



City of La Habra

Pension Funding Policy

This City Council adopted policy is intended to provide guidance and strategies for current and future City Councils to address the City's retirement system obligations and liabilities. This document includes policy directives and financing mechanisms.

Purpose

The purpose of this Pension Funding Policy is to provide guidance on the development and of a funding plan for any Unfunded Accrued Liabilities ("UAL") that are calculated annually by CalPERS, or for any unfunded accrued liabilities remaining immediately after the issuance of a Pension Obligation Bond (POB). This funding Policy should also support the decision-making and budgeting process of the City Council and be consistent with the overall purpose and goals of the City of La Habra's operations and pension obligations.

Background

The City of La Habra has a history of being fiscally conservative and maintaining fiscally responsible management and budgeting practices. The City recognizes that unfunded CalPERS liability can cause financial stress on the organization and redirect resources away from programs and services vital to City operations. To better address this challenge, the City seeks to stabilize its unfunded CalPERS liability in the most cost-efficient manner possible.

CalPERS Normal Cost represents the cost of pension benefits earned by current employees in the current fiscal year. Normal Costs are paid as a percentage of the City's payroll. UAL represents unfunded benefits accumulated for employees' prior years' service, as well as costs related to changes in investment performance, employee/retiree events, benefit levels, and actuarial assumptions. UAL payments are fixed dollar amounts adjusted annually by CalPERS.

Remaining Unfunded Accrued Liability

On November 15, 2021, the City Council approved the issuance of a POB in an amount up to or equal of 100% of the UAL. After the deposit of bond proceeds to CalPERS, the City may or may not have a remaining UAL still owed to CalPERS.

If the City issues a POB for less than 100% of the UAL, any remaining unfunded liability will be accounted for separately, for the purposes of this Policy, from any new increase in the accrued unfunded liability resulting from future annual actuarial valuation report changes.

The City will create a payoff / funding plan that will address this remaining unfunded liability immediately after the issuance of the POB. The remaining unfunded liability will be paid off or fully funded within a twenty (20) year period.

New Unfunded Accrued Liability

Every year, CalPERS issues a new actuarial valuation report and recalculates the City of La Habra's pension liability as of the new valuation date. If the value of the funded assets is not equivalent to this new liability amount, the City will incur a new UAL at that point in time. The UAL may increase or decrease from year to year, due to the following factors:

- Changes in actuarial assumptions and experience changes (e.g., changes in the discount (or expected earnings) rate of the pension system, changes in salaries, plan participants, etc.)
- Changes in actuarial gains and losses due to asset returns being higher or lower than expected
- Changes in plan benefits

Due to the possibility of a new UAL forming over time, the City of La Habra desires to create a policy in order to immediately address any new pension liabilities, or amortization bases, that arise (any new increase or decrease in the liability resulting from the annual actuarial valuation is identified as a separate line item, or amortization base, on the annual CalPERS actuarial valuation report). The table below describes the parameters for paying off and/or funding the UAL within a designated timeframe, based on the amount of the UAL, as follows:

New Unfunded Accrued Liability (Any new liability incurred after the June 30, 2020 valuation report)	Payoff/ Funding Time Period
\$0 to \$1,000,000	Within 1 to 5 years
\$1,000,001 to \$2,000,000	Within 1 to 10 years
\$2,000,001 to \$3,000,000	Within 1 to 15 years
Over \$3,000,000	Within 1 to 20 years

When the City is provided the annual valuation report from CALPERS each year, staff will present the matter to the City Council as part of the Mid-Year Budget Report. Staff's presentation will include the following:

- The dollar amount of the new UAL (new amortization base)
- The number of years that staff is recommending to pay off/fund the liability
- The dollar amount of the annual contribution to be made
- The funding source(s) of the payments
- The short-term and long-term financial impacts on the City's General Fund or other reserve balances

When a new amortization base results in a credit balance, the credit will be applied first, to any negative bases during the same period and, secondly, against any prior year bases until the credit is fully exhausted. The remaining outstanding liability will then be recalculated and a new payoff schedule and annual contribution will be determined based on the payoff schedule above.

Section 115 Trust

The City established a Section 115 Pension Trust Fund in 2018 in order to set funding aside for the express purpose of paying for pension related costs. The trust assets can be accessed to pay down CalPERS UAL

balances or to fund normal costs at any time to reduce volatility and offset unexpected pension rate increases. The trust has funds deposited into it at the discretion of the City Council, based on the availability of funding and recommendations made by City staff during the annual budget adoption process. For the calculation of funding levels, monies put in this trust will be treated the same as putting monies on deposit with CalPERS.

Additional Discretionary Payments

Additional Discretionary Payments (“ADP”) may also be deposited with CalPERS at any time. After completion of the annual audit, all discretionary fund reserve balances will be reviewed by City staff. Based on any budgetary constraints at that time, a determination may be made that it is in the best interest of the City to use any available reserves or one-time savings from the prior fiscal year to make ADP’s. ADP’s should not adversely affect the general operations or capital needs of the City. ADP’s could be deposited with CalPERS, or invested in the City’s Section 115 trust.

Annual Set-Aside of 50 percent of Pension Obligation Bond Savings

Based on the results of the POB issuance, the City will realize an estimated savings of \$_____ in the first full fiscal year after the issuance of the debt. To further strengthen the City’s future financial stability, 50 percent of the first year cash flow savings amount, calculated at \$_____, will be budgeted on an annual basis for deposit into the City’s Section 115 PARS Pension Trust Fund. The purpose of this action is to accumulate funding that can be used to offset any potential future UAL obligations that may arise. This base savings amount shall be adjusted each year by the annual Consumer Price Index for All Urban Consumers, all items, 1982-84 equals 100, as published by the United States Department of Labor, Bureau of Labor Statistics, for the Los Angeles/Long Beach/Anaheim Area for the 20 year term of the bonds, and will be budgeted as a transfer into the City’s Section 115 Trust Fund each fiscal year.

Allocation of Additional Resources

The City seeks to maintain adequate levels of reserves, with the goal of 25 percent of each fiscal year’s adopted General Fund expenditure budget. To the extent that the City has excess reserves, the City shall endeavor to apply a portion of such monies toward its unfunded retirement costs in the form of either Additional Discretionary Payments to CalPERS directly, or deposit funds in either a designated reserve or in its PARS Section 115 Trust. This amount will be in addition to the set-aside of 50 percent of pension refinance savings.

Prepayment Options

Prior to the beginning of each fiscal year, staff will analyze the costs and benefits of prepaying amounts due to CalPERS for the following fiscal year and will pre-fund the annual required pension payments as funding permits. The City strives to continue taking advantage of any prepayment discount that is afforded by CALPERS.

Funding Levels

The City’s target funding level for its pension plans will be near 100 percent of the accrued liability. The City will strive to achieve this funding level through debt refinancing, allocation of reserves, and/or cost containment measures. The total funding amount will be a combination of the amount on deposit with

CalPERS, the funds deposited in the City's Section 115 trust, and any funds reserved by the City that are designated by Council for pension liabilities.

Funding Options

Funding options for the remaining unfunded liability and/or any new unfunded accrued liabilities may include the use of assets held in the City's Section 115 Trust and/or allocating fund reserves from any allowable fund within the City.

Consideration of Future Pension Benefits

The issuance of a POB may result in the funding of the City's pension plan with CalPERS up to, and even in excess of, 100 percent of the plan assets necessary to pay all pension liabilities. Although this situation may occur, the City would remain obligated to make annual debt service payments on the bonds. These payments are in lieu of annual UAL payments that the City would have made to CalPERS at the time the bonds were issued.

To the extent that the City is making any annual debt service payments on an issued POB, it is fiscally responsible for the City to not offer any enhanced pension benefits to City employees. This will allow the City to focus its financial resources on its current operations and services to the community, its pension obligations to CalPERS, and its debt obligations to bondholders.