

CITY OF SANTA ROSA
CITY COUNCIL

TO: MAYOR AND CITY COUNCIL
FROM: SCOTT WAGNER, CHIEF FINANCIAL OFFICER, FINANCE
DEPARTMENT
SUBJECT: CALPERS PENSION UNFUNDED LIABILITY EXPENSES
OVERVIEW AND POTENTIAL COST AVOIDANCE STRATEGIES

AGENDA ACTION: STUDY SESSION

RECOMMENDATION

The Finance Department recommends that the City Council hold a Study Session regarding CalPERS pension expenses and potential cost avoidance strategies. This item is presented for the Council's information and no action is required. This item has no impact on current fiscal year budget.

EXECUTIVE SUMMARY

The City of Santa Rosa faces a citywide \$482 million Unfunded Accrued Liability (UAL) based on the most recent CalPERS valuation of the City's pension plans. Without intervention, General Fund pension payments are projected to rise to \$49 million by FY 2031. Following an evaluation by NHA Advisors, staff has identified a strategy that leverages \$26 million in restricted pension funds to achieve \$37 million in total cost avoidance, a more balanced amortization schedule and retire UAL debt six years earlier than currently scheduled.

GOAL

This item relates to Council Goal #1 - Achieve and Maintain Budgeting Excellence and Fiscal Stability through proactively managing pension liabilities.

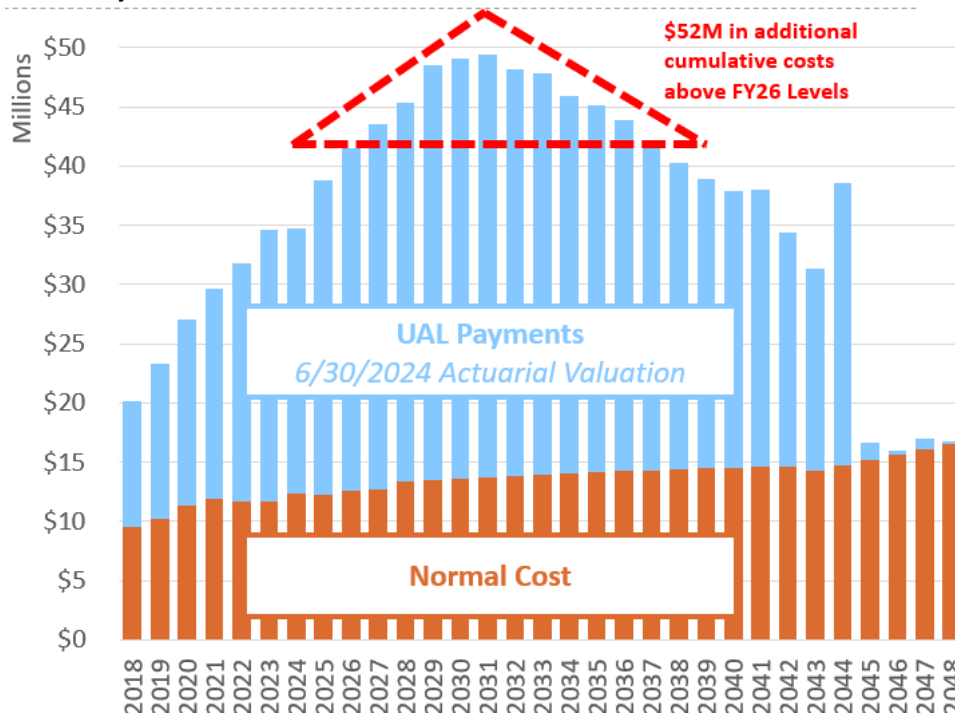
BACKGROUND/PRIOR COUNCIL REVIEW

The City's pension funded ratio stands at 71.1% as of the most recent CalPERS actuarial report of 6/30/2024. Of the \$482 million in citywide Unfunded Accrued Liability (UAL), \$331 million is directly attributable to the General Fund. This debt is highly fragmented through CalPERS amortization, consisting of 101 separate layers with repayment schedules ranging from 5 to 24 years. The composite result of these layers has created an amortization schedule which is imbalanced with costs projected to peak in 2031 and not decrease from current levels until 2036. Over the past decade,

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CalPERS amortization payments have increased sharply. This upward trend in pension costs is driven by increasingly conservative actuarial assumptions, such as factoring in longer life expectancies and lowering the discount rate from a high of 8.75% in the 1990s to 6.8% today. These adjusted assumptions, combined with the legacy costs of past benefit enhancements and lingering investment losses from the Great Recession, have significantly compounded the overall unfunded liability. Furthermore, while the Public Employees' Pension Reform Act (PEPRA) assists in managing long-term costs for newer employees, 99% of the City's current UAL is tied to Classic plans. The financial impact of these factors on the City's budget has compounded rapidly. The UAL portion of the City's General Fund CalPERS payment is rising the fastest, having roughly tripled from \$11 million in FY 2018 to \$31 million in FY 2026. If the current repayment schedule remains unchanged, the UAL payments for the General Fund are projected to peak at \$35.7 million by FY 2031. This steep trajectory represents \$52 million in additional cumulative costs above current FY 2026 levels by FY 2036.

Historical and Projected Cost increases:



To proactively mitigate these rising costs, the City has actively built up \$26 million in restricted funding to be used to provide pension stability. This total comprises two sources:

- Section 115 Pension Stability Trust (\$14.5 million): This trust was established with \$10 million in PG&E settlement funds resulting from the 2017 Tubbs Fire on May 10, 2022 (22-0359). Through positive investment returns the balance has grown to approximately \$14.5 million.
- Savings from Pension Obligation Bond (POB) Retirement: When the City Council adopted the Section 115 Pension Stability Trust, ongoing funding was identified

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from the annual savings achieved by paying off previously issued POBs. These savings were directed into a Pension Internal Service Fund. While contributions to this fund were suspended during recent budget reductions, the fund accumulated a balance of \$11.5 million prior to the pause.

ANALYSIS

City staff and our financial advisor, NHA Associates (NHA), have analyzed current CalPERS amortization schedules and available resources. This analysis focused on five key objectives: providing stable budgeting that matches expense growth with revenue growth; decreasing the total amount paid; accelerating the payoff of the unfunded liability; maintaining local control of local funding sources; and maximizing near-term cost avoidance.

CalPERS provides limited options for agencies to change their required contributions to pay down unfunded liabilities. The CalPERS Fresh Start is an actuarial tool that allows the City to re-amortize its UAL, essentially resetting the debt schedule to stabilize required employer contributions .

- Re-amortizing Debt: It combines multiple, separate UAL bases (debt layers from different years) into a single new base. Where the prior amortization schedule gave a variable payment structure with payments peaking in years 2027 through 2038 the fresh start provides a fixed payment schedule over a fixed period.
- Stabilizing Payments: This process smooths out increasing contribution requirements, preventing the additional spike projected over the next 8 years in required annual payments.
- Process & Implementation: The Fresh Start requires new amortization bases to exhibit overall savings and therefore can vary in length. Through analysis done by CalPERS actuary office, the City would expect a 16 year schedule.
- Choosing the Fresh Start option permanently locks the City into this CalPERS payment methodology for the existing UAL. However, it preserves the City's ability to issue a POB in the future for additional re-amortization.
- Opting into the Fresh Start would only address already existing amortization bases. Future gains, losses or assumption changes by CalPERS would be treated with the standard CalPERS amortization process and would add or subtract from the total due in future years.

CalPERS also provides the option to make Additional Discretionary Payments (ADPs). An ADP is a voluntary contribution that exceeds the City's required annual minimum payment. By directly reducing the UAL, this payment mitigates future interest charges from CalPERS, thereby generating long-term budgetary savings for the City.

NHA evaluated three primary options for the City:

Option 1 - Fresh Start (Recommended): Combines CalPERS Fresh Start with usage

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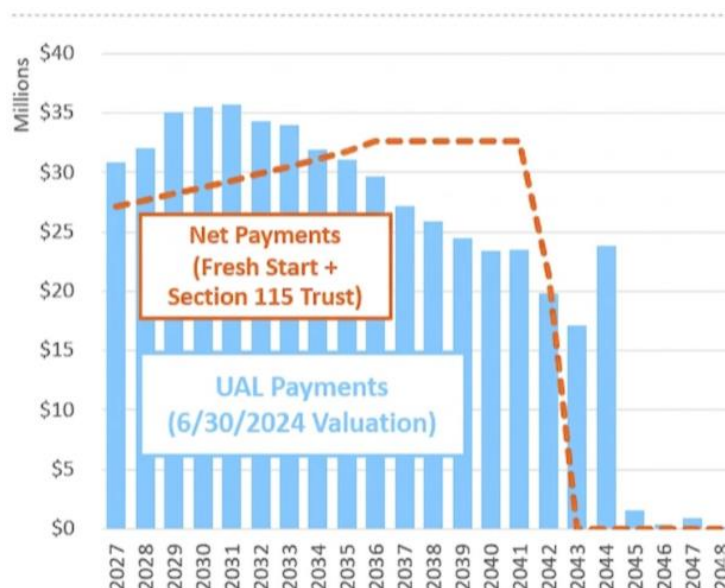
of \$26 million in available funding sources. This creates a predictable 2% linear payment growth and offers the highest savings (\$36.6M).

This option executes a CalPERS "Fresh Start" amortization (16 years for the Safety plan and 15 years for the Miscellaneous plan) combined with a gradual drawdown of the Section 115 Trust over a 9-year period (2027–2035).

- **Cost Avoidance:** Yields the highest total cost avoidance among the three options, estimated at \$36.6 million overall.
- **Near Term Impact:** \$28.2 million in cost avoidance in the first 5 years.
- **Budget Predictability:** Provides a more predictable budget structure by capping current UAL amortization payment growth to \$32.6 million versus a scheduled \$35.7 million peak. Creates a linear 2% per year growth of the payment schedule when combined with Section 115 Trust to grow the total expense gradually over time.
- **Debt Retirement:** It is the only option that accelerates the retirement of the UAL debt, paying it off 6 years earlier, fully paying off the existing UAL by 2042 versus 2048.
- **Local Control of Section 115 Trust Funds:** The City retains local investment control, liquidity, and budgetary flexibility because the funds remain in the Section 115 Trust rather than being sent directly to CalPERS.

The Fresh Start would result in higher payments versus our current projection in years 2036 through 2041 due to the level payment structure created. While the City would experience higher payments it would also benefit from a flat payment schedule against predictable revenue growth over time.

Projected Payment Schedule (current in bars, projected on dotted line):

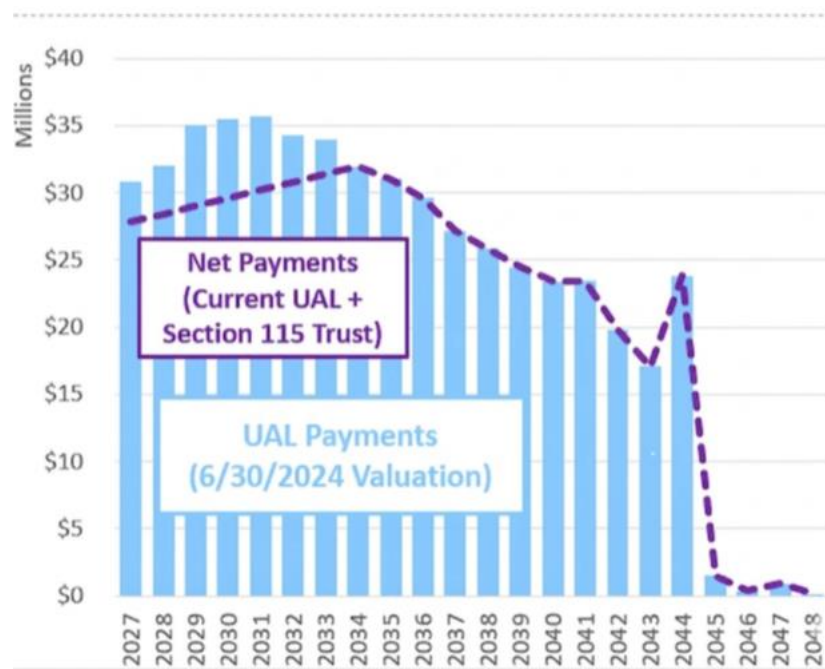


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Option 2: 100% Section 115 Trust Ramp-Up: This option does not utilize a CalPERS Fresh Start. Instead, it uses the \$26 million in Section 115 Trust assets over a 7-year timeframe (2027–2033) to offset current UAL costs and create a structured payment ramp-up.

- **Cost Avoidance:** Generates the lowest total cost avoidance of the three options, estimated at \$29.9 million
- **Near Term Impact:** \$23.9 million in cost avoidance in the first 5 years.
- **Budget Predictability:** Provides budget alignment with linear 2% annual payment growth (scaling from \$28 million to \$32 million) for 8 years.
- **Debt Retirement:** Does not result in the early retirement of the City's UAL debt.
- **Local Control:** Similar to Option 1, the City retains complete local investment control and liquidity over the Trust assets.

Projected Payment Schedule (current in bars, projected on dotted line):



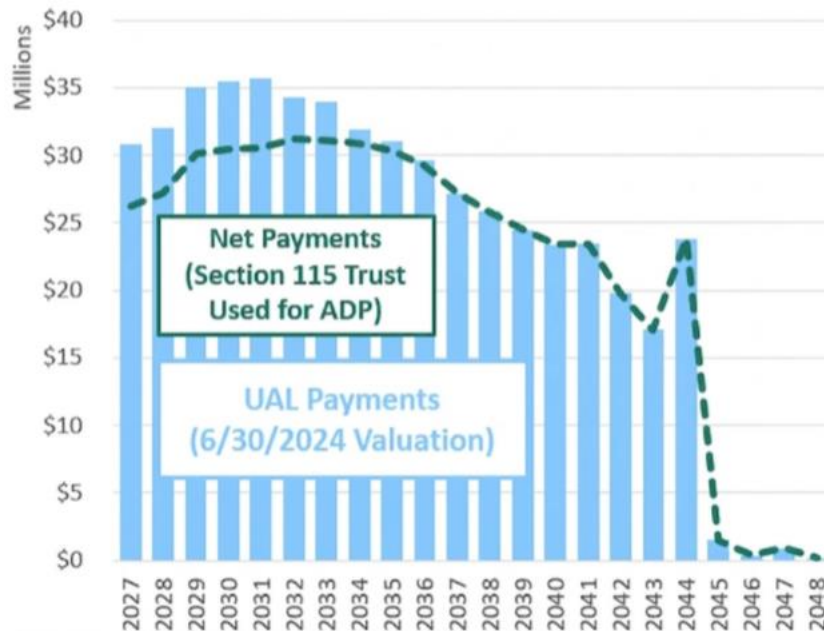
Option 3: 100% Additional Discretionary Payment (ADP): This strategy requires liquidating the \$26 million Section 115 Trust by the end of Fiscal Year 2026 to make an ADP to CalPERS. The \$26 million payment would be targeted to pay off specific UAL amortization bases of 5 to 10 years that contribute to the near-term cost peak.

- **Cost Avoidance:** Yields the second highest total cost avoidance at \$32.5 million
- **Near Term Impact:** \$24.4 million in cost avoidance in the first 5 years.
- **Budget Predictability:** Results in escalating payments for 7 years, offering less budgetary predictability and a less linear structure than Options 1 and 2.

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- **Debt Retirement:** Does not accelerate the retirement of the overall UAL debt.
- **Local Control:** The City permanently loses local investment control, budget flexibility, and liquidity over the Section 115 Trust funds, as they are transferred to CalPERS to pay down the liability.

Projected Payment Schedule (current in bars, projected on dotted line):



Staff recommend the Fresh Start Option 1 paired with usage of Section 115 Trust assets that provides the best balance of budget predictability, near term cost avoidance, overall savings, maintains local control of local funding, and retires the existing UAL six years early.

Evaluation Criteria	Option 1: Fresh Start (Recommended)	Option 2: 100% Section 115 Trust Ramp-Up	Option 3: 100% Additional Discretionary Payment (ADP)
Strategy Overview	CalPERS "Fresh Start" + gradual drawdown of \$26M Trust over 9 years (2027–2035).	No Fresh Start. Uses \$26M Trust over 7 years (2027–2033) to offset costs.	Liquidate \$26M Trust by FY 6/30/2026 to pay specific 5 to 10 year UAL bases directly to CalPERS.
Total Cost Avoidance	Highest: \$36.6 Million	Lowest: \$29.9 Million	Moderate: \$32.5 Million
Near-Term Impact (First 5 Years)	Highest: \$28.2 Million	Lowest: \$23.9 Million	Moderate: \$24.4 Million

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Budget Predictability	Highly Predictable: Linear 2% annual growth. Caps peak at \$32.6M (vs \$35.7M). Higher, but flat/predictable payments from 2036–2041.	Predictable: Linear 2% annual payment growth (\$28M to \$32M) for 8 years.	Less Predictable: Escalating payments for 7 years; lacks the linear structure of Options 1 & 2.
Debt Retirement	Accelerated: Pays off overall UAL debt 6 years early (by 2042 vs. 2048).	Standard: Does not accelerate the overall retirement timeline.	Standard: Does not accelerate overall UAL debt retirement timeline.
Local Control & Liquidity	Retained: City keeps investment control, liquidity, and flexibility via the Trust.	Retained: City keeps investment control, liquidity, and flexibility via the Trust.	Lost: Funds permanently transferred to CalPERS; loss of liquidity and flexibility.

FISCAL IMPACT

This Study Session has no direct impact on budgets as no formal action is to be taken. Future potential adoption of proposed strategies will produce varied financial impacts as described throughout report.

ENVIRONMENTAL IMPACT

Pursuant to CEQA Guidelines Section 15378, the recommended action is not a “project” subject to the California Environmental Quality Act (CEQA) because it consists of a study session for informational purposes only and does not involve a commitment to any specific action or result in a direct or reasonably foreseeable indirect physical change in the environment.

In the alternative, the recommended action is exempt from CEQA pursuant to CEQA Guidelines Section 15061(b)(3) because it can be seen with certainty that there is no possibility that the activity may have a significant effect on the environment.

BOARD/COMMISSION/COMMITTEE REVIEW AND RECOMMENDATIONS

This Study Session was previously considered by the Long Term Financial Planning and Audit Subcommittee on April 9, 2026 and recommended for City Council Review.

NOTIFICATION

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Not applicable.

ATTACHMENTS

Not applicable.

PRESENTER(S)

Scott Wagner, Chief Financial Officer, Finance Department
Michael Myer, Vice President, NHA Advisors