



TOWN OF LOS GATOS
FINANCE COMMITTEE REPORT

MEETING DATE: 4/9/2018

ITEM NO: 3

DATE: APRIL 3, 2018

TO: COUNCIL FINANCE COMMITTEE

FROM: LAUREL PREVETTI, TOWN MANAGER

SUBJECT: RECOMMEND TO THE TOWN COUNCIL A PROPOSED UNFUNDED ACTUARIAL LIABILITY (UAL) FUNDING POLICY FOR ADDITIONAL ANNUAL DISCRETIONARY PENSION PAYMENTS TOWARDS THE UAL TO OBTAIN INTEREST SAVINGS AND LOWER THE TOWN'S LONG-TERM UNFUNDED PENSION LIABILITY.

RECOMMENDATION:

Recommend to the Town Council a proposed unfunded actuarial liability (UAL) Funding Policy for additional annual discretionary pension payments towards the UAL to obtain interest savings and lower the Town's long-term unfunded pension liability.

BACKGROUND:

On February 12, 2018, the Council Finance Committee discussed staff's recommendation to review alternative strategies to proactively address the Town's pension unfunded actuarial liability (UAL). During the discussion, the Finance Committee received information about two potential approaches, the first being a "fresh start". A fresh start is a California Public Employees Retirement System (CalPERS) term for re-amortizing the current UAL over a shorter period of time. The current CalPERS amortization period is approximately 30 years.

The second alternative was the use of additional discretionary payments (ADP) or "lump-sum" payments made each year to effectively accomplish the same objective as the "fresh start." Staff recommended consideration of the voluntary ADP payoff strategy because of its flexibility and the ability to control timing and amounts of additional contributions. Staff also proposed that a UAL Funding Policy be adopted by Council to strengthen the implementation of the ADP

PREPARED BY: STEVE CONWAY
FINANCE DIRECTOR

Reviewed by: Town Manager, Assistant Town Manager, and Town Attorney

BACKGROUND Continued)::

strategy. The Committee reviewed the fiscal impacts and potential interest savings of both alternatives and directed staff to pursue the ADP strategy along with development of a UAL Funding Policy.

Pursuing this direction, staff has prepared an analysis reviewing the potential fiscal impacts of making additional discretionary payments and a recommended UAL Funding Policy (Attachment 1).

DISCUSSION:

Staff performed analysis on the approximate \$31.3 and \$23.3 million in unfunded actuarial liabilities related to the Town's CalPERS Miscellaneous and Safety employees' pension plans respectively, projected as of July 1, 2018. CalPERS actuarial staff assisted in modeling the amounts of additional annual discretionary payments required to achieve a reduction of the outstanding unfunded actuarial liability from an approximate 30-year to a 20-year amortization period. The analysis was designed to achieve consistent level ADPs over the 20-year period and includes the impacts of the lower future discount rate (7%). It is important to note that the analysis does not incorporate the potential of future assumption changes which could either increase or decrease employer contributions and some positive returns yet to be realized which will decrease employer contributions.

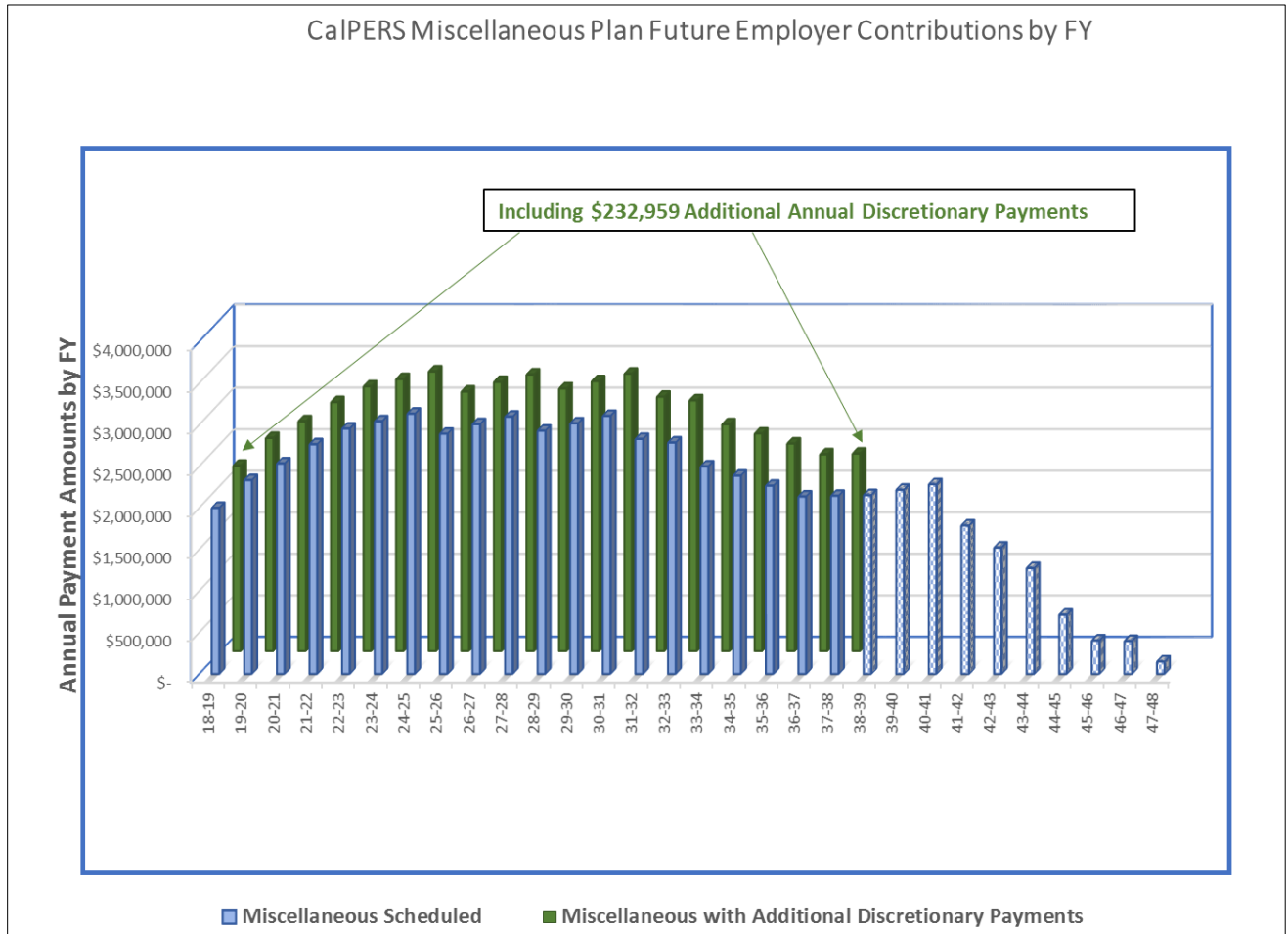
The current analysis indicates that ADPs in the amount of approximately \$235,000 for Miscellaneous and \$155,000 for Safety plans (totaling approximately \$390,000) would be required to emulate a 20-year amortization. These payments would be in addition to the existing annual required employer contributions under the current amortization schedule. The charts below present the increased annual payments with fixed ADPs above those currently scheduled to be made over an approximate 30-year period as scheduled in the latest CalPERS actuarial valuation report.

The first chart depicts the scheduled payments for the miscellaneous plan as detailed in the latest actuarial valuation alongside with the \$235K of ADPs made each year to accelerate the final payoff of the unfunded actuarial liability. In examining the total expenditures for the Miscellaneous plan, the payment schedules provided by CalPERS indicate a total savings of approximately \$8.2 million dollars if the Town maintains this annual ADP commitment.

SUBJECT: RECOMMEND TO THE TOWN COUNCIL A FUNDING POLICY FOR UNFUNDED PENSION AND OTHER POST RETIREMENT BENEFITS LIABILITIES

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DISCUSSION (Continued):

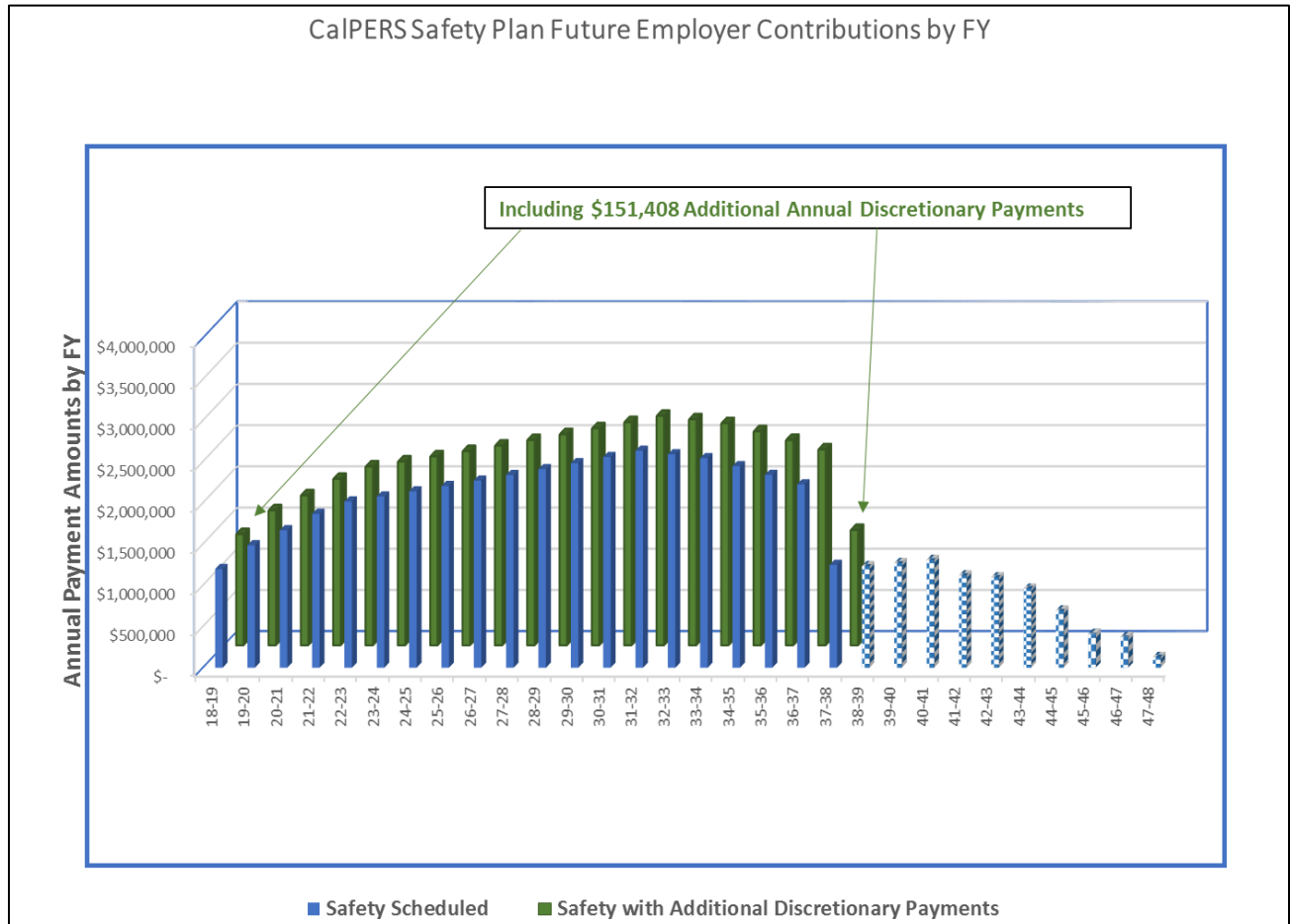


The following chart depicts the scheduled payments for the Safety plan as detailed in the latest actuarial valuation prepared by actuaries at CalPERS alongside with the \$155K of ADPs made each year to accelerate the final payoff of the unfunded actuarial liability. In examining the total cash outlays for the Miscellaneous plan, the schedules provided by CalPERS indicate a total savings in cash outlays of approximately \$5.6 million dollars if the Town maintains this annual ADP commitment.

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DISCUSSION (Continued):



As currently calculated, the expected total savings would be approximately \$13.8 million dollars for both plans if these ADPs are adopted versus the payments made under the current amortization schedule.

CONCLUSION:

The pension ADP analysis performed in conjunction with CalPERS indicates that 20-year amortization equivalence can be achieved through additional UAL payments of approximately \$400,000 per year. The total savings associated with the ADP methodology is approximately \$13.8 million versus the existing amortization schedules for both plans. The proposed UAL Funding Policy will ensure that the unfunded actuarial liability is reduced over a shorter time period and significant interest savings achieved.

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COORDINATION:

This report was coordinated with the Town Manager's Office, the Town Attorney's Office, and the Finance Department.

Attachment:

1. Proposed UAL Funding Policy.