



City of Fort Bragg

Pension Liability Assessment

DECEMBER 3, 2020





06/30/2019 Pension Funding Status

Description	Misc	Safety - Police	Safety - Fire	PEPRA Misc	PEPRA Police	Combined
Total Accrued Liability	\$20,558,134	\$16,231,807	\$273,759	\$753,045	\$409,874	\$38,226,619
Market Value of Assets	\$15,101,327	\$11,133,356	\$170,564	\$688,927	\$365,109	\$27,459,283
Unfunded Actuarial Liability (UAL)	\$5,456,807	\$5,098,451	\$103,195	\$64,118	\$44,765	\$10,767,336
% Funded	73.5%	68.6%	62.3%	91.5%	89.1%	71.8%

Source: CalPERS Actuarial Valuation as of June 30, 2019

Definitions:

- Total Accrued Liability = What You Need
- Market Value of Assets = What You Have
- Unfunded Actuarial Liability = What You Owe

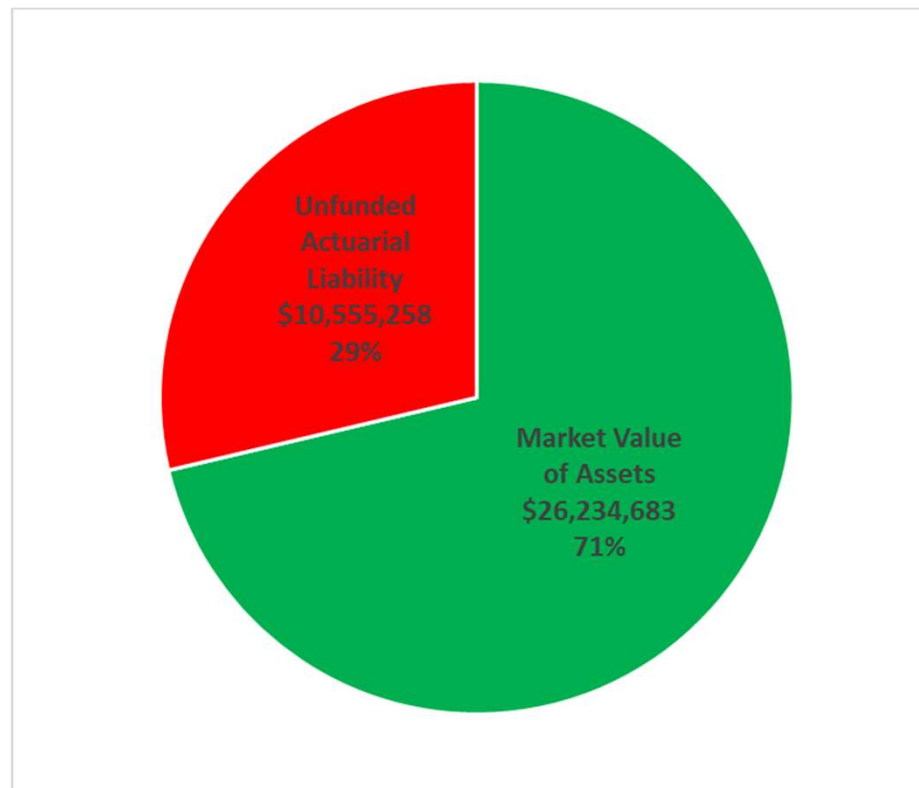
Five Pension Plans:

- Classic: Miscellaneous, Police, Fire
- PEPRA: Miscellaneous and Police

CLASSIC MISC and POLICE represent largest savings opportunity



06/30/2019 Pension Funding Status



- Total Pension Obligations = \$36.8M
- Pension Assets = \$26.2M
- Shortfall = \$10.6M (29% of what is needed)

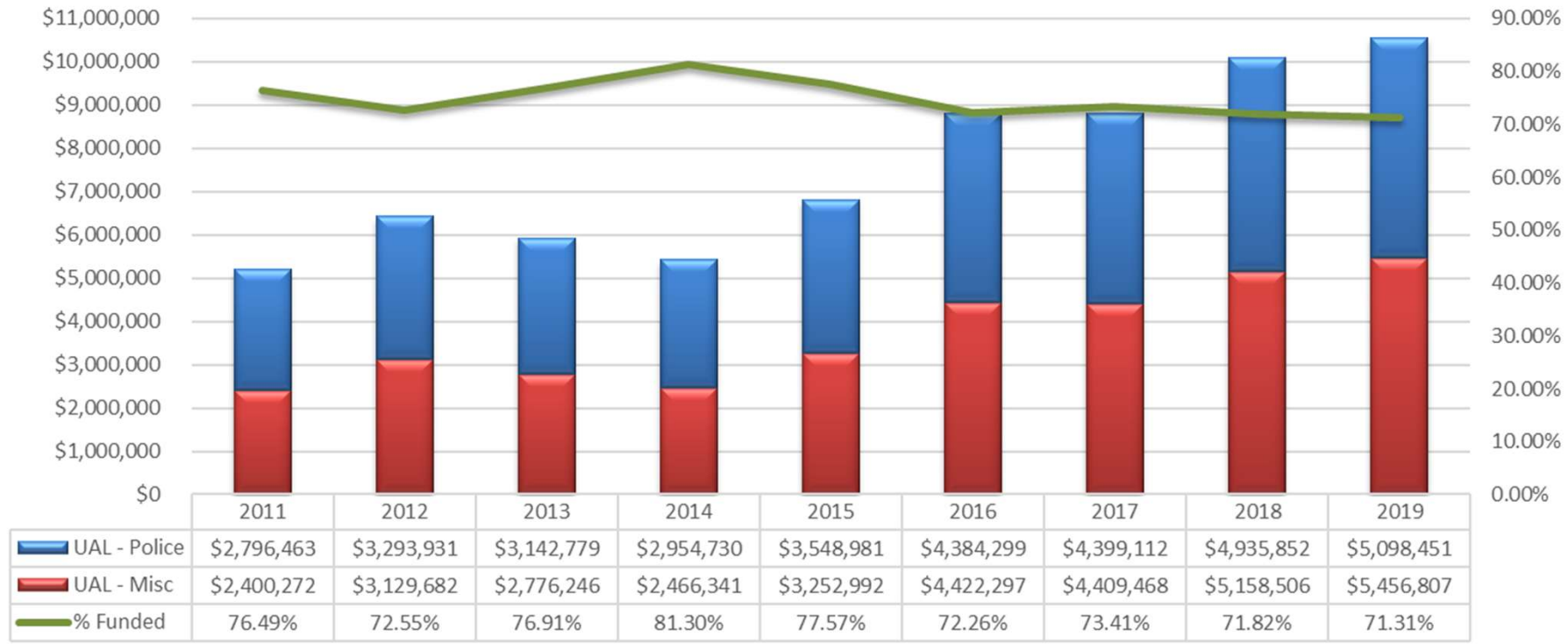
Shortfall (UAL) = DEBT:

- Owed to CalPERS
- Amortizes over time (20-30 years)
- Accrues interest at 7% interest rate (\$8.2M total)
- Reduced or delayed payments not allowed
- City's most expensive debt
- No prepayment restrictions or penalties



Pension Funding History

Unfunded Actuarial Liability & Funding Level



9 years later:

- Owe \$5.4M more
- Funded level 5.2% lower



Pension Costs - Overview

Pension Costs as % of Salaries

Category	Classic Misc	PEPRA Misc	Classic Safety	PEPRA Safety
Normal Cost - Employee	6.9%	7.3%	9.0%	13.0%
Normal Cost - City	11.1%	7.7%	18.2%	13.1%
UAL Payment - City	26.9%	0.9%	54.0%	1.5%
Total	44.9%	15.9%	81.1%	27.6%

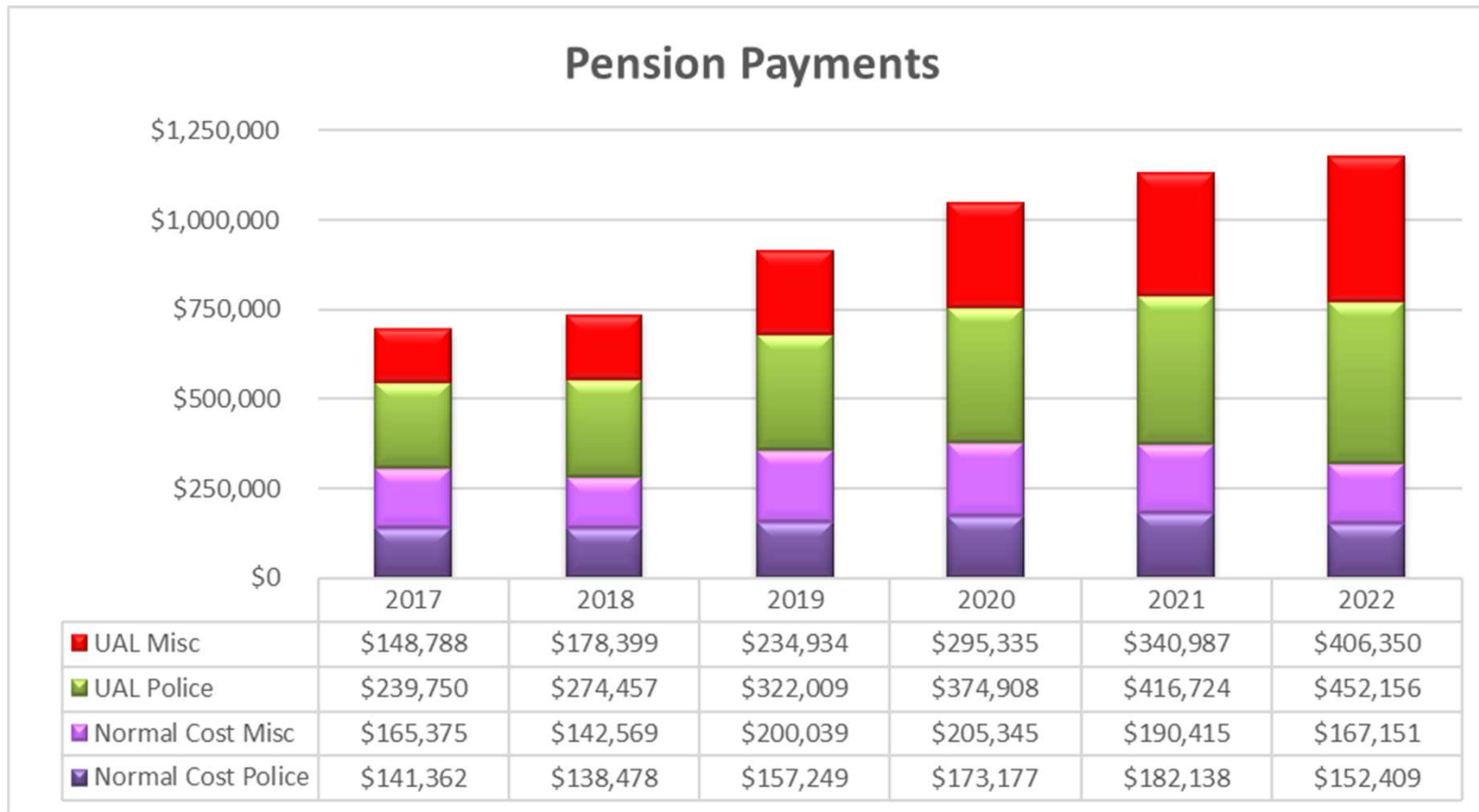
City makes two types of payments to CalPERS:

- **Normal Cost (split between City and employees):**
 - Annual cost of pension benefits for current employees
 - % of payroll
- **UAL Payment**
 - Repayment of pension funding shortfall
 - Fixed dollar amount

CalPERS charges **7%** interest rate on UAL (included in UAL Payment)



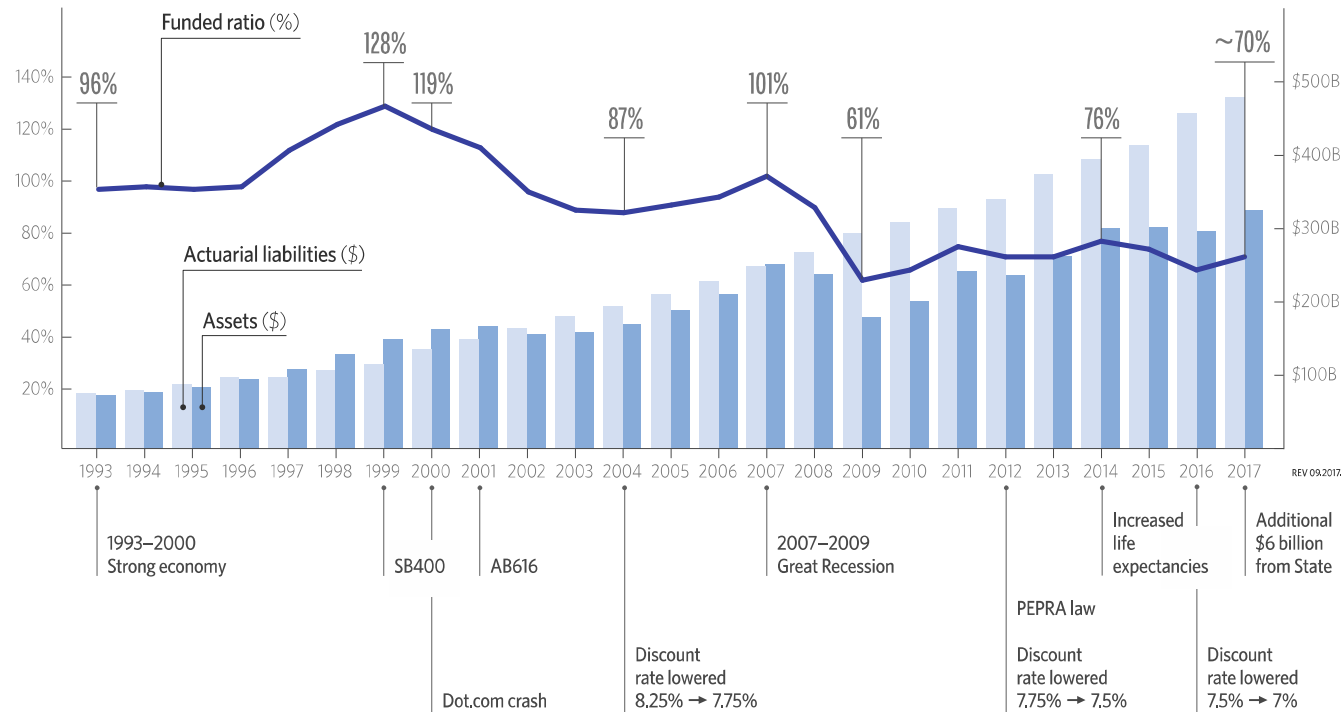
Pension Payments



Annual Pension Payments Increase:
\$483K in 6 years (69%)



CalPERS History Lesson



1999 – CalPERS 128% funded (“Super Funded” Status)

2000 – SB 400 / AB 616 increased benefits retroactively

2000-02 – dot.com investment losses:

- 2000-01: -7.2%
- 2001-02: -6.1%

Loss of “Super Funded” Status

2008-09 – The Great Recession:

- Investment Loss: - 27% (\$67 Bn)
- Full impact: - 34.75% (27% + 7.75% discount rate)
- CalPERS 61% funded

2012 – PEPRA reduced benefits for new employees

2020 – CalPERS is 71% funded



Pension Cost Increase Drivers

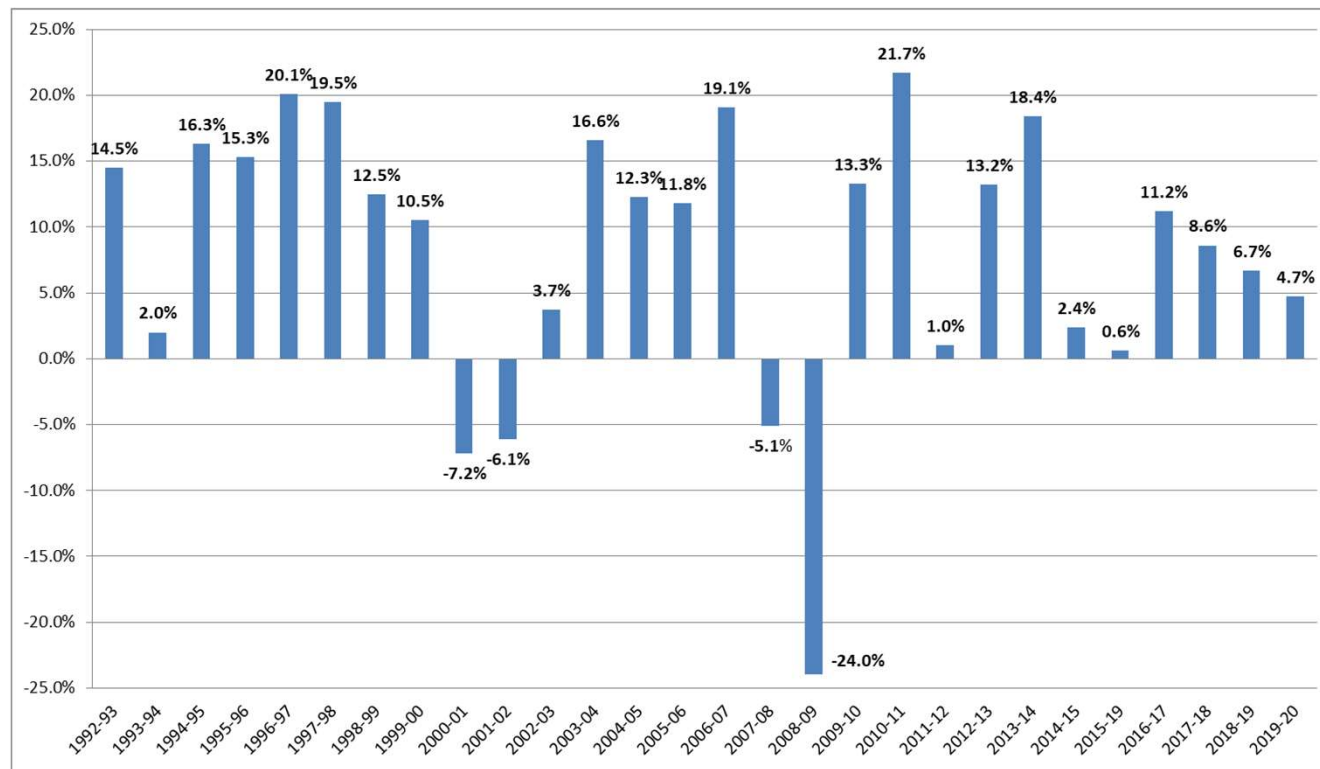
- Enhanced Pension Benefits (SB 400 / AB 616)
- Investment Performance vs Overly Optimistic Return Expectations
- People Living and Drawing Pensions Longer
- Fewer Active Workers for Each Retiree
- CalPERS Assumption Changes
 - Discount rate reduction
 - Actuarial Amortization Policy
 - Mortality rates
- Compensation Increases Above Plan Assumptions (2.75% per year)



Investment Risk and Returns

CalPERS Historical Average Rates of Return through 2019-20:

Past: 5 years – 6.3% 10 years – 8.5% 20 years – 5.5% 30 years – 8.0%



2019: 58% of pension benefits funded by investment returns

CalPERS manages pension investments

City bears all investment risk

Failure by CalPERS to achieve target investment returns does not relieve City from pension benefit guarantees to employees and retirees

Lower returns => higher UAL and higher pension payments by City



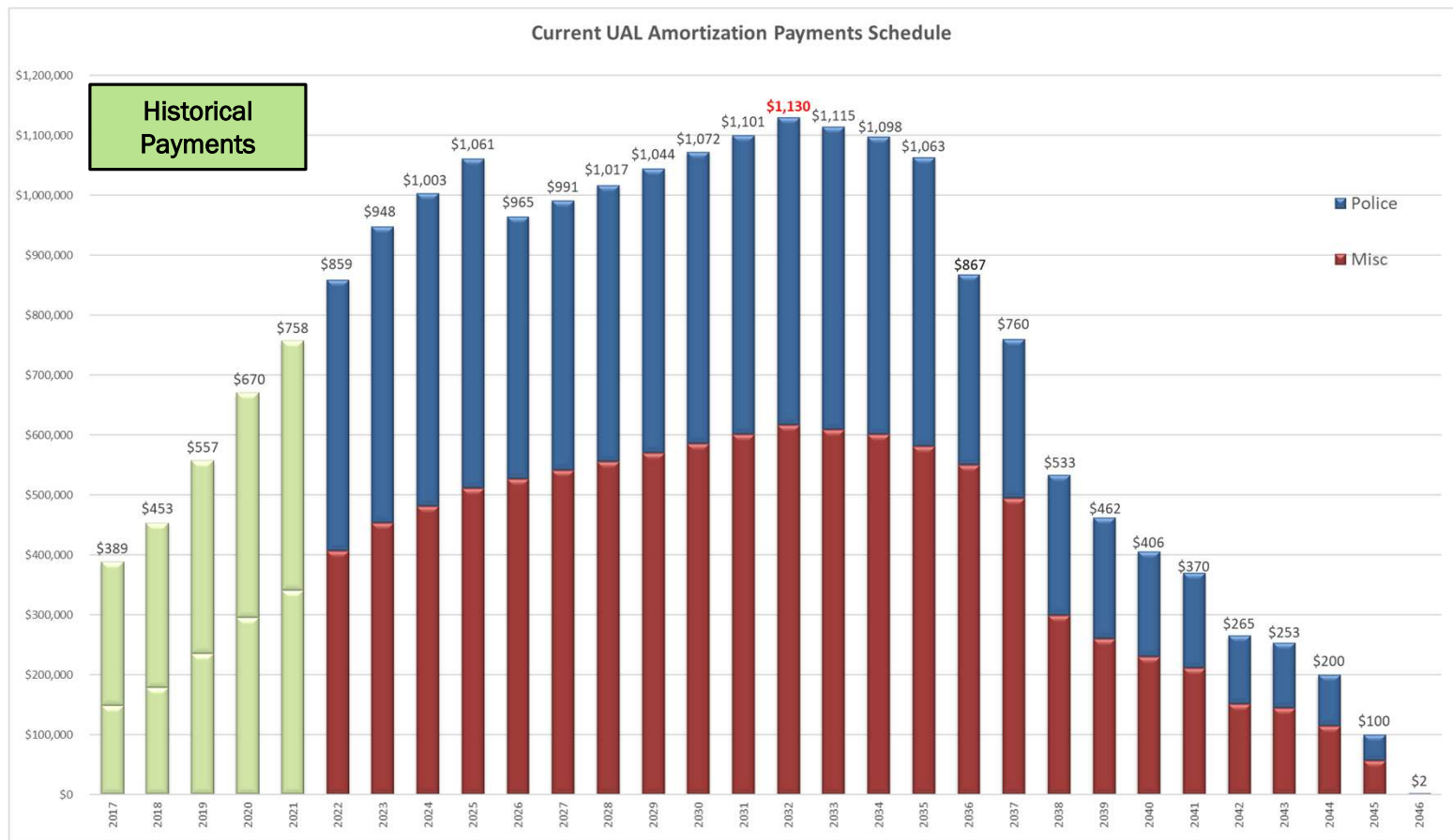
Future Trend Expectations

Lower overall return environment:

- CalPERS has been reducing discount rate / return expectations (8.75% in 1995 => 7.0% in 2019)
- CalPERS's 2020 return estimate is 4.7% (last updated 07/15/2020)
- Any return below 7% is a shortfall and leads to UAL increase
- 4.7% return is 2.3% funding shortfall (~\$604K UAL increase for Misc and Police)
- Conversations have started to further reduce discount rate to 6.50% (likely 5 years out)



Where Things Are



06/30/2019 Actuarial Valuation

UAL Payments Only

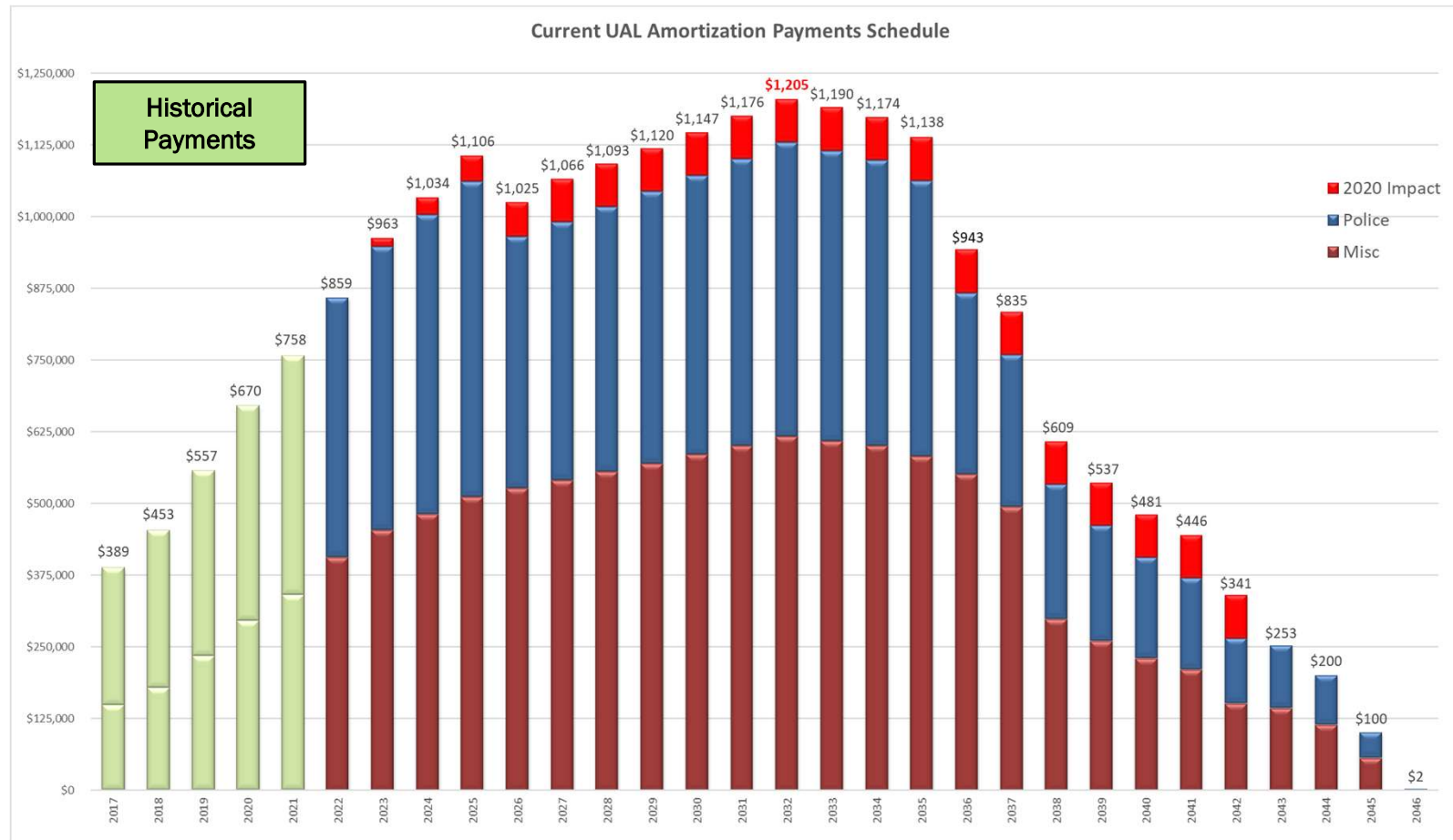
DOES NOT INCLUDE:

- Normal Cost:
 - 11.1%+ of salaries - Misc
 - 18.2%+ of salaries - Police
- 2020 COVID-19 impact

Total interest cost - \$8.2M



Adding 2020 Shortfall Impact



UAL Payments Only

Includes Estimated 2020 UAL Base Payments

DOES NOT INCLUDE:

- Normal Cost:
 - 11.1%+ of salaries - Misc
 - 18.2%+ of salaries - Police

Total interest cost - \$8.9M

(\$756K from 2020 UAL)



Pension Strategy Objectives

Pension costs cannot be viewed in a vacuum

Strategy must incorporate cash flow constraints, policy objectives, and current political dynamics

- Normal Cost - can only be reduced thru labor practices
- UAL Payments – can be reduced thru multiple strategies

Two approaches to pension cost management:

- Reduce annual payments – short-term cash flow management:
 - Extend UAL payments over longer term
 - Achieve interest cost savings comparing to 7% interest rate charged by CalPERS
- Reduce overall interest cost – long-term cost management:
 - Prepay or accelerate UAL payments



The Pension Toolbox

PAY DOWN

1. UAL Prepayment
 - a. Annual prepayment
 - b. From reserves, one-time revenues and fund surpluses
 - c. From savings of debt refundings
2. New Sources of Revenue

REFINANCE

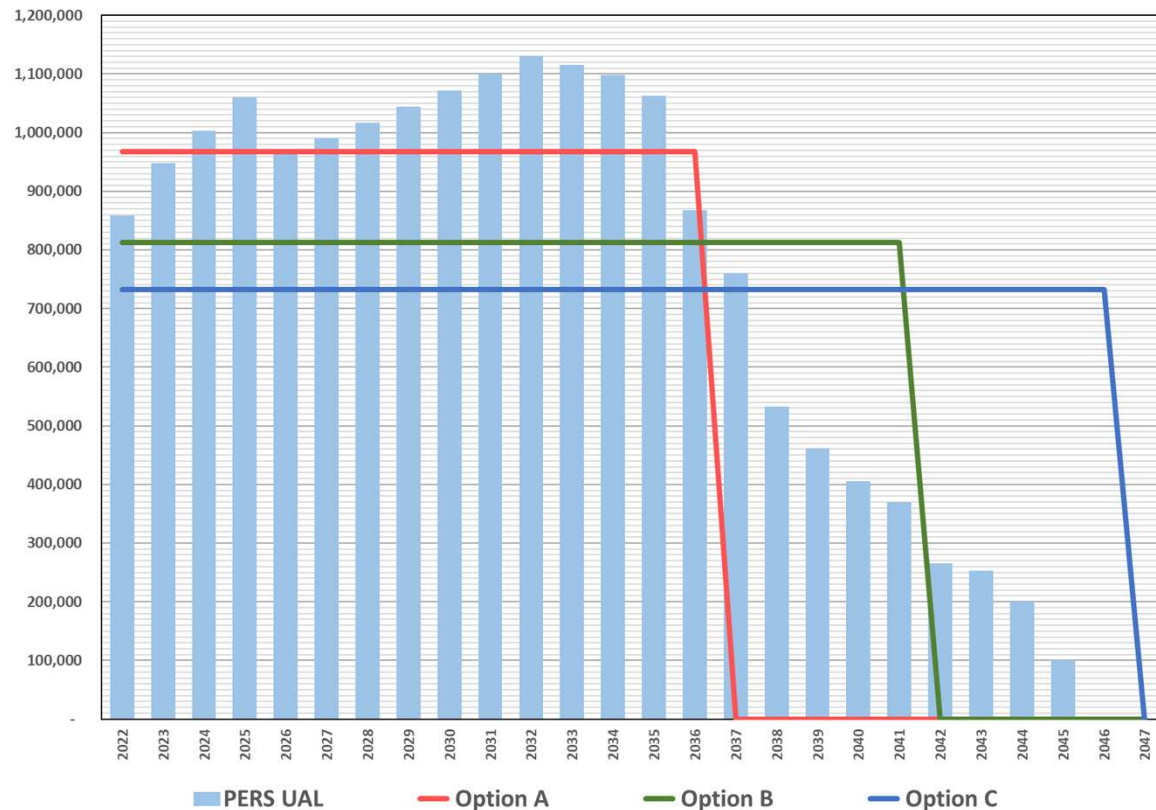
3. Intrafund Loans
4. Fresh Start / Informal Fresh Start
5. Capital Financing
6. Pension Obligation Bonds

OTHER

7. Labor Practices
8. Pension Rate Stabilization 115 Trust
9. Sale of non-essential assets / surplus properties to pay down UAL



Potential Refunding Options

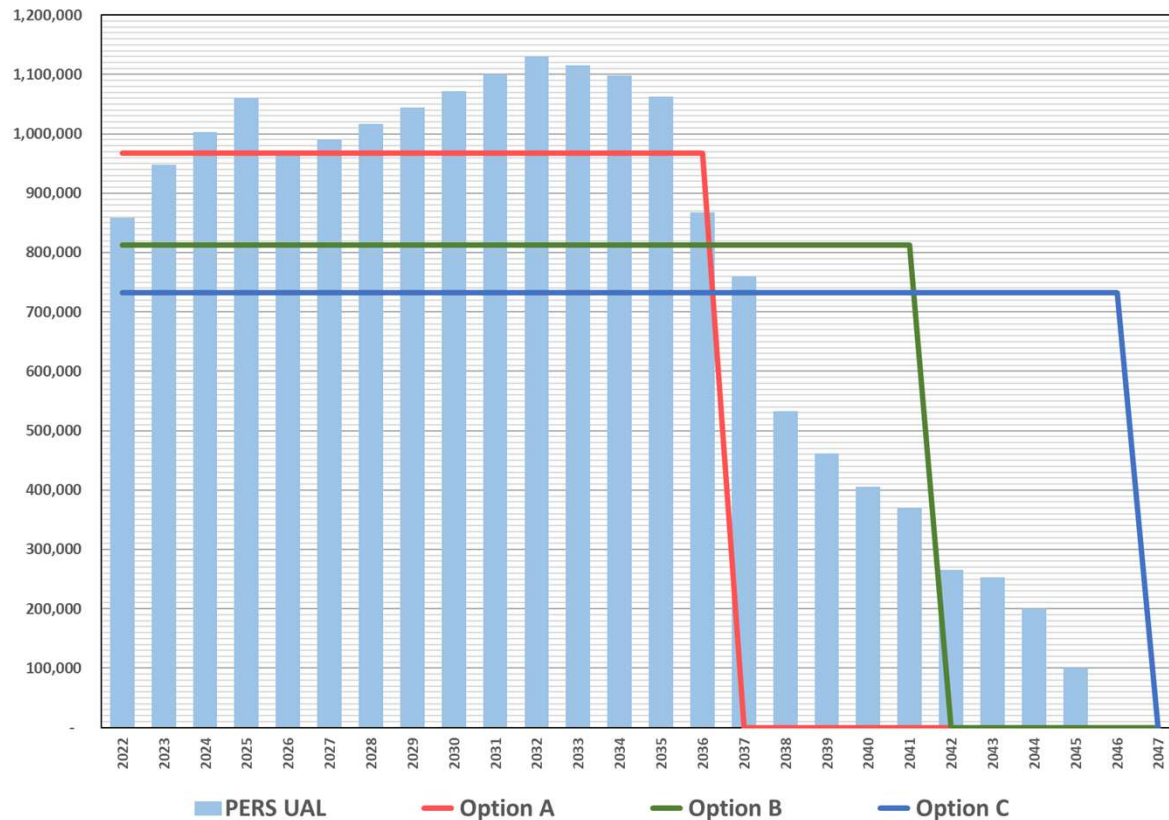


Option	Term	UAL Refunded		Annual UAL Cost Years 1-15 [1]		Cash Flow Savings [2]	Estimated Interest Rate [3]
		%	Amount	Min	Max		
Current CalPERS Schedule			\$10,508,160	\$859,000	\$1,130,000		
A	15 years	100%	\$10,508,160	\$967,000	\$967,000	\$4,176,000	4.25%
B	20 years	100%	\$10,508,160	\$813,000	\$813,000	\$2,424,000	4.50%
C	25 years	100%	\$10,508,160	\$732,000	\$732,000	\$378,000	4.75%

[1] Annual UAL Cost consists of semi-annual loan payments, payments on unrefunded bases, and includes amortization of costs of issuance (estimated at \$140,000 for public sale).
 [2] Savings are based on 7% CalPERS discount rate. PV savings depend on actual rate of return and may be different.
 [3] Interest rate estimate is based on current market rates. Actual rates may vary.



Potential Cash Flow Savings



Option	Term	% of UAL Refunded	Total Financing Cost [1]	Cash Flow Savings [2]			
				Years 1-10	Years 11-15	Years 15-25	Total
Current CalPERS Schedule			\$8,176,711				
A	15 years	100%	\$4,001,342	\$387,000	\$1,730,000	\$2,059,000	\$4,176,000
B	20 years	100%	\$5,752,593	\$1,929,000	\$875,000	(\$380,000)	\$2,424,000
C	25 years	100%	\$7,797,477	\$2,737,000	\$1,440,000	(\$3,799,000)	\$378,000

[1] Financing costs include interest and costs of issuance.

[2] Savings are based on 7% CalPERS discount rate. PV savings depend on actual rate of return and may be different.



Refunding Considerations – Benefits

- Enhanced budget predictability from new “flattened” repayment structure
- Estimated near-term cashflow savings from lower interest rates
- Present value (PV) savings achieved if CalPERS earns more than the refunding interest rate
- Increased “funded status” of City’s retirement plan
- Cash flow savings can be utilized to build up reserves, pay down future UAL increases, set up reserves for future OPEB costs, or any other legal purpose of the City
- Interest rates are presently at all-time lows



Refunding Considerations - Risks

- CalPERS Reinvestment Risk: CalPERS will have more money to invest
 - Same for any UAL prepayment
- PV Savings not guaranteed: CalPERS has to earn more than the refunding interest rate
 - Easier to achieve than earning CalPERS' own 7% discount rate
- Listed as “debt” on City’s financial statements
 - UAL is also shown as liability on financial statements
- For asset-secured structures, City’s owned assets may be required as collateral



Next Steps

- Identify City's Priorities
- Develop Appropriate Strategies
- Implement Time-Sensitive Strategies
- Adopt Comprehensive Pension Liability Management Plan
- Annual Reviews of Actuarial Valuation
- **There is no one-time fix!!!**



Finance Team Members and Responsibilities

- **California Municipal Advisors LLC – Independent Registered Municipal Advisor to City (Fiduciary)**
 - Assures City’s financial and policy interests are protected
 - Intermediary between Broker / Dealer or Placement Agent and City
 - Manages financial transaction details on behalf of City

- **The Weist Law Firm – City’s Bond Counsel (Fiduciary)**
 - Attorney to the City; assures City’s legal interests are protected
 - Prepares all legal documentation; assures bonds are “valid and legally binding obligations”



Questions?

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