

LAKE ARROWHEAD COMMUNITY SERVICES DISTRICT

MEMORANDUM

DATE: JUNE 25, 2019

TO: BOARD OF DIRECTORS
Lake Arrowhead Community Services District

FROM:



JOHN O'BRIEN, Finance Manager



CATHERINE CERRI, General Manager

SUBJECT: CALPERS PENSION PLAN UPDATE

A. RECOMMENDATION

This is an information item only.

B. REASON FOR RECOMMENDATION

This is an information item only.

C. BACKGROUND INFORMATION

The District is a member of the California Public Employee Retirement System (CalPERS) which is the nation's largest public pension fund with investments of \$365.75 billion in both domestic and international markets and is one of the largest private equity investors in the world.

District CalPERS Pension Plan Overview

Since 2003, the District has participated in the CalPERS Miscellaneous Risk Pool defined benefit plan. The District has three distinct plans within the Miscellaneous Risk Pool detailed as follows:

- Tier 1 Plan (2.5% @ 55) – closed plan and includes employees who were employed with the District prior to October 2011.
- Tier 2 Plan (2% @ 55) – plan open only to new employees who are current CalPERS members or members of reciprocal agencies prior to January 2013.
- PEPRA Plan (2% @ 62) – all new employees who are not members of CalPERS before January 2013.

District Participant Data History – Active Employees			
Plan	Before 1/1/2013	2018-19	Est. 2019-20
Tier 1	55	24	24
Tier 2	0	3	3
PEPRA	0	28	28
Total	55	55	55

CalPERS Pension Plan Changes

CalPERS has implemented several pension plan changes over the past few years to ensure its sustainability, including the following:

- Public Employee’s Pension Reform Act (PEPRA) (effective 2012-13)
- Assumption Changes in mortality rate (effective 2016-17)
- Investment/Discount Rate Changes (effective 2017-18)
- Risk Mitigation Policy (effective 2017-18, suspended until 2020-21)
- Amortization Policy (effective 2018-19)

Of the plan changes above, assumption changes, investment/discount rate changes and the amortization policy all directly impact the District’s annual pension expense.

District CalPERS Pension Plan Components

The District’s total pension liability is actuarially determined based upon participant history and various assumptions including retirement age, life expectancy, and inflation. All of these assumptions are periodically reviewed by CalPERS and adjusted based upon experience.

Funding for the pension liability consists of investment income and employee and employer contributions. Employer contributions have two major cost components which are the Employer Normal Cost contributions and the Unfunded Actuarial Liability (UAL) contributions. Employer Normal Cost contributions are based upon a percentage of payroll. UAL is based on the difference between the projected or anticipated return of investment and the actual return on investments.

2019-20 Contribution Rates – Normal Cost Portion			
Plan	Employer	Employee	Total
Tier 1	10.823%	7.951%	18.774%
Tier 2	9.680%	6.906%	16.586%
PEPRA	6.985%	6.750%	13.735%

Mainly due to underperforming investments, in December 2016, the CalPERS Board of Administration lowered the investment/discount rate from 7.5% to 7.0%.

Changing market conditions, more uncertainty in the financial forecast, and an attempt to close the cash flow funding gap were also goals of this change. The implementation of the discount rate change was rolled out using a three-year phase-in beginning in 2018-19.

As a result of the proposed investment/discount rate changes, the District's normal cost rates were impacted.

Fiscal Year	Discount Rate %	District Normal Cost Rate % - Employer Portion		
		Tier 1	Tier 2	PEPRA
2017-18	7.50	9.54	8.42	6.53
2018-19	7.375	10.02	8.89	6.84
2019-20	7.25	10.82	9.68	6.99
2020-21	7.00	11.60	10.30	7.50

District Projected CalPERS Pension Plan Costs

The District's total pension liability is \$30.2 million, which is 73.5% funded, resulting in an estimated \$8.0 million unfunded accrued liability.

District Plan Funded Status and UAL				
	Tier 1	Tier 2	PEPRA	Total District
Accrued Total Liability	29,713,266	69,155	530,445	30,312,866
Market Value of Assets	21,724,975	70,843	496,729	22,292,547
Unfunded Accrued Liability (UAL)	7,988,291	(1,688)	33,716	8,020,319
Funded Ratio	73.10%	102.40%	93.60%	73.52%

As stated above, the District makes two pension contributions to CalPERS annually, the Employer Normal Cost contributions and UAL. The District's estimated required contributions are as follows:

District Annual Pension Employer Contributions (Estimated)		
Plan	2018-19	2019-20
Tier 1	286,417	303,755
Tier 2	15,465	32,071
PEPRA	77,739	83,246
UAL	470,699	577,298
Total	850,320	996,370

District CalPERS UAL Funding Options

Currently, the District's employer UAL contribution is programmed on a 30-year amortization schedule with a five-year ramp up. The ramp up was provided to allow agencies to adjust to the increased cost. However, this five-year period results in negative amortization and an overall growth in liability. Additionally, the current schedule results in interest expense of nearly \$7.99 million.

Available funding options include:

- Current 30-year amortization schedule
- Fresh Start – permanent change to the amortization period
- Irrevocable IRS Section 115 Trust
- Additional annual lump sum payments

In August 2018, the District made a Board approved additional lump sum payment in the amount of \$300,000 with the idea of making five annual lump sum payments in that same amount.

As a reminder, the single additional lump sum of \$300,000 that was made in August 2018 will save the District approximately \$651,000 in interest over the life of the pension liability.

A second additional \$300,000 lump sum payment (presumably paid in August of 2019) would save the District approximately \$1,270,000 over the life of the liability.

Lastly, if the District was to make each of the planned additional \$300,000 lump sum payments for 5 years, the interest savings would amount to approximately \$3,000,000.

D. FISCAL IMPACT

This is an information item only.

E. ENVIRONMENTAL IMPACT

None.

F. ATTACHMENTS

None.