SUBMITTAL TO THE BOARD OF SUPERVISORS
COUNTY OF RIVERSIDE, STATE OF CALIFORNIA

ITEM: 3.4
(ID # 14461)
MEETING DATE:
Tuesday, February 09, 2021

FROM : EXECUTIVE OFFICE:

SUBJECT: EXECUTIVE OFFICE: Pension Debt Reduction Strategies, All Districts. [$0]

RECOMMENDED MOTION: That the Board of Supervisors:

1. Receive and file the report back to the Board regarding specific measures taken to date as requested in Item 3.15 from February 4, 2020.

2. Direct the Executive Office to work with LAFCO and report back as suggested in Recommendation 6.

ACTION:Policy

Don R. Kent, Assistant CEO-County Finance Officer 2/2/2021

MINUTES OF THE BOARD OF SUPERVISORS

On motion of Supervisor Jeffries, seconded by Supervisor Hewitt and duly carried by unanimous vote, IT WAS ORDERED that the above matter is approved as recommended.

Ayes:	Jeffries, Spiegel, Washington, Perez, and Hewitt
Nays:	None
Absent:	None
Date:	February 9, 2021
xc:	E.O.

Kecia R. Harper
Clerk of the Board
By:
Deputy

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FINANCIAL DATA	Current Fiscal Year:	Next Fiscal Year:	Total Cost:	Ongoing Cost
COST	$ 0	$ 0	$ 0	$ 0
NET COUNTY COST	$ 0	$ 0	$ 0	$ 0
SOURCE OF FUNDS: N/A			Budget Adjustment: No	
			For Fiscal Year: 20/21	

C.E.O. RECOMMENDATION: Approve

BACKGROUND:

Summary

At the February 4, 2020 Board of Supervisors meeting, Item 3.15 requested that the Executive Office return to the Board of Supervisors with specific pension debt reduction strategies or options to consider as part of the budget recommendations. It cited Board Policy B-25, Pension Management and Other Post-Employment Benefits which states, "The County seeks to maintain a minimum funding level of 80%...to the extent the funding level falls below that, the County will prepare a plan to address the issue." This applies to the CalPERS defined benefit pension plan (Miscellaneous and Safety), OPEB, and, the County's Temporary and Part-Time Employees' Retirement Plan (TAP).

Also mentioned in the Form 11 were the Special Districts. While not specifically mentioned in Board Policy B-25 as far as the minimum funding level, discussions have occurred with the leadership of the Riverside County Regional Park and Open-Space District, the Riverside County Flood Control and Water Conservation District, and, the Department of Waste Resources as to what steps they can take to also achieve the 80%.

Direction was also given to bring forward a report detailing any burden that might exist of outside agencies' employees on the County of Riverside and any strategies that might be employed to transfer their obligations elsewhere. These agencies included the Western Riverside County Regional Conservation Authority (RCA), Riverside Local Agency Formation Commission (LAFCO) and the Riverside County Children and Families Commission.

Additional background

Due to the COVID-19 pandemic that began to impact the nation, state and County within weeks of Item 3.15 being presented, and, with the projected $100 million shortfall between the County's discretionary general fund revenue and state budget impacts (as mentioned in the FY 19/20 Third Quarter Budget Report in May 2020), the option of paying more in the form of additional discretionary payments, or adjusting contribution rates higher to be charged to departments was not feasible due to economic and fiscal uncertainty. Other options were already a work in progress, which are covered later in this report.

County of Riverside Miscellaneous and Safety Plans

Series 2020 POBs - Shortly after Item 3.15 was discussed in February, the Board authorized the sale of $720 million of Series 2020 POBs in April 2020, thereby reducing interest cost on approximately 20% of the total unfunded liability, split between the Miscellaneous and Safety Plans.

This series of POBs has a break-even, all-in rate of 3.53% vs. CalPERS' interest cost on the unfunded liability of 7% (a spread of 3.47%). **This strategy results in payment reductions (savings) of nearly $231 million through 2038, and $77 million within five years.** The County prepaid $371.5 million to CalPERS for deposit to the Miscellaneous Plan, and, $344.2 million for the Safety Plan which reflected a discount for pre-payment of the selected bases. **These bond proceeds ($716 million, net of costs of issuance) served as a one-time additional discretionary payment into the plans.** To be clear, the $716 million that was owed to CalPERS is now owed to bondholders, albeit at a much-reduced rate, generating the savings which per Board direction is now flowing into the 2020 Section 115 Pension Trust (discussed below).

Impact of Sale - Examination of the $716 million of proceeds invested with CalPERS in May 2020 <u>(not including POB debt service)</u>, for the period 6/30/19 - 6/30/20, shows **the Miscellaneous Plan funded status increased from 71% to 75% while the Safety Plan increased from 71% to 79%. This action taken by the Board accelerated the projected funded status by one and eight years respectively for the Plans compared to last years' report.** As a result, the projection is that the County is moving closer to the 80% minimum funding level as specified in Board Policy B-25, section II, E. **As seen in the 2021 PARC Report, page 5, the Miscellaneous Plan is projected to be at an 80% funded status in 2027, while the Safety Plan is in 2021.** Actual results may vary depending upon various factors such as the investment performance of CalPERS and/or any new, additional actuarial assumption changes.

The June 30, 2021 projected net funded ratio of both Plans combined, <u>including the Series 2020 POBs deposit of proceeds with CalPERS, and outstanding amounts owed on the POBs is 71%</u> (an increase of 1.2% from prior year).

2020 Section 115 Pension Trust - To capture the savings through the eighteen-year life of the POBs, a dedicated Section 115 Pension Trust account was established. Funds are collected each pay period over the course of each year the POBs are outstanding. Funds are then dollar-cost averaged into the Trust as an investment strategy to reduce the impact of financial market volatility and will continue to accumulate. This, coupled with the first Section 115 Pension Trust that the County established in 2016 can and should be used as the primary source of funds to make additional discretionary payments, or to help independently mitigate CalPERS' contribution rate increases and act as a buffer at some point in the future for budgeting purposes. The Trust funds cannot be used for any other purposes except for making payments directly to CalPERS to pay down a portion of the unfunded liability, or for reimbursing the County for CalPERS contributions.

As of June 30, 2020, the balance in the 2016 Trust was $29.9 million, (an increase of $1.2 million from prior year) with an annual net rate of return of 4.27%. The annualized net rate of return since November 2016 inception is 5.98%. The balances and rate of return for the 2020 Section 115 Pension Trust account will be reported in the 2022 PARC Annual Report as a full fiscal year cycle will have occurred. Over time these balances will become more significant as assets accumulate in the account.

A few points for Board consideration as to staying the course in the asset accumulation stage: 1.) Given the current size of the $3.6 billion unfunded liability, the amount of money required today to have *any* real financial impact, thus an increase in the funded ratio, would have to be a substantially larger sum than what is currently in the Trust(s).

2.) Within five years there will be in excess of $100 million in contributions made to the Trust(s), and within ten years, in excess of $175 million. Also, the potential for earnings power is greater than the interest cost of the unfunded liability. 3.) Based upon the analysis as shown in the 2021 PARC Report, peak contribution rates as a percentage of payroll are not projected until the early 2030's. Trust balances could assist the County in the future should the need arise due to any adverse financial impacts such as a recession that would impact its fiscal outlook.

Recommendation 1 – The recommendation of the Executive Office is that with PARC, monitor the funded status of the Miscellaneous and Safety Plans, as well the activity, investment performance and balances between both Trust accounts for future deployment. The Section 115 Pension Trust accounts should be used as the sole and primary source for any additional discretionary payments made to CalPERS in the future, or for smoothing contribution rates to departments as they are anticipated to have in excess of $100 million in balances within five years (and in excess of $175 million in ten years).

Other Post-Employment Benefits (OPEB)

Funded Status - As of June 30, 2020, the OPEB Trust with CERBT had a balance of $53 million (an increase of $8 million over the prior year), and an annual net rate of return of 5.48%. The annualized net rate of return since inception in 2007 is 6.31%. **The unfunded actuarial accrued liability (UAAL) is $87 million (an increase of $29 million over the prior year), which represents a funded status of 38% (a decrease of 5.6% from 43.6% prior year), excluding implicit subsidy.** The implicit subsidy is defined as the difference between the true cost of coverage for the retiree medical plan and the actual rate paid. Such a difference arises if retirees and active employees are in the same rate class. **A major distinction from the CalPERS defined benefit pension plans is that no interest is charged on the OPEB's UAAL.**

Note, the 2020 PARC Report had stated in error "the funded ratio without the implicit subsidy as of June 30, 2019 is 81.5%," when it should have stated "the projected funded status, without the implicit subsidy as of June 30, 2020 is 81.5%." The total amount to be charged to departments, however, was increased in FY 20/21 pursuant to the actuarial schedule from AON to $9 million (an increase of $5 million, or, 0.33% as a percentage of payroll from the prior year).

The major difference between the two UAAL ratios is cited in the AON Report below:

Plan liabilities and annual costs are considerably higher than the prior valuation, primarily due to a change to provide the SEIU bargaining group access to CalPERS health plans, which have higher costs and participation rates that results in an increase in liability.

After consideration of the items above, the UAAL and costs are higher than expected based on a projection from the prior valuation, as a net result of the following factors: expected return on assets was reduced by CalPERS in the CERBT Strategy 2 assumed return of 7.01% to 6.15%, reflecting lower expectations. As a result, the discount rate similarly decreased, resulting in an increase in liability. Deferred retirees eligible for CalPERS health plans elected coverage higher than previously assumed, resulting in a liability loss. Investment return was lower than expected, resulting in an asset loss. See page iv of the AON report, Attachment 4 of the 2021 PARC Report.

Multi-Year Plan - In keeping with Board Policy, County staff requested a review from AON of a multi-year plan to achieve an 80% funded status for the retiree benefit portion of the OPEB liability.

The current actuarial schedule projects the Board Policy's 80% minimum funding level, excluding implicit subsidy, would be reached in 2027 with $16.9 million to be charged to departments annually beginning in FY 21/22, (an increase of $7.9 million from the current $9 million required in FY 20/21). As a percentage of payroll, the $16.9 million represents approximately 1.1% (an increase of 0.47% from the 0.63% charged in FY 20/21). See page v of the AON report, Attachment 4 of the 2021 PARC Report.

For now, the plan is to follow the schedule to meet the 80% in 2027. However, per the terms of the Laborers' International Union of North America (LIUNA), Local 777 Memorandum of Understanding (MOU), the transition to the CalPERS health plans for all employees will be effective April 1, 2021. With this addition of employees coming into the CalPERS health plans, the rate will likely increase to 2.25%, or more. Staff and PARC will continue to monitor the funded status of the OPEB Trust with next years' annual valuation report and adjust rates upward again in accordance with the actuarial schedule to achieve the 80% funded status.

In contrast to the CalPERS defined benefit pension plan liability, there is no direct connection between the implicit subsidy portion of the OPEB liability and the County's cost of providing the retiree healthcare benefit. Recognizing this, the Board adopted Policy B-25, Section III (A) Other Post-Employment Benefits (OPEB) which states, "the County seeks to maintain a minimum funding level of 80% in its OPEB plan, excluding any implicit subsidy liability." There could be some advantages to taking steps to funding a portion of the implicit subsidy in the future; staff and PARC will monitor the issue and bring any recommendations to the Board.

Investment Strategy - In consideration of the longer-term investment horizon of the OPEB Trust, and **to mitigate some of the pending rate increases due to more employees coming into the CalPERS health plans, PARC has reviewed and approved at its January 13, 2021 meeting the recommended change from CERBT's Strategy 2 (assumed return 6.15%) to Strategy 1 (assumed return 7.30%).** The difference between the two strategies is the mix of allocations amongst the various asset classes that makeup the portfolios (equity, fixed income, real estate, commodities, and cash). The funds will be dollar-cost averaged over an extended period in an effort to reduce market risk.

Recommendation 2 - The recommendation of the Executive Office is that with PARC, monitor the activity, investment performance and balances in the OPEB's CERBT Trust; continue to adjust rates upward in accordance with the actuarial schedule with each years' annual valuation report as part of the multi-year plan to achieve the 80% funded level by 2027, excluding the implicit subsidy.

Part-Time and Temporary Employees' Retirement Plan (TAP)

Funded Status - As of July 1, 2020 the Plan had a balance of $45.4 million (an increase of $1.9 million from the prior year) in the investment account with US Bank, an annual net rate of return of 3.72%, and, **a funded ratio of 77.7%.** The annualized net rate of return since inception in 2010 is 6.02%. The assumed rate of return is 6%. The Plan is not projected to be less than 80% in the future years after June 2021. A major distinction from the CalPERS defined benefit pension plans is that no interest is charged on the TAP Plan's UAAL.

AON projects a 79.8% funded status by June 30, 2021 (with only a $93,000 shortfall from the 80% level). The rate as a percentage of payroll will be going from 4.02% in FY 20/21 to 5.58% in FY 21/22 (an increase of 1.56%). Participants (the part-time employees) are required to contribute 3.75%.

Staff and PARC will continue to monitor the funded status of the Part-Time and Temporary Employees' Retirement Plan with next years' annual valuation report and adjust rates upward in accordance with the schedule to achieve the 80% funded status. See page ii & iii of the AON report, Attachment 5 of the 2021 PARC Report.

Recommendation 3 - The recommendation of the Executive Office is that with PARC, monitor the activity, investment performance and balances in the investment account with US Bank; continue to adjust rates in accordance with the actuarial schedule with each years' annual valuation report as part of the multi-year plan to achieve the 80% funded level.

Special District Plans

Similar to the County's Miscellaneous and Safety Plans, additional discretionary payments would be required to increase the funding level, thereby having budgetary impacts on the Districts (Parks and Flood), as well as the Department of Waste Resources, that may, or may not be feasible at this time due economic uncertainty caused by the COVID-19 pandemic.

The Riverside County Regional Park and Open-Space District has three rate plans. As of the annual valuation report(s) for June 30, 2019, the funded status of **Tier I was 73.5%** (a decrease of 0.5% from 74.0%, prior year) and has an accrued liability of $46.9 million, a market value of assets of $34.5 million, and, an unfunded liability of $12.4 million. Tier II's funded status is at 89.9% (no change from prior year) and has an accrued liability of $398,743, a market value of assets of $358,502, and, an unfunded liability of $40,241. Tier III's funded status is at 90.0% (an increase of 0.9% from 89.1%, prior year) and has an accrued liability of $1.4 million, a market value of assets of $1.3 million, and, an unfunded liability of $142,515.

The District's plan to address its Tier I status below 80% this fiscal year has been placed on hold due to financial implications caused by the COVID-19 pandemic. To date, the District has had to temporarily close 8 park sites, close campgrounds for overnight camping, transferred 3 park sites to alternate operators, experienced over $500,000 in loss of revenue, and, has laid off 7 employees resulting in leave payouts. The District will revisit the potential of additional discretionary payments at a later time when their financial outlook has stabilized.

The Riverside County Flood Control and Water Conservation District's annual valuation report for June 30, 2019, shows a **funded status of 63.7%** (a decrease of 0.20% from 63.9%, prior year). The District has an accrued liability of $213.9 million, a market value of assets of $136.3 million, and, an unfunded liability $77.6 million. **The District has developed a long-term plan that includes making additional discretionary payments to CalPERS in an effort to bring the funded status at or above 80% by fiscal year 2027, assuming all other factors remain constant. An additional $6.7 million was paid in FY 19/20, and, $6.1 million in FY 20/21.** According to CalPERS, these payments will be reflected starting in the next years' valuation report when the District is projected to reach a funded status of 67.6%. The District intends to continue making additional discretionary payments based on its ongoing assessment of its fiscal outlook for future years.

The Riverside County Waste Resources Management District was dissolved in 1998, with the exception of existing employees at that time electing to maintain their

District status. All new hires or transfers are designated as County employees; no new District employees have been added since 1998.

The District's annual valuation report for June 30, 2019 shows a **funded status of 70.1%** (a decrease of 0.70% from 70.8%, prior year). The District has an accrued liability of $53.4 million, a market value of assets of $37.5 million, and an unfunded liability $15.9 million. **In order to reach the 80% funded status, the Department of Waste Resources has doubled the minimum required payments as calculated by CalPERS to $2.2 million in FY 20/21, and $2.8 million in FY 21/22. Current projections indicate that under this revised payment schedule, the 80% level will be reached in FY 21/22.** The additional payments are voluntary and will allow the department the flexibility to adjust as budgets allow, leaving room for unforeseen events, mandates or regulatory changes.

Recommendation 4 - The recommendation of the Executive Office is that annually, with each CalPERS valuation report, monitor the funded status with the leadership of the Special Districts and the Department of Waste Resources. Discuss adjustments to contributions as part of their multi-year plan to achieve the 80% funded level within the confines of their budgets.

<u>Western Riverside County Regional Conservation Authority (RCA)</u>

On December 8, 2020, the Board of Supervisors approved agenda Item 3.1, amending and restating the agreement for services between RCA and the County of Riverside. Effective January 1, 2021, the Riverside County Transportation Commission began to provide the staffing and management agency role for RCA. As a result, a lump sum payment of $3.9 million was received from RCA as a pro-rata share of their unfunded pension liability obligation as well as any amounts owed for OPEB and the Replacement Benefit Plan since they are no longer in the County's Miscellaneous Plan. **The payoff of $2.6 million for the unfunded liability portion was made to CalPERS on January 20, 2021.**

Recommendation 5 – No further action is warranted as the unfunded liability portion has been paid off and eliminated as noted above.

<u>Local Agency Formation Commission (LAFCO)</u>

Riverside LAFCO's employees have been a part of the County's Miscellaneous Plan since its establishment. As cited in their Five Year Strategic Plan dated January 23, 2020, Strategic Objective (6): Pension & OPEB Unfunded Liabilities, the goal is to develop a plan to mitigate its existing and future liabilities in the most efficient and cost-effective manner. It was noted that any buydown plan would entail annual budget allocations to the various agencies that primarily fund LAFCO's annual budget. **The unfunded pension liability as stated in their audited financial statements for the fiscal year ended June 30, 2019 was $803,084, while OPEB was $5,055.**

Also stated in the plan of action is: 1.) Identify the process used by the County and LAFCO auditors for determining its pro-rated share of the unfunded liabilities and verify that the process is satisfactory. 2.) Determine the future unfunded liability over 10 years for each category. 3.) Identify a reasonable process for paydown of current and future unfunded liabilities. 4.) Develop a 5-year and/or 10-year payment plan for budget allocation to buydown each unfunded liability. The Commission is being charged the same rates as other County departments (which includes the normal cost, unfunded liability, POB debt service, OPEB, etc.).

Recommendation 6 - The recommendation of the Executive Office is that 1.) the Board direct County staff to work with LAFCO on its plan of action items 1 through 4 as noted in its Five Year Strategic Plan dated January 23, 2020, Strategic Objective (6): Pension & OPEB Unfunded Liabilities and report back within 90 days, or as soon as possible thereafter pending their June 30, 2020 audited financial statements. 2.) Upon future receipt(s) of its pro-rata share of unfunded liabilities, the Board direct County staff to either then make an additional discretionary payment to CalPERS, or (due to the very small size) deposit into the 2016 Section 115 Pension Trust.

<u>Riverside County Children and Families Commission</u>

The Commission was first established after the passage of Proposition 10 in November 1998 and was created through the adoption of Ordinance No. 784 in December 1998. At that time, the administrative support for the Commission was done through the Health Services Agency (which included Public Health, Environmental Health, and the Hospital). It was initially an independent Commission but has had County staffing since inception. It first became a County agency in July 2009 when Ordinance No. 784.9 became effective. In October 2019, Ordinance No. 784 was again amended through Ordinance No. 784.11 naming the Commission a department agency. It is being charged the same rates as other County departments (which includes the normal cost, unfunded liability, POB debt service, OPEB, etc.).

Recommendation 7 - No further action is warranted as this is a County department for all intents and purposes, therefore is included in the County's Miscellaneous Plan.

<u>Impact on Citizens and Businesses</u>:

Any decrease in long-term pension costs (which are not projected to peak until the early 2030's) will have budgetary impacts across all of the departments, and, as a result, would decrease the costs of services that are provided to citizens and residents of the County.

Lisa D Brandl 2/2/2021