BUDGET UPDATES

- CalPERS Rate Changes
- Unfunded Liabilities
- General Fund Reserves

AUGUST 13, 2013

CalPERS Rate Changes

THE IMPACT
ON THE
CITY OF LONG BEACH
BUDGET

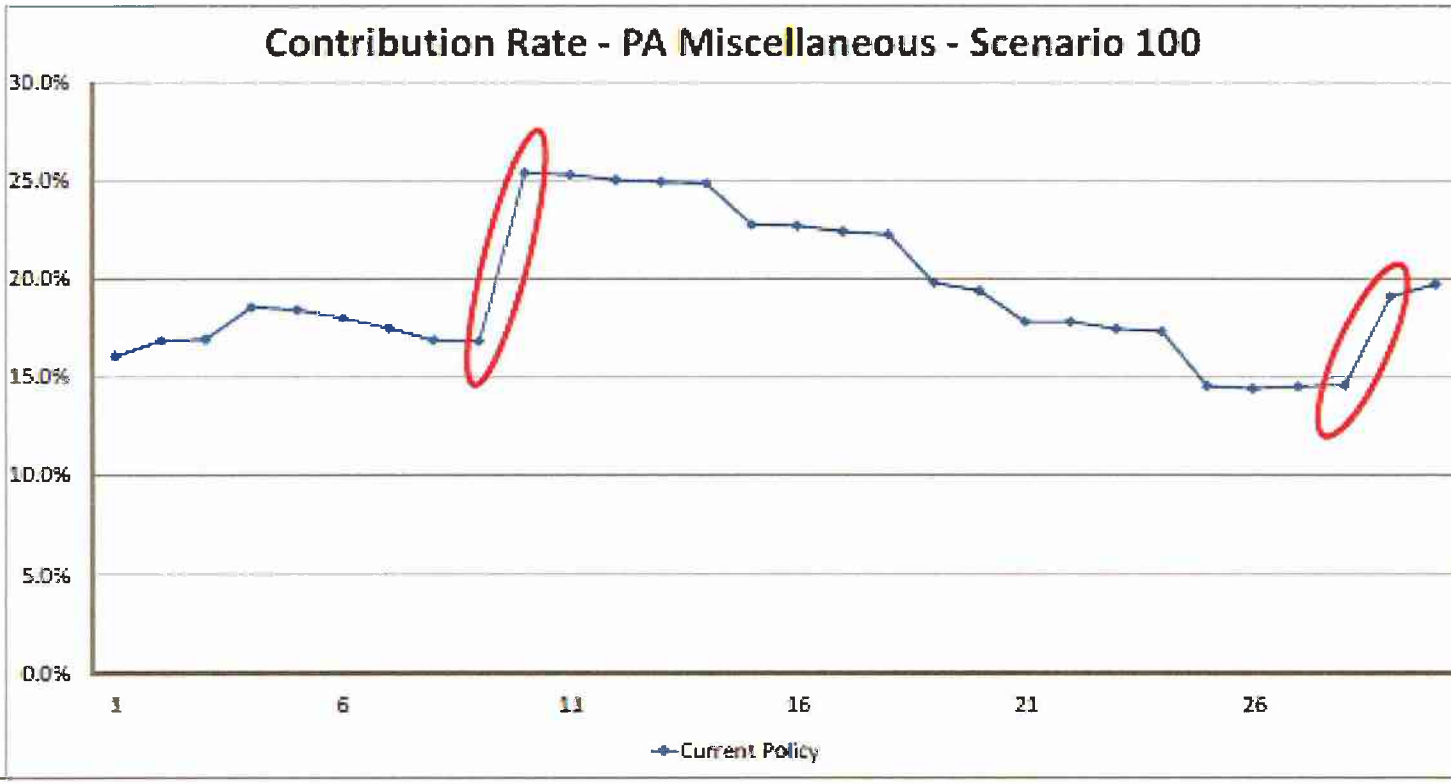
August 13, 2013

CalPERS Actions & Reasons

- In April 2013, CalPERS formally adopted a major change to the methodology of calculating employers' rates – the following reasons were given:
- CalPERS plan had too high a chance of funding problems under potential future adverse financial situations
- Full funding was not likely to be achieved
- Employer rate increases could be very steep and sudden under adverse financial conditions

CalPERS Slide: Large Cost Rate Jumps

Random Scenario – Returns Are Random



CalPERS Slide: Large Rate Jumps

Probability of employer contribution rate increasing by more than 5% of payroll in a single year

Smoothing Policy	Sample Miscellaneous Plan	Sample Safety Plan
Current Policy	47%	79%
New Policy	4%	45%

What Changed At CalPERS

- Ended
  - 15-year smoothing of gains and losses
  - Rolling 30-year amortization (funding period)
  - Actuarial (smoothed) valuation of assets
- Added
  - 5-year smoothing of employer contribution rate changes
  - 30-year fixed period amortization
  - Market value of assets

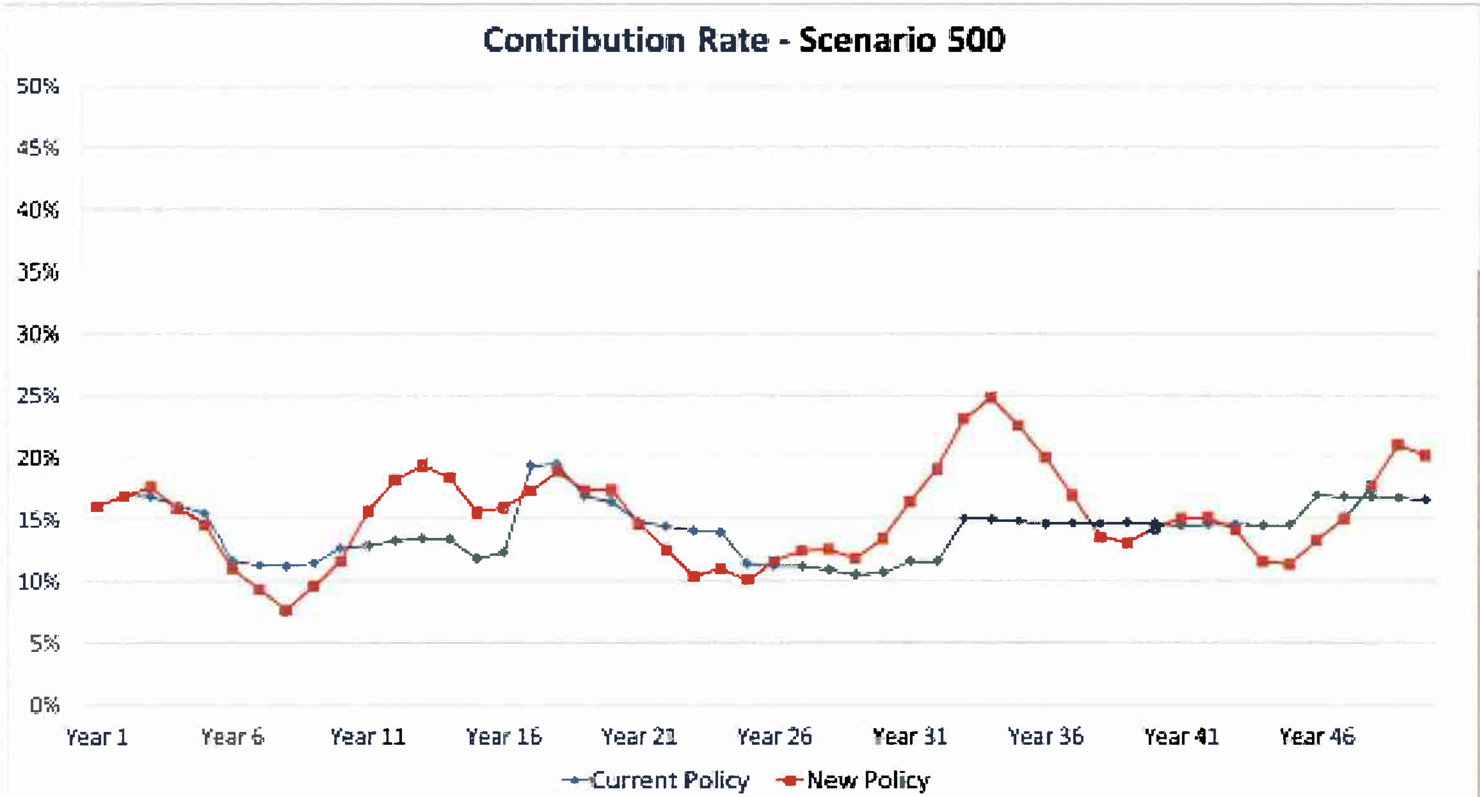
Does Not Change City Liability

- Does not change City's liability or pension cost
- Changes how fast the City pays off the liability – higher costs upfront
- Eliminates large, one-year spikes in rates
- Rates charged to employers will be more sensitive to the annual CalPERS' return on investments.
- New rate methodology will result in significant up and down cost patterns for the City

CalPERS Slide: Current vs. New

Current Method vs. New Method

Sample Miscellaneous Plan



Budgetary Impact on Long Beach

- Rate change effective in FY16
- General Fund net impact is projected to be about $1.4 m in FY16 (included in deficit projection)
- General Fund will have to absorb a projected additional $3.3 m each year for FY17 through FY20
- After FY20, the new rate structure will have been fully implemented

Projections With New CalPERS Rates

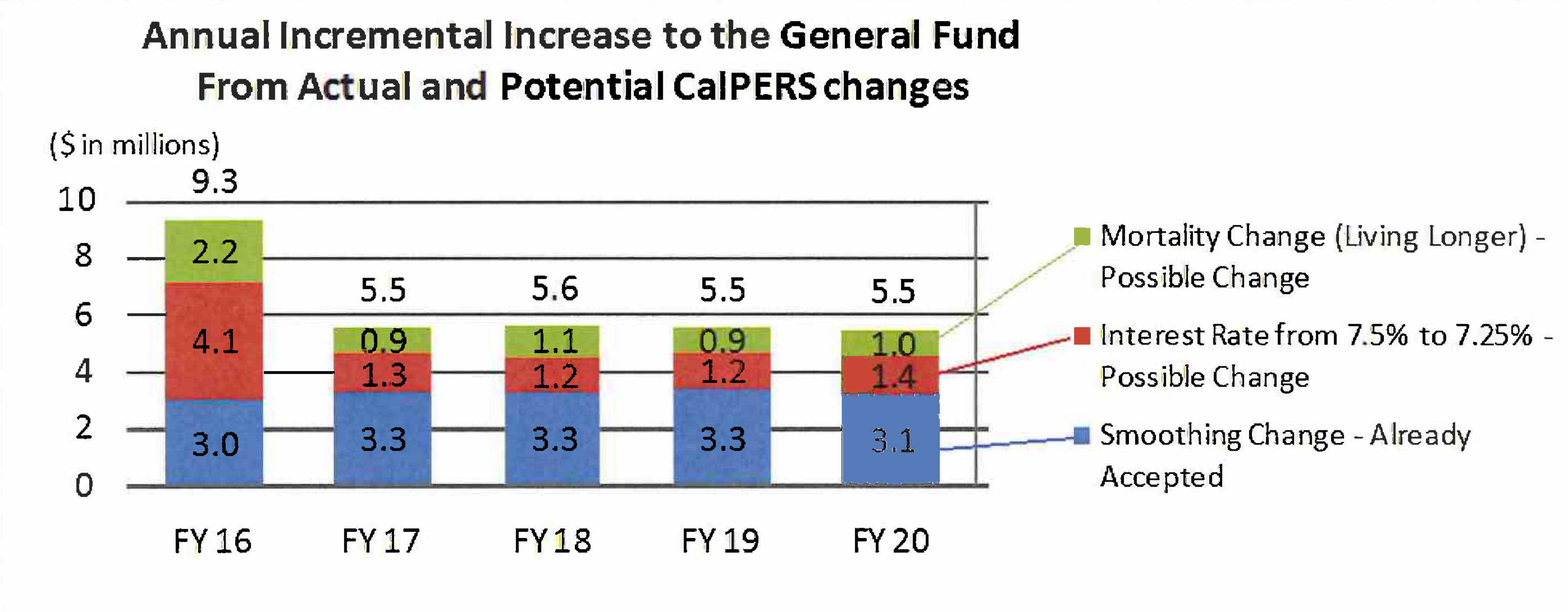
Three-Year General Fund Surplus (Deficit) Projection With New CalPERS Rates @ 7.5% rate of return ($ in millions)

	FY 14	FY 15	FY 16
Without CalPERS change	3.5	(2.5)	(0.9)
With CalPERS change	3.5	(2.5)	(2.3)
Budget With Carry Forward	3.5 Carry forward	1.0 Carry forward	(1.3)

Additional Costs Are Possible

- CalPERS is expected to consider two additional changes that could be implemented as early as FY16
- Mortality rate – additional costs & liabilities
  - $2.2 m in FY16 (General Fund)
  - $1.0 m for each of the next four years
- Reduced rate of return on investments? – additional costs and liabilities
  - $4.1m in FY16 (General Fund)
  - $1.3 m for each of the next four years
- It seems unlikely that both increases would be put in place at one time

Potential Cost of More CalPERS Changes



Rates Can Vary Significantly

- The new CalPERS rate formula is sensitive to changes in short-term rates of return

Preliminary Year General Fund Savings (Costs) With New CalPERS Rates And Varied Investment Earnings $ in millions

	FY16	FY17
CalPERS assumed rates (7.5%)	**(3.0)**	**(3.3)**
Low interest rates (0.2%)	(3.0)	(5.4)
High interest rates (11.6%)	(3.0)	(1.1)

Recommendations

- Watch for CalPERS actions next spring with regard to potential additional CalPERS cost increases in future years

- Create a CalPERS fluctuation reserve to help absorb temporary CalPERS cost increases due to CalPERS investment earnings fluctuations

CalPERS Rate Changes

THE IMPACT ON THE CITY OF LONG BEACH BUDGET

Update on Unfunded Liabilities

AUGUST 13, 2013

Defining The Issue

- Unfunded liabilities are costs for services already received, but not paid for by the City
- Pushes costs for current services into the future
- Bond rating agencies have expressed concern
- Workers' compensation, sick leave, retiree health insurance subsidy, and pensions

Options To Address

- No change to current practices (not a solution)
- Increase payments to slow growth of, or pay down, the unfunded liabilities
- Modify the benefits (where possible)
- Some combination of increased payments and modified benefits

Cost Savings with 30-Year Funding

General Fund Cost (Savings) From 30-Year Funding of Liabilities

General Fund $ in millions			
	1st Yr Cost	Savings After 30th Yr	Savings After 30th Yr in Today's Dollars
Workers' Compensation	2	(3)	(1)
Sick Leave*	1	(13)	(6)
Retiree Health Subsidy**	8	(24)	(11)
Pension	17	(71)	(31)
TOTAL	28	(111)	(49)

* Savings begin after 13 years

** Savings begin after 18 years

Cost Savings with 30-Year Funding

All Funds Cost (Savings) From 30-Year Funding of Liabilities

All Funds $ in millions			
	1st Yr Cost	Savings After 30st Yr	Savings After 30th Yr in Today's Dollars
Workers' Compensation	3	(4)	(2)
Sick Leave*	2	(24)	(11)
Retiree Health Subsidy**	14	(45)	(20)
Pension	33	(134)	(59)
TOTAL	52	(207)	(92)

* Savings begin after 13 years

** Savings begin after 18 years

Worker's Compensation

- **Solutions:** increase funding, focus on controlling and managing cost factors, work to influence State legislation to manage benefit levels, a combination
- **Updated suggestions:**
  - Annual budget to cover the current year's cost and potentially reduce liability
  - Control and manage cost factors
  - City Council could explore ways to help address the problem through legislation

Sick Leave

- **Solutions:** Increase funding, modify the benefits, a combination
- **Updated suggestions:**
  - Negotiate solutions based on some combination of funding and modifying the benefits

Pensions

- **Solutions:** Self-impose a higher contribution rate, modify benefits, a combination
- **Updated suggestions:**
  - Long Beach has accomplished Pension Reform and CalPERS has imposed a new contribution methodology designed to eliminate the liability within a reasonable time period
  - Consider additional strategies including more cost sharing as the City (employer) cost is high compared to employee cost

Retiree Health Subsidy

- **Solutions:** Increase funding, adjust or eliminate the subsidy, a combination
- **Updated suggestions:**
  - Consider adjusting or eliminating the subsidy

Other Long-Term "Liabilities"

- Deferred maintenance on buildings, roads, bridges and other infrastructure
- Deferred replacements and upgrades of systems hardware and software
- Incomplete funding for some vehicle replacements, e.g., fire vehicles
- Deferred investment in employee training and skill development

Actions Already Taken

- Long Beach pension reform
- California pension reform
- CalPERS rate increases re “smoothing” of earnings
- Identification and recognition of costs of sick leave, retiree health subsidy, and other deferred costs
- CalPERS consideration of further increases associated with interest rate and mortality assumptions
- Extra $1 million to City pension plan in FY14
- $322,000 allocation from one-time funds
- Improved funding of Worker’s Compensation
- Estimated $1.2 million for unfunded liabilities (all funds)

Options For Future

- Modification of costs associated with unfunded liabilities
- Budget policy discouraging increasing of liabilities
- Special maintenance and replacement funds
- Trust funds for benefit funding
- Targeted annual funding
- Funding from one-time revenues as available
- Ongoing reporting of status
- Some combination of above

Approaches For The Future

- Options focus around modifying costs and liabilities and funding the costs and liabilities, and may involve negotiations

- City Council may wish to consider and discuss each unfunded liability separately as a component of developing strategies and policies

Update on Unfunded Liabilities

AUGUST 13, 2013

General Fund Reserves

AUGUST 13, 2013

Updated Reserve Policy Adopted in 2011

2

- Brought City into compliance with new requirements of Generally Accepted Accounting Principles (GAAP)
- Clarified reserves and purposes for them
- City Council has increased reserves since then with some oil surplus funds

General Fund Unrestricted Reserves

General Fund FY12 Unrestricted Reserves With Subsidence Repayment

$ in millions

Reserve	$	% of Policy Level & Policy	
Funds Available (Budget)	0.4	0.1%	No policy level
Emergency Reserve	42.4	11.0%	Min of 8% and target of 10%
Operating Reserve	10.5	2.7%	Min of 2% and max of 8%
Reserve for Subsequent Year's Appropriations	5.5	1.4%	No policy level (will be spent)
Infrastructure, Systems Replacement, and Technology Reserve	1.0	0.3%	No policy level
Committed Funds (for pension unfunded liability)	1.0	0.3%	No policy level
Total Unrestricted Balances	60.8	15.7%	Target min of 16.7%

Reserve Levels

4

- Individual reserves are within policy ranges
- Total (unrestricted) reserves are below target minimum by1.0% or $3.8 m
- Percentages will change from year-to-year as total expenditures change

Recommendations

- Consider increasing reserve levels over time
- Use end of year surpluses or one-time revenues
- Establish a CalPERS fluctuation reserve

General Fund Reserves

AUGUST 13, 2013