



# City of Richmond Draft Budget, Five-Year Forecast, Pension Update – Cost Management Strategies Fiscal Year 2023-2024

June 6, 2023

Shasa Curl, City Manager

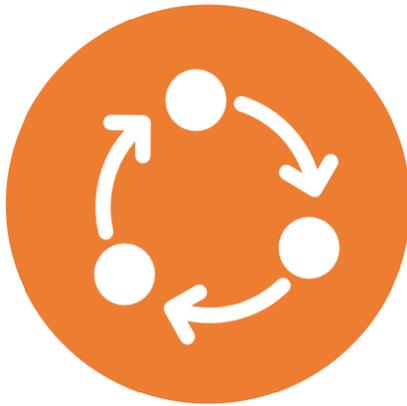
Nickie Mastay, Deputy City Manager

Mubeen Qader, Deputy Director of Finance

Antonio Banuelos, Accounting Manager

NHA Advisors

# Organizational Priorities



Day-to-Day Operations



Corrective Action Plan



New Council Requests



New Council Policy  
Direction

# Recommended Action

RECEIVE an update on the draft FY 2023-2024 Annual Operating Budget and FY2023-2028 Five-Year Capital Improvement Plan Budget; and RECEIVE DIRECTION from City Council prior to final budget adoption

# Questions?



Councilmembers may contact Lilia Corral at **510.620.6787** ([lilia\\_corral@ci.richmond.ca.us](mailto:lilia_corral@ci.richmond.ca.us)) to schedule meetings with the City Manager and Finance staff to review and discuss inquiries pertaining to the budget

# Overview

- FY2023-24 Budget Development Key Dates
- General Fund Revenue Assumptions
- Draft General Fund Revenue Budget
- General Fund Expenditure Assumptions
- Draft General Fund Expenditure Budget
- General Fund Operating Transfers Out
- Additional Appropriations (General Fund & Non-General Fund)
- Economic Development/Port Capital Projects
- Pending Budgetary Items
- State Audit-Corrective Action Plan - Five Year Financial Forecast
- State Audit-Corrective Action Plan-CalPERS Update-Cost Management Strategies
- Next Steps

# FY2023-2024 Budget Development -Milestones

ACTION / ACTIVITY	DATE
Budget Kick-Off Meeting	January 26
Budget Input Window	January 30 thru February 26
Budget Hearings:	March 13 thru March 23
Community Budget Meetings	April 10, 17, & 20
Union Budget Meeting	April 28
Study Session First Draft Budget	May 2
Economic Analysis (Beacon & GovInvest)	May 16
City Council Goal Setting Sessions	May 22, May 31, June 15
Second Draft Budget	June 6
Council to adopt FY 2023-24 Operating Budget, 5 Year Capital Improvement Plan, and GANN Limit	June 20
Adopted FY2023-24 budget available in MUNIS	July 1

# Budget Envelope

	FY 2022-23	FY 2023-24	FY 2023-24	PCT
GENERAL FUND	REVISED BUDGET	MAY 2, DRAFT BUDGET	JUNE 6, DRAFT BUDGET	CHANGE (Between FY 22-23 and 6/6/23 FY 23-24 budgets)
TOTAL REVENUES	(215,103,041)	(221,330,130)	(225,374,607)	4.78%
TOTAL EXPENDITURES	215,139,689	221,330,130	225,374,607	4.76%
NET (-SURPLUS)/+DEFICIT	36,648	-	-	-100.00%



# General Fund Revenue Assumptions

Revenue	Assumption
PROPERTY TAXES	Assuming 3.3% growth for secured, and other streams flat, using YTD actuals (not budgeted amount)
SALES & USE TAX	Using Avenue Consulting Sales Tax (Regular, two voter approved, and Prop 172) forecast models and reducing by amount paid to City of El Cerrito
UTILITY USERS TAX	Using % estimates from Avenue, coupled with YTD amounts from current fiscal year.
OTHER TAXES	UUT amounts for gas and Electricity, Cable, and Telecommunications based on projected FY23 revenues times growth in Avenue Consulting forecast. Operation based on the formula in RMC and estimate of CPI change with actual postings through May (June CPI posting pending).
LICENSES,PRMITS&FEES	Main item is Business Tax at \$10.5M - which is the expected base going forward. Estimate is based on gross receipts payments received YTD which corresponded to both calendar years 2022 and 2023.
FINES & FORFEITURES	Based on YTD amounts.
USE OF MONEY&PROPRTY CHARGES FOR SERVICES	Flat, based on YTD actuals. If interest rates and cash balances remain high, this could be revisited.
OTHER REVENUE	Decrease from budgeted amount but in line with YTD actuals and flat from there.
RENTAL INCOME	Other revenue is unpredictable. Budgeted amounts are department's best estimates.
INTERGOV STATE TAXES	Terminal 4 Lease (\$80k) moved from GF Port Fund
INTERGOV STATE GRANT	Flat - only item is Motor Vehicle Fees
INTERGOV OTHER GRANT	Flat - main item is State Mandated Costs Reimbursement
PROC FR SLE PROP	Flat - Only grant is Supplemental Law Enforcement
LOAN/BOND PROCEEDS	No surplus property planned for sale
OPER XFERS IN	Flat - based on CY actuals
	PTORS - AV Growth of 3.3% plus adjustments to the new 2022 Bond Schedule - leftover funds get rolled to GF

# Draft General Fund Revenues

GENERAL FUND	FY 2022-23 REVISED BUDGET	FY 2023-24 JUNE 6, DRAFT BUDGET	PCT CHANGE
Property Taxes	(48,608,929)	(50,567,173)	4.03%
Sales & Use Tax	(55,554,137)	(56,752,495)	2.16%
Utility Users Tax	(50,861,279)	(55,775,083)	9.66%
Other Taxes	(22,452,187)	(23,237,723)	3.50%
Licenses, Permits & Fees	(11,080,956)	(13,286,195)	19.90%
Fines & Forfeitures	(465,275)	(331,144)	-28.83%
Use Of Money & Property	(1,021,047)	(1,011,535)	-0.93%
Charges For Services	(3,568,792)	(2,561,992)	-28.21%
Other Revenue	(192,545)	(238,480)	23.86%
Rental Income	(874,506)	(777,028)	-11.15%
Intergovernmental State Taxes	(125,000)	(125,000)	0.00%
Intergovernmental State Grant	(175,000)	(110,000)	-37.14%
Intergovernmental Other Grant	(263,569)	(250,000)	-5.15%
Proceeds From Sale of Property	(100,000)	-	-100.00%
Loan/Bond Proceeds	(39,400)	(40,400)	2.54%
Operating Transfers-In	(19,720,418)	(20,310,358)	2.99%
<b>Total Revenues</b>	<b>(215,103,041)</b>	<b>(225,374,607)</b>	<b>4.78%</b>

# General Fund Expenditure Assumptions

Expenditures Category	Assumptions
Salaries and Wages	Approved MOUs for Fire L188, Police and Local 1021. Estimated costs for pending MOUs for Fire and Police Management, Executives, and Local 21.
Payroll Fringe Benefits	Healthcare costs at current rates as of FY 2022-23, Other Post-Employment Benefits per current Actuarial report, Retirement rates per current CalPERS rates. Worker's Comp rate 3.35 percent overall decrease in rates.
Professional and Admin Services	Baseline budget plus \$5.5 million for additional appropriations including an inflation factor of \$761K
Other Operating	Baseline budget with one-time appropriations removed plus an inflation factor of \$258K
Utilities	Baseline budget plus an inflation factor of \$257K
Equipment & Contract Services	Baseline budget based plus an inflation factor of \$130K
Provision for Insurance Loss	Insurance Premiums
Cost Pool (Vehicle Replacement)	Fleet Services provided list with prioritized items (draft - the budget will change)
Cost Pool (General Liability)	Pending final calculations (draft - the budget will change)
Cost Pool (Cost Allocation Plan - Admin Charges)	Unchanged pending new Cost Allocation Plan (draft - the budget may change)
Cost Pool (Civic Center Debt Allocation)	Charge derived from the debt service, cash balance, and square footage used by divisions
Asset Capital Outlay	As needed
Debt Service Expenditure	Based on the Debt Service Schedule
A87 Cost Plan Reimbursement	Based on the Cost Allocation Plan - Admin Charges
Grant Expenditures	Based on the awarded grants
Operating Transfer Out	Recurring and one-time subsidies to non-General Fund programs.

# Draft General Fund Expenditures

<b>GENERAL FUND</b>	<b>FY 2023-2024 REVISED BUDGET</b>	<b>FY 2023-2024 JUNE 6, DRAFT BUDGET</b>	<b>CHANGE</b>
Salaries and Wages	76,715,696	83,858,736	9.11%
Payroll/Fringe Benefits	66,846,458	64,156,480	-3.35%
Professional & Administrative	20,043,782	23,693,762	16.74%
Other Operating	6,954,201	7,029,392	1.08%
Utilities	5,387,756	5,286,750	-1.87%
Equipment & Contract Services	2,718,982	2,853,891	4.96%
Provision For Insurance Loss	29,641	32,200	8.63%
Cost Pool	15,277,766	21,777,297	42.54%
Asset/Capital Outlay	5,756,590	1,642,500	-71.47%
Debt Service Expenditures	1,037,009	841,353	-18.87%
A87 Cost Plan Reimbursements	(3,531,610)	(3,531,611)	0.00%
Grant Expenditures	117,990	19,155	-83.77%
Operating Transfers-Out	17,785,428	17,714,702	-0.40%
<b>Total Expenditures</b>	<b>215,139,689</b>	<b>225,374,607</b>	<b>4.76%</b>

# General Fund Operating Transfers Out

Debt Service	4,849,954
Hilltop Lighting and Landscaping District	235,988
Marina Bay Lighting and Landscaping District	476,309
Employment and Training (draft – will revise before adoption)	736,201
Information Technology Equipment Replacement	100,000
Department of Children and Youth	6,453,091
Richmond Housing Authority (draft – will revise before adoption)	1,261,082
Pension Fund	152,077
Reimagining Public Safety -Unhoused Intervention	1,320,000
Reimagining Public Safety -Youthworks	1,980,000
Rent Program General Liability Subsidy	150,000
<b>Total</b>	<b>17,714,702</b>

# General Fund Additional Appropriations

- **Economic Development (\$135,000)**
  - \$135,000 -- Increased contribution by \$45,000 to NAID, Richmond Art Center, and East Bay Performing Arts Center (total \$100,000 each)
- **City Manager (\$5,000)**
  - \$5,000 -- Increase funding for part-time student administrative intern to assist with City Council and City Manager directed priorities as required
- **Library (\$50,500)**
  - \$25,000 -- The library has experienced considerable turnover in staff and leadership and would like to offer staff trainings and workshops focused on workstyles, diversity and inclusion, and support effective communication, and emotional intelligence to ensure a professional and collegial work environment to maintain focus on community needs and service delivery. The requested funds will be used for professional services of consultants and trainers to address these departmental needs
  - \$25,500 -- The strategic planning process will raise community awareness of existing library services and direct the library's future investment in programs, services, and materials

# General Fund Additional Appropriations (Continued)

- **Recreation (\$326,992)**

- \$47,355 -- Additional resources and supplies to meet the need of in-person enrollment for the community to prepare for enhanced programming and extended hours at the community centers.
- \$50,008 -- Additional funds will be required to restore programs (youth soccer, basketball, tennis and volleyball, adult softball, outdoor adventure activities).
- \$36,959 -- Part-time staff for the Developing Personal Resources Center (DPRC)
- \$42,993 -- Part-time staff for the following special events: Chinese New Year, Black History Experience, Senior Info Day, Third of July, and Tree Lighting.
- \$29,309 -- Additional staff required due to enhanced precautionary measures in place for rescue scenarios at the swimming pools (as advised by American Red Cross and other CA and regional public pool operators)
- \$9,300 -- Postage for mailing additional Community Services program guides.
- \$40,000 -- Allocation of \$2,000 for each neighborhood council for community events and festivities. The budget would help activate and empower the councils, engage residents, and build community.
- \$71,068 -- Administrative Student Intern(s) to provide ongoing support for neighborhood councils and volunteer services as well as complete special projects related to volunteer services and community outreach.

# General Fund Additional Appropriations (Continued)

- **Fire (\$491,200)**

- \$2,000 -- General employee's overtime for special projects that need to be completed in a timely manner such as billing businesses after engine/truck company program inspections (mercantile, apartment)
- \$17,200 -- Acting pay of line personnel (Suppression) to fill vacant roster assignments, to meet the minimum staffing requirements, and to support the department's strategic goal of providing safer communities through fire and medical response coverage to the community
- \$10,000 -- The cost for plan reviews by third party needs to be outsourced to expedite the review process for FY23-24. It will allow the Fire Marshal and Deputy Fire Marshal to focus on the additional responsibilities as both have been assigned to perform due to the current staffing ratio. Completing plan reviews are vital to ensuring that new constructions and tenant improvements in the City are compliant with fire codes
- \$1,500 -- Public educational materials (e.g., junior fire hats, stickers, pamphlets) for community and school events
- \$16,000 -- Maintenance, diagnostic, and repair of chest compression devices and AED defibrillators.
- \$2,000 -- Fire apparatus (APD) and boat (PRISM) insurance due to the increase in premiums.
- \$2,000 -- HAZMAT registration fee which was previously funded by a grant
- \$14,500 -- Office of Emergency Services CERT supplies
- \$8,800 -- Firecom/DC headset replacement, wildland/structure nozzles, and rescue materials (MPD and Ropes)

# General Fund Additional Appropriations (Continued)

- **Fire (Continued)**
  - \$260,700 -- The Fire Department intends to conduct another fire academy in FY23-24 to fill future vacancies due to anticipated promotions. The additional funding will be used to buy new personal protective equipment for firefighter trainees and replacement of expired turnouts, and medical supplies.
  - \$8,500 -- Small equipment such as generators and portable lights used by the Emergency Operations division.
  - \$120,000 -- The Fire Department plans to conduct another series of promotional examinations (Battalion Chief, Fire Engineer, and Fire Inspector), and background investigations, (New Hires) in FY23-24. Part of the funds will be used for fire fighter's medical exam and screening.
  - \$28,000 -- The additional appropriation will be used by the Training Division: for (a) EMS Training due to the decrease in overall EMS funding from Chevron Community Benefit fund and HAZMAT grant.
- **Public Works (\$127,800)**
  - \$36,000 -- Overtime budget in Streets Maintenance division
  - \$7,000 -- Updated tools are needed to increase the efficiency and safety of traffic signs and lines installations.
  - \$32,000 -- Overtime budget to support Police Department at the Bart Station
  - \$2,900 -- Stationary Engineers training and travel for asbestos and swimming pool certification. Personnel training for all 4 modules of APWA advance management skills in public works.
  - \$9,900 -- Small tools, supplies, and materials
  - \$40,000 -- Carpenters and Painters, building materials

# General Fund Additional Appropriations (Continued)

- **Police (\$893,505)**

- \$125,005 -- Animal control agreement cost increase
- \$110,000 -- Police station lease increase
- \$253,500 -- Maintenance for Automated License Plate Reader.
- \$50,000 -- RPD entered a contract with RippleWorx to provide officers and non-sworn staff with a mental health application to monitor and provide improvement solutions to the users.
- \$180,000 -- RPD entered a contract with Public Safety Family Counseling Group to provide officers and non-sworn staff with specialized law enforcement counseling services provided by a physician aimed at mental health improvements and support. The amount requested is the amount due annually.
- \$100,000 -- Increase in training and ammunition supplies to account for the hiring of 30+ positions.
- \$50,000 -- Rental expenses to account for the hiring of 30+ positions.
- \$25,000 -- New speed trailer to address over speeding in the City

- **Information Technology (\$3,039,978)**

- \$3,039,978 -- Software replacement, network security, and other costs, final list pending to be finalized

# Non-General Fund Additional Appropriations

- Housing, \$250,000 -- Financial consultants to support 12th & Macdonald project and Home-key program for homeless housing.
- Housing, \$1,200 -- Amerinational Loan Service expense
- Housing, \$500,000 -- CalHome Loan Housing Improvement Loan Program
- Planning & Building, \$2,300,000 -- Pass through environmental impact review planning projects
- Planning & Building, \$750,000 -- Consultant to implement Priority Development Area grant program
- Planning & Building, \$450,000 -- Pass through legal services for planning projects
- Planning & Building, \$10,000 -- Additional legal notice requirement for Planning projects

# General Fund FY 2023-24 Budget

	FY 2022-23	FY 2023-24	FY 2023-24	PCT
GENERAL FUND	REVISED BUDGET	MAY 2, DRAFT BUDGET	JUNE 6, DRAFT BUDGET	CHANGE (Between FY 22-23 and 6/6/23 FY 23-24 budgets)
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**MQ0** Revenue and expenditure

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# Economic Development/Port Capital Projects

DESCRIPTION	LOCATION	TOTAL	FY24	FY25	FY26	FY27	FY28
Area FM CAP	-	924,842	924,842				
Terminals 7 and 8 Electrification	PPMT	1,700,000	1,700,000	-	-	-	-
Terminal 4 Demolition	T4	2,500,000	2,500,000				
Terminal 4 Wharf Removal	T4	2,687,316	2,687,316				
PPMT Electrical and Water Metering	PPMT	365,000	365,000				
Processing Building Window Repair	PPMT	350,000	350,000				
Electrical Maintenance	PPMT	200,000	60,000	30,000	35,000	35,000	40,000
Pavement Maintenance	PPMT	765,000	150,000	150,000	150,000	155,000	160,000
Riggers Loft Painting	PPMT	285,000	285,000				
Processing Building Ventilation	PPMT	55,000	55,000				
OU1 and OU2 Monitoring	PPMT	370,000	70,000	72,000	74,000	76,000	78,000
General Warehouse Monitoring	PPMT	80,000	25,000	15,000	10,000	18,000	12,000
Terminals 7 and 8 Dredging	PPMT	1,265,000	65,000		1,200,000		
Yacht Entrance Harbour Dredging	Channel	845,000	45,000	800,000			
	<b>TOTAL</b>	<b>12,392,158</b>	<b>9,282,158</b>	<b>1,067,000</b>	<b>1,469,000</b>	<b>284,000</b>	<b>290,000</b>

# Pending Budgetary Items

- **Fleet Analysis** :The equipment and vehicle replacement budget is a placeholder as City staff continue to develop a five-year equipment/vehicle replacement plan and Zero Emission Fleet Infrastructure Ten-Year Transition Plan. Upon completion of the plans, the budget will be revised for the next fiscal year and will also change based on the prioritized list of the equipment/vehicle.
- **Paving Index**: the City's average Pavement Condition Index (PCI) was fair (60), and the City needs \$22.9 million annually to maintain the PCI at 60.
- **Risk Reserve**: The City's General Liability and Workers Compensation rates are draft and aspire to gradually increase towards achieving an 80 percent confidence level over approximately five years. However, the final rates for General Liability and Workers Compensation are pending completion of the Matrix Consulting analysis and further review.

# **State Audit- Corrective Action Plan Five Year Financial Forecast**

# State Audit – Corrective Action Plan

## Five-Year Financial Forecast

On April 4, 2022, the City of Richmond was notified by the California State Auditor that they will be conducting an audit of the City as approved by the Joint Legislative Audit Committee on June 30, 2021. Richmond's risk assessment was conducted in February 2021 based upon the City's June 2020 financial statements.

At the conclusion of the audit, the State Auditors formalized 11 recommendations. The first recommendation regarding the Five-Year Financial Forecast was described as follows:

*“Richmond should include multiple scenarios in its financial projections, including scenarios with potential additional risks, such as economic downturns or recessions, and how the city would continue to fund its operations under those circumstances.” (California State Auditor’s 2021-806-Audit)*

# Five-Year Financial Forecast-Revenue Assumptions

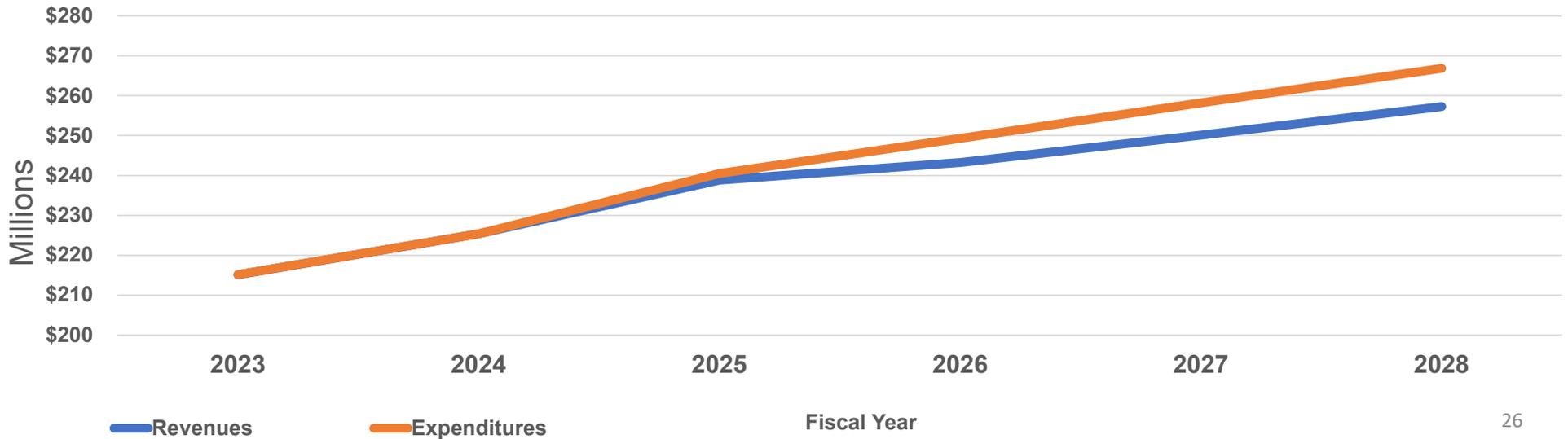
General Fund Revenues	FY24-25	FY25-26	FY26-27	FY27-28	FY28-29	FY29-30
30 - PROPERTY TAXES	5.04%	3.97%	5.12%	5.77%	5.98%	4.02%
31 - SALES & USE TAXES	6.03%	4.28%	3.03%	2.52%	2.56%	2.80%
32 - UTILITY USERS TAXES	2.26%	1.52%	0.96%	0.85%	0.53%	0.51%
33 - OTHER TAXES	15.42%	8.14%	9.63%	7.68%	6.31%	4.27%
33 - TRANSFER TAXES	15.42%	8.14%	9.63%	7.68%	6.31%	4.27%
34 - BUSINESS TAXES	12.57%	6.76%	2.50%	4.78%	2.41%	3.52%
34 - LICENSES, PRMITS & FEES	12.57%	6.76%	2.50%	4.78%	2.41%	3.52%
35 - FINES & FORFEITURES	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
36 - USE OF MONEY&PROPRTY	-1.14%	0.00%	0.00%	0.00%	0.00%	0.00%
37 - CHARGES FOR SERVICES	1.50%	1.50%	1.50%	1.50%	1.50%	1.50%
38 - OTHER REVENUE	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
39 - RENTAL INCOME	14.80%	2.00%	2.00%	2.00%	2.00%	2.00%
3A - INTERGOV STATE TAXES	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
3B - INTERGOV FED GRANT	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
3C - INTERGOV STATE GRANT	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
3D - INTERGOV OTHER GRANT	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
60 - PROC FR SLE PROP	0.00%	0.00%	0.00%	0.00%	0.00%	2.00%
61 - LOAN/BOND PROCEEDS	0.00%	0.00%	0.00%	0.00%	0.00%	2.00%
90 - OPER XFERS IN	3.05%	-8.95%	2.41%	2.46%	2.46%	2.51%
<b>TOTALS</b>	<b>6.64%</b>	<b>2.42%</b>	<b>3.33%</b>	<b>3.29%</b>	<b>3.75%</b>	<b>2.51%</b>

# Five-Year Financial Forecast-Expenditure Assumptions

	FY 23-24	FY 24-25	FY 25-26	FY 26-27	FY 27-28
<b>Universal Growth Rates (Personnel Costs)</b>					
Salaries & Wages	Proposed Budget	MOU	3%	3%	3%
Benefits	Proposed Budget	MOU	3%	3%	3%
CalPERS Normal Cost	PERS Rates	PERS Rates	PERS Rates	PERS Rates	PERS Rates
CalPERS Unfunded Liability	CalPERS	GovInvest	GovInvest	GovInvest	GovInvest
<b>Non-Personnel Costs</b>					
Pessimistic Scenario	Proposed Budget	0%	3%	3%	3%
Middle of the Road Scenario	Proposed Budget	0%	3%	3%	3%
Optimistic Scenario	Proposed Budget	2%	4%	4%	5%

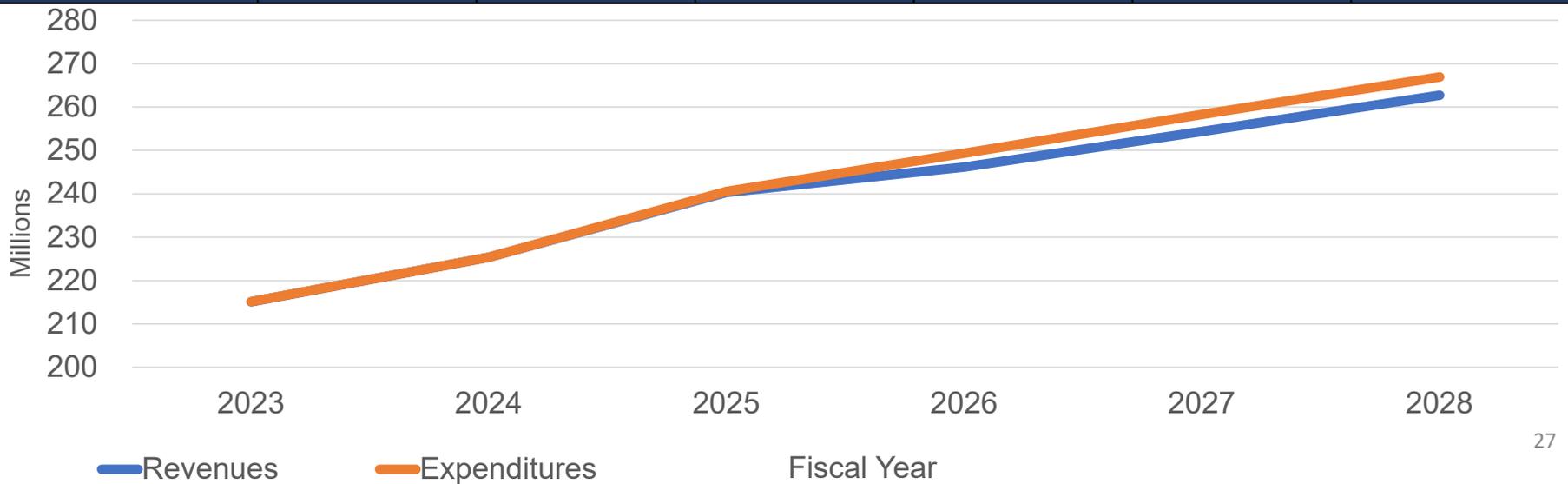
# Five-Year Financial Forecast – Pessimistic Scenario

	2023	2024	2025	2026	2027	2028
Revenues	215,103,041	225,374,607	238,843,933	243,243,012	250,092,434	257,279,354
Expenditures	215,139,687	225,374,607	240,503,329	249,276,243	258,213,985	266,846,849
Surplus/(Deficit)	(36,647)	-	(1,659,396)	(6,033,231)	(8,121,551)	(9,567,495)



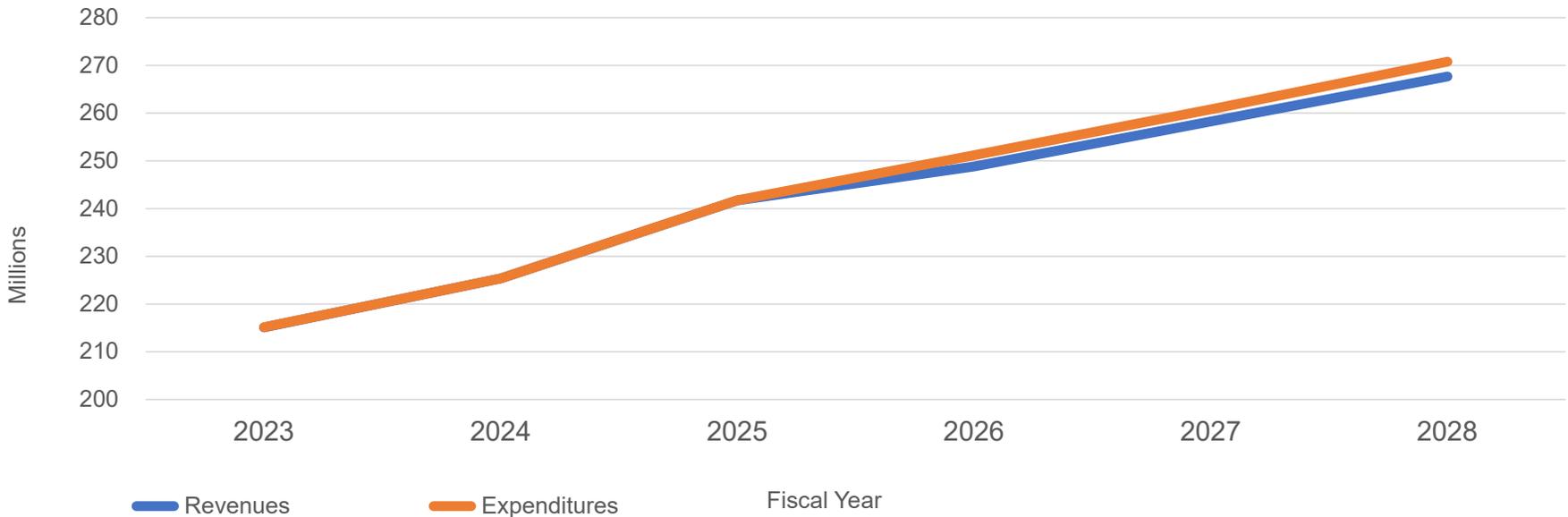
# Five-Year Financial Forecast – Middle of the Road Scenario

	2023	2024	2025	2026	2027	2028
Revenues	215,103,041	225,374,607	240,336,167	246,144,984	254,347,132	262,707,395
Expenditures	215,139,687	225,374,60	240,574,735	249,349,990	258,290,142	266,925,489
Surplus/(Deficit)	(36,647)	-	(238,567)	(3,205,006)	(3,943,009)	(4,218,095)



# Five-Year Financial Forecast - Optimistic Scenario

	2023	2024	2025	2026	2027	2028
Revenues	215,103,041	225,374,607	241,697,698	248,791,175	258,227,107	267,656,166
Expenditures	215,139,687	225,374,607	241,742,538	251,148,408	260,761,915	270,759,775
Surplus/(Deficit)	(36,647)	-	(44,841)	(2,357,232)	(2,534,808)	(3,103,608)



**State Audit - Corrective Action Plan  
Pension Update  
Cost Management Strategies**



CITY OF

*Richmond* CALIFORNIA

# CALPERS UNFUNDED ACCRUED LIABILITY (UAL) COST MANAGEMENT STRATEGIES DISCUSSION

**NHA | ADVISORS**  
Financial & Policy Strategies.  
Delivered.

JUNE 6, 2023

## Executive Summary

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- ▶ City of Richmond has a projected \$381.5M CalPERS Unfunded Accrued Liability (UAL)
  - ▶ Reflects -7.5% CalPERS investment returns in FY 2022, which will increase the UAL from \$248.6M
- ▶ City also has \$154M of outstanding Pension Obligation Bonds (POBs)
- ▶ City has historically taken proactive steps toward managing pension costs
  - ▶ **Annual UAL Prepayment Discount:** City captures annual UAL prepayment benefit ( $\approx$  3.3% discount)
  - ▶ **2022 Pension Refunding Bonds:** City restructured prior POBs & eliminated interest rate swaps
  - ▶ **Section 115 Trust:** Established in 2022
  - ▶ **Educational Presentations:** Two in 2022 (NHA), GovInvest (May 2023) and ongoing
- ▶ Presentation tonight will build off the recent GovInvest presentation made to City Council in May 2023 to include:
  - ▶ Discussion of Pension Tax Override Revenue (PTORS) and 2022 POBs in addition to the CalPERS UAL
  - ▶ Cost Management Strategies: Section 115 Trust, UAL Pay Down and UAL Restructuring
  - ▶ Pension Funding Policy Considerations

#### Historical PERS Returns

5-Year: 10.3%

10-Year: 8.5%

20-Year: 6.9%

30-Year: 8.4%

## Background: Why CalPERS Costs have Trended Higher

### Then (late 1990s)...

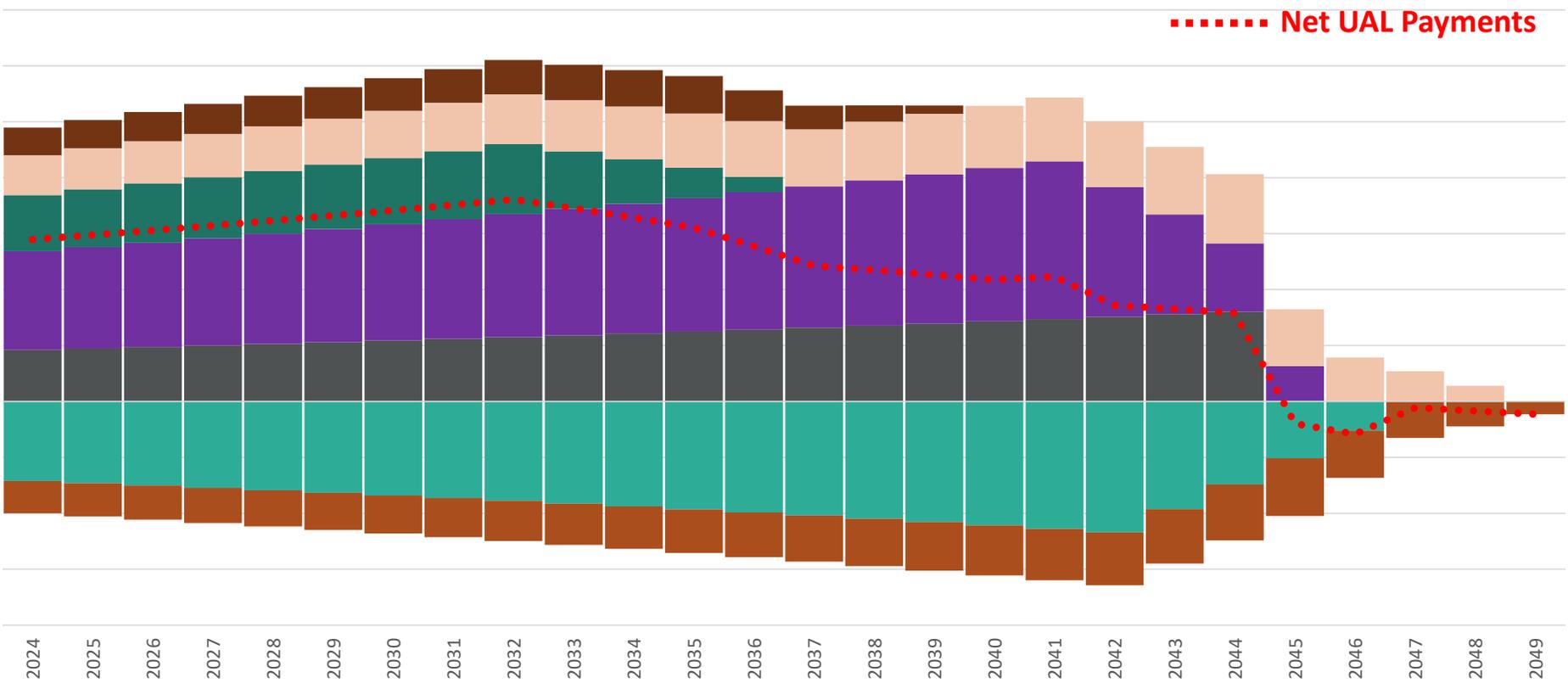
- ▶ Robust investment returns (10%+)
  - ▶ Retirement plans were “Super-Funded” through the late 1990s
  - ▶ Earnings on funds were more than adequate to cover retirement costs
- ▶ Super-funded Status induced widespread retirement benefits enhancements....

### Now ...

- ▶ Sluggish returns outlook (<7%)
- ▶ Assumptions have changed/changing
  - ▶ Discount Rate: 8.25% → 7.00% → 6.80%
  - ▶ Inflation rate (prices going up)
  - ▶ Mortality rates (people living longer)
  - ▶ Actuarial Valuation → Market Valuation
  - ▶ Shorter (20 year) amortization
- ▶ UAL payments have grown rapidly from past changes, remain exposed to the effects from future poor investment returns and assumption changes

# UAL Payments are like a “Layer Cake”

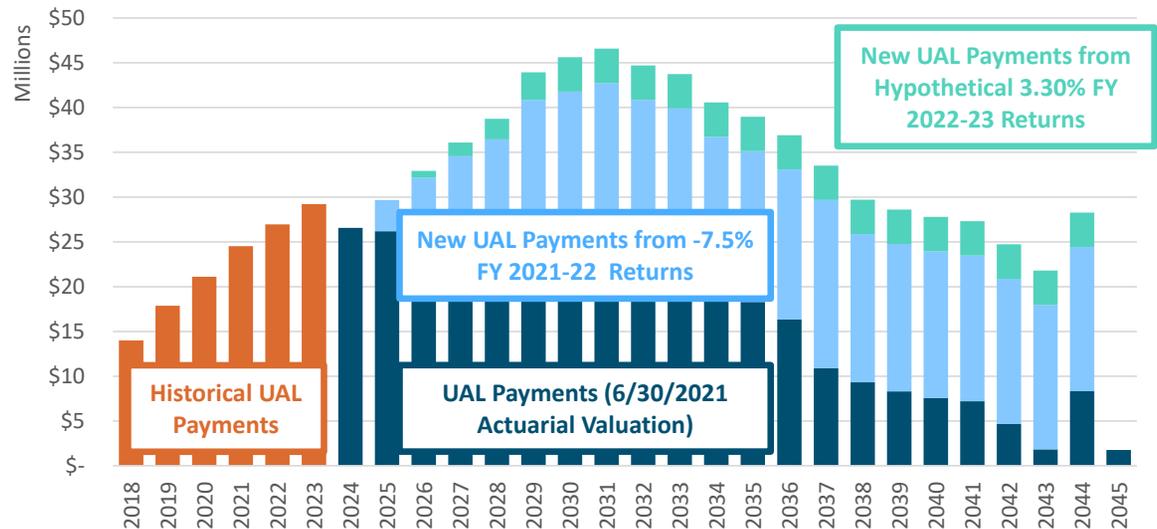
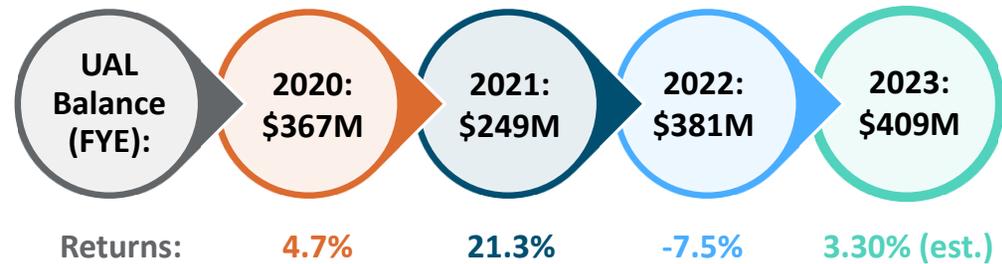
*More Layers Each Year; Increasing or Decreasing Height and Shape of “Cake”*



*Note: The numbers and charts in this presentation are a representation of a sample California public agency's CalPERS UAL and are provided here for educational purposes.*

# Historical and Projected UAL Payment Schedule

- ▶ The City's UAL has increased 45% over the last 7 years (\$263.3M → \$381.5M)
- ▶ The City's UAL balance would increase to \$409.3M if CalPERS earns 3.3% in FY 2022-23 (3.3% = returns through March 31, 2023)
- ▶ The annual UAL payment has more than doubled from 2018 (\$14M) to 2023(\$29M)
  - ▶ Projected to increase another 60% from 2023 to 2031 (\$45M)
- ▶ Along with POB (\$6M) and CalPERS Normal Cost (\$12M), overall pension costs for FY 2023 est. @ \$47M



# Pension Tax Override Revenues (PTORs)

## Overview

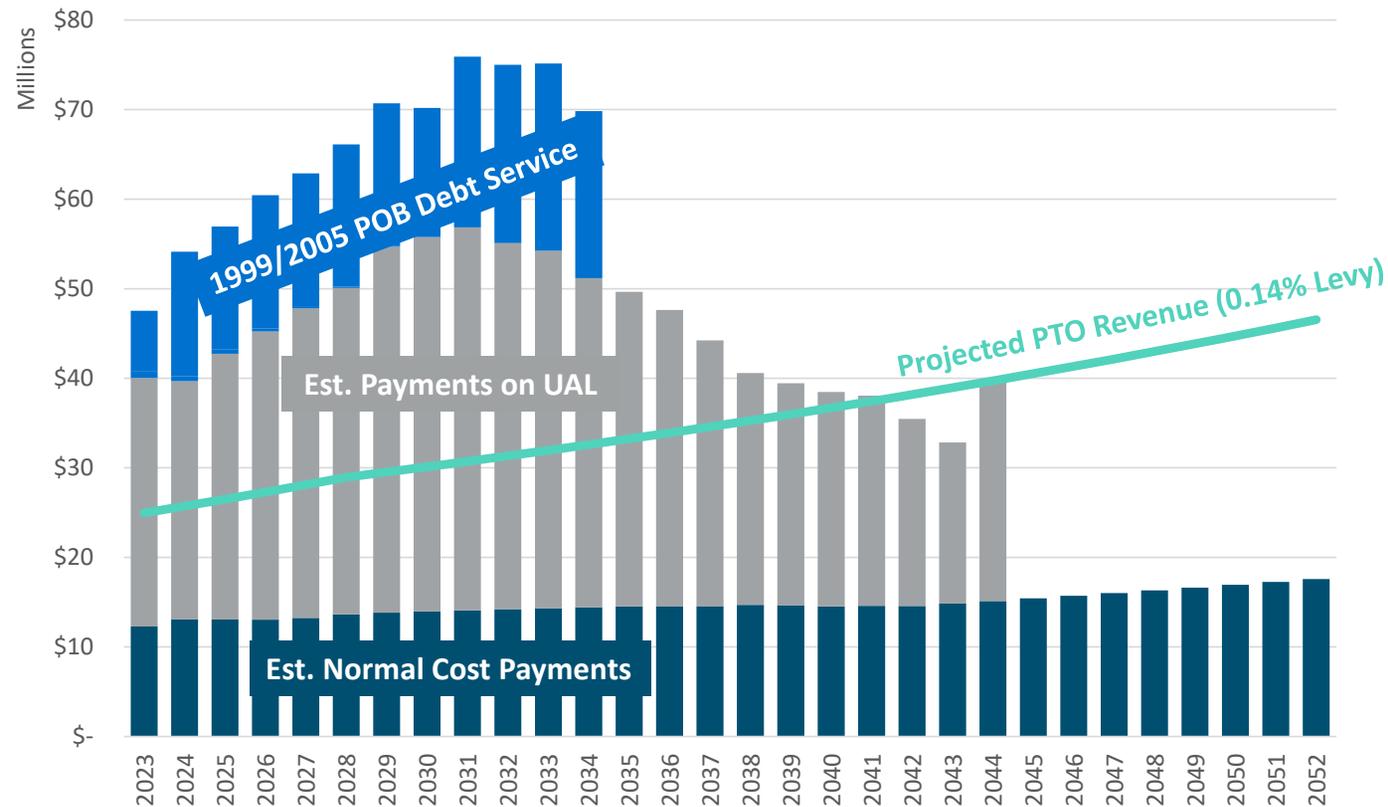
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- ▶ City is one of 20 cities statewide that levies a property tax to cover a portion (related to benefits in place prior to 1978) of pension costs
- ▶ **Currently, 82% of total pension costs (including POBs), can legally be paid for by the PTORs (as determined by independent actuary)**
  - ▶ \$ amount and % of PTO-eligible costs project to grow annually over next decade
- ▶ **However, PTORs levy is also limited by the rate set in 1982/83, which is 0.14% of AV**
  - ▶ 0.14% levy expected to generate about \$25M in FY 2023
  - ▶ Covers 53% of total \$47M FY 2023 pension expenses
- ▶ Remainder of pension expenses (\$22M) primarily paid for by the General Fund (non-PTORS)

# Projected PTORs vs. Projected Pension Costs

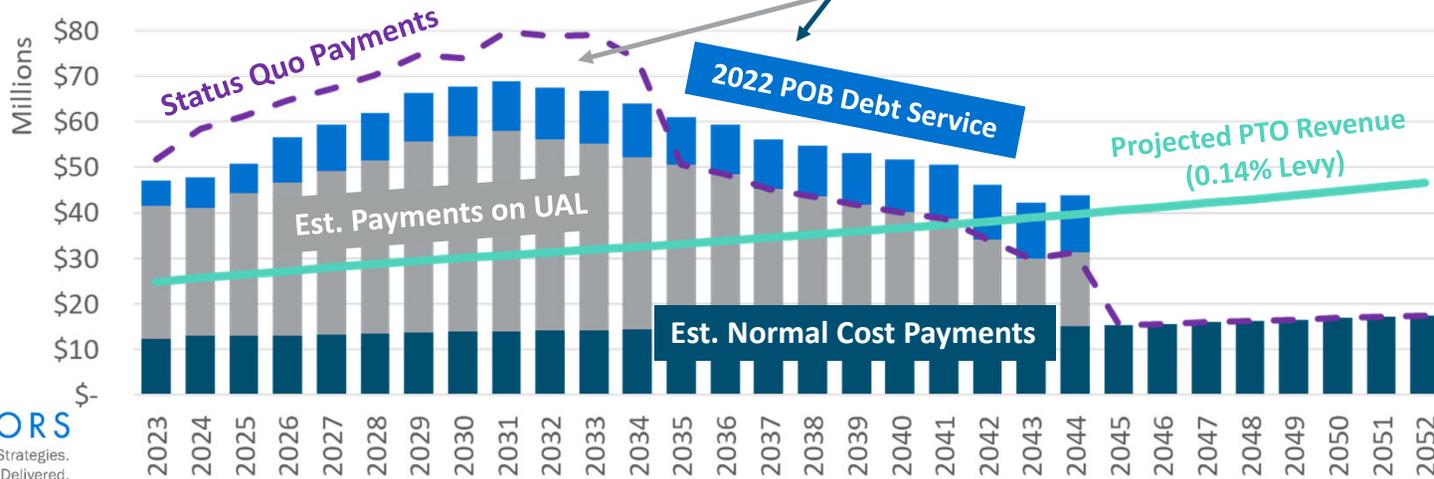
## Situation Prior to the 2022 POB Restructuring

- ▶ Lower availability of PTORs in earlier years and escalating/uneven annual payments payable by General Fund for pension expenses, particularly over the next decade, posed a challenge
- ▶ Staff, City Council and the financing team analyzed dozens of options to better re-align pension expenses with PTORs



# RECAP: 2022 Pension Bond Restructuring

## Multipronged Structuring Strategy and Policy Goals



# Ongoing Cost-Containment Strategies

## Not Mutually Exclusive

### (1) Prepay UAL early in Fiscal Year ( $\approx 3.3\%$ discount)



### (2) Fresh Start Amortization offered by CalPERS

Currently not recommended

- Pros: Smooths payment, shortens repayment period; reduces overall interest paid from shorter amortization period
- Cons: New structure “locked-in” + increased annual payments in near term; still amortized at discount rate

### (3) Use Cash Reserves to Pay Extra (two options)



- 3A Section 115 Trust - Separate trust solely dedicated to pension/OPEB
  - City has established a Section 115 Trust
- 3B Lump Sum Pay Down of UAL – Reduce UAL through “Additional Discretionary Payments” (ADPs)
  - Choose optimal amortization bases to pay off

### (4) Restructure All or Portion of Remaining UAL

- Restructure portion of UAL at lower bond interest rate and “smooth out” payments for enhanced budget predictability, near and mid-term potential savings, more optimal alignment of pension expenses to PTORs revenues

Previously Done; Continue to Monitor/ Assess

# Use Cash Reserves: Section 115 Trust

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- ▶ **What is it?** Dedicated (restricted to pension/OPEB) account
- ▶ **Pros:**
  - ▶ Potential for increased investment returns vs. current General Fund reserves
    - ▶ General Fund investments restricted by Government Code (limits types of instruments and maturities)
    - ▶ Flexibility – more investment options than CalPERS and can decide when and how to use
      - City's 115 Trust is with PARS and has 10 different portfolio options
  - ▶ Longer-Term: Trust funds can grow over time and pay off full UAL in the future
  - ▶ Shorter-Term: Apply during challenging budget years or to “smooth” payment spikes
  - ▶ Potential shock absorber for volatility from CalPERS investment performance & assumption changes
  - ▶ Can also be used for Normal Cost “smoothing” and for OPEB
- ▶ **Cons:**
  - ▶ Market risk (dependent on type of investment portfolio)
  - ▶ The Trust will show up as an asset on the City's financial statements, but will not technically offset UAL until funds are transferred to CalPERS
  - ▶ **City will need to use reserves or annual surplus to fund the 115 Trust**

## Use Cash Reserves: ADP

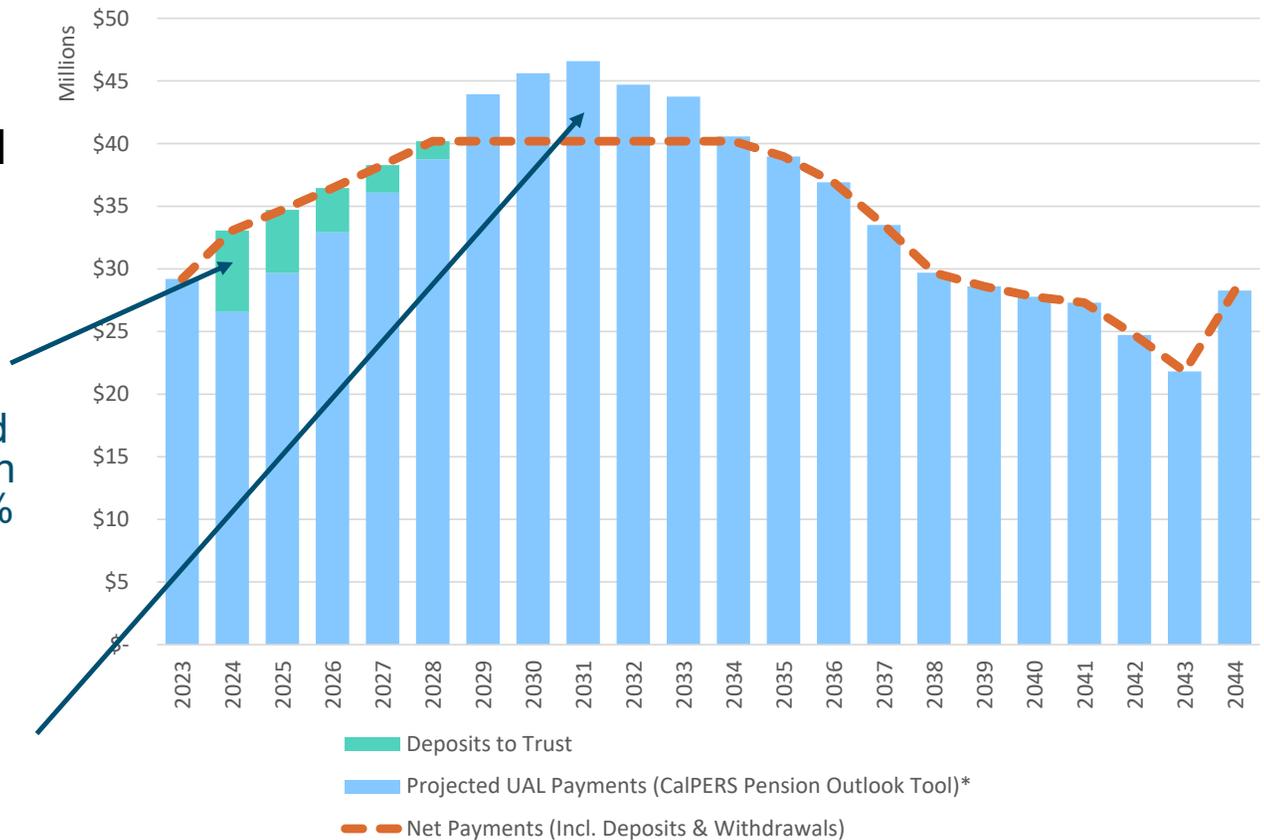
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- ▶ What is it? City makes Additional Discretionary Payment (ADP) directly to CalPERS and designates which amortization base(s) / layer(s) shall be paid off
  - ▶ CalPERS will eliminate payments associated with the portion of the UAL paid off, essentially giving the City credit at the discount/interest rate (currently 6.8%)
    - ▶ Actual credit given over time will be at CalPERS' actual future reinvestment returns
- ▶ **Pros:**
  - ▶ Reduced future payments
  - ▶ Reduced UAL and higher CalPERS funding ratio
- ▶ **Cons:**
  - ▶ Market risk
  - ▶ No options for other investment portfolios like there is with Section 115
  - ▶ Reduced liquidity/budgetary flexibility vs. Section 115 Trust
  - ▶ **City will need to use reserves or annual surplus to fund the 115 Trust**

# Section 115 Trust – Hypothetical Short-Term Example

## Assets Used to Smooth Out Near- and Mid-Term Fluctuations

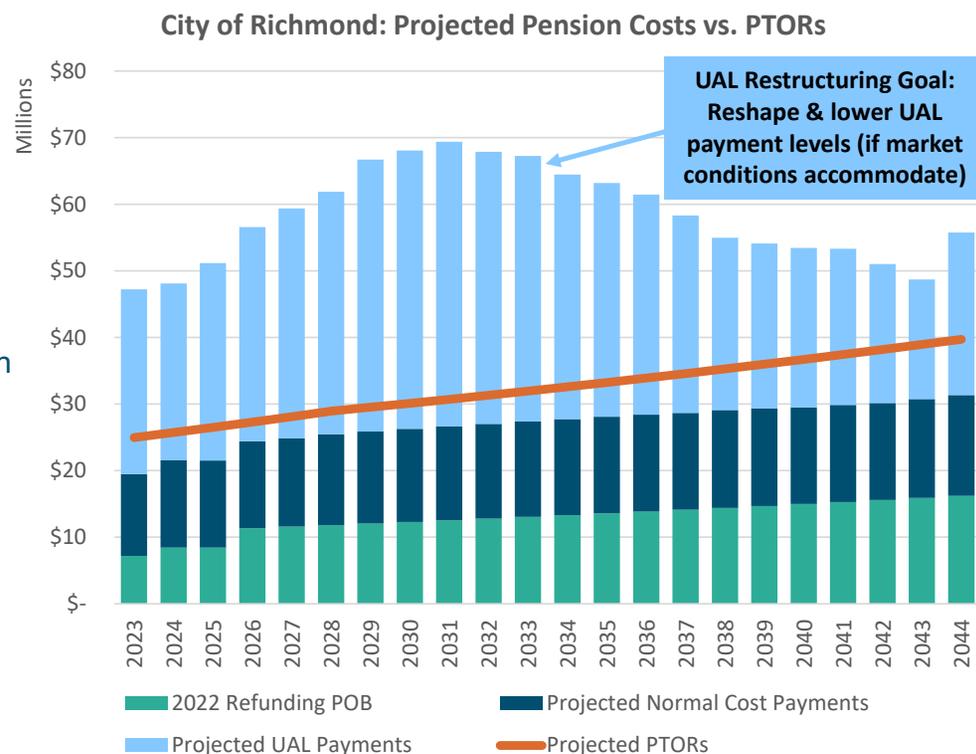
- ▶ City can leverage reserves and/or some near-term projected savings from the 2022 Refunding POB to fund and grow the Section 115 Trust
- ▶ Hypothetical Example in Chart:
  - ▶ Assumes ~\$19M is contributed to the Section 115 trust through FY 2028, and invested @ 4.5%
  - ▶ Funds could be withdrawn during higher UAL payment years to stabilize net impact to the General Fund
  - ▶ Payment peak reduced from \$45M to \$40M



\*Assumes 6.80% Discount Rate, -7.5% FY 2021-22 Investment Returns, 3.3% FY 2022-23 Investment Returns, 6.80% Investment Returns from FY 2023-24 onward

## Restructuring UAL using Debt (Pension Bond): Overview

- ▶ **What is it?** Borrow money to pay off all or a portion of 6.8% UAL Debt with CalPERS (i.e. very large ADP)
  - ▶ Pension Obligation Bond (POB) structure is typically utilized
- ▶ Savings potential if POB interest rates are materially lower than CalPERS discount rate (6.8%)
- ▶ Restructuring annual UAL payments into a smoother, predictable schedule is a core objective
  - ▶ For Richmond, this would mean reshaping debt to better match PTORs revenue stream
- ▶ **Key Risks:** Re-investment risk and market timing risk of bond proceeds sent to CalPERS
- ▶ Borrowing rates are currently high (above 6%), but staff and its financing team will monitor & assess this opportunity, including risks & benefits, in the future



## Conclusion & Next Steps

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- ▶ Rising pension costs are a challenge facing most public agencies, including the City
  - ▶ Richmond has been active in addressing this challenge (e.g., Section 115 Trust; 2022 Refunding POB for cost restructuring & elimination of interest rate swaps; third-party actuarial reports)
  - ▶ Rising pension costs still remain a significant challenge, even with annual PTORs
  - ▶ City should incorporate latest estimates into budget and planning process; conduct sensitivity analysis and conservatively plan for CalPERS underperformance
- ▶ City's Section 115 Trust provides opportunity to create enhanced budget predictability and/or pay off more UAL sooner if City can fund the trust to meaningful levels
- ▶ Long term plan should be developed; Staff and NHA (with guidance from Council) will return to Council with additional analysis and information at future meetings/workshops
- ▶ Staff and NHA will also put together a proposed pension funding policy for Council consideration
  - ▶ Policy would identify roadmap and strategy for managing rising pension costs long term
  - ▶ May include recommendation on amount of annual surplus (or one-time revenues) that should be dedicated towards pensions
- ▶ UAL restructuring concept to better align expenses to PTO revenue will continue to be monitored and would be introduced to Council in more detail if market conditions improved in the future

# Recommended Action

RECEIVE an update on the draft FY 2023-2024 Annual Operating Budget and FY2023-2028 Five-Year Capital Improvement Plan Budget; and RECEIVE DIRECTION from City Council prior to final budget adoption

# Next Steps

- Staff will bring proposed FY 2023-24 Budget for adoption on June 20, 2023
- In September/October City Council will have additional opportunities to amend the FY 2023-24 budget according to their facilitated Goal Setting Sessions.

# FY 2022-23 Close & FY 2023-24 Budget Update

ACTION / ACTIVITY	DATE
FY 2022-23 Interim Audit	Currently In Progress
FY 2022-23 Close	July –September
FY 2022-23 Annual Audit	October - December
FY 2022-23 Year-End update, Direction on allocating Unspent Funds	September-October
FY 2023-24 Q1 Budget Update (City Council updates the budget per their priorities)	October-November
FY 2022-23 Annual Certified Financial Report (ACFR)	January – February 2024
FY 2022-23 Single Audit	February 2024



# **THANK YOU & QUESTIONS**