



CITY OF BEVERLY HILLS STAFF REPORT

Meeting Date: March 6, 2012
To: Honorable Mayor & City Council
From: Scott G. Miller, CFO / Director, Administrative Services
Mark A. Brower, Senior Budget & Financial Analyst
Subject: Approval of Phase 2 of the Alternative Retiree Medical Program
(ARMP) For Eligible Non-Safety Employees and Phase 1 for
Eligible Safety Employees
Attachments: None

INTRODUCTION

In December of 2010, Staff successfully completed full implementation of Phase 1 of the Alternative Retiree Medical Program (ARMP) as approved by the City Council in December of 2009. This program was one of the five programs developed by staff and the City Council designed to help significantly reduce long term benefit costs the City would incur by giving current non-safety employees the opportunity to opt out of their existing benefit in exchange for a defined contribution plan or a one-time lump sum payout. 58% of the eligible employees opted to take this program. With this robust level of participation, the City's actuary calculated the estimated cost savings in unfunded liabilities to the city to total more than \$40 Million over 40 years for this program alone.

DISCUSSION

ARMP for Non-Safety Employees

Phase 1 of ARMP generated a groundswell of interest from the remaining eligible employees after the program was completed.

To achieve further long-term savings for the City, Staff recommends offering this program again to qualifying employees who decided not to elect the ARMP in the first phase. Phase 2 is almost identical to the first phase with the exception that the amount offered to employees will be reduced by 10%.

ARMP enables the City to substantially decrease its future risk exposure to unfunded liabilities inherent in the prior defined benefit model of retiree health care. This is an example of Beverly Hills' proactive and innovative approach to implementing long term solutions to systemic issues.

Based on the success of this program and the expressed interest from remaining eligible employees, Staff recommends offering a second phase of ARMP to qualified employees.

ARMP for Safety Employees (Police & Fire)

Staff also seeks City Council approval to offer the ARMP to eligible safety employees. This would be similar to the Phase 1 program offered to eligible non-safety employees.

Staff has the additional option to negotiate a lump sum transition amount paid directly to the safety associations trusts, which would eliminate 100% of the unfunded OPEB liability associated with eligible active safety employees.

With 100% participation in ARMP or the lump sum program, the unfunded OPEB liability for safety employees is projected to be reduced by \$45.2 million.

FISCAL IMPACT

Summary

ARMP for Non-Safety Employees (100% participation)

With 100% participation, the City's unfunded OPEB liability is projected to be reduced by \$25.9M. Costs would be slightly over \$17M with debt service and residual payments.

	Debt Service (Principal + Interest)	Residual Amount	Total
Year 1	\$ 830,000	\$ 557,888	\$ 1,387,888
Year 2	\$ 830,000	\$ 504,114	\$ 1,334,114
Year 3	\$ 830,000	\$ 439,245	\$ 1,269,245
Year 4	\$ 830,000	\$ 359,501	\$ 1,189,501
Year 5	\$ 830,000	\$ 344,416	\$ 1,174,416
Year 6	\$ 830,000	\$ 336,389	\$ 1,166,389
Year 7	\$ 830,000	\$ 317,996	\$ 1,147,996
Year 8	\$ 830,000	\$ 301,004	\$ 1,131,004
Year 9	\$ 830,000	\$ 287,831	\$ 1,117,831
Year 10	\$ 830,000	\$ 272,956	\$ 1,102,956
Year 11	\$ 830,000	\$ 253,762	\$ 1,083,762
Year 12	\$ 830,000	\$ 210,106	\$ 1,040,106
Year 13	\$ 830,000	\$ 210,106	\$ 1,040,106
Year 14	\$ 830,000	\$ 127,918	\$ 957,918
Year 15	\$ 830,000	\$ 73,181	\$ 903,181
Year 16	\$ -	\$ 27,779	\$ 27,779
TOTAL	\$ 12,450,000	\$ 4,624,194	\$ 17,074,194

73% of ARMP 2.0 is projected to be allocated to the General Fund and the remaining 27% is projected to be allocated to Enterprise Funds.

	Total General Fund Payment	Total Enterprise Fund Payment	TOTAL
Year 1	\$ 1,013,159	\$ 374,730	\$ 1,387,888
Year 2	\$ 973,903	\$ 360,211	\$ 1,334,114
Year 3	\$ 926,549	\$ 342,696	\$ 1,269,245
Year 4	\$ 868,336	\$ 321,165	\$ 1,189,501
Year 5	\$ 857,324	\$ 317,092	\$ 1,174,416
Year 6	\$ 851,464	\$ 314,925	\$ 1,166,389
Year 7	\$ 838,037	\$ 309,959	\$ 1,147,996
Year 8	\$ 825,633	\$ 305,371	\$ 1,131,004
Year 9	\$ 816,017	\$ 301,814	\$ 1,117,831
Year 10	\$ 805,158	\$ 297,798	\$ 1,102,956
Year 11	\$ 791,146	\$ 292,616	\$ 1,083,762
Year 12	\$ 759,277	\$ 280,829	\$ 1,040,106
Year 13	\$ 759,277	\$ 280,829	\$ 1,040,106
Year 14	\$ 699,280	\$ 258,638	\$ 957,918
Year 15	\$ 659,322	\$ 243,859	\$ 903,181
Year 16	\$ 20,278	\$ 7,500	\$ 27,779
TOTAL	\$ 12,464,162	\$ 4,610,032	\$ 17,074,194

ARMP for Safety Employees (100% participation)

The projected total cost to offer ARMP Phase 1 to all eligible safety employees is \$30.6M accounting for debt service, and residual amounts.

The projected cost of offering a lump sum transition amount to safety employee association trusts is \$26.3M. The lump sum option is less than the total cost of ARMP since it includes the net present value (NPV) of the residual payments.

	Police Debt Service (Principal + Interest)	Fire Debt Service (Principal + Interest)	Total Annual Debt Service	Police Residual Amount	Fire Residual Amount	Total Residual Amount	Grand Total
Year 1	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 772,584	\$ 228,201	\$ 1,000,785	\$ 2,323,347
Year 2	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 761,904	\$ 228,201	\$ 990,106	\$ 2,312,668
Year 3	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 738,291	\$ 195,915	\$ 934,205	\$ 2,256,767
Year 4	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 738,291	\$ 181,212	\$ 919,503	\$ 2,242,065
Year 5	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 683,918	\$ 181,212	\$ 865,130	\$ 2,187,692
Year 6	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 652,345	\$ 181,212	\$ 833,558	\$ 2,156,120
Year 7	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 591,217	\$ 181,212	\$ 772,429	\$ 2,094,991
Year 8	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 539,695	\$ 181,212	\$ 720,908	\$ 2,043,470
Year 9	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 532,342	\$ 149,632	\$ 681,975	\$ 2,004,537
Year 10	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 491,135	\$ 101,002	\$ 592,136	\$ 1,914,698
Year 11	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 368,378	\$ 96,853	\$ 465,231	\$ 1,787,793
Year 12	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 341,365	\$ 86,521	\$ 427,887	\$ 1,750,449
Year 13	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 323,490	\$ 86,521	\$ 410,011	\$ 1,732,573
Year 14	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 279,445	\$ 70,435	\$ 349,880	\$ 1,672,442
Year 15	\$ 914,254	\$ 408,308	\$ 1,322,562	\$ 205,492	\$ 70,435	\$ 275,927	\$ 1,598,489
Year 16	\$ -	\$ -	\$ -	\$ 170,583	\$ 58,996	\$ 229,579	\$ 229,579
Year 17	\$ -	\$ -	\$ -	\$ 86,005	\$ 25,854	\$ 111,858	\$ 111,858
Year 18	\$ -	\$ -	\$ -	\$ 77,635	\$ 25,854	\$ 103,489	\$ 103,489
Year 19	\$ -	\$ -	\$ -	\$ 77,635	\$ 25,854	\$ 103,489	\$ 103,489
TOTAL	\$ 13,713,814	\$ 6,124,616	\$ 19,838,430	\$ 8,431,750	\$ 2,356,335	\$ 10,788,085	\$ 30,626,515

Total Payments for Debt Service + Residual Payments for Lump Sum

	Debt Service (with Residual Amounts included) on the Lump Sum Amount for Police & Fire
Year 1	\$1,750,000
Year 2	\$1,750,000
Year 3	\$1,750,000
Year 4	\$1,750,000
Year 5	\$1,750,000
Year 6	\$1,750,000
Year 7	\$1,750,000
Year 8	\$1,750,000
Year 9	\$1,750,000
Year 10	\$1,750,000
Year 11	\$1,750,000
Year 12	\$1,750,000
Year 13	\$1,750,000
Year 14	\$1,750,000
Year 15	\$1,750,000
TOTAL	\$26,250,000

Financing Options:

The projected cost to fund the programs is detailed below:

ARMP for Non-Safety and ARMP for Safety:

	Bonds (4%)	General Fund Reserves
Non Safety	\$17,100,000	\$14,000,000
Safety	\$30,600,000	\$25,600,000
Total	\$47,700,000	\$39,600,000

ARMP for Non-Safety and Lump-Sum for Safety:

	Bonds (4%)	General Fund Reserves
Non Safety	\$17,100,000	\$14,000,000
Safety	\$30,600,000	\$26,300,000
Total	\$47,700,000	\$40,300,000

Pros & Cons of the Financing Options:

Bonds: ARMP and the Lump Sum program can be financed through the issuance of bonds.

Pros:

- Allows the City to spread the cost of the program over 15 years.
- Able to take advantage of historically low interest rates

Cons:

- The cost of the program is increased by the interest expense and cost of issuance associated with the bonds.

Use Existing City Savings (Internal Loan from the General Fund): ARMP can be financed through the use of General Fund reserves.

Pros:

- City determines the interest rate.
 - Low to no interest expense.
 - Interest would be paid to the City, not a 3rd party.
- Flexibility with payment schedule.
- No cost of issuance, which is associated with Bonds or Bank loans.

Cons:

- Reduces the General Fund reserve level.

Other options such as commercial bank loans and internal loans were investigated but were not as beneficial as a bond issuance or funding totally from general fund reserve.

The Use of General Fund Reserves:

The City's General Fund reserve policy states:

"It is a goal of the City to obtain and maintain a general operating reserve in the form of cash, of at least 40% of operating revenues. The first 25% shall be considered a contingency reserve to cover normal seasonal cash flow variations, as well as unforeseen emergency or catastrophic impacts upon the City. Funds in excess of 25% may be used for short term economic investment in the community when justified by projected financial return to the City and specifically authorized by the City Council, upon recommendation of the Chief Financial Officer."

The City's General Fund current reserve level is 60.5%. Of the City's \$98 million reserve, \$64 million is unrestricted.

The maximum cost related to the transition amounts or lump sum program for both non-safety and safety employees is \$27.9 million, which if taken from General Fund reserves would reduce the City's reserve percentage to 43%. In addition to the long-term savings realized by the City by implementing these programs, the City Council can adopt a policy to repay the general fund contribution over time.

AUDIT COMMITTEE RECOMMENDATION:

The Audit Committee of the City along with the City Treasurer investigated several options to reduce the City's OPEB unfunded liabilities. Through their findings, both the committee and the City Treasurer noted that current City reserves are earning roughly 1% return in the current market. Given the projected 4% bond rate for a prospective issuance for the program, the City Treasurer and the Audit Committee have recommended employing General Fund reserves for the ARMP.

RECOMMENDATION

In order to further reduce the City's unfunded other post employment benefits (OPEB) liabilities it is recommended that the City Council:

- 1) Approve Phase 2 of the Alternative Retiree Medical Program (ARMP) for eligible non-safety employees.
- 2) Direct staff to implement the programs including communication with the City's Employee Association Groups as part of the implementation.
- 3) Approve a financing option for the program.
 - Staff recommends the use of General Fund reserves in order to minimize the total cost of the program and achieve the maximum long-term financial benefit for the City.
- 4) Authorize the Chief Financial Officer to sign all necessary documents and forms related to this program.



Scott G. Miller
CFO / Director, Administrative
Services