Midpeninsula Regional
Open Space District

R-17-70
Meeting 17-14
June 14, 2017

AGENDA ITEM 2

AGENDA ITEM

Authorization to Reduce the District's Unfunded Pension Liability by Making a $1 Million Pre-Payment to the California Public Employees Retirement System (CalPERS)

GENERAL MANAGER'S RECOMMENDATION

Authorization to deposit $1 Million into the Midpeninsula Regional Open Space District's (District) CalPERS account to reduce the District's unfunded pension liability.

SUMMARY

In June 2016, the Board approved a $3 million prepayment to CalPERS in order to reduce the District's unfunded pension liability and achieve estimated savings of $6.3 million over twenty years ($3.3 million net savings). The District's general fund reserves are sufficient to allow a further prepayment this year, with proportionate estimated long-term savings, and the Controller and I recommend a $1 million prepayment.

DISCUSSION

In March 2017, the District received its CalPERS Annual Valuation Report as of June 30, 2015. As of June 2015, the District' CalPERS account had an actuarial liability of $51.0 Million and held assets with a market value of $40.0 Million. Hence, the District's unfunded liability was $11.0 Million, or a funded ratio of 78.4%. This was above average, as the average CalPERS funded ratio was 72.7%. Including the favorable impact of our $3 million prepayment in June 2016, the District's unfunded liability would have been $8.0 million, or an effective funded ratio of 84.3%.

CalPERS investment returns were again poor in fiscal 2016, reporting only a 0.6% return, below the weak 2.4% return in fiscal 2015, and well below the new target of 6.5%. Due to this investment performance, our funded ratio has clearly declined since June 2015, probably to under 80%. Importantly, these calculations assume future CalPERS investment returns of 7.5% per year. However, in November 2015, CalPERS announced a new de-risking policy, under which it will shift its asset allocation to less volatile investments and gradually reduce the assumed rate of return to 6.5% over twenty years. Depending on how fast this transition occurs, the District's current adjusted funded ratio may be under 75%. The consequence of this policy change and inadequate recent investment returns will be rapidly escalating CalPERS charges. Last year, our actuary projected that the District CalPERS charges would, without prepayments, increase approximately 6% per year for the next twenty years. Put another way, our CalPERS charges as a percent of payroll were projected to increase from 14.7% in FY2015-16 to 26.4% in FY2031-32.

The preferred method to mitigate the scale of these projected pension expense increases is to pay down the unfunded liability with pre-payments. CalPERS continues to encourage its clients to consider such pre-payments. According to actuarial analysis, last year's $3 Million pre-payment was projected to save $6.3 Million over twenty years, generating a 6.9% annual return on investment. This return is clearly much higher than the District could otherwise earn on its general fund cash. The Controller and I recommend another prepayment this year, in the amount of $1 million. At the new 6.5% target return, such a prepayment is expected to save approximately $2 million over the next twenty years. A $1 Million pre-payment would also increase the District's funded ratio by some 1.6 percentage points—a clear benefit to the employees.

BOARD COMMITTEE REVIEW

This item was not reviewed by any Committee.

FISCAL IMPACT

Based on last year's actuarial analysis, we estimate net savings in retirement plan payments of $18,000 in FY2017-18 and $2 Million over the next twenty years.

PUBLIC NOTICE

Public notice was provided pursuant to the Brown Act. No additional notice is required.

CEQA COMPLIANCE

The recommended action is not a project for purposes of the California Environmental Quality Act.

NEXT STEPS

Upon approval, transfer $1 million to CalPERS prior to the end of the Fiscal Year on June 30, 2017.

Prepared by:
Mike Foster, Controller