

Pension Funding Policy Discussion

Beaumont, CA



GFOA Recommends Governments Rethink Their Reserves



Government Finance Officers' Association (GFOA)

GFOA has found that framing the reserves explicitly as a risk management tool and linking the reserve to concrete risks that decision-makers can appreciate is a great way to communicate why reserves are important.

Develop a Risk-Aware Reserves Policy

- Express your reserves policy as a range of desired reserves, with a floor and a ceiling.
- Conduct a risk analysis to get a sense of how the risks you face impact the reserves you should hold.
- Quantification of risk offers important advantages over subjective approaches.
- A chance-based simulation is better; it is how insurance companies conduct their analysis.

Recommended Pension Funding Policy



1. Refine Pension Funding Policy to include Pension Volatility Reserve (115 Trust) and assets with CalPERS
2. Consider minimum and maximum target balances
3. Consider funded status triggers to guide staff and future Councils to increase or decrease discretionary pension funding

Pension Funding Policy



- Documents Pension Management Goals
- Demonstrates Council Intent to Fulfill Promised Benefit
- Demonstrates Long-term Fiscal Discipline
- Reassures Council commitment to Creditors, Staff & Stakeholders
- Provide General Roadmap for Staff and Future Councils
- Identifies Transparency and Governance Procedures

How Should Uncertainty be Addressed by Policy



Unprecedented
Market Dynamics



Source:





2 years



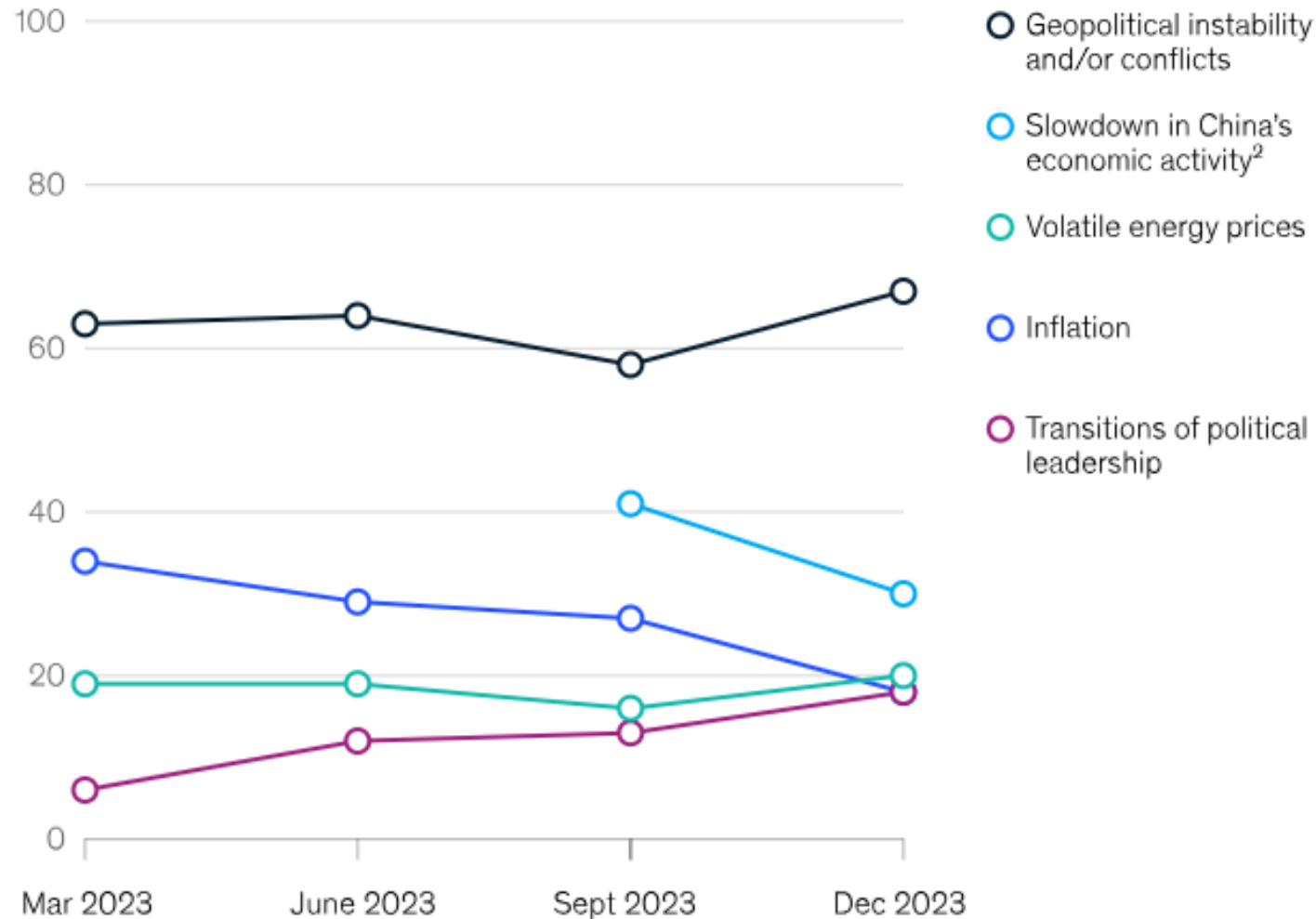
10 years



Geopolitical Present Threat to Global Growth



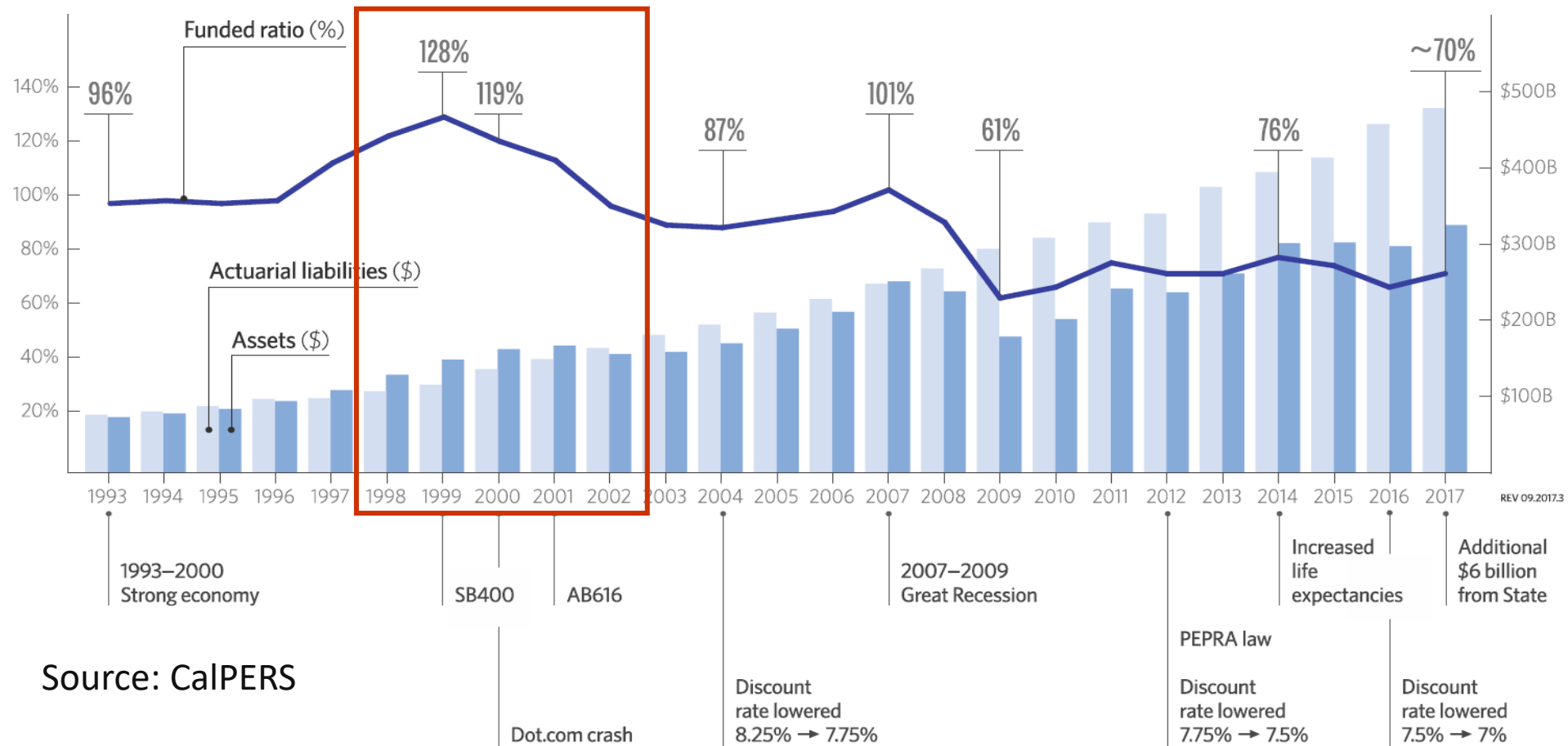
Biggest potential risks to global economic growth, next 12 months,¹ % of respondents



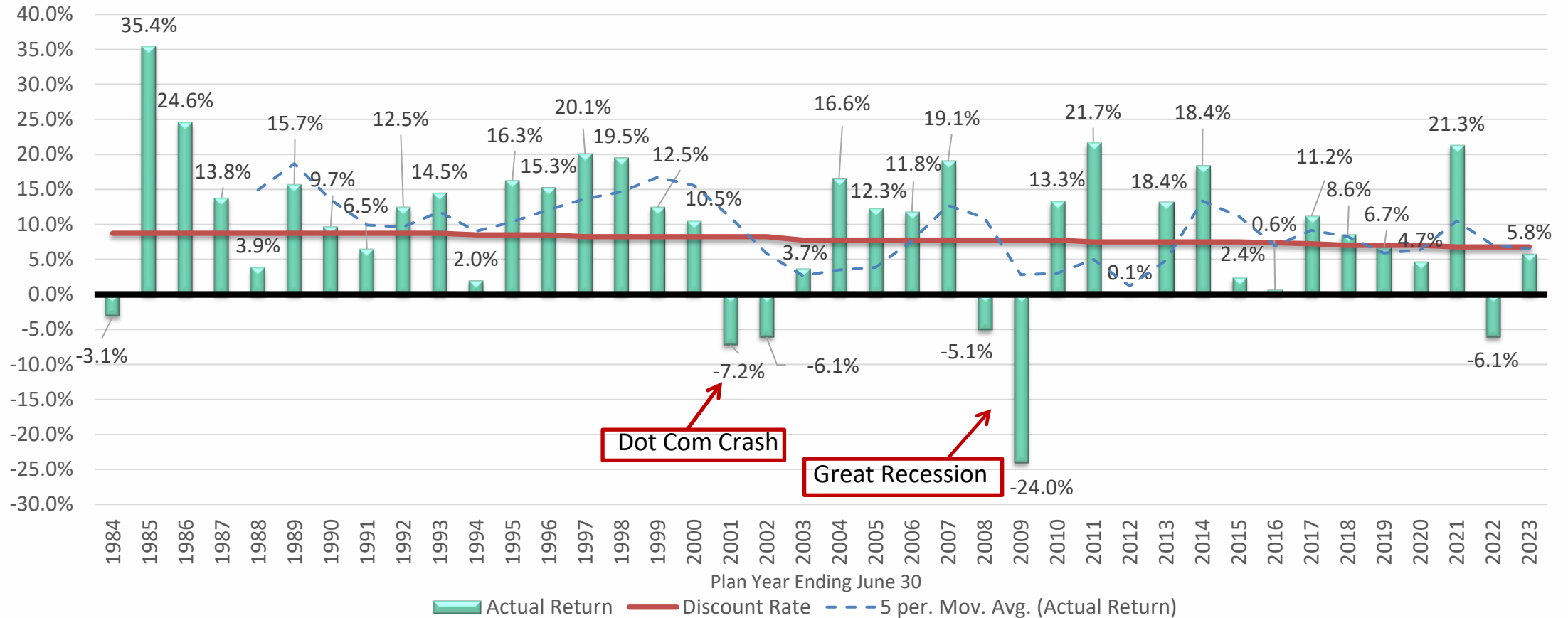
Historical Factors Impacting Funded Status



Challenge Yourself to Look Beyond What You See Today

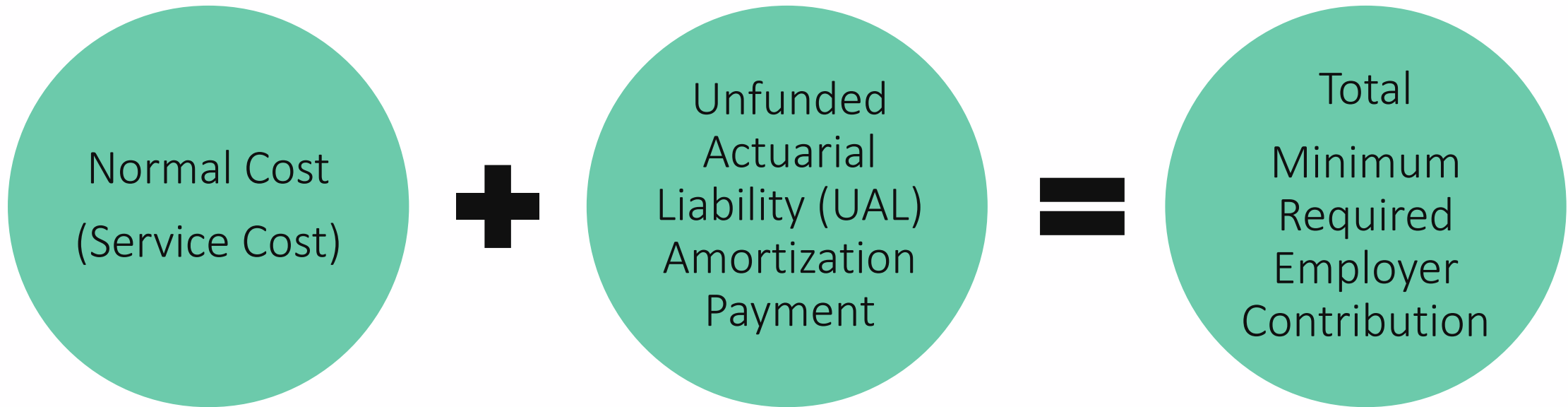


CalPERS Historical Investment Returns



Compound Annual Rates of Return through June 30, 2023					
	1 Year	5 Year	10 Year	20 Year	30 Year
Compound Annual Return	5.8%	6.1%	7.1%	7.0%	7.5%

Components of Required Employer Contribution



Normal Cost – the cost for current service paid as a percent of payroll. Increases when payroll increases, decreases when payroll decreases

Relatively stable – Generally expected to grow with payroll

UAL Contribution – payment toward past service. Paid as a fixed dollar amount each year.

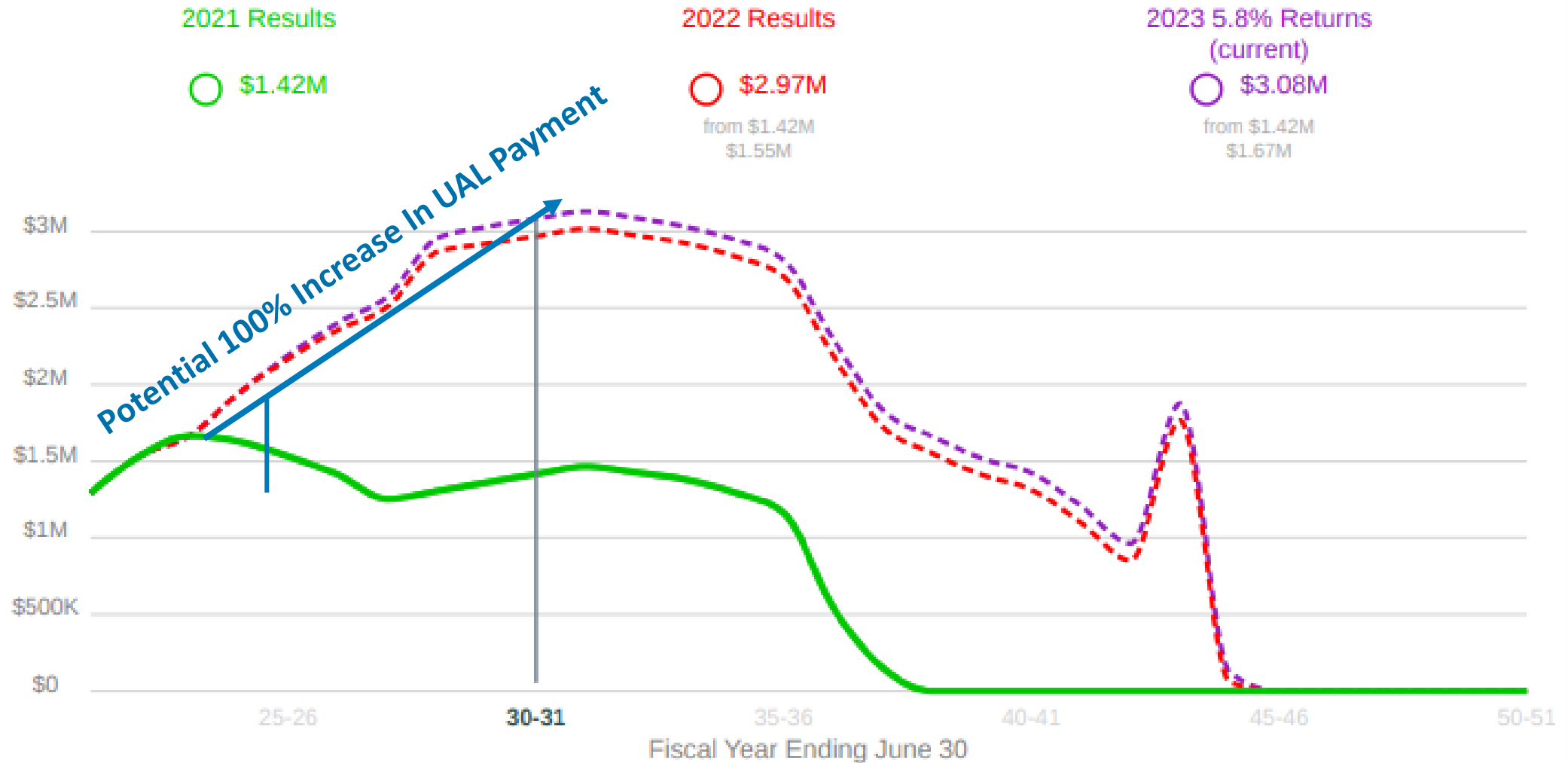
Volatile - Pension assets and resulting funded status are at the whim of the markets

Funded Status Trend



Fiscal Year End (FYE)	2020	2021	2022	2023
Accrued Liability (AL)	\$90,442,292	\$103,480,939	\$110,441,965	\$121,620,376
Market Value of Assets (MVA)	\$68,431,486	\$90,339,743	\$82,987,384	\$90,220,049
\$115 Pension Trust Balance			\$2,344,101	\$2,529,271
Unfunded Accrued Liability (UAL)	\$22,010,806	\$13,141,196	\$25,110,480	\$28,871,056
Funded Status	75.66%	87.30%	77.26%	76.26%
Invest Return				
Assumption	7.00%	7.00%	6.80%	6.80%
Actual	5.0%	22.4	-7.5%	6.00%
Experience Gain(Loss)	-2.00%	15.4%	-14.3%	-.70%

Impact on Annual Amortization Payment



2022 Investment Loss Amortization



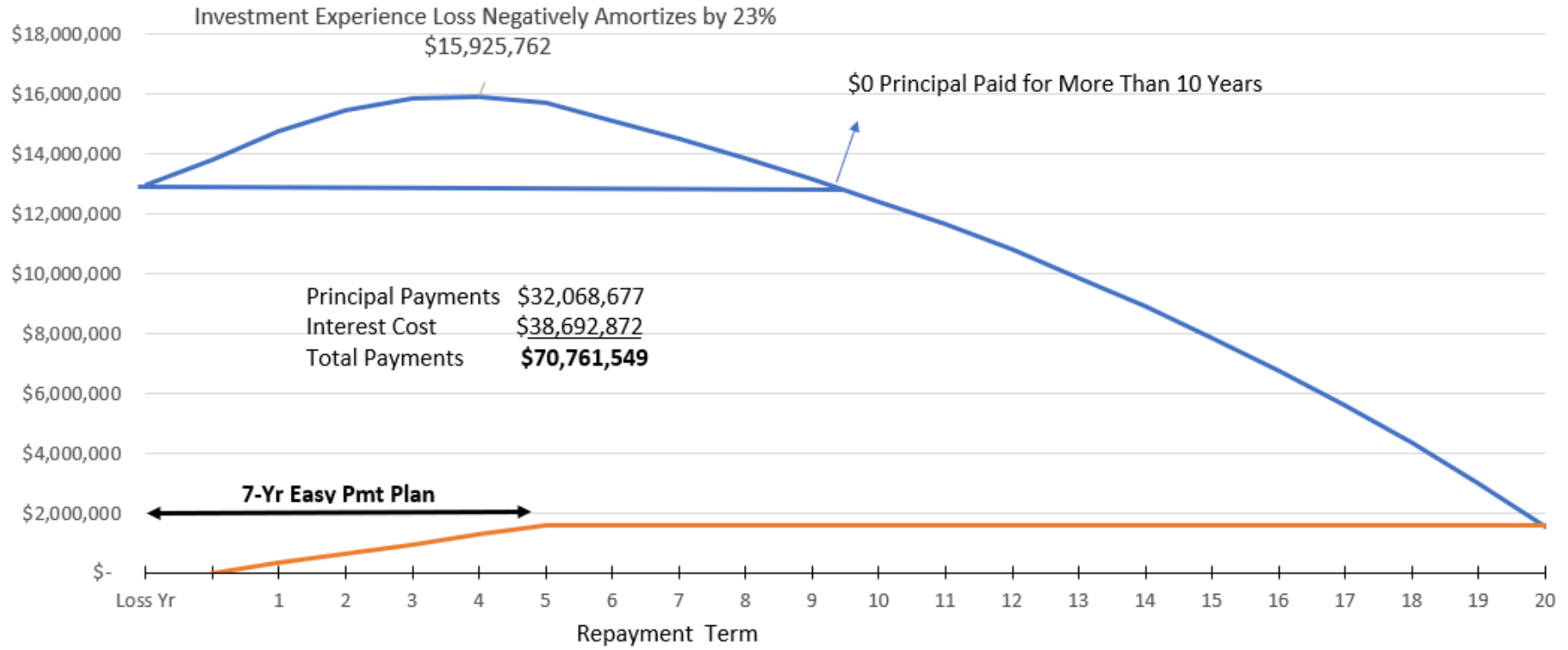
Count	Bud FY
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Option A - Default	
Level \$ 5Yr Ramp Up	
Start Paying in 24-25	
	20
Balance	Payment

No Principal Paid for 10 Years

Loss Yr	Count	Bud FY	Balance	Payment
			\$ 12,942,930	
			\$ 13,823,049	\$ -
1	24-25	1	\$ 14,763,017	\$ 317,327
2	25-26	2	\$ 15,438,964	\$ 634,653
3	26-27	3	\$ 15,832,937	\$ 951,980
4	27-28	4	\$ 15,925,762	\$ 1,269,306
5	28-29	5	\$ 15,696,961	\$ 1,586,633
6	29-30	6	\$ 15,124,663	\$ 1,586,633
7	30-31	7	\$ 14,513,449	\$ 1,586,633
8	31-32	8	\$ 13,860,673	\$ 1,586,633
9	32-33	9	\$ 13,163,508	\$ 1,586,633
10	33-34	10	\$ 12,418,935	\$ 1,586,633
11	34-35	11	\$ 11,623,732	\$ 1,586,633
12	35-36	12	\$ 10,774,454	\$ 1,586,633
13	36-37	13	\$ 9,867,426	\$ 1,586,633
14	37-38	14	\$ 8,898,720	\$ 1,586,633
15	38-39	15	\$ 7,864,142	\$ 1,586,633
16	39-40	16	\$ 6,759,213	\$ 1,586,633
17	40-41	17	\$ 5,579,149	\$ 1,586,633
18	41-42	18	\$ 4,318,840	\$ 1,586,633
19	42-43	19	\$ 2,972,830	\$ 1,586,633
20	43-44	20	\$ 1,535,291	\$ 1,586,633

Payment Total	\$ 28,559,387
Interest Cost	\$ 15,616,457
Payment Savings	NA



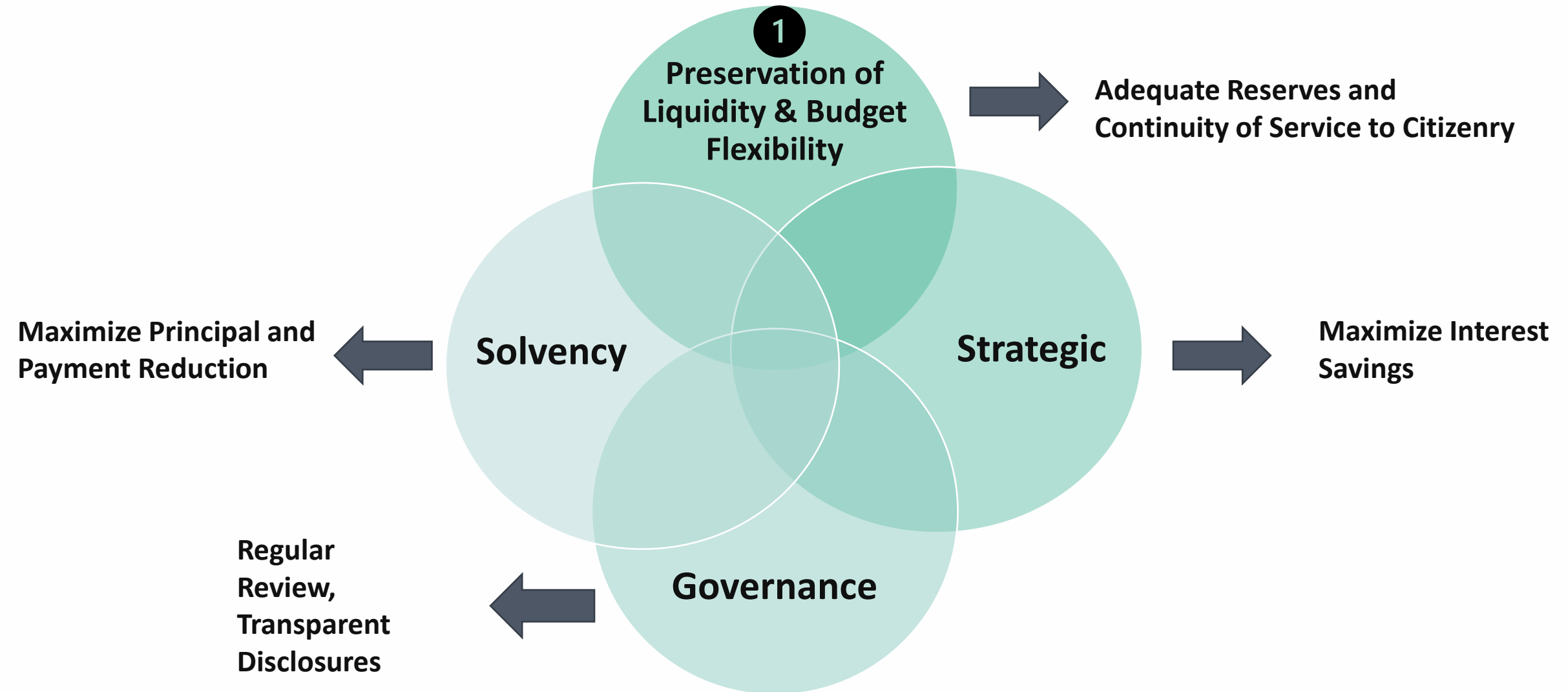
Reduce Interest Costs 13% to 24% by Starting Early and Bi-passing Ramp

Pension Management Tools



- Additional Discretionary Payments
 - Near-term Savings
 - Long-term Savings
- Full or Partial Restructuring of UAL Payment Schedule
- Pension Volatility Reserve
 - Internal Reserve (Substantial Increase in Fixed Income Yields Over Last Yr.)
 - S115 Trust (Higher Potential Long-term Returns; Short Term Volatility)
- Pension Funding and Reserve Policies

Pension Management Goals



Balancing and Applying Financial Resources



Objectives with Potentially Opposing Priorities:

1. Funding Long-Term Obligations
2. Meeting Current Service Needs
3. Cost Matching Principle
4. Volatility Management
5. Cash Flow Matching and Volatility Management
6. Interest Savings

Goals of Policy Parameters



1) Purpose of Min Max Targets

- a) Establish Minimum Pension Reserve Goal to Preserve Financial Flexibility
- b) Establish Maximum Pension Reserve Goal to Balance Needs of Community while Mitigating Funding Risk
- c) Empower Staff to Reduce Pension Interest Costs with Funds Between Minimum and Maximum Targets

2) Establish Funding Guidelines to Achieve Goals of the Policy

Sample Proposed Policy Parameters based on Pension Accrued Liability (AL)



Recommended Funded Status Guidelines	Recommended Policy % of (AL)		Recommended Targets based On Current (AL) \$120 M (\$ For Illustration Purposes)	
	Target Min.	Max	Target Min.	Max
Pension Reserve (115 Trust)	3%	20%	\$3,600,000	\$24,000,000
Assets with CalPERS	70%	90%	\$84,000,000	\$108,000,000
Combined Funded Status	90%	110%**	\$108,000,000	\$132,000,000**

Funding Guidelines*	Minimum Contribution Policy	Minimum Contribution Guidelines (\$ For Illustration Purposes)
If greater than 90% funded status	ADC +.25% AL	\$300,000
If greater than 75% but less than 90%	ADC + .50% AL	\$600,000
If less than 75% but greater than 65%	ADC + .75% of AL	\$900,000
If less than 65% of	ADC + 1% of AL	\$1,200,000

*Actuarial Determined Contribution (ADC) is the minimum required employer contribution. Additional contribution may be directed to increase to the City's 115 Pension Trust or to direct contribution to CalPERS provided the contribution would not foreseeably result in a funded status greater than 90% at CalPERS.

**Funds in excess of combined funded status guidelines shall be used to make the minimum required employer contributions (ADC).

Recommendations



- Finance and Audit Committee Reviewed January 22, 2024
- Recommended Policy be adopted by City Council

Staff Report Recommendations

- 1) Adopt Policy as Drafted or;
- 2) Recommend Revisions

Reference



		Hypothetical Funding Loss			
Count	Val Yr.	Level \$ 5Yr Ramp Up		Funding Loss	
		Hypothetical Loss Balance	20 Payment		
	2022	\$ 26,400,000	<i>Initial loss</i>	-22.00%	
	Pmt Yr	\$ 28,195,200	<i>Loss Repayment</i>	Est. UAL Pmt	Total
1	2025	\$ 30,112,474	\$ 647,258		\$ 647,258
2	2026	\$ 31,491,219	\$ 1,294,517		\$ 1,294,517
3	2028	\$ 32,294,815	\$ 1,941,775		\$ 1,941,775
4	2029	\$ 32,484,152	\$ 2,589,034		\$ 2,589,034
5	2031	\$ 32,017,462	\$ 3,236,292		\$ 3,236,292
		AL	Target 115 Bal.		% of AL
		\$ 120,000,000	\$ 1,941,775	2 Yrs.	1.6%
			\$ 3,883,550	3 Yrs.	3.2%
			\$ 9,708,876	5 Yrs.	8.1%



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