



AGENCY: Finance & Admin Committee
MEETING DATE: September 14, 2022
DEPARTMENT: Finance
PRESENTED BY: Isaac Whippy
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AGENDA ITEM SUMMARY

TITLE:

Receive Recommendation on the Section 115 Investment Strategy with Public Agency Retirement Services (Pars) for the Purpose of Pre-Funding the City's Future Unfunded Liability with the California Public Employees' Retirement System (CalPERS) and Make Recommendation to the Fort Bragg City Council

BACKGROUND:

A Request for Proposals (RFP) for Section 115 Pension Trust Services was issued in April 2022. Two proposals were received from Public Agency Retirement Services (PARS) and CalPERS California Employers' Pension Prefunding Trust (CEPPT). The proposals were evaluated based on the firms' experience providing Section 115 pension trust services to other California municipalities and the managed funds' performance history and costs.

On June 25, 2022, the City Council approved establishing a Pension 115 Trust with Public Employees Retirement System (PARS). The next steps in the process were to model financial scenarios and provide Council with options on an investment strategy with a recommendation from the Finance Committee to fund the Trust. Once the investment strategy has been chosen, PARS will provide an investment policy tailored to the chosen investment strategy for the Finance Committee to review and recommend to Council for approval.

The City of Fort Bragg issued \$7.4 million in taxable Lease Revenue Bonds in November 2021 to reduce the City's unfunded pension liability. Additionally, CalPERS recognized a record 21.3% investment return for the fiscal year ended June 30, 2021, reducing the City's UAL. Unfortunately, as of June 2022, CalPERS is at -4%, which will result in a new significant UAL next year.

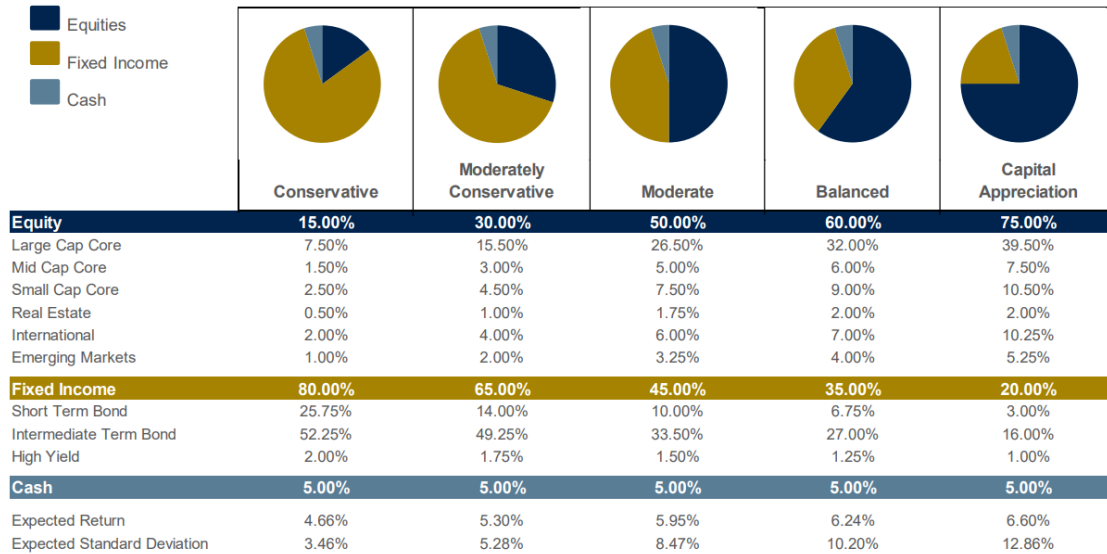
Pension 115 Trust Investment Strategy

PARS provides five (5) different strategy options, with each option either an active or passive approach. An active approach allows for actively buying and selling assets in the hope of making profits and outperforming a benchmark. A passive approach is a long-term strategy in which investors buy and hold a diversified mix of assets in an effort to match not beat, the market. Staff has modeled out the five options with potential scenarios based on the 5-year return for each of the strategies at an active level.

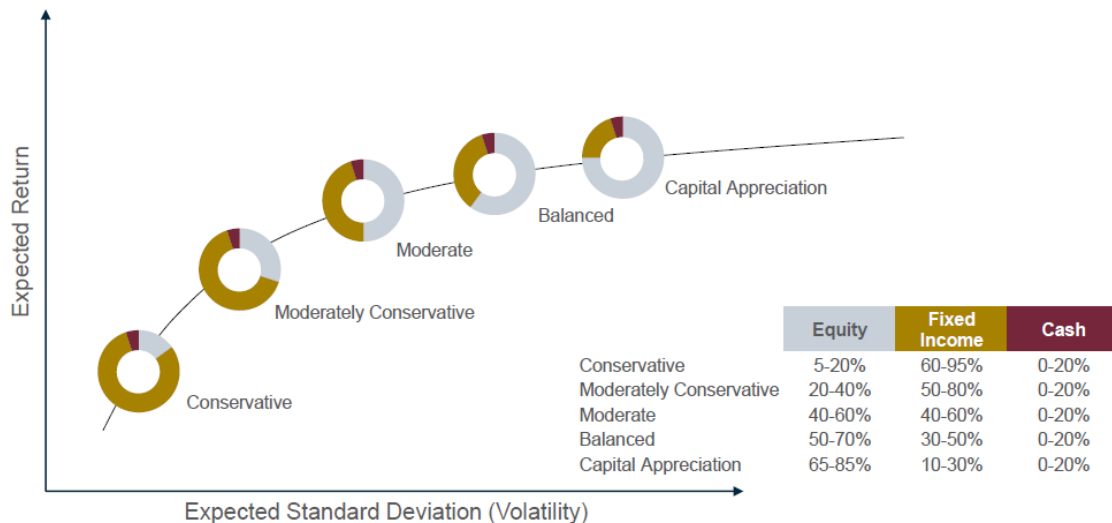
With regards to investment strategy, the five asset allocation strategies offered by PARS were reviewed: Conservative, Moderately Conservative, Moderate, Balanced and Capital Appreciation. Yield (risk) varied from the low equities/high fixed income Conservative

portfolio (20/80 allocation) to the high equities/low fixed income Capital Appreciation portfolio (80/20 allocation).

PARS Investment Objectives
As of April 2022



Returns over the past five years varied between 3.73% (Conservative) to 10.08% (Capital Appreciation). To preserve capital yet obtain a higher yield than we currently obtain under our regular investment program, staff focused on the Moderately Conservative (40/60 allocation) and Moderate (50/50 allocation) portfolios, and ultimately recommended the Moderately Conservative portfolio to the Finance Committee. PARS also requires that an agency select whether they desire Active Management or Index (Passive) Management; staff recommended Active Management, however it was noted that while Active Management obtained higher returns in the short-term; the 10-year benchmark showed them to be relatively equivalent.



Staff Recommendations

Staff recommends starting with an **active moderately conservative investment strategy** to have a target funding level of 90% with a minimum funding level of 80% and a maximum level of 100%. Steps will be taken during the budget process to determine if the City can make a minimum annual contribution of \$250k towards the Trust. Costs of this funding policy could be reduced should the pension 115 trust outperform the model. Providing an active approach will potentially allow the investment earnings to outperform the benchmark, reducing the amount needed to be input to the Trust.

Fiscal Impact

Sufficient funds are currently available to make an initial contribution of \$1,100,000 to the Section 115 Trust (\$750,000 set aside in the Unassigned Reserves – 50% of Surplus from FY 2020/21, \$350,000 budgeted in the FY 2021/22 Adopted Budget and \$250,000 budgeted in FY 2022/23 Adopted Budget.

The long-term impact of this near-term pension-related set of actions is impossible to quantify. It is fair to assume, however, that reserving funds for pension costs now and into the future will bring significant budgetary benefits over time. Over the past several years, CalPERS has lowered its discount rate by 50 basis points in recognition of the likelihood that the fund will not achieve projected investment returns. It is not unlikely that CalPERS will continue to reduce its discount rate. By fully funding its pension liabilities and using a more balanced rate of projected return, the City would set aside enough money to ensure that increasing pension-related costs will not crowd spending on other essential City projects and functions. This is both fiscally prudent and far-sighted.

Fees resulting from managing the Trust are embedded within the investment returns. There are no other costs associated with this action.

GREENHOUSE GAS EMISSIONS IMPACT:

There is no direct impact on greenhouse gas emissions.

CONSISTENCY:

The Pension Funding Policy incorporates the City Council policy of paying 50% of any year's General Fund surplus towards the City's UAL and furthers the City Council budget priority No. 6: Provide for additional contributions to CalPERS to pay the unfunded liability off earlier than 30 years.

ATTACHMENTS:

Investment Projections - PARS

NOTIFICATION:

N/A