



# **CITY COUNCIL AGENDA REPORT**

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MEETING DATE: February 4, 2014

ITEM NUMBER:

SUBJECT: PENSION COST REDUCTION RECOMMENDATIONS—FIRST STEPS

DATE: JANUARY 24, 2014

FROM: FINANCE DEPARTMENT

PRESENTATION BY: STEPHEN DUNIVENT, INTERIM FINANCE DIRECTOR

FOR FURTHER INFORMATION CONTACT: STEPHEN DUNIVENT, INTERIM FINANCE DIRECTOR,  
(714) 754-5243

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## **RECOMMENDED ACTION:**

1. With respect to the Pension Oversight Committee
  - a. Receive and file the Pension Oversight Committee Report
  - b. Approve the distribution of the Committee Facts Volumes 1, 2 and 3.
  - c. Provide direction regarding the Committee's future activities
2. Authorize the lump-sum prepayment of the City's annual required contribution for the Miscellaneous and Police Retirement Plans beginning in July 2014.
3. Authorize the use of the City's annual savings from the lump-sum prepayment of the Miscellaneous and Police Retirement Plans to make additional payments to the Fire Side Fund beginning in July 2014 with the goal of paying off this fund early.
4. Authorize the Finance Director, with the concurrence of the City CEO, to annually review recommended actions two and three and implement or suspend them each fiscal year as appropriate to the City's financial condition at the time.
5. Authorize a one-time additional \$1,000,000 payment to the Fire Side Fund this fiscal year using funds that were budgeted in FY 2012-13 and FY 2013-14.
6. Provide direction on continuing the practice of budgeting an additional \$500,000 per year for the purpose of paying down unfunded pension liabilities.

## **BACKGROUND:**

Retirement plans for City employees are administered by the California Public Employees' Retirement System (CalPERS or PERS). The City's current annual cost for retirement benefits is \$18,006,842 or nearly 17.5% of the City's General Fund budget. (Attachment A) As of June 30, 2012, the Unfunded Actuarial Accrued Liability (unfunded liability) for the City's three retirement plans combined is \$228 million. (Attachment B) The City wants to find ways to reduce both the annual retirement cost and the unfunded liability of these retirement plans.

As part of the last two budget cycles, the City set aside a total of \$1,000,000 for the purpose of reducing the unfunded pension liabilities.

The City Council established a Pension Oversight Committee in February 2013. Its mission is to review pension and pension financial matters and to evaluate and advise

the Council on pension issues. Attachment C is the committee's first report on its work and accomplishments. The committee drafted initial recommendations that range from actions that can be taken now, issues that need further analysis and items that are part of the labor negotiation process or would require legislative changes.

This staff report outlines actions that can be taken now as first steps with existing resources to reduce the City's annual pension cost and unfunded liability. The recommendations in this report were reviewed by the Pension Oversight Committee on January 8, 2014. A majority of the members support the recommendations in this agenda report.

### **ANALYSIS:**

Annual Pension Contribution Lump-sum Prepayment: The City traditionally pays its annual required contribution to PERS on a bi-weekly basis as part of the payroll process. PERS offers a lump-sum prepayment option that allows employers to prepay the entire annual contribution at a discounted amount. The discount is approximately 3.5% of the total annual contribution in consideration that the funds will be invested with PERS for a longer period of time. This discount compares favorably to the composite interest rate of less than 0.5% currently earned on cash and investments held by the City. The lump-sum prepayment is required after June 30 and before the first payroll of the new fiscal year. The lump-sum prepayment amounts and savings for each retirement plan are shown on Attachment B. The lump-sum prepayments would save \$226,551 on the Miscellaneous Employee Plan, \$263,225 on Police employee Plan, and \$177,176 on Fire employee Plan. Staff recommends prepaying only the Miscellaneous and Police Plans at this time due to the cash flow impact and because the Fire employees are in a pooled plan with safety employees of other employers. The total lump-sum prepayment for the two groups is \$13,301,139. The combined gross savings from the lump-sum prepayment for the Miscellaneous and Police Plans is \$489,776 less the lost interest income of \$33,253 for a net annual savings of \$456,523.

Cash Flow Analysis: The lump-sum prepayment of the Miscellaneous and Police Plans will require \$13,301,139 in cash (plus the regular Fire Plan bi-weekly payment) in early July. Cash investments will be managed to provide for this payment. Cash flow projections (Attachment D) are based on the current fiscal year actual/projected revenues (with modest increases of \$1 million each in property taxes and sales tax for next fiscal year) and expenses overlaid with next fiscal year retirement costs and the lump sum prepayment. The cash flow model also assumes the rescheduling of the General Fund lump sum contribution to the Capital Improvement Program Fund to December. With the lump-sum prepayment, the General Fund cash balance would temporarily dip to a low point of \$15,041,249, staying above the reserve threshold of \$14,125,000. The cash balance would be restored over the fiscal year as the City's bi-weekly payments to PERS for the two groups would not be required.

Fire Side Fund: At the time the City retirement plan for Fire employees was placed into PERS, there were fewer than 100 City Fire employees. Therefore the employees were placed in the general PERS Fire safety pool. The funded status of the City's Fire Plan was less than that of the general PERS Fire safety pool therefore PERS required that a

City Fire Side Fund be created to account for the difference in funding. The difference in the funding status was valued at \$22,690,635 on June 30, 2010. (Attachment E) The current balance of the Side Fund as of June 30, 2013 has grown to \$24,941,538 due to payroll variances and the offering of retirement incentives in 2010 and 2011. The annual payment of the side fund is 17.741% of payroll or \$1,826,662 estimated for this fiscal year. PERS charges the city an annual interest rate of 7.5% on this fund. Under the current payment plan, the fund will be paid off in 20 years.

This fund is a good candidate for early payment for several reasons. First, the balance is small enough in comparison to the other unfunded liability amounts to be paid off early in a reasonable amount of time and in amounts that the City can currently afford. Second, early payoff will save the city 7.5% in interest cost on the unpaid balance. Finally, when the fund is paid off, the employer contribution rates for Fire employees will be reduced by the 17.741% yielding a 38% reduction in the City's retirement cost for these employees.

An additional payment of \$1,000,000 can be made to the Fire Side Fund this fiscal year using funds already set aside for the purpose of pension liability reduction. If this were the only additional payment, all other assumptions being equal, the Fire side fund would be paid off two years early saving over \$4 million. (Attachment E, Projection 1)

Staff recommends investing the \$489,776 gross savings from the annual lump-sum prepayment of the Miscellaneous and Police Plans in July 2014 as an additional annual payment to the Fire Side Fund. If this is done on an annual basis, combined with the one-time \$1,000,000 payment, the Fire side fund would be paid off seven years early saving nearly \$12 million. (Attachment E, Projection 3) Attachment F illustrates the impact of additional payments to the Fire Side Fund.

Self-Sustaining Plan: The recommendations above are designed to create a self-sustaining retirement cost reduction plan. Savings from annual lump-sum prepayment of the Miscellaneous and Police Plans can be dedicated toward paying down the unfunded liability of the Fire side fund. In the future, when the Fire side fund is paid off, savings could be directed to paying down the remaining unfunded liabilities in the Miscellaneous and Police Plans. The City could also free up the budgeted amount of \$500,000 per year that has been set aside for this purpose and redirect it for other needs of the City such as the rebuilding of reserves.

#### **ALTERNATIVES:**

The Council has several alternatives to the staff recommendations. Regarding the annual contribution lump-sum prepayment, none, one or all three of the plans could be prepaid. Two plans are recommended for lump-sum prepayment at this time due to the cash flow impacts and the fact that Fire employees are in a pooled fund. The annual savings from lump-sum prepayment could be directed elsewhere but this would hinder progress toward the goal of further reducing pension unfunded liabilities and cost.


The \$1,000,000 already set aside could be reserved for future use or directed toward liabilities other than the Fire side fund. The recommended use of the \$1,000,000 for

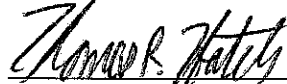
the Fire side fund represents a significant step toward reducing the unfunded liability and the associated 7.5% interest cost in that fund.

The annual appropriation of \$500,000 per year for reduction of pension liabilities could be continued. This would make the funds unavailable for other City purposes such as rebuilding reserves.

**CONCLUSION:**

Gross annual savings of \$489,776 (\$456,523 net) can be achieved by prepaying the annual contribution for the Miscellaneous and Police Plans. Using the gross savings plus the \$1,000,000 budgeted in the last two years to make additional payments to the Fire Side Fund can completely pay down the liability of this fund seven years early saving over \$12 million. The recommended plan is self-sustaining by using savings from the lump-sum prepayment to pay down the Fire Side Fund. This plan could also free up \$500,000 in the City budget for other purposes.

  
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Stephen Dunivent  
Interim Finance Director

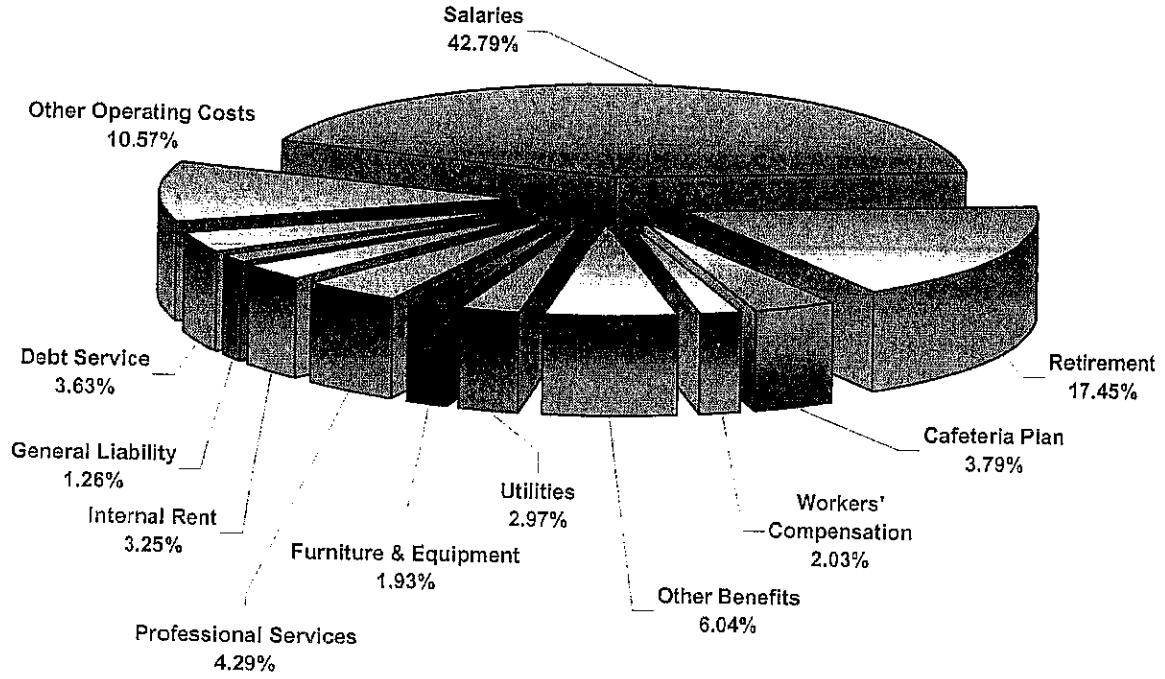
  
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Thomas R. Hatch  
City CEO

- Attachments:
- A. FY 2013-14 City Budget Chart—General Fund Appropriations
  - B. CalPERS Actuarial Valuation Summary Information
  - C. Pension Oversight Committee Initial Report
  - D. General Fund Cash Flow Projection
  - E. Fire Side Fund Projections
  - F. Fire Side Fund Graph

# GENERAL FUND RESOURCES & APPROPRIATIONS

## FISCAL YEAR 2013-2014

GENERAL FUND APPROPRIATIONS - TOTAL \$103,191,271



Attachment B

CalPERS Actuarial Valuation

City of Costa Mesa  
 As of June 30, 2012  
 For FY 2014-15 rates  
 Summary of Information

<u>Investment Return:</u>	Misc.	Police	Fire	Total
FY 2011 - 2012				0.1%
FY 2012 - 2013				12.5%
YTD 2013 - 2014				16.2% as of 12/31/13

Plan's Funded Status

Entry Age Normal Accrued Liability	\$ 225,186,488	\$ 212,645,063	\$ 161,328,098	\$ 599,159,649
Market Value of Assets (MVA)	\$ 141,225,952	\$ 129,017,818	\$ 100,677,450	\$ 370,921,220
Unfunded Liability (MVA Basis)	\$ 83,960,536	\$ 83,627,245	\$ 60,650,648	\$ 228,238,429
Funded Ratio (MVA Basis)	62.7%	60.7%	62.4%	61.9%

Employer Contribution Rates

FY 2010 - 2011	14.613%	30.145%	25.968%
FY 2011 - 2012	19.052%	34.063%	26.242%
FY 2012 - 2013	21.803%	36.286%	37.404%
FY 2013 - 2014	27.383%	38.542%	45.618%
FY 2014 - 2015	29.783%	41.456%	47.452%
FY 2015 - 2016	31.500%	43.300%	49.500%

Prepayment Option

Projected Contribution	\$ 6,379,126	\$ 7,411,789	\$ 4,988,842	\$ 18,779,757
Prepayment Amount	\$ 6,152,575	\$ 7,148,564	\$ 4,811,666	\$ 18,112,805
Prepayment Savings	\$ 226,551	\$ 263,225	\$ 177,176	\$ 666,952

Fire Side Fund

Valuation	\$ 24,803,797
Payment	\$ 1,661,369

FY 2014-15  
 rate = 17.896% of payroll  
 included in Fire rates above

Members

Active	270	133	78	481
Transferred	273	32	10	315
Separated	307	30	5	342
Retired	403	144	114	661

# Costa Mesa Pension Oversight Committee

## Report to the Costa Mesa Community & City Council

January 21, 2014

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### Costa Mesa Pension Oversight Committee

#### Voting Members

Jeff Arthur – Chairman • Ralph Taboada – Vice Chairman • Gene Hutchins, Member  
Rick Kapko, Member • Kent Mora, Member • Gary Parkin, Member  
Ron Robertson, Member • Tim Sesler, Member • John Stephens, Member

**Costa Mesa Pension Oversight Committee**  
**<http://www.costamesaca.gov/index.aspx?page=1603>**  
**Report to the Costa Mesa Community & City Council**  
**January 21, 2014**

## **Introduction**

Meeting for the first time in May of 2013, the Costa Mesa Pension Oversight Committee (POC) has worked diligently to comprehend the complexities of Costa Mesa's three employee pension plans, Police, Fire, and Miscellaneous. All plans are administered by CalPERS, the California Public Employees Retirement System, and are influenced by multiple layers of regulations and actuarial assumptions.

The POC is a non-partisan group of nine unpaid volunteers who are Costa Mesa residents. Coming from various business and professional backgrounds, current members with voting rights include Messrs. Jeff Arthur, Gene Hutchins, Rick Kapko, Kent Mora, Gary Parkin, Ron Robertson, Timothy Sesler, John Stephens and Ralph Taboada. POC activities are supported by city staff members including Interim Finance Director Steve Dunivent, Human Resources Director Lance Nakamoto, and Human Resources Analyst Ryan Thomas. City Council liaisons include Mayor Jim Righeimer and Mayor's Designee, Mayor Pro Tem Stephen Mensinger.

You may communicate with the POC by attending our meetings which are open to the public. Committee meetings are scheduled on the first and third Wednesday of each month, at 4:30 p.m., in City Hall conference room 1-A.

In our attempt to present an unbiased, non-partisan analysis of the plans and their effects on all stakeholders, the answers to many questions simply lead to additional questions. This report is intended to share POC findings to date and provide a foundation for further dialogue between city decision makers, city employees, and the citizens of Costa Mesa.

## **PART I**

### **POC Activities to Date**

Initial activities included study and analysis of the following:

- Comprehensive review of all three plans including pension formulas, historical changes in pension formulas, retiree medical benefits, and supplemental benefits.
- Study of legal and accounting environments related to CalPERS, Federal and state laws affecting pensions, and Costa Mesa budgets.
- Review of current events including municipal bankruptcies and national efforts related to pension reform.
- Research and analysis of possible courses of action (which will be reviewed in-depth later in this report).



## PART II

### Understanding Public Pensions

#### ***CalPERS – California Public Employees Retirement System***

Costa Mesa contracts with CalPERS to administer pensions for city employees. CalPERS administers pensions for over 1.6 million active employees and retirees including state, county, and municipal employees as well as public school and state university employees.

Each year, CalPERS sets the pension contribution rates that the city will pay to fund employee pensions for that year. In addition to setting the contribution rates, CalPERS administrative duties include investing the pension contributions, managing those investments, and issuing pension checks to retirees.

While CalPERS sets the contribution rates, manages the investments, and serves as the administrator of the plans, they have no obligation for any financial shortfall that occurs if their contribution rates or investment performance fails to reach their own projections. The responsibility for correcting any financial shortfall is the sole responsibility of the agencies that offer pensions to their employees. In the case of our Costa Mesa pensions, the ultimate responsibility for the payment of these guaranteed pension benefits is exclusively that of the city and taxpayers of Costa Mesa, not CalPERS.

#### ***Pension Formulas***

The key to understanding the structure of public pensions starts with the pension formula. Simply stated, public pension formulas are defined as a percentage of salary, per year of service, payable at a minimum retirement age. In the case of the majority of Costa Mesa Police officers, the pension formula is 3% at 50. An example of this would be a 50 year old officer, who has worked for the city for 25 years. This officer may retire with a first year pension benefit of 75% (3% times 25 years of service) of his single highest year of pensionable salary. Pensionable salary excludes certain compensation such as overtime and accrued sick pay, but does include compensation beyond base salary such as uniform allowance and premiums paid for advanced training.

In the example cited above, if the officer retired at age 50, with only 23 years of service, the first year pension benefit would be 69% (3% times 23 years of service) of the single highest year of pensionable salary. Similarly, if the officer worked five years beyond the minimum retirement age of 50, to 55 years old, and by that time accumulated 30 years of service, the first year pension benefit would be 90% (30 years times 3%) of the single highest year of pensionable salary. By plan design, maximum first year pension benefits may not exceed 90% of pensionable compensation and employees who retire before the minimum retirement age stated in the pension formula receive discounted first year pension benefits.

As mentioned, Costa Mesa has three retirement groups, Safety Police ("on the street" police officers and management), Safety Fire ("on the street" fire personnel and management), and Miscellaneous employees (all other city employees, managers, and police and fire administrative employees). The following table presents the various pension formulas currently in effect for each group:

Costa Mesa Retirement Formulas July 1, 2013	
"Classic" Employees	
Employee Group	Benefit Formula
Miscellaneous - Non Management	2.5% @ 55
Miscellaneous - Management	2.5% @ 55
Miscellaneous FT - 2nd Tier*	2% @ 60
Police - Sworn Officers	3% @ 50
Chief of Police	3% @ 50
Fire & Fire Management	3% @ 50
Fire & Fire Management - 2nd Tier**	2% @ 50
* Full time employees hired after 3/11/12	
** Full time employees hired after 12/30/12	
"New" Employees (hired on or after 1/1/13 - subject to PEPR)	
Miscellaneous - 3rd Tier	2% @ 62
Police - Sworn Officers - 2nd Tier	2.7% @ 57
Fire - 3rd Tier	2.7% @ 57
For clarity, table does not include part-time employees	

**Pension Contribution Rates and Cost Sharing**

CalPERS annually assigns pension contribution rates for each employee group based upon the pension formula. The contribution rate assigned by CalPERS is expressed as a percentage of total pensionable salary.

Contribution rates consist of two components, "Normal" costs and "Unfunded" costs. Normal cost is the anticipated cost to fund the pension benefit for those currently employed. Unfunded cost is the amount that is required to make up for past investment performance below expectation or to fund enhanced retirement benefits that were not fully funded by prior normal cost contributions.

Cost sharing is determined by collective bargaining with each employee group. In cost sharing, the employees pay a percentage of their salary towards their pension benefit and the city pays the remainder. The following table illustrates the current total pension contribution rate and the cost sharing allocation for each employee group.

Costa Mesa CalPERS Contribution Rates & Cost Sharing					
July 1, 2013					
"Classic" Employees					
Employee Group	Contribution Rate as % of Pensionable Salary				
	Total Contribution Rate	Employee Contribution Rate	City Contribution Rate	% of Total Rate Paid by Employee	% of Total Rate paid by City
Miscellaneous - Non Management	35.383%	8.520%	26.863%	24.079%	75.921%
Miscellaneous – Management	35.383%	10.469%	24.914%	29.588%	70.412%
Miscellaneous FT - 2nd Tier*	34.383%	8.000%	26.383%	23.267%	76.733%
Police - Sworn Officers	47.542%	5.000%	42.542%	10.517%	89.483%
Chief of Police	47.542%	9.000%	38.542%	18.931%	81.069%
Fire & Fire Management	54.618%	5.000%	49.618%	9.154%	90.846%
Fire & Fire Management - 2nd Tier**	28.900%	9.000%	19.900%	31.142%	68.858%
* Full time employees hired after 3/11/12					
** Full time employees hired after 12/30/12					
"New" Employees (hired on or after 1/1/13 - subject to PEPR)					
Miscellaneous - 3rd Tier	34.133%	7.750%	26.383%	22.705%	77.295%
Police - Sworn Officers - 2nd Tier	51.292%	12.750%	38.542%	24.858%	75.142%
Fire - 3rd Tier	23.000%	11.500%	11.500%	50.000%	50.000%
For clarity, table does not include part-time employees					

In the tables presented, there are formulas and rates for "Classic" and "New" employees. These designations were created with the enactment of PEPR, the Public Employees' Pension Reform Act. "Classic" employees include those hired prior to January 1, 2013, and any employees hired on or after January 1, 2013 who previously accrued CalPERS retirement benefits with another CalPERS participating city or agency (example: a policeman from another city who transfers to Costa Mesa). "New" employees include employees hired on or after January 1, 2103 with no prior employment with a CalPERS city or agency.

#### PEPRA – The Public Employees' Pension Reform Act

In response to widespread concerns regarding the health and viability of California public employee pensions, the state legislature passed the Public Employees' Pension Reform Act ("PEPRA") in 2012. Most of its provisions went into effect on January 1, 2013 and following are some highlights from the legislation:

- **Reductions in Benefit Formulas** - reduced benefits for new employees, but does not change benefit formulas for existing employees.
- **Reduced Benefits Formulas For Miscellaneous Employees** – under PEPRA, the maximum benefit formula for "New" Miscellaneous employees has been reduced to 2% @ 62, rather than the existing 2.5% @ 55 for "Classic" Costa Mesa Miscellaneous employees.
- **Reduced Benefits Formulas for Safety Employees** – the maximum pension formula for "New" Police and Fire employees is 2.7% @ 57 as compared to the existing 3% @ 50 for "Classic" Costa Mesa Police and Fire employees.
- **Cost Sharing of Normal Cost**- PEPRA provides that the standard for cost sharing of normal costs should be employers and employees paying an equal share. It does however limit cost sharing by placing caps

on employee contributions; Miscellaneous employees may not pay in excess of 8% of pensionable compensation and Police and Fire employees may not pay in excess of 12% of pensionable compensation.

- **Three Year Average of Compensation** – when calculating the first year pension benefit, the single highest year of pensionable compensation shall not be used for “New” employees. Rather, the benefit shall be based upon the average of the highest three years of pensionable compensation.
- **Cap on Pensionable Compensation** - for “New” employees, in addition to reduced benefit formulas and limiting pensionable compensation to the 3-year average, PEPRAs sets a cap on pensionable compensation. The cap for “New” employees equates to 120 percent of the value of the Social Security wage index limit – approximately \$136,000. The amount of the cap is increased each year to reflect changes in the Consumer Price Index.

PEPRA was designed to address a wide range of issues involving public employee pensions. However, since PEPRA’s new benefit formulas apply mainly to employees hired after January 1, 2013, they will not provide material short-term savings. Various aspects of PEPRA should result in savings in the long run as new employees are hired and ultimately retire.

### PART III

## Summary of Major POC Findings

Following is a summary of major POC findings to date. The majority of these matters were discussed in open forum with CalPERS Senior Pension Actuary Kerry Worgan on November 20, 2013. A video recording of the complete meeting with Mr. Worgan may be accessed online on the Costa Mesa website at the following link: [http://costamesa.granicus.com/MediaPlayer.php?view\\_id=10&clip\\_id=2260](http://costamesa.granicus.com/MediaPlayer.php?view_id=10&clip_id=2260).

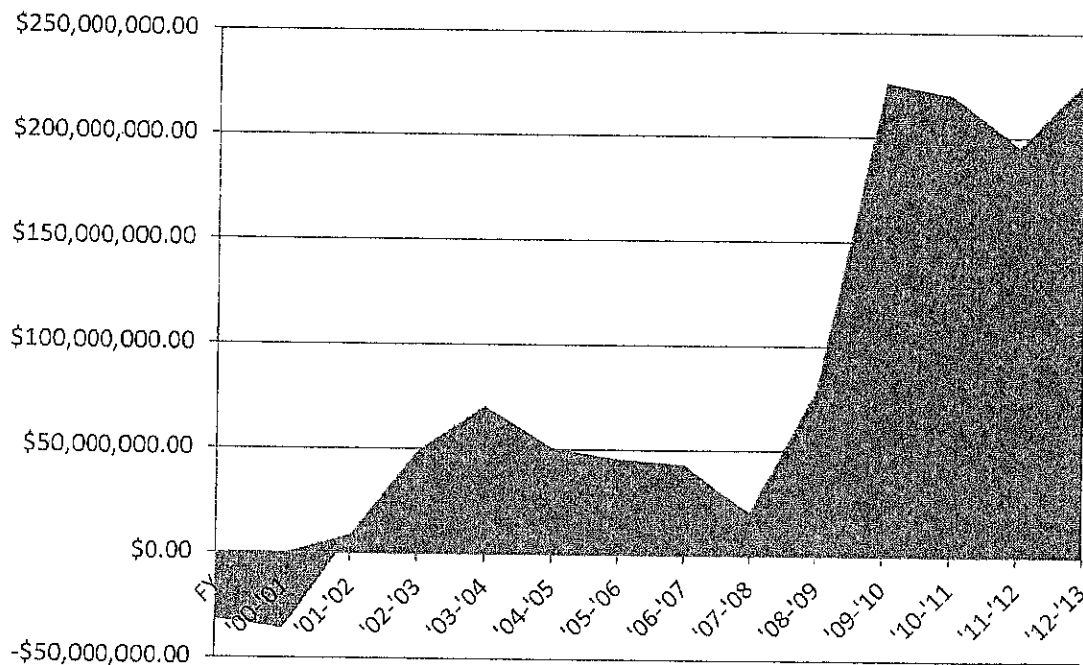
#### ***Costa Mesa Unfunded Liabilities***

The greatest threat to our pension plans and city finances is the accumulation of unfunded liabilities. Unfunded liabilities occur when the amounts invested to pay current and future retirement benefits are insufficient to make those payments.

In sum, the three Costa Mesa retirement plans are currently underfunded by approximately \$228 million (Police \$83 million, Fire \$61 million, Miscellaneous \$84 million). Simply stated, the current level of Costa Mesa unfunded liabilities is more than twice the total city General Fund budget for the 2013-2014 fiscal year.

The following graph illustrates the growth in Costa Mesa's unfunded obligations over the past 14 years:

Costa Mesa Unfunded Pension Liabilities FY2002-2015



As demonstrated in the graph, in the past 12 years, unfunded liabilities have increased from approximately \$9 million to the current \$228 million.

#### ***Reasons for Growth in Unfunded Liabilities***

POC has identified numerous drivers for the increase in unfunded liabilities including:

- CalPERS investment returns
- Increased pension benefits granted to employees, including retroactive increases

- Salary growth and COLA's (Cost of Living Adjustments)
- Changes in CalPERS actuarial assumptions

**CalPERS Investment Returns**

Mr. Worgan suggests that the most significant factor relating to the growth in unfunded liabilities is CalPERS investment performance. Using a constant discount rate of 7.5%, CalPERS projects that over the long-term, their investments will earn a positive return on investment of 7.5% annually. The investment losses of 2008 and 2009 negatively and severely influence current unfunded liabilities. While POC recognizes the effects of the recession and the '08 and '09 losses, it is important to also recognize that Costa Mesa unfunded liabilities were already of material concern prior to 2008. In fact, our unfunded liabilities were worrisome in the period 2004 through 2007 when the average CalPERS return on investment was nearly 15% annually.

The use of the 7.5% return on investment (ROI) assumption is highly debated. While numerous public pension systems currently use similar rates, private pensions are required by Federal regulation to use more conservative assumptions, typically ranging from 3.5% to 5.5%. While CalPERS defends the use of the current ROI assumption, critics of CalPERS contend that the use of the higher ROI assumption understates true pension costs.

In 2003, CalPERS reduced the ROI assumption from 8.25% to 7.75%. Subsequently in 2011, CalPERS again reduced the assumption to the current 7.5%. However, further reductions have been resisted by the CalPERS Board of Directors. It is important to recognize that each decrease in the ROI assumption requires member agencies to make increased payments to the pension fund.

The impact of the discount rate/ROI assumption is clearly illustrated in the table that follows. This table provides a cash flow analysis of the Police pension plan for fiscal year 2011-2012. During that year, the discount rate assumed positive investment income of 7.5%. However, CalPERS investment performance in the year was a slight loss of 0.2%.

The cumulative result for this period was negative cash flow, where benefit payments from the fund exceeded fund income by nearly \$2 million. During that same period, unfunded liabilities related specifically to the Police retirement fund increased over \$10,000,000.

<b>Costa Mesa Police Fund Cash Flow FY 2011-2012</b>	
<b>Fund Opening Balance MVA</b>	131,227,456
Investment Income & Refunds	(339,187)
Employer & Employee Contributions	7,525,278
Transfers Net of Receivables	(304,131)
Benefits Paid to Retirees	<u>(9,091,598)</u>
<b>Fund Closing Balance MVA</b>	<b>129,017,818</b>
<b>Negative Fund Cash Flow</b>	<b>(2,209,638)</b>
Unfunded Police Liabilities - Beginning of FY	73,503,949
Unfunded Police Liabilities - End of FY	<u>83,627,245</u>
<b>FY Increase in Police Unfunded Liabilities</b>	<b>10,123,296</b>

### ***Increased Pension Benefits***

Through collective bargaining, pension benefits have increased in two manners; enhanced benefit formulas and retroactive benefit increases. In 2008, the enhanced benefit formula for Miscellaneous employees increased their pension benefits by 25%, with only part of this increase paid by cost sharing. In 2010, Fire employees negotiated an enhanced benefit formula that reduced their eligible retirement age from 55 to 50 years old.

In granting retroactive benefit increases, employees received the negotiated benefit increases not only for their future years of service, but retroactively for all prior years of service that had originally been contracted at a lower benefit level.

When the city negotiated the retroactive increases, it relied in part, on the projections of city staff and CalPERS. These projections indicated that the cost of the increased benefits would be largely offset by departmental operating savings. In retrospect, the city may have misjudged the projected cost savings and the volatility of the CalPERS system. The ultimate result of the action was granting future benefits without creating adequate savings to pay for them.

Impacts of these increases, combined with salary increases and inflation, have led to significant increases in pension benefits. The table below illustrates that the average first year pension benefit for new retirees has increased 63% in the last 10 years. It further illustrates the growth in the number of retirees receiving first year pension benefits exceeding \$100,000.

<b>Average First Year Pensions - All Classifications</b>				
<b>Year</b>	<b>Retirees</b>	<b>Weighted Average First Year Pension</b>	<b>Number of Retirees with Pensions Exceeding \$100,000 in First Year</b>	<b>% of Retiring Employees with \$100,000 First Year Pensions</b>
2012	22	\$ 83,539	8	36.4%
2011	17	\$ 76,877	4	23.5%
2010	27	\$ 84,471	14	51.9%
2009	57	\$ 72,425	14	24.6%
2008	18	\$ 65,045	3	16.7%
2007	21	\$ 75,397	5	23.8%
2006	18	\$ 69,321	5	27.8%
2005	30	\$ 53,947	3	10.0%
2004	21	\$ 46,321	2	9.5%
2003	24	\$ 51,320	1	4.2%

Most recipients of \$100,000 pensions are high ranking management staff, Police and Fire employees. However, the increased number of retirees receiving such pension payouts is significant. In the three years 2003-2005, the city experienced 75 full-time retirements and 8% of those retirees received such benefits. In the three years 2010-2012, 39% of all city full-time retirees received first year benefits exceeding \$100,000.

As employees have retired, and continue to retire at these higher benefit levels, the time has come to pay the pensions. Based upon our unfunded liabilities, the funds to make these payments is insufficient.

### ***Salary Growth and COLA's (Cost of Living Adjustments)***

**Salary Growth** – In addition to pension growth, Costa Mesa employees have experienced growth in direct compensation. In our meeting with Mr. Worgan, who serves as actuary for cities and agencies in Orange, Riverside, and Ventura counties, he stated that in addition to generous pension formulas, the Costa Mesa pay

scale is at the upper end of the spectrum. The city, as part of its openness and transparency policy, provides annual compensations report on the city website. The compensation report may be viewed at <http://www.costamesaca.gov/index.aspx?page=692>.

**COLA's** - In the previous section, there are repeated references to "first year pension benefits". This is intentional as all pensions have guaranteed annual cost of living increases (COLA's). The average annual COLA is 2% which means, that on average, pension payments automatically increase 2% each year. A recent study completed by city staff and the POC concluded that the average age of a Costa Mesa retiree is 55 years old. Assuming the retiree lives to their full life expectancy of 83, benefits will be paid for roughly 29 years. Over that period, the first year pension benefit will grow by 74%. In the case of a 2012 retiree receiving a first year pension of \$100,000, that pension will grow to \$174,000 in 2041.

Pensions are further inflation protected. Should inflation spike, pensions are guaranteed with 80% purchasing power protection (indexed for inflation, the purchasing power of pension payments are guaranteed to meet or exceed 80% of the first year pension benefit). In the event this inflation protection is required, it will be necessary for the city to make additional contributions to the pension plan to cover this additional unfunded cost.

#### ***Changes in CalPERS Actuarial Assumptions***

The changes in the discount rate/ROI assumption, from 8.25% to 7.75% in 2003 and from 7.75% to 7.5% in 2011 have a material effect on unfunded liabilities. It is notable that after the rate change in 2003, unfunded liabilities increased from \$9 million to approximately \$50 million by 2006. The amount of that increase attributable to the rate change is difficult to ascertain, but during that same period, investment returns were above the 7.5% discount rate, averaging 11.1% over the four years.

The calculation of future unfunded liabilities and contribution rates will be significantly influenced by recent changes directed by GASB, the Governmental Accounting Standards Board. GASB is an independent organization that establishes and improves standards of accounting and financial reporting for U.S. state and local governments.

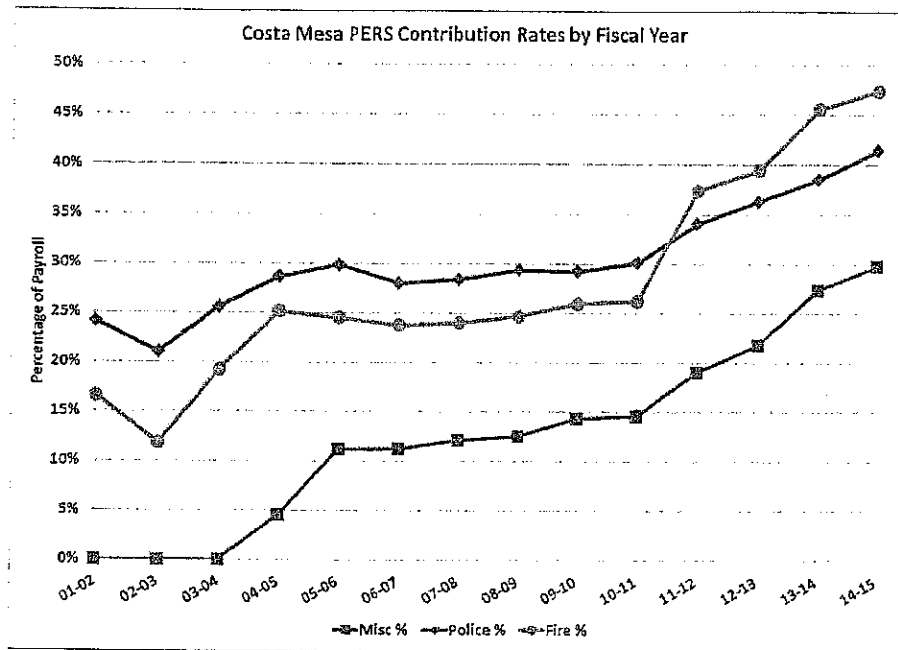
In a recent decision, GASB instructed all public pension plans to discontinue the practice of valuing assets by the AVA, Actuarial Value of Assets, method. The AVA method formerly allowed pension administrators to report assets at values exceeding their current market value. In lieu, GASB now requires that assets be reported by MVA, the Market Value of Assets. MVA is the current and true market value of the assets. This change will end the longstanding CalPERS practice of using AVA for calculating unfunded liabilities.

Since MVA is a more conservative valuation method, its use will increase reported unfunded liabilities which will directly increase the total contribution rates for pension plans. CalPERS recognizes the significant impact of this accounting change and has elected to "phase in" MVA reporting over the next 5 years.

#### ***Pension Contribution Rates***

As mentioned previously, Costa Mesa makes pension contributions for each employee group based upon CalPERS defined pension formulas and actuarial projections. The following graph illustrates the growth in Costa Mesa employer pension contribution rates over the past 12 years and projected by CalPERS for the next two years.





As indicated, the contribution rate for Miscellaneous employees will grow from 11.2% in 2005-2006 to 29.8% by 2014-2015. Of this growth, the normal cost increased a small percentage, from 8.7% to 9.0%. However, unfunded costs increased from 2.6% in 2005 to 20.8% in 2014-2015.

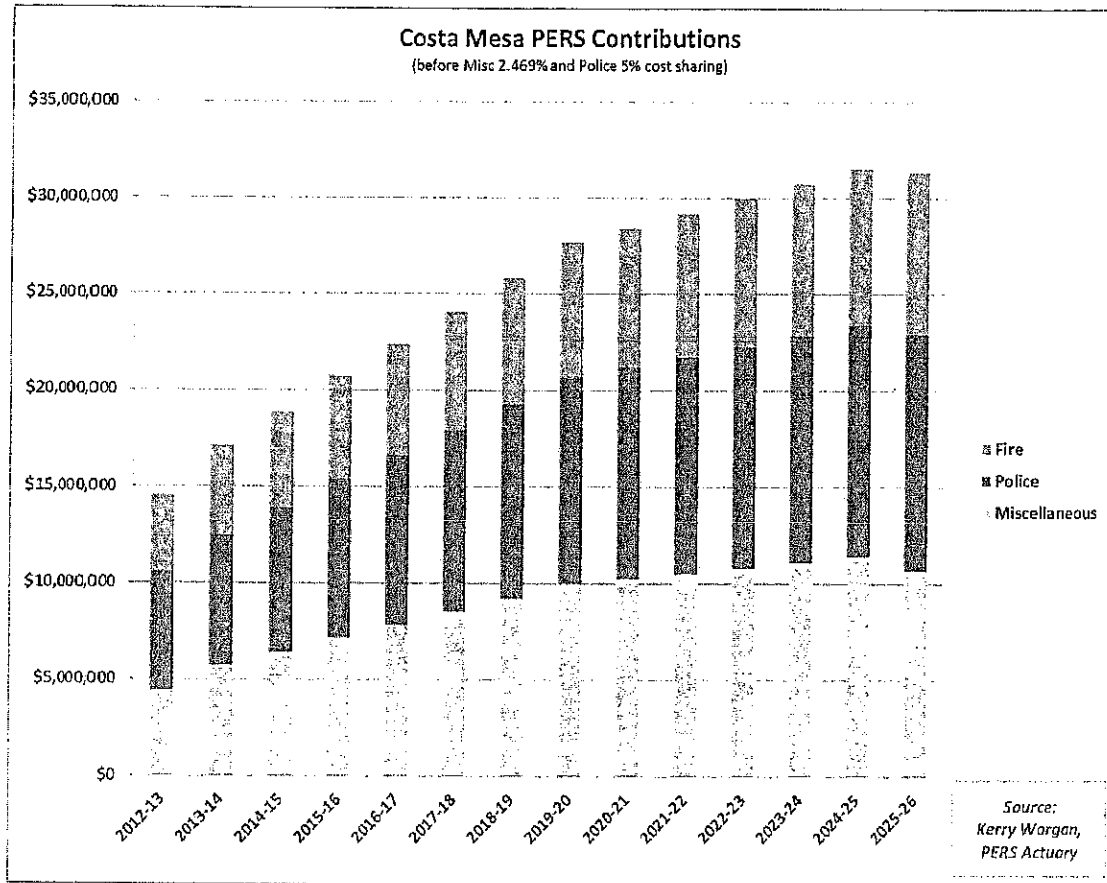
Similar growth is indicated for Police employees. In 2005-2006, the total contribution rate of 29.9% consisted of 17.1% for normal costs and 12.8% for unfunded costs. In 2014-15, the total rate of 41.4% will consist of 19.9% for normal costs and 21.5% for unfunded miscs.

The following table further presents contribution rates for Miscellaneous and Police employees, including just the past five years. As the table illustrates, the cost to cover unfunded costs has grown dramatically for Miscellaneous employees due to benefit enhancements negotiated in 2008. The increases for Police employees are also significant, without enhanced pension benefits.

Costa Mesa Pension Contribution Rates												
Fiscal Years 2010-2011 thru 2014-2015												
Employee Group			Fiscal Year									
			2010-2011		2011-2012		2012-2013		2013-2014		2014-2015	
Miscellaneous	Total Contribution Rate	Normal Cost Rate	14.6%	8.9%	19.1%	8.8%	21.8%	8.8%	27.4%	9.6%	29.8%	9.0%
		Unfunded Cost Rate		5.7%		10.3%		13.0%		17.8%		20.8%
Police	Total Contribution Rate	Normal Cost Rate	30.1%	17.6%	34.0%	19.0%	36.3%	19.1%	38.5%	19.6%	41.5%	20.0%
		Unfunded Cost Rate		12.5%		15.0%		17.2%		18.9%		21.5%
Contribution rates as a % of pensionable salary Fire employees participate in a pooled account and are reported in a different format CalPERS sets rates approximately 6 months in advance of the coming fiscal year												

**Projected Pension Contribution Increases**

Understanding the magnitude of our unfunded pension liabilities, the POC asked Mr. Worgan of CalPERS to present his estimate of future pension costs for Costa Mesa. Following is a graph summarizing the projections provided by Mr. Worgan, distributed by employee group.



As the graph illustrates, over the next five years, pension costs (not including OPEB's) are anticipated to grow 60%, from nearly \$15 million in FY 2012-13 to \$24 million in FY 2017-18. Examining costs over the next ten years, from FY 2012-13 to 2022-23, our costs will double from nearly \$15 million to \$30 million.

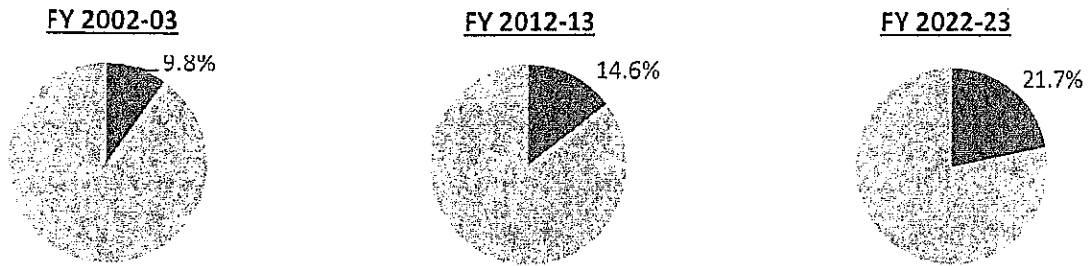
**OPEB – Other Post-Employment Benefits**

In addition to pension benefits, all full-time employees who were hired prior to January 1, 2004 also receive certain medical benefits upon retirement. These benefits include payments for medical insurance for those under age 65 as well as payments for Medicare supplemental insurance for those over age 65. Insurance benefits extend for the life of the retiree and currently cost the city over \$1.6 million. Over the next 10 years, the cost of these benefits is projected to exceed \$2.3 million annually.

**Impact of Pension Payments on City Finances**

Based upon the contribution rates and amounts above, it is appropriate to review the actual dollar impact on city finances. In the interest of a consistent discussion of the costs, in this section we will only discuss the amounts paid by the city for pension benefits. Employee contributions to the plan will not be included and OPEB's are not included.

The following charts illustrate two important dollar metrics that greatly impact the city, its ability to fund pensions, and for that matter, all city functions. The first metric is the city General Fund (essentially the city operating budget for the year) and the second metric is the amount paid by the city to fund employee pensions.



Costa Mesa Pension Costs as % of General Fund					
Fiscal Year	2002-03	2007-08	2012-13	2017-18*	2022-23*
General Fund	\$ 82	\$ 103	\$ 103	\$ 119	\$ 138
Pension Costs	\$ 8	\$ 14	\$ 15	\$ 24	\$ 30
Pension Cost as % of General Fund	9.8%	13.6%	14.6%	20.2%	21.7%
\$ in millions					
* General Fund assumed to increase 3% per year					

As these charts illustrate, in FY 2002-03, the city general fund was approximately \$82 million and \$8 million (9.8% of the General Fund) was paid for pension benefits. In FY 2012-13, the general fund was approximately \$103 million and approximately \$15 million was paid for pension benefits (14.6% of the General Fund).

Based upon assumed 3% annual increases in the amount of the city General Fund, and CalPERS projections of future pension costs, in the next five years, pension costs will increase nearly 40% to 20.2% of the annual General Fund. By FY 2022-23, pension costs are projected to reach 21.7% of the annual General Fund.

**Other Potential Contribution Increases**

Beyond the contribution increases discussed previously, Mr. Worgan stated that changing assumptions used by CalPERS actuaries could have additional upward pressure on contribution rates. In particular, CalPERS is currently reviewing their mortality assumptions. Retirees are living longer and therefore benefits are being paid for a longer period of time. Mr. Worgan indicated that the increased mortality could increase contribution rates by 2 – 4 percentage points annually.

In addition to mortality increases, the continuing debate related to the ROI assumption could affect contribution rates. Should the ROI assumption be decreased, or should investment returns fall below the current 7.5% annual projection, CalPERS will likely need to further increase contribution rates.

**Will Increased Contribution Rates Affect Unfunded Liabilities?**

In his presentation to the POC, Mr. Worgan provided his analysis related to the future of Costa Mesa unfunded liabilities. His analysis concluded that unless Costa Mesa makes additional contributions beyond those indicated in the projections above, there is not likely to be any meaningful reduction in the amount of our unfunded liabilities for at least the next 10 years.

### **Conclusions**

Understanding the multi-layered components discussed above, the POC has concluded the following:

- Despite increasing annual pension contributions by 40% over the past 10 years, unfunded liabilities have increased from \$9 million to \$228 million.
- Based upon the current state of Costa Mesa unfunded liabilities, as well as those of many other cities, counties, and state agencies, the assumptions used by CalPERS likely fail to accurately reflect pension realities.
- The projected growth of pension obligations over the next 10 years jeopardizes the ability of every city department to deliver their services and similarly jeopardizes the very employees the pensions are designed to reward and protect.
- PEPRRA, the legislation intended to help correct deficiencies in public pensions, will provide little to no meaningful relief in the next ten years.
- Acknowledging the current financial condition of our pension plans, and the financial projections for the next ten years, these plans as currently structured are unsustainable.

## PART IV Courses of Action

Acknowledging the conclusions reached in the previous sections, and compounding those conclusions with the financial corollaries, the POC has initiated discussion on what can be done to rectify the problems related to our employee pensions. Many actions, which might initially seem common sense, are hamstrung by the myriad of laws and regulations that permeate public pension structure. Hence, in this part of our report, we offer limited suggestions for specific courses of action. Rather, we appeal to all stakeholders, city employees, the citizens of Costa Mesa, and city decision makers to first, understand the magnitude of the issues, and then move forward in mutual best interest to resolve the matters.

### ***Confirmation of POC Findings***

The first logical step is likely to confirm the POC findings presented in Part III of this report. The POC has worked with city staff in each step of our analysis. We now invite all stakeholders who have not previously participated in this process to review the POC work completed, understanding that it is important to develop a consensus for structuring a viable and fiscally responsible pension plan for Costa Mesa employees.

### **Obstacles to Pension Reform**

There are many obstacles to pension reform, some in the form of state laws, others in the structure of our employee contracts. Following is a discussion of the most pertinent.

#### ***The "California Rule"***

The single largest obstacle to pension reform is a statute commonly referred to as the "California Rule." This rule prohibits reducing public pension benefit formulas in perpetuity; from the first day of employment, until the death of the retiree (and his/her spouse if survivor benefits are selected).

Even if the city, city employees and their bargaining units agreed that the current financial situation was unsustainable, and modifications were appropriate with reduced benefits, the implementation of such changes would be prohibited by current law. Efforts to change this law have been discussed at multiple levels for a number of years, but to date, the political climate has restricted any action to remove this obstacle.

#### ***CalPERS***

The California Government Code vests in the CalPERS Board the management and control of the Retirement System for government agency employees. The California Constitution provides that the Board shall have total authority and fiduciary responsibility for the investment of moneys and administrations of the retirement system.

The CalPERS Board is comprised of 13 members, 6 elected by CalPERS members, 3 appointed, and 4 ex officio members. Of the ex officio members, it is mandated that 2 are financial professionals and 2 shall be human resource professionals.

Costa Mesa is not the only city with over-burdened pension plans. In fact, nearly every CalPERS city and agency faces underfunding of their plans. Statewide, underfunding of public employee pension plans has been estimated between \$300 and \$500 billion.

In response to criticism over the current state of many pension plans, CalPERS commonly dismisses the notion that their actuarial assumptions might be flawed. In particular, Mr. Worgan stated that Costa Mesa should recognize that their employees are well paid and the benefit formulas offered to employees are generous. He further defends CalPERS positions and points to the effects of the Great Recession as the major reason for

unfunded liabilities. When questioned as to what Costa Mesa could do to reduce unfunded liabilities, one of his suggestions was "make larger payments" to CalPERS.

Due to its sheer size, change at CalPERS appears very slow. Considering the structural composition of CalPERS and the fact that they have no financial obligation for funding the payments to their members, it could be construed that there is a natural conflict of interest.

### ***Collective Bargaining***

All Costa Mesa employee groups are represented by bargaining units in their negotiations with the city. Some representatives of these bargaining units also negotiate for employees with other cities and agencies, and historically, changes in the contracts with one city often influence contracts with other cities and agencies.

Needless to say, this is a very sensitive process. Easy when times are good and benefits are increasing, much more difficult when times are tough and concessions are on the table.

### ***What Will Affect Unfunded Liabilities?***

In an effort to resolve the matter of unfunded liabilities, the POC has reviewed numerous options. Following is a discussion of concepts, their advantages and disadvantages.

#### ***Pension Bond to Retire Unfunded Liability***

The committee discussed the concept of issuing a \$228 million, 30 year bond, with the proceeds being used to pay off the unfunded liability.

##### **Pros:**

- The current unfunded liability with CalPERS would be retired.
- Savings from CalPERS payments could be used to make part of the debt payment. (The city presently pays CalPERS approximately \$10 million annually towards the unfunded liability.)

##### **Cons:**

- The city would be assuming \$228 million in debt to retire this obligation.
- The payment on such a debt would be in the range of \$15 million annually. (While a certain amount could be paid by the savings mentioned above, there is no current revenue for the remainder of the payment.)
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.
- Does not preclude future increases in unfunded liabilities.

#### ***Raise Taxes to Increase CalPERS Payments***

The committee discussed the concept of increasing the city sales tax or property taxes with the proceeds being used to pay off the unfunded liability.

##### **Pros:**

- The current unfunded liability with CalPERS would be retired.

##### **Cons:**

- City would need to implement a sales tax ranging from 3/8% to 5/8% for 30 years to retire the current \$228 million unfunded liability.
- Estimated property tax increase of approximately \$100 per \$100,000 in assessed value, paid for 30 years, could be used to eliminate the current unfunded liability.
- Tax increases of this nature would need to be approved by a majority of the voters in Costa Mesa.
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.

- Does not preclude future increases in unfunded liabilities.

#### ***Sell Assets to Raise Funds for Pension Payments***

The committee discussed the concept of selling assets to raise funds for pension payments. Discussions centered on selling major assets such as the sale and lease-back of City Hall or the sale of park land. (The sale of minor assets was not considered as such action would not make a significant impact on our obligations.)

Pros:

- Part of the unfunded liability with CalPERS would be retired.

Cons:

- Difficult to determine which assets could be sold to make meaningful payments to the unfunded liabilities.
- After assets are sold, they are likely unrecoverable.
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.
- Does not preclude future increases in unfunded liabilities.

#### ***Increase Payments to CalPERS by Reducing City Services***

The committee discussed the option redirecting General Fund revenue to CalPERS at the expense of other city services.

Pros:

- Payments would reduce the unfunded liabilities from existing revenue without increased taxes.

Cons:

- Difficulty in identifying what services would be reduced based upon current revenues and expenditures.
- Does not create a meaningful plan that could be quantified.
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.
- Does not preclude future increases in unfunded liabilities.

#### ***Annual Prepayment of CalPERS Contribution***

CalPERS determines contribution rates for any given year based upon the projected total contribution required for the plan year. Based upon the annual contribution, if a city or agency is willing to prepay their annual contribution, lump sum at the start of the fiscal year, CalPERS will extend a discount for the annual payment. The estimated annual discount for Costa Mesa is approximately \$450,000. The POC discussed the merits of this type of annual prepayment and approves this as a possible course of action based on the following:

Pros:

- Estimated savings in pension contributions of approximately \$450,000 per year.
- Accumulated savings could be used to pay down unfunded liabilities over time.
- Leaves opportunity to work with CalPERS for constructive reform.

Cons:

- Limited, assuming the city has adequate cash flow to fund the prepayment of approximately \$15 million in the current year.
- Annual prepayment amount would increase each year as outlined earlier in this report.
- Need clarification from CalPERS on how prepayments are affected if CalPERS investments fail to earn the 7.5% ROI assumption.
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.
- Does not preclude future increases in unfunded liabilities.

### ***Payment of the Fire Side Fund with General Fund Revenue***

The Fire Side Fund (FSF), with unfunded liabilities of approximately \$20 million, was created when pension benefits were increased retroactively for Fire employees in 2008. Originally it was projected that cost sharing and other savings would pay off the FSF over 20 years. However, with the investment losses of 2008 and 2009, the FSF has experienced increased payments to make up for those investment losses.

In each of the past two years, the city has earmarked \$500,000 to be used for payments on outstanding pension obligations. Using the \$1,000,000 earmarked over the past two years as a lump sum payment on the FSF would reduce some of its unfunded obligations and hopefully return the FSF closer to its intended course. The POC approves this course of action based upon the following:

#### **Pros:**

- The \$1,000,000 payment would be a first step in attempting to retire one of our unfunded obligations.
- While CalPERS does not guarantee a 7.5% return on investment in the general portfolios, there has been some indication that they might indeed guarantee such a return in the FSF. Confirmation of this scenario is required and it should be clearly resolved with CalPERS if this course of action is considered likely.

#### **Cons:**

- Other employee groups may feel that an equal share of the \$1,000,000 should be allocated to their unfunded obligations.
- A single payment to CalPERS does nothing to establish a logical plan that will be followed not only by the current city council, but by councils in the future.
- Does not address our concerns regarding structural flaws in CalPERS benefit formulas and actuarial assumptions.
- Does not preclude future increases in unfunded liabilities.

### ***Improved Investment Performance by CalPERS***

If CalPERS investment performance exceeds the current ROI assumption of 7.5%, our unfunded liabilities will decline on their own without increased payments.

#### **Pros:**

- No cost to the city.
- Decreased annual payments to CalPERS.

#### **Cons:**

- Based upon recent investment results from CalPERS and economic forecasts, the likelihood of investment performance exceeding 7.5% annually, for a sustained period, is at best unlikely.
- It is rarely a good idea to hope that a significant problem will simply vaporize on its own.

### ***Contract Modifications Through Collective Bargaining***

As discussed, all employee groups participate in collective bargaining through their unions or associations. Over time, the POC would hope that all parties will recognize that this situation requires concessions on all sides. Understanding the size of the financial burden, it would be imprudent for any side to assume that all of the responsibility for correcting this situation should fall onto the shoulders of another party.

Uniquely, PEPPRA has already modified pension benefits for new employees, but the benefits of PEPPRA will not be significant for 15-20 years. During that time, absent changes in the existing benefit levels or modification of CalPERS actuarial assumptions, it is possible that the deficits we face today will only increase.

### ***Contract Modifications for Classic Employees***

The California Rule currently makes modifications to pension formulas illegal. It would be logical for city leaders to consult with other parties of interest who advocate changing this rule.



In the interim, future contracts negotiated with Classic employees need to be scrutinized for opportunities to reduce pension costs without violating the law. Options to consider include:

- Increased employee cost sharing, particularly for Police and Fire employees. Currently the majority of Police and Fire employees contribute 5% of their salary towards their pension. In the private sector, all employees pay 6.2% for Social Security, a benefit that pays far less than Costa Mesa employee pensions.
- When pension contribution rates increase, apply some amount of future wage increases to pension costs.
- Reduce future COLA payments. The current annual 2% increase is noted as a significant driver of cost increases.
- Modify the pensionable salary calculation from the single highest year of compensation to an average of the highest 3 or 5 years of compensation.
- Work with appropriate parties to construct a cap on pensionable salary similar to those required in PEPRA.
- Reconstruct compensation schedules to reclassify certain pay types in a fashion that they would no longer be included as part of the pensionable salary. (Example: uniform allowance is currently paid as part of pensionable salary. If the uniform allowance was paid as part of an expense reimbursement, it would be removed from pensionable salary.)

#### ***Contract Modifications for New Employees***

While PEPRA has made some progress on reducing costs for new employees, additional study is necessary to identify what the true savings might be. Even with PEPRA, we remain exposed to the same CalPERS actuarial assumptions related to the ROI assumption and longevity that have created the untenable situation we address today.

#### ***Recognize the Two-Tiered Compensation Structure***

In collective bargaining, recognition of the two-tiered compensation structure between Classic and New employees is important. PEPRA has mandated that New employees will receive lower pension benefits. Employees working shoulder-to-shoulder are receiving different pension benefits, so it is logical that they would also be receiving different base compensation.

This relates to the comment above where it was suggested that Classic employees might be asked to allocate an increased amount of their wage increases to help fund their pensions. At the same time, New employees might be entitled to increased direct compensation.

#### ***Future Employees and Future Retirement Plans***

Waiting to see if PEPRA results in material savings is likely insufficient. It may be in the best interest of the city if decision makers immediately begin researching alternative retirement plans for future employees. Some of the components to consider include:

- **Increasing the minimum retirement age** – the aforementioned study conducted by the Costa Mesa Human Resources Department concluded that the average age of a Costa Mesa retiree is 55 years old, following 22 years of service with the city. Assuming normal mortality of 83 years, we are paying retirement benefits to former employees for more years than they worked for the city.
- **Include Social Security in Retirement Plans** - Currently, Costa Mesa employees do not contribute to nor participate in Social Security. However, a large number of CalPERS members who work for other cities or agencies are covered by a combination of Social Security and a CalPERS pension. This model may be practical for Costa Mesa sometime in the future. With such an arrangement, pension benefits would be protected by two layers. The “base” retirement would be Social Security and the CalPERS

pension would be smaller and secondary. In this model, all parties would be insulated from the dramatic impact we currently experience with the CalPERS pensions.

- **Implementation of 401(k) Type Plans** - The conversion of our current defined benefit pension plan to a defined contribution 401(k) type retirement plan should also be investigated. The majority of private sector employers and multiple state public employers have abandoned pensions in favor of 401(k) type plans. This has typically occurred after they experienced the same loss of cost control that the city and Costa Mesa taxpayers currently experience.

### ***Working with CalPERS to Better Manage Pension Plans***

Early in the POC meeting with Mr. Worgan, a question was raised regarding what it would take for Costa Mesa to abandon the existing plans with CalPERS. Beyond the need to reach agreement with the employees and their bargaining agents, Mr. Worgan 'guesstimated' that it would require a payment of approximately \$800 million. Understanding this reality, the discussion advanced to what CalPERS and Costa Mesa can do in a unified effort to secure the viability of our pension plans. Some of the ideas discussed included:

- **Select other CalPERS plans for future employees** – CalPERS offers plans with less generous benefit formulas. Assuming collective bargaining hurdles are cleared, these could be implemented for future employees.
- **Work with CalPERS to modify actuarial assumptions** - Example: CalPERS assumes that all payrolls will increase 3% annually. When Costa Mesa reduced payroll during the recession, payrolls actually decreased. Since CalPERS assumed increased payroll during that period, the contribution rates they set for those years were understated and contributed to increases in our unfunded liabilities.
- **Work with CalPERS to effect a further reduction in the discount rate/ROI assumption** - In 2011, when CalPERS reduced the discount rate from 7.75% to 7.5%, CalPERS Chief Actuary Alan Milligan actually advocated for a reduction to 7.25%. Mr. Milligan was overridden by the CalPERS Board of Directors and the rate was set at 7.5%. With pressure from cities and agencies, movement to a more conservative discount rate could be evaluated, understanding that the reduced discount rate would result in increased contribution rates for cities and agencies.
- **Work with CalPERS to advance pension reform** – It is important to understand that meaningful pension reform requires changes to the California Rule and the state constitution. The most expedient way to achieve such change would likely require unified effort by all parties of interest, cities and agencies, employee groups, and CalPERS. Absent that effort, the needs of the individual parties will likely fall prey to the current political whim, leading to continued deterioration of the pension system.

### ***Outsourcing – Part of the Solution?***

During the meeting with Mr. Worgan, questions were raised about the effect of outsourcing. Outsourcing is a process where city jobs are eliminated and services are provided by outside vendors. Newport Beach recently outsourced trash collection and is currently reviewing a proposal to outsource part of their lifeguard services, mainly in an effort to rein in pension costs.

At this time, the single most compelling reason for Costa Mesa to implement outsourcing is the uncertain nature of CalPERS pension plans. If Costa Mesa cannot contain and manage its current and future costs, the City should not exacerbate the problem for future generations by enrolling additional employees in these plans.

The current unfunded liabilities are a lump sum amount. They are not materially influenced by increases or decreases in city payroll. Unfunded liabilities are only reduced by annual payments to CalPERS for unfunded costs or when CalPERS investment results exceed the ROI assumption. If the annual city payroll decreases for any reason, the contribution rate for unfunded liabilities will increase because it is simply calculated as a percentage of total payroll. However, this does not increase our unfunded liability.

Assuming the cost of outsourcing services is equal to the current cost of city employees performing those services; outsourcing is a logical option because the enrollment of new participants into the CalPERS pension system is reduced. If the cost of outsourcing services is less than the cost of city employees performing those services, the savings from outsourcing could be used to make additional payments to reduce the unfunded liabilities.

Prior to any implementation of outsourcing, it is in the best interest of all decision makers to work with city staff and CalPERS to fully understand all costs and any financial impact related to reclassifying terminated employees in the CalPERS system. It is additionally important to balance any costs or savings with the desire to maintain a professional and dedicated workforce.

## PART V Summary and Conclusions

### Summary and Conclusions

The POC recognizes that this report does not identify a specific course of action for reconciling the outstanding obligations. As stated in the Introduction, the purpose of this report is to share the POC findings to date and provide a foundation for future dialogue between all stakeholders. As a basis for that dialogue, it would be prudent to all parties to acknowledge the following:

- In just over ten years, the city has seen an unprecedented increase in its unfunded pension liabilities to \$228 million dollars.
- During that same period, pension plan contribution rates increased nearly 100% for Miscellaneous and Fire employees, and nearly 50% for Police employees.
- In the period 2002 to 2012, average first year pension payments increased by 63%. During that same period, the Consumer Price Index increased 26%.
- Based on CalPERS projections, in the next decade, pension payments are projected to double.
- Based on CalPERS projections, even with the known increased payments over the next decade, unfunded liabilities are not likely to be reduced.
- In FY 2002-2003, pension payments consumed 9.8% of the city General Fund Budget. In FY 2022-2023, they are projected to consume 21.7% of that same budget.
- Based on current city finances; revenues, expenditures, and reserves, it appears the city has limited resources to dedicate to the problem of unfunded liabilities.
- It will be important for city leaders to reach out to other cities and agencies, as well as CalPERS and legislators, to advance pension reform on a statewide basis.
- Progress on this issue is unlikely until all stakeholders; city employees, city decision makers, and the citizens of Costa Mesa, unite and commit themselves to a resolution.

**CMPOC**  
**Fast**  
**Facts**

# COSTA MESA CREATES PENSION OVERSIGHT COMMITTEE

Vol. 1 November 23, 2013

Throughout the nation, the subject of “Unfunded Public Pension Liabilities” has captivated headlines serving as vivid illustrations of how they place city finances in peril. Unfunded liabilities occur when the amount of money set aside to pay guaranteed public pension benefits is insufficient to cover their anticipated costs. As unfunded liabilities increase, they consume a growing percentage of our financial resources and jeopardize our ability to fund important municipal services including police and fire protection, parks, and road maintenance.

The city of Costa Mesa is not immune to the dangerous developments in unfunded pension liabilities. A recent study of our financial position indicates that Costa Mesa pensions are underfunded by as much as \$196 million. Additionally, the fund that provides for retiree medical benefits is estimated to be underfunded by \$32 million. As a point of reference, for the current year, the General Fund Budget for the entire city is \$103 million. Simply stated, it is possible that the unfunded amount of our future obligations exceeds twice our annual city budget.

In response to the magnitude of these matters, the Costa Mesa City Council approved development of the Pension Oversight Committee (POC) in February of 2013. Following public notice, volunteers were interviewed by council members and then appointed to the POC at the April 16, 2013 council meeting.

The mission of the POC is to focus on current and long term pension obligations in a non-partisan fashion. Key points of emphasis include:

- Review annual and long term pension commitments as they pertain to the City’s CalPERS retirement account with an emphasis on controlling unfunded obligations.
- Study and advise on what financial triggers led to an unfunded position of approximately \$196 million.

- Encourage the City to maintain adequate reserves and ratios per council guidelines and prudent fiscal management.
- Review negotiated pension and compensation packages as they pertain to each employee bargaining unit.
- Evaluate potential changes to pension benefits and advise the employees, City Council, and the citizens of Costa Mesa of their anticipated impact.

The nine volunteers who serve on the POC were appointed to two year terms. All are Costa Mesa residents coming from various business and professional backgrounds. Current members with voting rights include Messrs. Jeff Arthur, Gene Hutchins, Rick Kapko, Kent Mora, Gary Parkin, Ron Robertson, Timothy Sesler, John Stephens and Ralph Taboada. POC activities are supported by city staff members including Interim Finance Director Steve Dunivent, Human Resources Director Lance Nakamoto, and Human Resources Analyst Ryan Thomas. City Council liaisons include Mayor Jim Righeimer and Mayor’s Designee, Mayor Pro Tem Stephen Mensinger.

The POC recognizes that a critical function of their role is educating all stakeholders by communicating their findings. Numerous resources are accessible on the city website and additional information will be posted as it develops. You can find this information by going to [www.CostaMesaCA.gov](http://www.CostaMesaCA.gov), clicking on the “City Hall” tab, locating the “Commissions and Committees” section, and then finding the “Pension Oversight Committee” page.

You may communicate with the committee by attending their meetings which are open to the public. Committee meetings are scheduled on the first and third Wednesday of each month, at 4:30 p.m., in City Hall conference room 1-A. The committee may also be reached via email at [CMPOC@CostaMesaCA.gov](mailto:CMPOC@CostaMesaCA.gov).

# Pension Terminology

Vol. 2 November 29, 2013

*At a minimum, pension terminology can be challenging, at a maximum, it is outright confusing. In this edition of Fast Facts we attempt to define some of the more commonly used pension terminology. By sharing this basic terminology we hope to expand your understanding of complicated terms in an uncomplicated manner.*

**CalPERS** - Costa Mesa contracts with CalPERS, the California Public Employees Retirement System, to administer pensions for city employees. CalPERS administers pensions for over 1.6 million active employees and retirees including state, county, and municipal employees as well as public school and state university employees. While CalPERS is the administrator of our employee pensions, the payments are guaranteed by the taxpayers of Costa Mesa, not CalPERS.

**Defined Benefit Plans (DBP)** – Pensions are referred to as Defined Benefit Plans. DBP's establish a formula for pension payouts based upon age, years of service, and salary level. Costa Mesa benefit payments are guaranteed for the life of the employee and if a lesser benefit is selected, for the life of the employees' spouse. Pension benefits increase annually, and the pension benefits received by retirees are not affected by the investment results achieved by CalPERS.

**Defined Contribution Plans (DCP)** – Retirement plans funded by a set contribution formula, most commonly a percentage of salary. The most common DCP is a 401(k) plan where employers and employees contribute to an employee account, the employee directs the investment, and there is no guaranteed investment return.

**Employee Groups** – Costa Mesa employees are divided into three different groups. Safety Police (“on the street”

police officers), Safety Fire (“on the street” fire personnel), and Miscellaneous employees (all other city employees, managers, and police and fire administrative employees). Through their bargaining units (union or association representation), each employee group has negotiated their own pension benefit formula.

**Pension Benefit Formulas** – Pension formulas are expressed as a percentage of salary for each year of service with a minimum retirement age. In the case of Safety Police and Fire Safety employees hired before January 1, 2013, the benefit formula is 3% at 50 (employees hired after 1/1/13 have a slightly reduced formula). To calculate their pension benefit, employees in these classes are eligible to retire at age 50 and they receive 3% of their salary for each year of service. The salary used to calculate their benefit is their highest single year of salary any time during their employment. Example: 50 year old employee with 24 years of service with a highest annual salary of \$90,000; benefit formula =  $3\% \times 24 \text{ years} = 72\% \times \$90,000 = \$64,800$  first year pension benefit. The benefit formula for Costa Mesa Miscellaneous employees hired before January 1, 2013 is 2-1/2% at 55.

**Service Credits** – Employees vest service credits after 5 years of employment and employees are not subject to mandatory retirement. If they continue working, they continue to accrue service credits (additional years of service). In the example cited above, if the employee continued to work until age 55, his pension benefit would grow to  $3\% \times 29 \text{ years of service}$  which equals 87% of his highest salary. Employees who retire before the age expressed in their stated benefit formula receive a reduced benefit and for all employees, the maximum benefit payable is 90% of highest salary.

**COLA**– All Costa Mesa pensions are subject to an automatic Cost of Living Allowance or “COLA” which increases the benefit annually. Historically, this increase

is 2% per year throughout their lifetime. If the first year benefit is \$60,000, the second year benefit is \$61,200, the third year benefit is \$62,424, etc.

**Contributions Rates** – Based upon salaries, past and estimated investment returns, and benefit formulas, CalPERS annually establishes the Contribution Rate for each employee group. The Contribution Rate is the percentage of salary (for each employee) that Costa Mesa must pay to CalPERS to fund the pension plan for that year. Contribution Rates consist of two elements: Normal Cost (the amount required to fund the benefit for each working employee) and Unfunded Liability (the amount required to make up for insufficient prior saving or poor investment return). Contribution Rates will be discussed in-depth in a future Fast Facts article.

**Discount Rate** – Contributions paid to CalPERS are invested to help fund benefit payments. The investment rate of return is called the Discount Rate. The current CalPERS discount rate is 7.5% which means that including market fluctuations, CalPERS has concluded they will average 7.5% return on investment per year.

**Actuaries** – Financial professionals who make projections on the value of assets based on historical performance, typically on a long-term basis. Some actuaries make conservative estimates and others make liberal estimates. This can lead to a wide disparity in their long-term financial projections.

**Smoothing** – A process that allows actuaries to apply a consistent discount rate over an extended period of time. In this process, the actuary makes their projection assuming assets that may have dropped in value will ultimately increase in value. Assets that have experienced an unusually high rate of appreciation are reduced in value in this process.

**Market Value of Assets (MVA)** – the current market value of an investment or group of investments.

**Actuarial Value of Assets (AVA)** – the projected value of an investment or group of investments as determined by an actuary after “smoothing”.

**Funded Ratio** - The actuaries’ estimate of AVA divided by the projected future cost of benefit payments. If the funded ratio exceeds 100%, the plan is designated

“overfunded”. If the ratio is less than 100%, the plan is designated “underfunded”. In 2012, Costa Mesa pensions were underfunded with a funded ratio of approximately 65%.

**Unfunded Liabilities** – The difference between the amount of money that will be required to pay pension benefits and the amount that has been paid by the employer, as determined by CalPERS actuaries, to fund that benefit. Based on MVA, in 2012, Costa Mesa unfunded pension liabilities were \$196,000,000.

**PEPRA** – Public Employees’ Pension Reform Act – The California law that became effective January 1, 2013 which is intended to constrain pension benefits deemed excessive. Most provisions of PEPRA apply only to new employees who are hired after 12/31/12 and will not provide immediate savings to employers.

**Classic Employees** - Employees hired prior to January 1, 2013 whose benefit formulas are not subject the restrictions of PEPRA.

**Pension Spiking** – An intentional, late-career effort to maximize compensation to increase pension benefits. In Costa Mesa, policies to minimize “spiking” are in place.

**EPMC** – The City and Employees both contribute to the cost of pensions. The City also makes Employer Paid Member Contributions (EPMC’s) which are payments that are added to the employees’ highest year of pay for pension benefit calculation purposes.

**GASB** – The Governmental Accounting Standards Board (GASB) sets the policies for how public pension plan finances are evaluated and reported. Recently enacted changes by GASB will have a significant upward impact on the contribution rates paid by California CalPERS member agencies including Costa Mesa.

**OPEB** – Other Post-Employment Benefits (OPEB’s) are fringe benefits such as retiree medical insurance paid partially or in full by the employer.

**CMPOC**  
**Fast**  
**Facts**

**PEPRA – The Public  
Employees’ Pension  
Reform Act**

Vol. 3 December 6, 2013

*This edition of Fast Facts will discuss PEPRA, the Public Employees’ Pension Reform Act. PEPRA was created to address structural concerns related to California public employee pensions. Recognized as a positive step to help agencies better manage future pension costs, most provisions of PEPRA apply only to employees hired after December 31, 2012 who have not prior PERS service. Thus, it will not provide immediate relief for the many cities, counties and public agencies who face increasing employee pension costs.*

**Summary of PEPRA**

The Public Employees’ Pension Reform Act (“PEPRA”) was passed in 2012 and most of its provisions went into effect on January 1, 2013. PEPRA was designed to address a wide range of issues involving public employee pensions. Because PEPRA’s new benefits formulas apply only to employees hired after January 1, 2013, they will not provide material short-term savings, but they will result in savings in the long run as new employees are hired and ultimately retire. In addition, PEPRA reforms many of the aspects of public employee pension system that resulted in the current underfunding status such as retroactively enhanced benefits, contribution holidays, and “spiking” of pensionable compensation. PEPRA also creates negotiating tools public agencies can use to achieve equal sharing of normal benefit costs with employees. Below is a brief description of the provisions of PEPRA that are most pertinent to the City of Costa Mesa.

**Reductions in Benefit Formulas**

PEPRA creates a reduced tier of benefits for new employees. PEPRA does not change benefit

formulas for existing employees. Generally, lateral hires from other agencies or Costa Mesa employees that are rehired are not new employees under PEPRA. Any person who is a new employee may only be offered the applicable pension benefit plan specified in PEPRA.

**Basic Benefits Formulas For Non-safety Employees**

The formula for non-safety employees is called the “2 percent at age 62” formula. The normal age of retirement is 62 and the employee receives a benefit equal to 2% of pensionable compensation for each year of service. Therefore, an employee who retires at the age of 62 after 30 years of service would receive an annual pension benefit equating to 60% of his or her pensionable compensation. The minimum age to receive retirement benefits is 52, and employee’s pension benefit is reduced if the employee retires before the age of 62.

**Basic Benefits Formulas for Safety Employees**

There are different benefit formula plans for safety employees (police officers and firefighters), but in general the “normal age” of retirement for a safety employee under PEPRA is 57 with a 2.7 percent benefit. The minimum age for a safety employee to receive retirement benefits is 50 and the employee’s pension benefit is reduced if the employee retires before the age of 57.

**Provisions Regarding Employee Pension Contributions**

PEPRA provides that the standard for pension contribution sharing should be employers and employees paying an equal share of normal costs with employees paying at least 50 percent of normal contributions (“normal” costs/contributions is the

amount of money required to fund the anticipated pension benefit for a currently active employee). Through negotiations, employees can agree to pay more than 50 percent of the normal cost, but an employer cannot impose a higher contribution rate through any labor negotiation.

PEPRA changes the law in that, under PEPRA, employers are not permitted to pay any part of required employee contributions for new employees, i.e., Employer Paid Member Contributions (EPMC). PEPRA does not impact the payment of EPMC's for existing employees.

Under PEPRA, an employer may impose a 50 percent employee contribution rate for normal costs on January 1, 2018. This applies to all employees unless there is a provision in the applicable contract negotiation specifying otherwise. If imposed, the 50 percent employee contribution rate cannot exceed 8 percent of pay for miscellaneous employees or 12 percent of pay for police officers and firefighters.

Employers are not required to make changes to current employee contribution levels, including the payment of EPMC's, unless they so choose. PEPRA simply provides additional negotiating tools, including the ability to impose higher employee contributions after negotiating impasse beginning in 2018.

#### **Limitations When Calculating Pensionable Compensation/Anti-Spiking**

PEPRA makes several changes to the method by which pensionable compensation is calculated.

When calculating an employee's pensionable compensation, the average of the highest three years of the new employee's compensation is used. PEPRA also requires pension benefits for all new employees to be calculated based on the employee's base pay, defined as the normal monthly rate of pay paid in cash to similarly situated members in the same group or class of employment.

Compensation paid to enhance an employee's retirement benefit ("spiking") must be excluded.

Examples of compensation that cannot be included in pensionable compensation include: overtime, bonuses, severance pay, cash-outs for unused leave time, vacation or sick leave, and payments for additional services rendered by the employee outside of normal working hours.

#### **Cap on Pensionable Compensation**

For new employees, in addition to a reduced benefit formula and limiting pensionable compensation to the 3-year average of base pay, PEPRA sets a cap on pensionable compensation. For those who participate in Social Security, the cap equates to the Social Security wage index limit, approximately \$113,000. For new employees who are excluded from Social Security, the cap equates to 120 percent of the value of the Social Security wage index limit – approximately \$136,000. The amount of the cap is increased each year to reflect changes in the Consumer Price Index

#### **Elimination of "Air Time"**

Before PEPRA, agencies could offer members the opportunity to purchase up to five years of service credit, sometimes called "air time." PEPRA prohibits a retirement system from allowing employees to purchase of air time service credit on or after January 1, 2013.

#### **Prohibition of Contribution Holidays**

Contribution holidays occur when an employer decides not to fund the normal cost of the pension benefits in a given year. This normally happens when the pension benefits are determined to be "overfunded" (when CalPERS advises the sponsoring agency that adequate funds are in place to pay future pensions). PEPRA prohibits contribution holidays. With limited exceptions, employer and employee contributions together must equal or exceed the normal cost of benefits for the given fiscal year.

#### **Prohibition of Retroactive Benefit Enhancement**

PEPRA prohibits a public agency from granting retroactive pension benefit enhancements that apply to service performed before the date of the enhancement. This limitation applies to new and existing employee benefits.



### Cash Flow Projection

Attachment D

Bi-weekly Retirement Contribution Revenue	Actual Jul-13	Actual Aug-13	Actual Sep-13	Actual Oct-13	Actual Nov-13	Actual Dec-13	Projected Jan-14	Projected Feb-14	Projected Mar-14	Projected Apr-14	Projected May-14	Projected Jun-14
Total Property Tax	(28,328)	210,364	556,940	149,531	1,759,259	9,144,361	1,801,000	132,500	1,082,000	6,986,000	1,289,500	679,500
Property Tax In-Lieu of VLF Sales Tax	-	33,137	6,029	28,834	7,764	38,812	4,320,000	-	-	14,000	4,331,000	35,000
Sales & Use Tax	(3,171,647)	3,184,600	3,159,501	2,384,951	3,188,400	3,755,293	2,521,000	3,180,000	3,167,000	2,158,000	5,509,378	8,913,000
Sales Tax In-Lieu	-	-	-	-	-	5,792,619	-	-	-	-	5,509,378	933
Transient Occupancy Tax	-	714,810	803,629	604,613	611,574	548,114	473,000	485,000	616,000	656,000	628,000	1,323,000
Rental - Golf Course Operations	-	235,989	205,432	182,738	155,182	156,140	160,000	153,000	153,000	181,000	170,000	418,000
Total Other Revenue	66,245	1,255,141	1,443,700	1,065,518	1,103,276	733,885	935,381	1,135,500	1,356,000	2,672,000	1,369,122	1,966,567
<b>Total Revenue</b>	<b>(3,133,750)</b>	<b>5,613,741</b>	<b>6,175,231</b>	<b>4,416,085</b>	<b>6,825,455</b>	<b>14,376,605</b>	<b>16,003,000</b>	<b>5,086,000</b>	<b>6,374,000</b>	<b>12,667,000</b>	<b>16,169,000</b>	<b>13,336,000</b>
<b>Expenditure</b>												
Payroll Expenditure	1,673,064	5,221,313	3,271,247	3,332,129	3,288,162	3,614,355	3,294,000	3,291,000	4,948,000	3,260,000	3,356,000	4,942,000
Retirement Expenditure	633,777	1,806,559	1,243,065	1,190,015	1,210,376	1,249,590	1,111,000	1,099,000	1,621,000	1,046,000	1,073,000	1,607,000
Total other Expenditure	5,382,067	2,375,609	5,593,774	2,813,954	2,091,151	2,133,992	3,187,000	2,058,000	6,573,000	2,621,000	5,426,000	3,880,000
<b>Total Expenditure</b>	<b>7,688,908</b>	<b>9,403,481</b>	<b>10,108,086</b>	<b>7,336,098</b>	<b>6,589,689</b>	<b>6,997,937</b>	<b>7,592,000</b>	<b>6,448,000</b>	<b>13,142,000</b>	<b>6,927,000</b>	<b>9,855,000</b>	<b>10,429,000</b>
<b>Net Cash Flow</b>	<b>(10,822,636)</b>	<b>(3,789,740)</b>	<b>(3,932,855)</b>	<b>(2,920,013)</b>	<b>235,766</b>	<b>7,378,668</b>	<b>8,411,000</b>	<b>(1,362,000)</b>	<b>(6,768,000)</b>	<b>5,740,000</b>	<b>6,314,000</b>	<b>2,967,000</b>
FY Cumulative Cash Flow	(10,822,636)	(14,612,376)	(18,545,233)	(21,465,246)	(21,229,480)	(13,850,812)	(5,439,812)	(6,801,812)	(13,569,812)	(7,829,812)	(1,515,812)	1,391,188
General Fund Balance	31,404,456	27,614,716	23,681,861	20,761,848	20,997,614	28,376,282	36,787,282	35,425,282	28,657,282	34,397,282	40,711,282	43,618,282
<b>With Prepayment Revenue</b>												
Total Property Tax	(29,521)	219,220	580,387	156,826	1,833,324	9,529,339	1,876,822	138,078	1,127,552	7,280,111	1,343,788	708,107
Property Tax In-Lieu of VLF Sales Tax	-	33,137	6,029	28,834	7,764	38,812	4,320,000	-	-	14,000	4,331,000	35,000
Sales & Use Tax	(3,261,405)	3,254,158	3,248,915	2,452,342	3,278,632	3,861,568	2,592,344	3,269,994	3,256,626	2,219,071	2,953,278	9,165,238
Sales Tax In-Lieu	-	-	-	-	-	5,792,619	-	-	-	-	5,509,378	933
Transient Occupancy Tax	-	714,810	803,629	604,613	611,574	548,114	473,000	485,000	616,000	656,000	628,000	1,323,000
Rental - Golf Course Operations	-	235,689	205,432	182,738	155,182	156,140	160,000	153,000	153,000	181,000	170,000	418,000
Total Other Revenue	66,245	1,255,141	1,443,700	1,065,518	1,103,276	733,885	935,381	1,135,500	1,356,000	2,672,000	1,369,122	1,966,567
<b>Total Revenue</b>	<b>(3,224,680)</b>	<b>5,712,156</b>	<b>6,288,092</b>	<b>4,489,872</b>	<b>6,989,752</b>	<b>14,867,657</b>	<b>16,150,166</b>	<b>5,181,572</b>	<b>6,509,178</b>	<b>13,022,182</b>	<b>16,304,566</b>	<b>13,616,845</b>
<b>Expenditure</b>												
Payroll Expenditure	1,673,064	5,221,313	3,271,247	3,332,129	3,288,162	3,614,355	3,294,000	3,291,000	4,948,000	3,260,000	3,356,000	4,942,000
Retirement Expenditure	13,702,111	400,972	400,972	400,972	400,972	400,972	400,972	400,972	400,972	400,972	400,972	400,972
Total other Expenditure	1,447,067	2,375,609	5,593,774	2,813,954	2,091,151	6,069,992	3,187,000	2,058,000	6,573,000	2,621,000	5,426,000	3,880,000
<b>Total Expenditure</b>	<b>16,822,242</b>	<b>7,997,894</b>	<b>9,265,993</b>	<b>6,547,055</b>	<b>5,780,285</b>	<b>10,084,319</b>	<b>6,881,972</b>	<b>5,749,972</b>	<b>11,921,972</b>	<b>6,281,972</b>	<b>9,182,972</b>	<b>9,222,972</b>
<b>Net Cash Flow</b>	<b>(20,046,922)</b>	<b>(2,285,738)</b>	<b>(2,977,901)</b>	<b>(2,057,184)</b>	<b>1,209,466</b>	<b>4,783,538</b>	<b>9,268,194</b>	<b>(568,400)</b>	<b>(5,412,794)</b>	<b>6,740,210</b>	<b>7,121,593</b>	<b>4,393,873</b>
FY Cumulative Cash Flow	(20,046,922)	(22,332,661)	(25,310,562)	(27,367,746)	(26,158,279)	(21,374,741)	(12,106,547)	(12,674,947)	(18,087,741)	(11,347,531)	(4,225,938)	167,935
General Fund Balance	22,362,072	20,076,333	17,098,432	15,041,249	16,250,715	21,084,253	30,302,447	29,734,047	24,321,254	31,061,463	38,183,057	42,576,929

Projection includes \$2,000,000 annual increase in Property Tax and Sales Tax, per HDL forecast. Analysis adjusted CIP of \$3,935 million from July to December.

City of Costa Mesa - Safety Fire Plan  
 Side Fund Amortization Schedule @7.50%  
 Valuation at 6/30/2012

Date	Side Fund		Projected Payroll	Rate	Special Payment	Side Fund Balance	PROJECTION 1		PROJECTION 2		PROJECTION 3		
	Balance	Payment					Special Payment	Side Fund Balance	Payment	Special Payment	Side Fund Balance	Payment	Special Payment
6/30/2010	(22,950,635)	1,518,711			1,000,000	(23,918,230)	1,933,664	1,226,551	(23,691,679)	1,915,348	1,489,776	(23,428,454)	1,894,068
6/30/2011	(24,530,390)	1,568,069	w/ golden handshake		-	(23,707,232)	1,991,674	233,348	(23,249,332)	1,953,205	504,469	(22,717,307)	1,989,851
6/30/2012	(24,803,797)	1,661,369	12,768,459	13.012%	-	(23,420,263)	2,051,424	240,348	(22,727,558)	1,990,748	519,603	(21,838,381)	2,001,914
6/30/2013	(24,941,538)	1,826,662	10,295,027	17.741%	-	(23,049,822)	2,112,966	247,558	(22,120,515)	2,131,333	535,191	(20,865,439)	2,123,593
6/30/2014	(24,918,230)	1,881,462	10,513,535	17.896%	-	(22,587,788)	2,176,355	254,985	(21,314,755)	2,169,322	551,247	(19,677,312)	2,127,694
6/30/2015	(24,836,356)	1,937,905	10,828,941	17.896%	-	(22,025,379)	2,241,646	262,635	(20,401,526)	2,206,003	567,785	(18,379,286)	2,292,623
6/30/2016	(24,689,820)	1,996,043	11,153,809	17.896%	-	(21,353,054)	2,308,895	270,514	(19,373,894)	2,240,894	584,818	(16,795,872)	2,281,946
6/30/2017	(24,472,015)	2,055,924	11,488,424	17.896%	-	(20,560,662)	2,378,162	278,629	(18,224,899)	2,476,099	602,363	(15,087,228)	2,531,292
6/30/2018	(24,175,789)	2,117,602	11,833,076	17.896%	-	(19,636,981)	2,449,507	285,988	(16,737,504)	2,507,389	620,434	(12,973,836)	2,488,239
6/30/2019	(23,793,397)	2,181,130	12,188,069	17.896%	-	(18,570,051)	2,522,992	295,598	(15,097,503)	2,533,016	639,047	(10,727,967)	2,961,572
6/30/2020	(23,316,459)	2,246,564	12,553,711	17.896%	-	(17,346,911)	2,598,682	304,466	(13,299,063)	2,550,613	658,218	(7,803,723)	2,813,140
6/30/2021	(22,735,906)	2,313,960	12,930,322	17.896%	-	(15,953,558)	2,676,643	313,600	(11,338,361)	3,130,078	677,965	(4,794,312)	2,538,557
6/30/2022	(22,041,934)	2,383,379	13,318,232	17.896%	-	(14,374,873)	2,756,942	323,008	(8,620,396)	3,107,540	698,303	(1,823,550)	1,890,697
6/30/2023	(21,223,939)	2,454,881	13,717,779	17.896%	-	(12,594,530)	2,839,650	332,698	(5,712,262)	3,024,605			
6/30/2024	(20,270,460)	2,528,527	14,129,312	17.896%	-	(10,594,908)	2,924,840	342,679	(2,662,025)	2,760,047			
6/30/2025	(19,169,112)	2,604,383	14,553,191	17.896%	-	(8,356,987)	3,012,585		(0)				
6/30/2026	(17,906,513)	2,682,514	14,989,787	17.896%	-	(5,860,247)	3,102,962						
6/30/2027	(16,468,212)	2,762,990	15,439,481	17.896%	-	(3,082,546)	3,196,051						
6/30/2028	(14,838,599)	2,845,879	15,902,665	17.896%	-	(0)							
6/30/2029	(13,000,823)	2,931,256	16,379,745	17.896%	-								
6/30/2030	(10,936,694)	3,019,194	16,871,138	17.896%	-								
6/30/2031	(8,626,580)	3,109,769	17,377,272	17.896%	-								
6/30/2032	(6,049,256)	3,203,062	17,898,590	17.896%	-								
6/30/2033	(3,181,987)	3,299,154	18,435,548	17.896%	-								
6/30/2034	-	-	18,988,614	0.000%	-								
<b>Total Payments</b>		50,555,578								41,909,844			38,584,404
<b>Total Interest</b>		25,637,348					46,275,642			16,991,614			13,666,175
<b>Savings</b>							21,357,412			8,645,734			11,974,173
<b>Interest wage</b>							4,279,936						

