San Diego County Taxpayers Association
Taxpayers watchdog since 1945
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An Update and Comparison of the Region's Upcoming Pension Costs

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Summary

Fourteen of 17 cities in San Diego County will see an increase in pension payments in the upcoming fiscal year[1], their total pension debt stands close to **$800 million** and the annual costs per household are as high as **$573**, according to a new analysis by the **San Diego County Taxpayers Association** (SDCTA or Association).

The new analysis is in stark contrast to last year's report, which saw reduced pension costs in 10 of the 17 cities. Next fiscal year (FY 2015), cities can expect to see even greater increases to their unfunded liabilities due to CalPERS experiencing a 0.1 percent rate of return on its investments in FY 2012.

According to SDCTA's latest analysis, the cities that will see the largest increases in their pension costs in FY 2014, which begins this July, are:

- Coronado – 9 percent increase
- Lemon Grove – 9 percent increase
- Del Mar – 6 percent increase

The top cities on the other end of the spectrum are:

- Solana Beach – 7 percent decline in pension costs
- Escondido – 1 percent decline
- Vista – 0.1 percent decline

Analyzing pension costs between cities on a per household basis shows Del Mar taxpayers shoulder the largest burden, with each household paying $573 and responsible for over $3,000 of the massive unfunded pension debt. Imperial Beach has the lowest pension costs per household, with each household paying $92 and responsible for just under $500 in the unfunded pension debt.

This report is based off of each city's actuarial pension valuation for FY 2011, which outlines the costs to be paid in FY 2014. Cities were asked to confirm current benefits offered to employees to ensure accuracy.

[1] This analysis of pension costs assumes each city utilizes the Annual Lump Sum Prepayment Option offered by CalPERS.

Background

The 17 cities analyzed in this report are members of the **California Public Employees' Retirement System** (CalPERS), which recently released its annual pension valuations for the 2011 fiscal year. Those valuations dictate each city's pension payment for fiscal year 2014, which begins July 1. SDCTA's analysis does not include the City of San Diego because its employees are in separate pension system. The Association has released a series of reports examining the region's government employee pension plans, focusing on the impact upon local governments' budgets. In June 2009, SDCTA issued a study with formal recommendations on pension reform for the 17 incorporated cities enrolled in CalPERS.

The Association also developed a Pension Certification Program to educate public officials, civic leaders and members of the news media on the complex issues encompassing local government retirement benefits.

This annual report examines what taxpayers can expect their respective cities to pay in pension costs for the upcoming fiscal year. Despite many reforms implemented at the local level, including cities eliminating the subsidization of employee pension costs and introducing lower cost pension benefits to new employees, costs have increased. Increases in unfunded liabilities due to underperforming investments are a primary driver of increased costs.

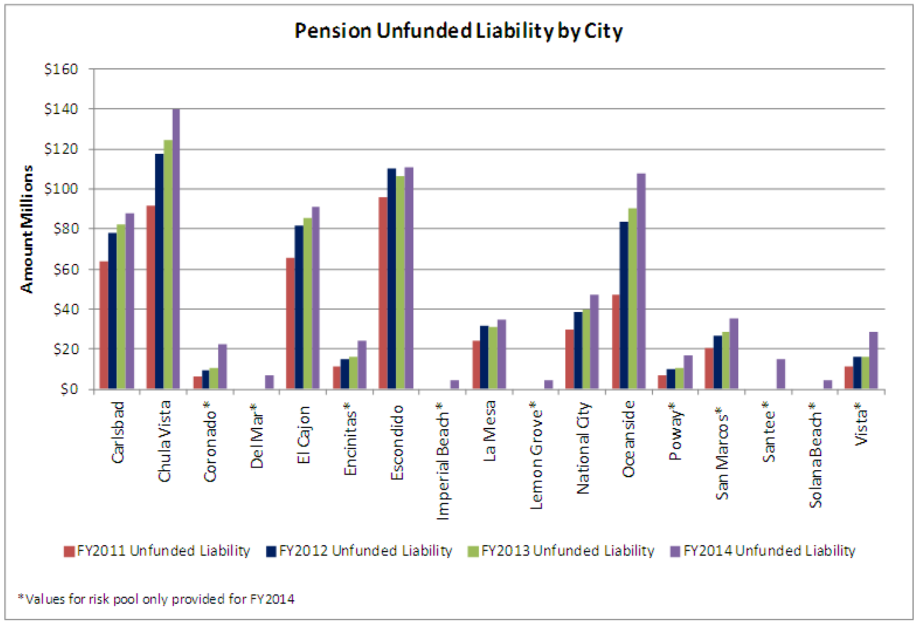
It's also important to note that Governor Jerry Brown signed Assembly Bill 340 late last year. The California Public Employees' Pension Reform Act of 2013, which most notably outlines reforms for new employees hired by cities enrolled in CalPERS, includes mandating adoption of a new lower cost level of pension benefits for new hires, requiring new employees share in pension costs and redefining what type of compensation is "pensionable."[2]

CalPERS recently issued a letter outlining their interpretation of "pensionable compensation" as allowed under the reform law. Within their letter, CalPERS states a number of additional premium pays, such as various educational pays and bilingual pay, can be included in an employee's salary when calculating pension earnings. This interpretation could potentially eliminate future savings for cities that would have been generated if pensionable compensation was limited to base pay alone, and not any other specialty or premium pays.

[2] Please refer to SDCTA Backgrounder: Review of California Public Employees' Pension Reform Act of 2013 for more information.

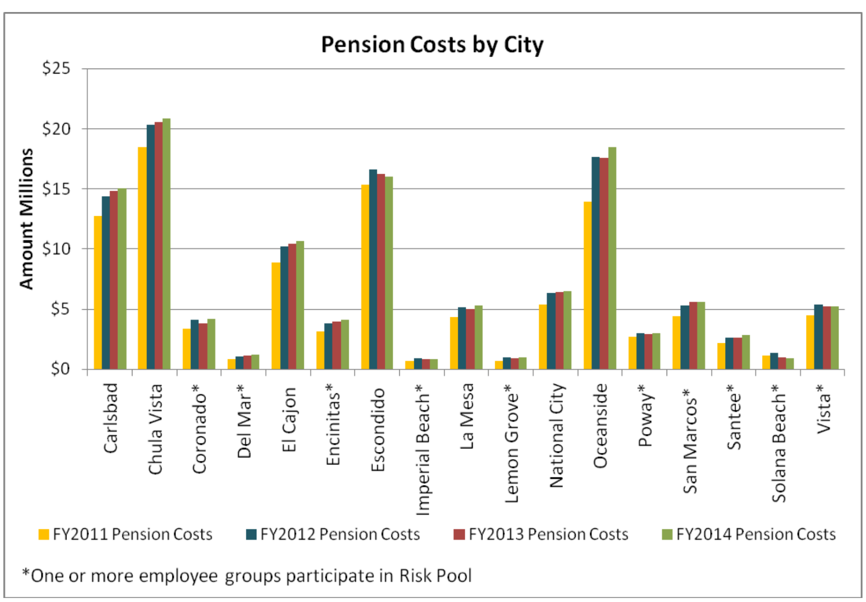
Findings:

Unfunded Liabilities by the Numbers
Some cities can expect to see an increase in pension costs for the upcoming fiscal year due to an increase in unfunded liabilities. An **unfunded liability** occurs when factors such as investments and employee costs do not match assumptions made by CalPERS to forecast costs. For example, if investment returns are lower than expected, or salary increases are greater than expected, an unfunded liability is created. The total amount of the unfunded liability is not paid all at once, but rather in annual payments set by CalPERS. Increases in the unfunded liability and the resulting increases in annual payments place greater pressure on municipal budgets that are already stressed.



While some cities have implemented significant reforms in an effort to reduce annual pension costs, actuarial assumption changes made by CalPERS have led to an increase in unfunded liabilities for cities for the upcoming year. Last year, CalPERS reduced its expected rate of return from 7.75% to 7.5%. This decision increased the unfunded liability of each city. CalPERS decided the resulting cost increase of this reduction will be paid for over two years as opposed to the cost being paid in one year.

In the most recent pension fund valuations, CalPERS began identifying the unfunded liabilities for risk pool cities – cities with a minimal amount of employees that pool their multiple plans in order to share the risk of investment returns. The total unfunded liability for all cities stands at **$787.5 million**.



Between FY 2013 and FY 2014, the **City of Oceanside** held the largest increase in its reported unfunded liability – 19.1%, followed by **National City** at 18.5% and **La Mesa** at 12.8%. No cities saw a decrease in their unfunded liability. Risk pool cities in which unfunded liabilities have been presented for the first time cannot be measured since those amounts were not displayed in previous years.

In FY 2015, cities can expect to see even greater increases to their unfunded liabilities due to CalPERS experiencing a 0.1% rate of return on their investments in FY 2012. These costs will be outlined in SDCTA's next report in early 2014.

Annual Required Contributions by the Numbers
All but three cities within the county will see an increase in their **Annual Required Contribution (ARC)** payments for FY 2014. This is due in part to increases in each city's unfunded liability. Cities may have also hired new employees or increased salaries which also contribute to the increase in pension costs.

For the upcoming year, the cities of **Coronado**, **Lemon Grove** and **Del Mar** will see ARC payment increases of 9.4%, 8.7% and 6.3%, accordingly. The **City of Solana Beach** will see the largest decline in its pension cost at 6.9%. The cities of **Escondido** and **Vista** will see slight declines in pension costs at 1.1% and 0.1%, respectively. In the case of Solana Beach, reductions in the number of employees and payroll, as well as the introduction of a lower tier pension plan for new non-safety employees led to a decline in pension costs. Both Escondido and Vista experienced declines in the number of payrolls and thus a small lowering of their respective ARCs.

While examining the ARC is one way to measure pension costs, comparing **employer contribution rates** allows for the comparison of pension costs between cities. The employer contribution rate is the cost held by each city to provide the pensions benefit as a percent of payroll, and it includes both the normal cost of the benefit and the payment on the unfunded liability. In other words, for every dollar a city contributes toward compensation, it also contributes a percentage of that amount determined by the employer contribution rate for employee pension plans.

Table 1 highlights the cities with the five highest contribution rates.

Table 1: Most Expensive Pension Plans for FY 2013			
Safety Employees		***Misc. Employees***	
City	**Contribution Rate**	**City**	**Contribution Rate**
Del Mar (Fire)	52.49%	Santee	33.09%
National City	38.01%	El Cajon	27.41%
El Cajon	37.53%	Chula Vista	25.44%
Escondido	34.49%	San Marcos	25.28%
Carlsbad	33.92%	Escondido	25.15%
Source: FY 2011 CalPERS Actuarial Valuations			

Costs by Household

Another way to compare costs between cities is on a per household basis. While the nominal dollar amounts each city is paying toward pensions may not seem relatively high when compared to others, when analyzed on a per household basis, we can gain an understanding of how much each household is contributing toward pension costs via their tax dollars – similar to a household budget.

While **Del Mar** is paying only $1.1 million for employee pensions next year, each household would need to contribute more than $3,000 of their tax dollars toward their city's unfunded pension bill if the debt is required to be paid off immediately. While this is not the case, we are able to track over time whether this amount increases or decreases as a measurement of pension costs within the city.

Next year, each household in Del mar is paying $573 toward their city's annual pension bill. This is an amount that must be paid for the fiscal year beginning July 1. Again, this is another measurement tool to evaluate pension costs within each city. Del Mar's unfunded liability and pension cost per household is over 500 percent higher than the lowest city in the county, **Imperial Beach**. Imperial Beach has both the lowest pension cost and unfunded liability per household for the upcoming fiscal year.

Table 2: Evaluation by Population		
City	**FY2014 Unfunded Liability Per Household**	**FY2014 Annual Pension Cost Per Household**
Del Mar	$3,331	$573
National City	$3,059	$419
Coronado	$2,992	$565
El Cajon	$2,664	$313
Escondido	$2,431	$353
Carlsbad	$2,129	$363
Chula Vista	$1,850	$276
Oceanside	$1,822	$312
La Mesa	$1,422	$215
San Marcos	$1,310	$205
Encinitas	$1,193	$169
Poway	$1,053	$185
Vista	$976	$179
Solana Beach	$814	$158
Santee	$789	$146
Lemon Grove	$558	$116
Imperial Beach	$489	$92
Sources: 2010 Census and FY 2011 Actuarial Valuations		

Have Cities Made Reforms?

Many cities have adopted lower pension benefits for newly hired employees. A lower level of benefits allows cities to reduce future retirement costs for their employees. Depending on the implementation of each city's reforms, it may take some time before the effects will be realized and included in each actuarial valuation completed by CalPERS.

Table 3 is a list of cities that have adopted a lower level of benefits for all employees, some employees and no employees (additional information on these cities and the respective benefit formulas is available upon request). As mentioned previously, beginning January 1, 2013 new employees are to be enrolled in lower tier retirement benefits. The resulting savings of these new benefit tiers will not be realized for some time though.

CalPERS requires that employees contribute a certain amount of their pay to their pension plan. However, cities have been allowed to **"pick up"** a portion or the entire employee share of the employees' pension costs. In doing so,

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each city that has done so has increased the pension burden to taxpayers and its budget.

Table 3: Cities with Lower Benefit Levels for New Employees		
All Employees	**Some Employees**	**No Employees**
Poway	El Cajon	Coronado
La Mesa	Oceanside	Vista
San Marcos	Lemon Grove	
Carlsbad		
Santee		
Solana Beach		
Chula Vista		
Del Mar		
Imperial Beach		
Escondido		
National City		
Encinitas		
Source: Memoranda of Understanding for CalPERS Cities		

Table 4: City Share of Pick-Up Rates - 2012 and 2013				
City	**2012**	**2013**	**2012**	**2013**
	Safety Employees	**Safety Employees**	**Misc Employees**	**Misc Employees**
Carlsbad	0%	0%	0-3.5%	0-3.5%**
Chula Vista	0%	0%	0%	0%
Coronado	0%	0%	0%	0%
Del Mar	0-2.5%*	0%	0%	0%
El Cajon	4%*	0%	4%*	0%
Encinitas	0-6%	0-6%*	8%	0%
Escondido	0-9%	0%	0-7%	0%
Imperial Beach	0-4.5%	0%	0%	0%
La Mesa	0%	0%	0%	0%
Lemon Grove	0%	0%	0%	0%
National City	0-4%*	0%	0%	0%
Oceanside	0-5%	0%	0%	0%
Poway	0-1%	0%	0%	0%
San Marcos	0%	0%	0%	0%
Santee	5%	5%	4%	4%
Solana Beach	0%	0%	0%	0%
Vista	0-1%	0-1%*	0%	0%
**Notes Labor contract eliminates pick-up in future years*				
*** Notes employee group with pick-up currently in contract negotiations*				
Source: Memoranda of Understanding for CalPERS Cities				

Since the release of our first pension report in 2009, a number of cities have implemented reforms and reduced the pick-up amount of employee pension costs. Table 4 outlines the changes to the pick-up by each city since the last report released in 2012. Once current labor contracts expire, employees will be required to pay at least half of the normal cost, while cities will be prohibited from paying a portion of the employee share of pension costs. Cities were asked to confirm all information provided in Tables 3 and 4 to ensure accuracy.

The pension plan picture is incomplete till one views the **funding status** of the plan.

The funding status measures how "on track" the pension plan is with respect to how much is available to pay for the benefits promised to employees. Losses in the market and increases in benefits contribute to the drop in the funding status of each city's pension plan. Table 5 depicts the funding status of each city.

Table: 5 FY 2013 Funding Status for Pension Plans (Actuarial Value of Assets)		
City	**Safety Employees**	**Miscellaneous Employees**
Carlsbad	81.1%	79.6%
Chula Vista	85.6%	75.5%
Coronado	88.3%	80.2%
Del Mar	Fire: 78.4% Lifeguard: 90.3%	76.6%
El Cajon	76.5%	78.5%
Encinitas	Fire: 89.6% Lifeguard: 89.6%	74.3%
Escondido	82.8%	77.5%
Imperial Beach	Fire: 88.3% Lifeguard: 88.1%	85.2%
La Mesa	84.1%	81.6%
Lemon Grove	82.7%	76.4%
National City	76.0%	84.9%
Oceanside	86.6%	80.7%
Poway	88.3%	84.3%
San Marcos	82.9%	67.5%
Santee	87.3%	82.0%
Solana Beach	Fire: 88.3% Lifeguard: 88.3%	Tier 1: 85.5% Tier 2: 93.5%
Vista	81.3%	83.2%
Source: FY 2011 CalPERS Actuarial Valuations		

Conclusion

Even though many cities have made reforms, all cities are seeing increases in their unfunded pension liability. **Oceanside** and **National City** will see large increases in their unfunded liabilities, **19 percent** and **18 percent** respectively. Both **Coronado** and **Lemon Grove** will see a **9 percent** increase in their annual pension costs for the new fiscal year beginning July 1. Looking at pension costs based on households, **Del Mar** homeowners will pay the most this year and **Imperial Beach** homeowners will pay the least.

Though the increased costs might not cause severe budget limitations, elected officials should be aware that in FY 2015 cities should expect to see additional increases in unfunded liabilities as a result of much lower than expected investment returns by CalPERS.

Since SDCTA's first pension report in 2009, cities across the county have implemented a number of reforms in an effort to reduce costs. Some cities, however, such as **Coronado** and **Vista**, have not yet adopted lower-cost benefit plans for newly hired employees. In addition, **Santee** is still continuing to subsidize a large portion of the employee's share of pension costs. While cities have begun the process of implementing reforms to reduce pension costs, reforms under AB 340 will be required to be implemented once current labor contracts expire. It will take some time though for savings from these reforms to be realized.

SDCTA recommends cities limit pensionable compensation strictly to base pay, as was adopted under Proposition B in the City of San Diego. Despite the initial interpretation of "pensionable compensation" by CalPERS, SDCTA believes individual cities can negotiate, and if necessary impose, a more strict definition of "pensionable compensation" as was outlined under Proposition B and was the spirit of the law signed by the governor. This will allow for reduced pension costs for employees that have yet to be hired, thus reducing future costs to cities and taxpayers.

*The **San Diego County Taxpayers Association** is a non-profit, non-partisan organization, dedicated to promoting accountable, cost-effective and efficient government and opposing unnecessary taxes and fees. Founded in 1945, SDCTA has spent the past six decades saving the region's taxpayers billions of dollars, as well as generating information to help educate the public.*

Table 6: Comparison of Pension Costs and Unfunded Liabilities Among CalPERS Cities

City	FY2013 Total Contribution	FY2013 Unfunded Liability	FY2014 Total Contribution	FY2014 Unfunded Liability	Contribution Increase as a percentage	Increase in Unfunded Liability as a percentage
Carlsbad	$14,824,377	$82,655,795	$15,012,254	$88,032,688	1.27%	6.51%
Chula Vista	$20,551,946	$124,310,652	$20,809,418	$139,726,604	1.25%	12.40%
Coronado*	$3,823,320	$10,843,757	$4,183,084	$22,170,725	9.41%	-
Del Mar*	$1,112,746	$0	$1,183,124	$6,874,170	6.32%	-
El Cajon	$10,415,533	$85,748,690	$10,683,319	$90,918,890	2.57%	6.03%
Encinitas*	$3,948,210	$16,171,755	$4,075,851	$24,274,377	3.23%	-
Escondido	$16,232,270	$106,593,692	$16,046,768	$110,585,642	-1.14%	3.75%
Imperial Beach*	$813,037	$0	$841,270	$4,453,419	3.47%	-
La Mesa	$5,017,117	$30,901,599	$5,265,043	$34,858,617	4.94%	12.81%
Lemon Grove*	$902,246	$0	$980,555	$4,706,708	8.68%	-
National City	$6,413,726	$39,999,513	$6,501,153	$47,414,751	1.36%	18.54%
Oceanside	$17,583,576	$90,643,055	$18,464,163	$107,949,532	5.01%	19.09%
Poway*	$2,891,705	$10,846,900	$2,987,831	$16,980,017	3.32%	-
San Marcos*	$5,573,861	$28,301,761	$5,581,048	$35,631,932	0.13%	-
Santee*	$2,650,133	$0	$2,813,751	$15,230,682	6.17%	-
Solana Beach*	$956,928	$0	$890,990	$4,601,177	-6.89%	-
Vista*	$5,264,308	$16,410,858	$5,258,359	$28,624,197	-0.11%	-

**Total FY 2013 unfunded liability for all employee groups not available*

Source: FY 2010 & FY 2011 CalPERS Actuarial Valuations