DATE: April 25, 2019

TO: Kensington Police Protection and Community Services District Finance Committee

FROM: Bill Zenoni, Sloan Sakai Yeung & Wong

Subject: May 2, 2019 Finance Committee Discussion of Pension Funding Options

The Finance Committee has, on several occasions, discussed the District's pension liability and the possibility of paying that outstanding obligation over a shorter amortization period. With preparation of the Fiscal Year 2019-20 budget currently underway, it is an appropriate time to continue this discussion. I have presented below some background information and possible options for consideration which can be discussed in further detail at next weeks Finance Committee meeting.

Background Information

Basic Pension Rule:

> Contributions + Investment Earnings = Pension Benefits + Expenses

In order for a pension system to remain viable, contributions from employees/employers plus investment earnings on funds contributed must be sufficient to fund pension benefits and administrative costs.

For CalPERS, approximately 41% of pension costs are funded from employer and employee contributions, with the remaining 59% funded from investment earnings
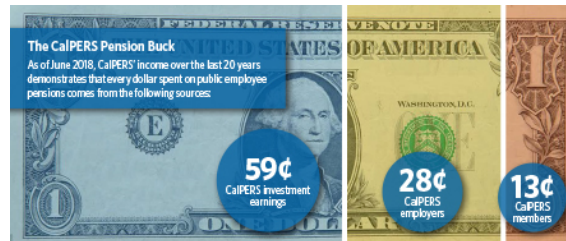
The District's unfunded accrued pension liability at June 30, 2019 (as reported in the CalPERS August 2018 annual valuation report) is projected to be $3.9 million. CalPERS is currently using a 30 year amortization schedule to amortize the repayment of this amount. Projected payments over the next six year period are as follows:

Fiscal Year	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25
UAL Payment	$250,446	$286,000	$326,000	$360,000	$380,000	$400,000

Because the retirement system has not been performing as anticipated, the CalPERS Board of Directors has made several significant changes over the past several years:

- Mortality Assumptions
- Discount Rate Assumption
  - 7.5% to 7.0%
- Move to more conservative investments over time

- Amendment to Amortization Policy
  - Amortize gains/losses over 20 years rather than 30 years. The amortization policy change was approved in February 2018 and applies to gains and losses reported after June 30, 2019

While the long-term goal of these changes is to ensure that the pension system is adequately funded, the short-term impact will be increased employer contribution rates.

Options for Consideration

There are several options which might be considered for addressing the pension liability and increasing employer contribution costs. We will discuss these options and the advantages/disadvantages of each at your May 2nd meeting.

Option 1: Continue to pay with the current 30 year amortization schedule and fund the anticipated cost increases in the budget each year.

Option 2: Request that CalPERS prepare a "fresh start" with a reduced 20 year amortization period. While this would reduce the District's overall interest payments to CalPERS and provide for a quicker pay down of the unfunded liability, it should be understood that not only would the annual payments increase, but the District would not be able to return to a 30 year amortization schedule in the future if financial conditions changed.

Option 3: Maintain the current 30 year amortization schedule but make additional voluntary payments to CalPERS to reduce the liability in those years when excess funds are available.

Option 4: Establish a 115 Retirement Trust. The District currently has a 115 Trust for other postemployment benefits (OPEB). A similar trust could be established to set aside funds to be used for smoothing future cost increases and/or to pay down the liability. One advantage of this alternative over Option 3 is that the funds would remain under the control of the District rather than CalPERS and would therefore not be subject to the investment earnings volatility of CalPERS. For the 2018 calendar year, CalPERS posted a net return of -3.5%.

I will be available at the May 2nd meeting to discuss this information in further detail and to hopefully answer any questions.