



FILED
OFFICE OF THE CITY CLERK
OAKLAND

2019 JAN 18 AM 9:06 **AGENDA REPORT**

TO: Sabrina B. Landreth
City Administrator

FROM: Katano Kasaine
Director of Finance

SUBJECT: OPEB Funding Policy

DATE: January 7, 2019

City Administrator
Approval

Date

1/17/19

RECOMMENDATION

Staff Recommends That The City Council Adopt A Resolution Adopting The Other Post-Employment Benefits Funding Policy Of The City Of Oakland.

EXECUTIVE SUMMARY

The attached study titled, "Other Post-Employment Benefits (OPEB) Funding Analysis and Policy" (**Attachment A**) was jointly prepared by independent consultants PFM Group Consulting LLC (PFM) and Cheiron, Inc. in response to the City Council's request for the development of a plan to address the City of Oakland's (City) significant OPEB unfunded liabilities. The report provides significant detail on the challenges facing the City, benchmarks the benefits provided to City employees against regional and other large public employers, and provides a financial framework for achieving a more sustainable retiree health benefits program over a long-term period.

The City's current approach to funding OPEB is not sustainable even with recent reforms from the Police and Fire. It is critical that the city adopt a policy to address the problem of rising OPEB liabilities because pay-as-you-go is not a sustainable option long-term. OPEB funding policy and progress are becoming increasingly important among the factors that rating agencies (Moody's, Standard and Poor's and Fitch Ratings) use to evaluate a City's long-term fiscal capacity and creditworthiness. A large OPEB obligation and no policy in place to sufficiently address the unfunded liabilities is view as a credit weakness to rating agencies. A lower credit rating could result in higher borrowing costs to the City and limits the access to the credit market.

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Below are some highlights of the challenges of funding retirement costs from ratings reports issued specific to City of Oakland in 2018:

Moody's Investors Service, "City of Oakland, CA, Update to Credit Analysis" (April 19, 2018)

- *"Oakland has a large unfunded OPEB liability of \$860.0 million, an exceptionally high 238.3% of covered payroll, as of the July 1, 2015 actuarial valuation date."*
- *"Factors that could lead to a downgrade: Inability to manage retirement costs."*

S&P Global Ratings, "Summary: Oakland, California; Appropriations; General Obligation" (April 20, 2018)

- *"In our opinion, a credit weakness is Oakland's large pension and OPEB obligation, without a plan in place that we think will sufficiently address the obligation."*

In addition, by adopting the proposed policy will address some key concerns outlined in the Final Report of the FY 2017-18 Alameda County Grand Jury.

- *"The city of Oakland currently has no meaningful plan to address its...unfunded OPEB liability, jeopardizing the city's long-term financial viability..."*
- *The city of Oakland must develop and implement a long-term comprehensive plan to address its... unfunded OPEB liability.*
- *Any long-term OPEB plan must include discussion of additional city funding and substantial structural change in benefits that are responsible for these growing liabilities."*

Based on the recommendations of the independent consultants, Staff developed the "City of Oakland Other Post-Employment Benefits (OPEB) Funding Policy" (the "OPEB Funding Policy") which is included as **Attachment B**, herein. If adopted by City Council, the recommended City of Oakland OPEB Policy provides the City with a balanced plan, as called for by the rating agencies and Alameda County Grand Jury, to place the OPEB program on a sustainable path toward stable funding

BACKGROUND LEGISLATIVE HISTORY

Resolution No. 87208 C.M.S., which was approved by the City Council on May 29, 2018, directed the City Administrator to develop an OPEB Funding Policy for the City Council's consideration.

ANALYSIS AND POLICY ALTERNATIVES

A detailed analysis of the OPEB funding challenge is included in **Attachment A**, which was prepared jointly by PFM and Cheiron, Inc. with input from Staff. The report culminates in an OPEB Funding Policy that was developed by Staff based on independent consultants' recommendations as **Attachment B, herein**. Key components of the OPEB Funding Policy are summarized below and are further expanded in the PFM-Cheiron report:

Program Objectives

- **Affordable** in the near-term, without crowding out the City's capacity to deliver quality services to the public or to provide reasonable salary increases to active employees;
- **Sustainable** over the long-term, ensuring that benefits will be secure and reliable for career employees throughout retirement, with substantial intergenerational equity for taxpayers in regard to the funding of benefit costs; and,
- **Competitive**, to support effective recruitment and retention of a strong municipal workforce.

Funding Goals

- Maintain a stable or increasing ratio of trust assets to accrued liabilities, with the goal of reaching a 100percent funded ratio (full funding) for all explicit subsidy benefits.
- Develop a pattern of stable and regular contribution rates when expressed as a percentage of member payroll as measured by valuations prepared in accordance with the principles of practice prescribed by the Actuarial Standards Board.
- Manage the cost of benefits through labor-management partnership and collective bargaining to reach and maintain an affordable and sustainable level of coverage.

Benefit Program

- The recommended OPEB Funding Policy affirms that specific benefit structures will be subject to collective bargaining for represented employees.
- Within this context, the OPEB Funding Policy calls for regular reviews of the City's retiree healthcare benefits relative to offerings among other Bay Area governments and large California cities.
- As retiree healthcare benefits are periodically reviewed and renegotiated, the OPEB Funding Policy also sets forth the following principles as guidelines for pursuit of any adjustments:

- Until the City's OPEB Trust is fully funded, the affordability and sustainability of the City's retiree medical benefits offerings would be evaluated on the basis of whether the City's actuarially determined contribution (ADC) for explicit subsidy benefits can be fully funded with a combination of full pay as you go ("pay-go") funding plus a supplemental employer contribution of no higher than 2.5percent of payroll.
- Periodic adjustments to benefits will be pursued as required to ensure full funding and plan sustainability. If the ADC for explicit subsidy benefits exceeds pay-go costs plus a supplemental City payment of 2.5percent of payroll, then the City would seek to negotiate approaches to modify benefits to close this sustainability gap. Among the potential approaches for closing this gap, the City may pursue retiree benefit modifications and/or contributions toward future OPEB coverage from active employees.

OPEB Funding Policy for Sustainable Benefits

- At a minimum, the OPEB Funding Policy reaffirms that the City will fully fund its "pay-go" commitments to eligible retirees and beneficiaries for the benefits they receive each year.
- Until the Trust is 100percent funded for explicit subsidy benefits, however, the OPEB Funding Policy calls for City to make contributions in excess of the annual pay-go cost for current retirees and beneficiaries toward achieving full funding, as outlined below:
 - Beginning in FY 2019-20, the City would contribute an additional 2.5percent of payroll above pay-go into the OPEB Trust on an annual basis.
 - If the sum of annual pay-go costs plus the supplemental 2.5percent of payroll contribution is less than the ADC for explicit subsidy payments in that same year, then the City would seek to negotiate benefit and/or employee contributions sufficient to close this sustainability gap.
 - In addition to the above annual contributions, the City would continue to make further one-time contributions to the OPEB Trust consistent with the Consolidated Fiscal Policy, when Excess Real Estate Transfer Tax (RETT) thresholds are met. This approach will help to build OPEB funding more rapidly, thereby improving plan stability and reducing future contribution requirements.
- **In the event of a severe economic downturn, the City would seek to continue the above payment structure in full. If certain revenue decline thresholds as defined in the recommended OPEB Funding Policy are met, however, and if authorized via Council Resolution, the City could temporarily reduce or defer its supplemental payments above pay-go until the City's revenues have recovered.**

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Projected Results

If adopted by City Council, the recommended OPEB Funding Policy provides the City with a balanced plan, placing the OPEB program on a sustainable path toward stable funding.

Based on projections by Cheiron, Inc. using assumptions consistent with the City's current actuarial valuations and the proposed OPEB Funding Policy, this approach is projected to achieve the following progress:

- The OPEB Funding Policy would be projected to build the City's overall OPEB funded ratio steadily from 3.0percent in FY 2018-19 to approximately 25.0percent within a decade, and to over 50.0percent in less than 20 years.
- The OPEB Funding Policy would increase the City's funded ratio for the explicit subsidy component of the OPEB liability from 4.0percent in FY 2018-19 to more than one-third funded within a decade, to over 75.0percent funded within 20 years, and to full funding in less than 25 years.
- With additional resources from any Excess Real Estate Transfer Tax transfers under the Consolidated Fiscal Policy and/or further negotiated benefit adjustments, full funding could potentially be reached even sooner.

Given that the City's current OPEB funding shortfall has been decades in the making, such steady progress toward achieving true sustainability, improved affordability, and continued benefit competitiveness would represent a meaningful plan and positive fiscal stewardship

FISCAL IMPACT

Adoption of the proposed resolution and the OPEB Funding Policy (Attachment B) will require the City to contribute an additional 2.5% of payroll above pay-go into the OPEB Trust on an annual basis until the liability associated with the explicit subsidy is fully funded, commencing in FY 2019-2020. This additional contribution would be set aside in the City's irrevocable OPEB Trust through the California Employers' Retiree Benefit Trust (CERBT). As the OPEB Funding Policy expresses the City's OPEB trust contribution as a percentage of salary, the amount contributed to the CERBT would fluctuate based upon staffing levels and wage growth in future years.

PUBLIC OUTREACH / INTEREST

No outreach was deemed necessary for this informational report beyond the standard City Council agenda noticing procedures. As part of the development of the report and recommended OPEB Funding Policy, City Staff and outside consultants met with all of the City's bargaining units, the Budget Advisory Commission, and various other City leadership.

COORDINATION

This report and resolution has been prepared by the Finance Department in coordination with Human Resources Management Department. Staff in Finance Department worked with the Human Resources Management Department in developing the OPEB Funding Policy.

SUSTAINABLE OPPORTUNITIES

Economic: There are no economic opportunities associated with this item.

Environmental: There are no environmental opportunities associated with this item.

Social Equity: There are no social equity opportunities associated with this item.

ACTION REQUESTED OF THE CITY COUNCIL

Staff Recommends That The City Council Adopt A Resolution Adopting The Other Post-Employment Benefits Funding Policy Of The City Of Oakland.

For questions regarding this report, please contact Adam Benson, Budget Administrator, at (510) 238-2026.

Respectfully submitted,



KATANO KASAINÉ
Director of Finance

Reviewed by:
David Jones, Treasury Administrator

Prepared by:
Adam Benson, Budget Administrator

Attachment (2):

- (1) Attachment A - Other Post-Employment Benefits (OPEB) Funding Analysis and Policy
- (2) City of Oakland Other Post-Employment Benefits (OPEB) Funding Policy

FILED
OFFICE OF THE CITY CLERK
OAKLAND

OAKLAND CITY COUNCIL

Macanlay
City Attorney

2019 JAN 18 AM 9:00 RESOLUTION No. _____ C.M.S.

Introduced by Councilmember _____

RESOLUTION ADOPTING THE OTHER POST-EMPLOYMENT BENEFITS FUNDING POLICY OF THE CITY OF OAKLAND

WHEREAS, the City of Oakland ("City") has three programs in place to partially pay health insurance premiums for certain classes of retirees from City employment meeting certain requirements relating to age and service pursuant to labor agreements between the City and local unions and in City resolutions; and

WHEREAS, beginning in the fiscal year ending June 30, 2018, the City must recognize the Other Post-Employment Benefits ("OPEB") unfunded liabilities in its Comprehensive Annual Financial Report due to the implementation of Governmental Accounting Standards Board Statement No. 74 and 75; and

WHEREAS, the City's current pay-as-you-go ("pay-go") funding approach for OPEB is not financially sustainable over the long-term; and

WHEREAS, Resolution No. 87208 C.M.S., which was approved by the City Council on May 29, 2018, directed the City Administrator to develop an OPEB Funding Policy for the City Council's consideration; and

WHEREAS, an OPEB Funding Policy provides guidance to the City Council by establishing pre-funding targets that will improve the long-term viability of the retiree health benefit program; now, therefore be it

RESOLVED: That the City of Oakland OPEB Funding Policy, in substantially the form attached to the staff report accompanying this resolution, is hereby approved and adopted; and be it

FURTHER RESOLVED: That this Resolution shall take effect immediately upon its passage.

IN COUNCIL, OAKLAND, CALIFORNIA, _____

PASSED BY THE FOLLOWING VOTE:

AYES - FORTUNATO BAS, GALLO, GIBSON MCELHANEY, KALB, REID, TAYLOR, THAO, AND PRESIDENT KAPLAN

NOES -

ABSENT -

ABSTENTION -

ATTEST: _____
LaTonda Simmons
City Clerk and Clerk of the Council
of the City of Oakland, California