are not recognized as an expense (outflows) or income (inflows) in the year in which they are created. For example, changes in net pension debt resulting from a difference between projected and actual earnings are spread over five years on CAFRs. Again, there is little commonality between AVRs and CAFRs – the discount rate is even different – and AVRs are more relevant for budget planning purposes.

Evaluation of Changes in Belvedere's Pension Debt with CalPERS (2013-2019)

- Despite $4.8 million of extraordinary debt repayments to CalPERS between June 30, 2013 and June 30, 2019 ($2.6 million of which was debt financed), the City's unfunded accrued liability (UAL) with CalPERS shrunk by just $2.0 million.
- This is because $2.7 million of new CalPERS' unfunded pension debt was created during the six-year period, but not because investment returns fell short of CalPERS' investment target/discount rate. Returns were volatile, but cumulatively they slightly exceeded target over the period (see Table 2).
- Investment returns did fall sharply below target in FY19-20 (4.7% versus a target of 7.0%), so significant new investment losses (estimated to be circa $840,000) are expected as of June 30, 2020.
- The creation of new net pension debt in the six years to June 30, 2019 was almost entirely due to changes in assumptions, critically a stepped lowering of the discount rate from 7.5% to 7.0%, and longer post-retirement life expectancy revealed in CalPERS' January 2014 Experience Study.
- The December 2017 Experience Study revealed negligible further improvement in life expectancy. The next Experience Study is due in late 2021/early 2022 and will likely record a *lowering* of life expectancy because of COVID-19 and other social/health factors.
- In 2014, CalPERS merged all existing risk pools into two aggregate risk pools – one for safety workers and one for non-safety workers – making prior trend analysis difficult.

Table 1: Annual Change in City of Belvedere's UAL: CalPERS Accounts Only

US$ million	6/30/2020	6/30/2019	6/30/2018	6/30/2017	6/30/2016	6/30/2015	6/30/2014
UAL as of Prior FY-End (1)	1.580	1.311	4.335	4.661	3.325	2.439	**3.625**
Extraordinary Debt Repayment (2)	-	-	-3.600	-0.300	-	-	-0.854
Anticipated UAL Change excl. Debt Repay't (3) [a]	-	0.063	-0.035	0.183	0.137	0.113	0.135
Unanticipated Change in UAL (4)	-	**0.205**	**0.612**	**-0.209**	**1.200**	**0.773**	**-0.466**
- Investment (Gain)/Loss	-	0.109	-0.212	-0.552	1.045	0.813	-1.223
- Non-Investment (Gain)/Loss	-	0.096	0.081	-0.011	-0.141	-0.040	0.006
- Change in Assumptions	-	-	**0.587**	**0.355**	**0.295**	-	**0.751**
- Change in Methods	-	-	0.155 [b]	-	-	-	-
Total Change in UAL (5=2+3+4)	-	0.268	-3.024	-0.326	1.337	0.885	-1.185
UAL as of FY-End (1+5)	-	**1.580**	1.311	4.335	4.661	3.325	2.439
Associated Information							
- CalPERS' Investment Return	4.70	6.70	8.60	11.20	0.60	2.40	18.40
- Discount Rate	7.00	7.00	7.00	7.25	7.375	7.50	7.50

[a] Based on projected interest cost, service cost, return on assets, benefit payments, contributions, and admin expenses.
[b] Created by adoption of new actuarial valuation software. Source: CalPERS

Table 2: Cumulative Change in UAL by Source: CalPERS Accounts Only

Line Item	US$
UAL as of June 30, 2013	3,624,579
UAL as of June 30, 2019	1,579,848
Change over 6-Year Period	-2,044,731
Causes	
- Extraordinary Debt Repayments	-4,754,000
- Expected Change in UAL excl. Debt Repayments	595,145
- Unanticipated Change in UAL	2,114,124
of which	
Investment (Gain)/Loss	-20,246
Non-Investment (Gain)/Loss	-8,434
Change in Assumptions	**1,988,003**
Change in Methods	154,800

Source: CalPERS

Table 3: Cumulative Change in City's Total Net Pension Debt by Account Type

Account, US$	June 30, 2019	June 30, 2013	Change
Classic Safety	654,663	1,440,840	-786,177
Classic Non-Safety	868,221	2,183,781	-1,315,560
PEPRA Safety	21,376	-	21,376
PEPRA Non-Safety	35,588	-42	35,630
Total CALPERS	**1,579,848**	**3,624,579**	**-2,044,731**
PARS Plan	178,065	186,947	-8,882
Lease Leaseback Debt	2,455,000	0	2,455,000
Total Pension Debt	**4,212,911**	**3,811,526**	**401,387**

Source: CalPERS

Table 4: CalPERS' Net Investment Returns (June 30, 2020)

Year	Compounded Rate of Return
1 year	4.7%
5 years	6.3%
10 years	8.5%
20 years	5.5%

Source: CalPERS

Attachment 5

Timeline and Workplan for Taskforce on Pensions & OPEBs

	Lead	Completed
Interactions with Finance Committee, City Council, and Staff		
January		
- Seek Finance Committee approval to establish Taskforce on Pensions & OPEBs	SW/AJ	1/6/21
- Develop charter, budget, and timeline. Seek Finance Committee approval	SW/AJ	1/12/21
March		
- Deliver interim findings to Finance Committee		
- Begin discussions with staff and BPOA over reform direction (ongoing)		
April/May		
- Deliver final report and recommendations to Finance Committee for discussion & approval		
- Deliver FC-approved recommendations to City Council for discussion & approval		
- Incorporate reforms into MOU with BPOA, and staff handbook for FY2021-22		
Pensions		
January/February		
- Review pension status and reform efforts/models of neighboring/other municipalities		
- Undertake analysis of appropriate discount rate selection		
- Agree actuarial contract requirements. Seek quotes and delivery time		
- Undertake Section 115 trust analysis: Cost, flexibility, relative performance vis a vis CalPERS		
- Undertake legal and comparative analysis of higher Classic employee contribution rates		
- Undertake legal and comparative analysis of non-pensionable components of employee compensation		
- Research legal constraints and precedent for creating new hiring entity		
- Undertake trend analysis of budget & reserves to determine scope for pension paydown		
- Confirm understanding of GASB and credit rating impacts of accelerated pension debt paydown		
February		
- Agree discount rate selection methodology		
- Action actuarial analysis		
March/April		
- Review actuarial analysis		
- Agree paydown/amortization policy, within confines of budget modeling		
- Agree changes to employee contribution rates (if any)		
- Agree formation of new hiring entity (if any)		
- Select Section 115 trust and funding policy (if any)		
April/May		
- Prepare final report		
OPEBs		
January/February		
- Review OPEB status and reform efforts/models of neighboring/other municipalities		

- Ascertain legal status of Belvedere's OPEB commitments (normal & city manager classes)		
- Agree actuarial contract requirements. Seek quotes and delivery time		
- Explore options for securing non-CalPERS health insurance quotes		
- Undertake Section 115 trust analysis: Cost, flexibility, relative performance		
- Explore benefits of funding trust, including optimal funding level & discount rate impacts		
- Explore employee cost sharing of OPEB trust, including tax impacts		
- Undertake trend analysis of budget & reserves to determine scope for OPEB paydown		
- Confirm understanding of GASB and credit rating impacts of OPEB debt paydown		
February		
- Action actuarial analysis		
- Secure non-CalPERS health insurance quotes for active pool, and/or bifurcated active/retiree pools		
February/March		
- Explore possible buyout/alternative benefit options for retirees/active employees		
March/April		
- Review actuarial analysis		
- Agree paydown policy, within confines of budget modeling (if any)		
- Select Section 115 trust and funding policy (if any)		
- Select new non-CalPERS health plan (if any)		
- Agree employee cost sharing of trust (if any)		
- Agree cost containment measures/buyout/alternative benefit measures (if any)		
April/May		
- Prepare final report		

Anticipated Outside Service Providers (*paid services)

- Pension and OPEB actuarial services*
- GASB and tax accountants*
- Section 115 trust services
- Health benefits broker
- Employment benefits legal services*
- Public law services*
- Rating agency services

Taskforce Meeting Schedule

- Taskforce will meet as needed, initially every 2 weeks, moving to monthly meetings if/when workload tapers

Associated Work (Outside of Taskforce)

- Develop Medium-Term Fiscal Sustainability Plan
- Reform Staff Compensation Structures