

City of Rancho Palos Verdes Pension Plan Guidelines

Overview

The Rancho Palos Verdes Pension Plan Guidelines provide a framework to enable the City to develop sound funding policies and provide Staff with direction to adequately and appropriately monitor the City's pension plans and obligations.

Purpose and Objectives

In accordance with the 2020-21 City Council Goals under "Government Efficiency and Transparency," the purpose of the pension guidelines is to proactively manage ongoing contributions to the City's pension plans and Unfunded Accrued Liabilities (UAL).

The Pension Plan Guidelines document the methods the City will use to determine its annual pension contributions. Annual pension contributions fund the long-term cost of benefits to the plan's participants and annuitants. Nothing within these guidelines shall constitute an obligation upon the City, nor an implied contract. The City Council, with recommendations from the City's Finance Advisory Committee (FAC), may revoke or amend the guidelines at any time when in the best interest of the City.

The objectives of the Pension Plan Guidelines are as follows:

- Provide guidance to decision-makers during the annual budget process,
- Demonstrate prudent financial management practices, and
- Promote fiscal transparency to the public and employees on how pensions will be funded.

Definitions

Defined Benefit Plan – a pension plan where retirement benefits are based on a formula.

The City has three benefit levels currently offered to eligible employees:

- Tier 1 – Employees hired prior to local pension reform action by City Council on September 20, 2011; earn 2.5% of salary for each year employed with the City (single highest year) at the age of 55. **The employee contribution rate for Tier 1 is 8.00% of their annual salary.**
- Tier 2 – Employees hired after local pension reform on September 20, 2011, who previously worked for another governmental agency with a reciprocating pension plan; earn 2% of salary for each year employed with the City (based on a three-year average) at the age of 60. **The employee contribution rate for Tier 2 is 7.00% of their annual salary.**
- Tier 3 (PEPRA) – Employees subject to the California Public Employees' Pension Reform Act of 2013 (PEPRA); who have not previously worked for another governmental agency with a reciprocating pension plan or have not worked for such an agency within six months of being hired by the City. These employees

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earn 2% of salary for each year employed with the City (based on a three-year average) at the age of 62. **The determination of PEPRA member contribution rates is based on 50% of the total normal cost rate from the AVR. Effective July 1, 2023, the Tier 3 rate is 6.75% of their annual salary.**

Full-time Employee – a competitive service employee that is regularly scheduled to work at least 40 hours a week.

Part-time Employee – an employee that is scheduled to work on an irregular basis not more than an average of 32 hours a week and worked at least 1,000 hours in a fiscal year (July 1 – June 30).

Actuarial Valuation Report (AVR) – an annual report prepared by CalPERS that contains actuarial information about City pension plans and determines the required contribution rates for the fiscal year beginning two years after the valuation date.

Normal Costs – the annual cost of service accrual expressed as a percentage of total active payroll and viewed as the long-term contribution rate.

Unfunded Accrued Liability (UAL) – an unfunded accrued liability, or UAL, is present when the Market Value of Assets for a pension plan is less than the plan's Accrued Liabilities. The UAL balance is amortized in accordance with CalPERS' amortization policy and included in the total minimum required employer contribution.

Market Value of Assets (MVA) – the value of a plan's assets in the open marketplace on a specific date.

Accrued Liability (AL) – the total dollars needed as of the valuation date to fund all benefits earned in the past for current members.

Amortization of UAL – a separate payment schedule for different portions of the Unfunded Liability. Payment periods are determined by Board policy and vary based on the cause of the change.

Schedule of Amortization Bases – gain or loss bases are the plan's allocated share of the risk pool's experience and assumption change. Positive or negative bases result from a plan's experience or change that either increases or decreases the UAL balance and are amortized in accordance with the CalPERS amortization policy.

Background

The City of Rancho Palos Verdes provides its employees a defined benefit retirement plan through the California Public Employees' Retirement System (CalPERS) per a City Council-approved contract dated December 1, 1974. CalPERS is a multiple-employer public employee defined benefit pension plan.

All full-time and part-time employees, if they worked more than 1,000 hours per fiscal year, are eligible to participate in CalPERS. CalPERS provides retirement, disability, and death benefits and annual cost of living adjustments to plan members and their

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beneficiaries. CalPERS acts as a common investment and administrative agent for participating public entities with the State of California. Benefit provisions and all other requirements are established by state statute.

The financial objective of a defined benefit pension plan is to fund the long-term cost of benefits provided to the plan members. To assure that the plan is financially sustainable, the plan should accumulate adequate resources in a systematic and disciplined manner over the active service life of benefitting employees. This funding guideline outlines the method the City will utilize to determine its Actuarially Determined Contributions to fund the long-term cost of benefits to the plan members and annuitants.

Pension Funding: A Guide for Elected Officials, issued by eleven national groups including the U.S. Conference of Mayors, the International Agency/County Management Association, and the Government Finance Officers Association, established the following five general policy objectives for a pension funding policy:

- Actuarially Determined Contributions - a pension funding plan should be based upon an actuarially determined contribution (ADC) that incorporates both the cost of benefits in the current year and the amortization of the plan's unfunded actuarial accrued liability.
- Fund Discipline - a commitment to make timely, actuarially determined contributions to the retirement system is needed to ensure that sufficient assets are available for all current and future retirees.
- Intergenerational equity - annual contributions should be reasonably related to the expected and actual cost of each year of service so that the cost of employee benefits is paid by the generation of taxpayers who receives from those employees.
- Contributions as a stable percentage of payroll - contributions should be managed so that employer costs remain consistent as a percentage of payroll over time.
- Accountability and transparency - clear reporting of pension funding should include an assessment of whether, how, and when the plan sponsor will ensure sufficient assets are available for all current and future retirees.

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Guidelines

A. Goals

1. To stabilize annual contributions and mitigate long-term impacts from the City's UAL. Required contribution rates are determined by CalPERS and reported in the actuarial valuation report for each pension plan.
2. To achieve and maintain a 90% funding level for City pension plans over the next seven to ten years ending in FY 2030-31. A plan's funded status is determined by CalPERS and reported in the actuarial valuation report.

B. Actuarial Determination of Plan Cost

The actuarial determination of plan contributions are prepared by CalPERS and include the normal cost for current service and amortization of the UAL. Both components are calculated based on a set of actuarial assumptions approved and reviewed by the CalPERS Board of Administration. This set of assumptions can be categorized as demographic assumptions and economic assumptions.

- Total minimum required employer contributions will be paid in accordance with the actuarial determination of plan costs. Additionally, the City will review actuarial valuations annually to assess changes since the prior year's valuation and actuarial methods and assumptions.

C. Employee Pension Plan Service Fund

To address the increasing annual payment of the UAL, the City may set aside funding in an Employee's Pension Plan Service Fund, as an Internal Service Fund, to relieve the General Fund of payments exceeding \$900,000.

1. Employee Pension Plan Service Fund Contribution Options:

- Initial contribution - the City may consider an initial contribution equivalent to at least two years but no more than three years of the incremental increases to the annual UAL payment from the General Fund Unrestricted Excess Reserve to the Employee Pension Plan Service Fund.
- Annual contributions - the City may consider, on an annual basis, to contribute at least 10% but no more than 25% of the annual General Fund surplus (revenues minus expenditures, including transfers) to the Employee Pension Plan Service Fund.
 - The surplus is to be calculated after closing the fiscal year and will be included in the staff report to the City Council during the budget meetings.

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2. Employee Pension Plan Service Fund Usage Options:

- The City may use the accumulated funds in the fund to stabilize contributions to CalPERS when the annual UAL lump-sum payment exceeds \$900,000 rather than utilizing the General Fund.

D. Additional Discretionary Payments (ADPs)

To stabilize contributions and mitigate long-term impacts from the UAL, the City can elect to make ADPs at any time and in any amount to reduce the UAL. Additional contributions may be considered either on an ad hoc basis or in accordance with an internal funding plan during the annual budget process. ADPs are nonobligatory and do not commit the City to any additional payment schedules.

1. ADP Usage Options:

- Ad hoc basis – ADPs can increase a plan's funded status, stabilize future contributions, and reduce long-term debt. As a supplement to minimum required contributions, the City may consider making an ADP at any time and in any amount.
- Internal funding plan– the City Council, with recommendations from the FAC, may adopt an internal funding plan to proactively manage the City's UAL. Given this occurrence, ADPs will be considered during the annual budget process in accordance with the funding strategy or as determined by the City Council.

E. Section 115 Pension Trust Contribution

To address the City's rising UAL, the City Council may consider establishing a Section 115 Trust to pre-fund pension obligations. The objective of the Section 115 Pension Trust is to achieve and maintain the 90% funding level for City pension plans over the next seven to ten years ending in FY 2030-31.

115 Trust Contribution Options:

- Initial contribution - the City may consider an initial contribution of at least \$500,000 but no more than 25% of the General Fund Unrestricted Excess Reserve to the 115 Pension Trust.
- Annual contributions - the City may consider, on an annual basis, contributing equivalent to the savings from making a lump-sum payment of the UAL or the annual positive variances between the projected year-end revenues and the actual revenues in the General Fund, whichever is more, to the 115 Pension Trust.

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- The variance is to be calculated after closing of the fiscal year and will be included in the staff report to the City Council.

115 Trust Usage Options:

The City shall maintain the balance in the Section 115 Trust to achieve the 90% funded level, unless:

- The Employee Pension Plan Service Fund does not have sufficient funding to cover the excess of \$900,000 in the annual lump-sum payment. The City may use the accumulated funds from the Section 115 Trust to stabilize the annual UAL contributions to CalPERS.
- The General Fund experience a loss in revenue of 10% or more. The City may use accumulated funds from the Section 115 Trust to make ADC contributions.

F. Transparency and Reporting

The City's pension plans should be transparent to vested parties, including plan members, annuitants, the City Council, and the Rancho Palos Verdes residents. To promote transparency, the following information shall be made available:

- An annual actuarial valuation will be presented to the City Council within 60 days but no later than 90 days after its release by CalPERS.
- The City's Annual Comprehensive Financial Report (ACFR) shall be published on the website. This report includes information on the City's annual contributions to the pension systems and funding status.
- The City's operating budget shall include the contributions to CalPERS.
- The City's annual contribution, usage, and balance of the Employee Pension Plan Service Fund and 115 Pension Trust (if established) shall be included in the year-end financial report to the City Council.
- The City's Pension Plan Guidelines and actuarial valuation reports shall be published on the City website.

G. Review of Funding Guidelines

Funding a defined benefit pension plan requires a long-term horizon. As such, the City will review the guidelines every three years or as needed to determine if changes are warranted and to ensure adequate resources are being accumulated.