PARS Post Employment Benefit Trust Program

City of Costa Mesa

August 12, 2015

PUBLIC AGENCY RETIREMENT SERVICES
PARS
TRUSTED SOLUTIONS. LASTING RESULTS.

Current Retiree Health Care Landscape

Retiree Health Benefits

- City currently provides retiree health benefits for 362 employees
- In addition, there are 395 active employees that may one day qualify for retiree health benefits in the future assuming they meet plan eligibility requirements
- In 2014, the City paid $1.52 million in retiree benefit costs
- Retiree benefit costs will continue to rise over the next couple of decades
- All benefits are currently funded on a pay-as-you-go basis

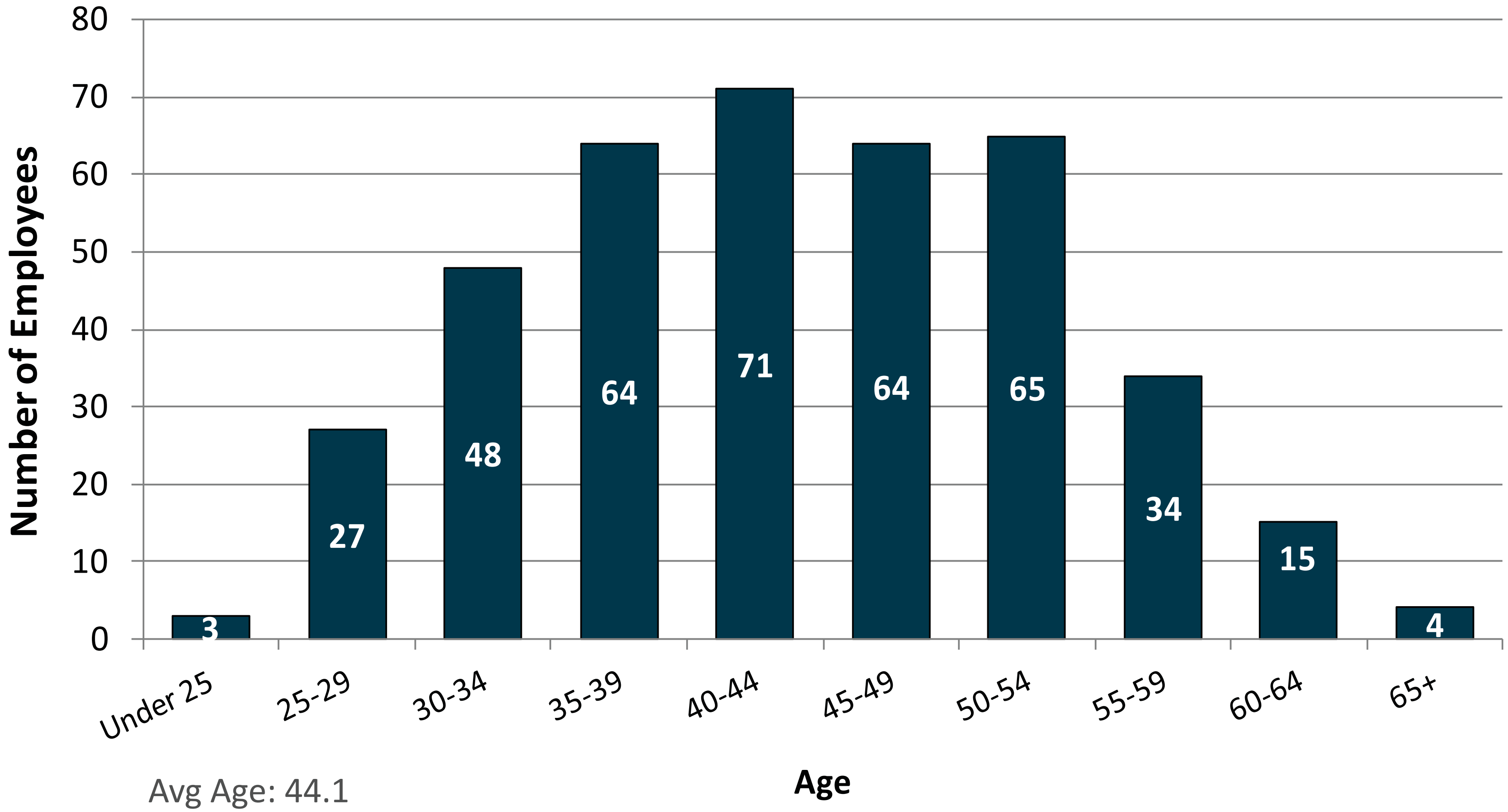
Retiree Health Liability

Valuation Date: June 30, 2014	Pay-As-You-Go Discount Rate: 4.50%
(A) Actuarial Accrued Liability (AAL)	$36,492,341
(B) Actuarial Value of Assets	$0*
(C) Funded Ratio (A/B)	0%

* As of June 30, 2014, City currently has $3,310,261 in reserves for OPEB. For GASB purposes, assets must be placed in an irrevocable trust fund to offset OPEB liabilities

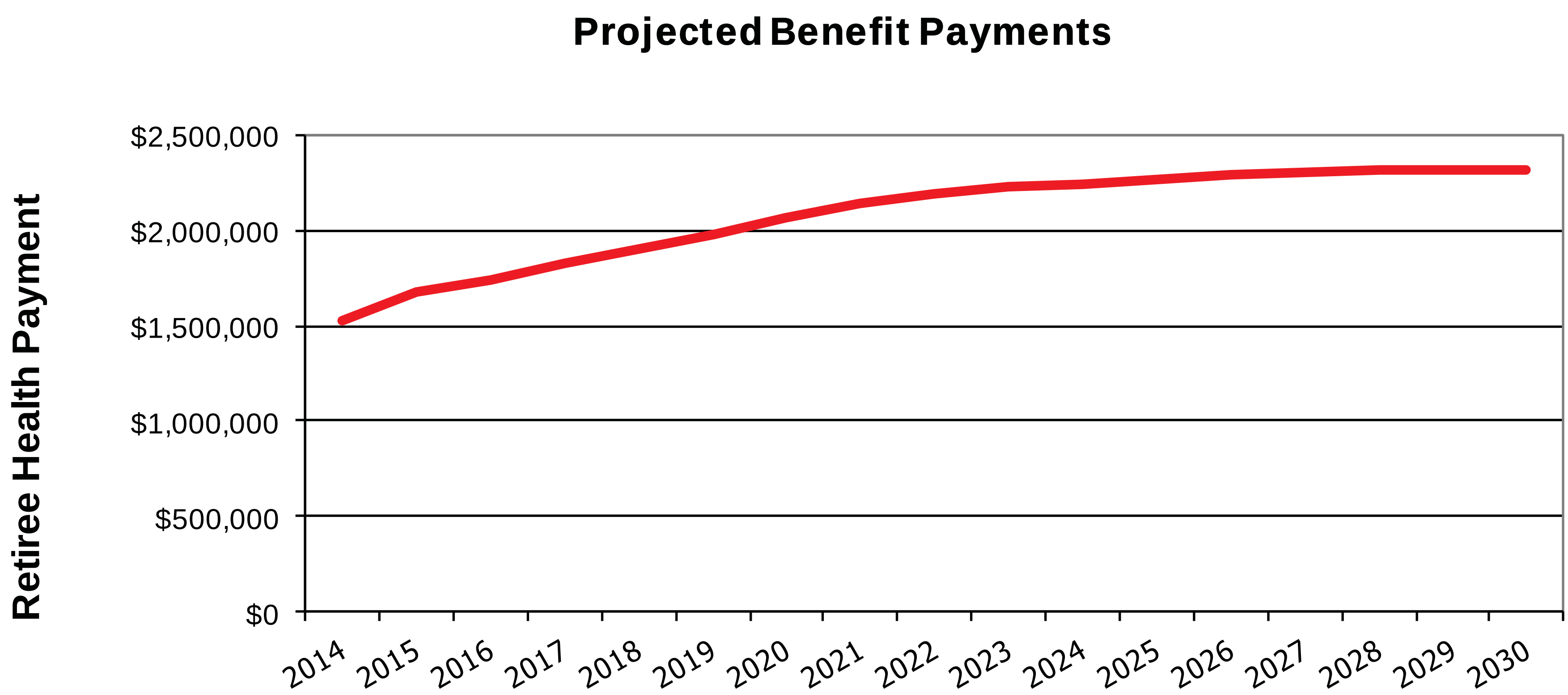
Demographic Overview

Age Distribution of 395 Active Employees



Avg Age: 44.1

Future Cost Trend



Why Pre-Fund your retiree health care obligations (OPEB)?

Advantages of Pre-Funding

Stabilized cost

- Funding over time prevents the growth of the City's unfunded liability

Benefit security for employees

- Assets in the trust provide employees with security that they will receive the benefit when promised

Investment flexibility (Govt. Code Section 53620)

- Since assets are held in trust outside the assets of the employer, diversified investment strategies may be utilized which may generate higher returns over time

Funding equity

- Avoids future generation of employees bearing a heavy burden for current/past generations

Credit implications

- Failure to provide funding may adversely impact the City's credit rating and ability to borrow

Advantages of Pre-Funding

Lower Liabilities on Financial Statements

- Contributions into the trust are “assets” that can offset liabilities on financial statements (GASB 75)
- Rule of Thumb: For every 1% increase in discount rate, you can lower your liabilities by about 10 - 12%

GFOA considers pre-funding as a “Best Practice”

- “Financing of postemployment benefits as they are earned (i.e., prefunding v. pay-as-you-go funding) offers significant advantages”

Prudent way to address a long-term benefit obligation

- Retiree health care obligations are no different than a pension plan obligations and should be funded in a similar way

Current Pension Landscape

CalPERS Pension Programs

- City maintains 3 CalPERS retirement Programs
  - Miscellaneous (66% funded as of 6/30/2013)
  - Fire Safety (66% funded as of 6/30/2013)
  - Police Safety (64% funded as of 6/30/2013)
- Plans have a combined asset value of $405 million
- Plans have a combined $218 million in unfunded liabilities
- In 2014, the City contributes approximately $16 million in contributions as required by CalPERS and approximately $2.6 million in City paid EPMC
- New GASB 68 requirements (beginning in FY 14-15) to disclose Net Pension Liability ($218 Million unfunded liability) on financial statements

New Alternative for Pre-Funding Pension and OPEB liabilities

Alternative to funding through CalPERS

- Previously, only way to reduce CalPERS unfunded pension liability was to send excess contributions in excess of annual required contribution
- In response to the lack of options, PARS has developed a Section 115 trust program to enable public agencies to pre-fund retirement and OPEB obligations through a locally controlled trust
- Plan has received a Private Letter Ruling (PLR) from the IRS
- Once contributions are placed into trust, assets from the trust can only be used for retirement benefit purposes

  - reimburse employer for CalPERS contributions
  - assets can be transferred to CalPERS at anytime
  - pay on-going retiree health obligations

What type of agencies are adopting the Section 115 Trust Program?

- Cities that are very concerned about reducing their CalPERS unfunded liability
- Cities that are concerned about CalPERS having too much of Costa Mesa's assets (i.e., putting all your eggs in one basket) without any input on risk tolerance level
- Cities that are concerned about CalPERS contribution volatility
- Cities that want to have the capability of pre-funding their OPEB and Pension Liabilities within the same Trust Program with contributions and distributions made at the City's discretion

Advantages of Using the PARS Program

- **Complete Local Control over Assets** - Account can be accessed at anytime as long as it is used to pay the employer's pension obligation
- **Pension rate stabilization** - Assets can be transferred to CalPERS plan at the City's direction, which will reduce or eliminate large fluctuations in Employer contributions to CalPERS
- **Rainy Day Fund -** Emergency source of funds when Employer revenues are impaired based on economic or other conditions
- **Lower Costs –** 115 Trust can have lower overall administrative and investment management costs compared to the CalPERS pension program (As of 13/14 CAFR, CalPERS has admin fees of $636 million and $1.34 billion in investment mgt fees ~ 66 bps)

Advantages of Using the PARS Program

- **Lower Net Pension Liability (NPL)** - Contributions placed in an exclusive benefit trust reduces City's unfunded pension liability
- **Investment Flexibility –** Investment oversight maintained by the City and can be tailored to the City's unique demographics and risk tolerance level
- **Improved Credit Ratings** – Rating agencies may look favorably upon actions to reduce liabilities
- **Actuarially Sound Retirement System** - Provide integrity and security for the source of funding for retirement benefits.

PARS Advantages

PARS Trust Team

	PUBLIC AGENCY RETIREMENT SERVICES PARS	usbank	HIGHMARK® CAPITAL MANAGEMENT
Role	Trust Administrator and Consultant • Recordkeeping/Sub-trust accounting • Actuarial Coordination •Monitor Contributions/ Process Disbursements • Monitor Plan Compliance • Ongoing Client Liaison •Pre-fund Pension Option	Trustee • Safeguard plan assets • Oversight protection • Plan Fiduciary • Custodian of assets	Investment Manager • An investment sub-advisor to U.S. Bank • Open architecture • Investment policy assistance
Corporate Experience	31 years *(1984 – 2015)*	152 years *(1863 – 2015)*	96 years *(1919 – 2015)*
Section 115 Trust Experience	19 years	10 years	19 years
Dollars under administration	More than $1.7 billion	More than $4 trillion	More than $5 billion under management
Office Location providing Services	Newport Beach, CA	Irvine, CA	Irvine, CA

WHY PARS?

1. Most experienced provider of **post-retirement health care trust in California** (started in 1996)
2. PARS received the **first ever IRS Private Letter Ruling** given for a multiple-employer Section 115 Trust to pre-fund both OPEB and pension liabilities
3. Provide OPEB and Pension pre-funding services for **170 agencies**, including the following nearby Orange County agencies:

- **California JPIA**
- **City of Fountain Valley**
- **City of Lake Forest**
- **Mesa Water District**
- **Municipal Water District of Orange County**
- **Orange County Vector Control District**
- **Orange County Water District**
- **South Orange County Wastewater Authority**
- **Orange County Superior Court**

WHY PARS?

4. **Widest range of investment options**: active or passive; model or custom
5. **Full service approach** – dedicated Senior Consultant and Portfolio Manager (has fiduciary responsibility; assists with investment policy statement; onsite reviews and cell phone access)
6. **Local Control** over plan design, investments, actuarial assumptions, sub-accounts

PARS INVESTMENT RETURNS COMPARED TO CALPERS CERBT

	3 Month	1-YEAR	3-YEAR	5-YEAR
PARS 115 Trust Returns	0.30%	3.65%	11.73%	11.77%
CalPERS CERBT Returns	-0.93%	-0.11%	9.79%	10.62%
Difference	1.23%	3.76%	1.94%	1.15%

- The following are the investment returns as of June 30, 2015 comparing the PARS Capital Appreciation strategy to CalPERS CERBT Strategy #1.
- Returns greater than 1 year are annualized

Implementation Steps

Step 1 Recommendation by committee to establish trust to address liabilities

Step 2 City Council authorizes establishment of a 115 Trust and appoints a Plan Administrator;

Step 3 PARS provide legal documents for signature by Plan Administrator

Step 4 Develop investment policy and guidelines for Investment Manager

- setting discount rate
- risk tolerance
- Active or Passive
- prohibited investments

Step 5 Develop policies and procedures for future annual contributions and/or disbursements

Step 6 Annual Review of Investment Performance

Contacts

PARS

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Dennis has worked for PARS since 1994 and is responsible for developing customized retirement plans, including supplemental and stand-alone retirement systems. He offers a wide range of technical expertise to agencies involved in plan design and implementation – particularly in developing complex financial models to address multi-faceted scenarios. He has been involved in the development of more than 300 PARS retirement plans. Dennis has also been a speaker at various conferences, including CalPELRA and NPELRA, on topics such as defined benefit design, early retirement incentives, post-retirement health benefits and options available to public agencies after the implementation of PEPRA.

Education:

Dennis has a Bachelor of Arts in Economics from the University of California, Irvine, where he graduated cum laude. He also completed an MBA at the Anderson School at UCLA as well as the Certified Employee Benefits Specialist (CEBS) designation and Certificated of Achievement in Public Plan Policy (CAPPP) through the Wharton School at the University of Pennsylvania and International Foundation of Employee Benefit Plans.