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Most California Cities Back New Pension Strategy Despite Cost.

SAN FRANCISCO — Most California cities support a new strategy by the nation's largest public pension fund to make its investment portfolio more conservative, even though the move could gradually increase how much employers pay into the fund.

Still, some cities expressed serious reservations about a California Public Employees' Retirement System plan to incrementally lower the $293 billion fund's assumed rate of investment returns following periods of strong performance.

The League of California Cities surveyed its members, which have been struggling to shoulder the burden of growing pension costs. The survey found that many cities prefer a more gradual increase in costs, as opposed to spikes following market downturns, said Bruce Channing, Laguna Hills city manager.

"As employers, more predictability and less spiking of rates from one year to the next is preferable," said Channing, who is also chair of the league's city managers pension reform task force.

Next week, the Calpers board will consider a new policy to gradually reduce the assumed return rate from 7.5 percent to 6.5 percent over a few decades. The average return rate across 126 funds tracked by the National Association of State Retirement Administrators was 7.68 percent as of May.

Calpers intends to reduce portfolio volatility as California's baby boomers retire and payouts exceed active workers' contributions. The idea is similar to that of an individual nearing retirement adopting a more conservative investment strategy.

But a lower, albeit less volatile, rate of return will necessitate higher contributions from local governments and public workers.

The league said 77 percent of those surveyed supported Calpers' strategy to reduce portfolio risk, even though the move would over time raise pension contributions more than currently planned. Ten percent of respondents opposed the strategy, and the rest were unsure, the survey of 115 cities found.

Opponents of higher contributions included Alameda, a city of nearly 76,000 near San Francisco. Its pension costs for safety workers like police and fire consume 48 cents of every dollar paid in salary and are expected to grow to 65 cents in five years.

"It's devastating on our bottom line," said Alameda Interim City Manager Liz Warmerdam. "We have very little input. Whatever they want to do, local governments have to sit here and deal with it. It's extremely frustrating."

Massive pension costs contributed to a handful of recent municipal bankruptcies across the country, including in the California cities of Vallejo, Stockton and San Bernardino.

Stockton and Vallejho have emerged from bankruptcy. Vallejo City Manager Daniel Keen said he supports actions to ensure Calpers' ability to pay benefits, but added it may require sacrifices.

"While this plan does cause us more pain on the part of our budget, it is pain we were anticipating," said Keen. "It is going to require adjustments in our budget and might result in cuts to some services."

"It's undeniable that we have to deal with the fact that there are significantly fewer active employees paying in," said Leyne Milstein, Sacramento's finance director. "We need to make sure this system is sustainable."

But like many cities across the state, Sacramento's budget is not keeping pace with rising pension costs. Next year, the city's expenses are expected to exceed revenues by $8.8 million, of which $5.8 million is pension growth, Milstein said. In five years, Sacramento expects to pay close to $80 million in pension costs from its general fund, up from $60 million today.

"This will be extremely painful on local government budgets, but it's the honest approach to address the large unfunded liabilities," said Senator John Moorlach (R-Costa Mesa), a pension reform supporter. "Unfortunately, it's the taxpayers who are on the hook as pension debt eats up public funds meant for police and fire protection, as well as other services."

By REUTERS

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(Reporting by Robin Respaut and Rory Carroll; Editing by David Gregorio)