

California Public Employees' Retirement System

Fiscal Year 2015-16 Mid-Year Budget Proposal

Second Reading
December 15, 2015

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Background

The Total CalPERS budget is composed of Administrative Operating Costs, Enterprise Projects, Headquarters Building Account, Investment Expenses, and Third Party Administrator Fees.

The purpose of the Mid-Year Budget process is to address enterprise critical, unforeseen, and emergency resources not included in the Fiscal Year (FY) 2015-16 Annual Budget. Examples may include: requests to address new legislative mandates, compliance with new laws or regulations, or new Board initiatives. All Formal Budget Requests submitted were required to meet these criteria for consideration and inclusion in the mid-year budget process.

The Mid-Year Budget process provides an opportunity to review current financial information and adjust the authorized budget based on a more accurate 2015-16 forecast for the remainder of the fiscal year.

Summary

The FY 2015-16 Mid-Year Total Budget of \$1.81 billion represents an overall decrease of \$12.1 million (-0.7 percent) from the FY 2015-16 Annual Total Budget. More specifically, this is a \$1.2 million increase to the Administrative Budget offset by a \$13.3 million decrease to the Third Party Administrator Fees Budget. There is no change being requested to the 2,765 authorized positions approved in the FY 2015-16 Annual Budget.

Major highlights of the FY 2015-16 Mid-Year Budget of \$1.81 billion include:

- Fourth formal budget process that the budget has been reduced.
- Net reduction of \$13.3 million in Third Party Administrator fees:
 - Long Term Care Program - \$1.7 million increase
 - Self-Funded Health Program - \$15.0 million decrease
- Reduction of \$2.3 million due to additional salary savings forecasted for the remainder of the year. The Annual Budget included a 5.0 percent vacancy factor and the year-to-date vacancy factor is at 6.6 percent. We are anticipating an overall increase in the vacancy rate from 5.0 percent to 6.0 percent for the year.
- Reduction of \$1.1 million for the 2015 Retired Member Election. The incumbent ran unopposed so the funds are not needed.
- Increase of \$4.6 million for administrative technical adjustments related to increased salary costs per collective bargaining agreements effective July 1, 2015 and employee benefits which include retirement, dental and health coverage. The increase totals \$9.3 million; however, \$4.7 million is already reflected in the Annual Budget.

A. Total CalPERS Budget

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Fiscal Year 2015-16 Mid-Year CalPERS Total Budget

(in thousands)	FY 2015-16 Annual Budget	Mid-Year Adjustments	FY 2015-16 Proposed Mid-Year Budget	% Change From Annual
Administrative Operating Costs	\$443,546	\$1,151	\$444,697	0.3%
Investment Operating Costs ¹	82,959	-	82,959	-
Investment External Management Fees ²	930,726	-	930,726	-
Subtotal: Operating Costs	\$1,457,231	\$1,151	\$1,458,382	0.1%
Enterprise Projects Costs	37,508	-	37,508	-
Headquarters Building Costs	30,350	-	30,350	-
Third Party Administrator Fees	294,619	(13,259)	281,360	(4.5%)
CalPERS Total Budget	<u>\$1,819,708</u>	<u>(\$12,108)</u>	<u>\$1,807,600</u>	<u>(0.7%)</u>
Total Positions	2,765.0	-	2,765.0	0.0%

¹ Investment operating expenses are not part of CalPERS Administrative Operating Costs and therefore not to be included in CalPERS pro-rata assessment

² Investment External Management Fees consist of both Base Fees and Performance Fees

B. FY 2015-16 Mid-Year Budget Revisions

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The table below provides a breakdown of the FY 2015-16 Mid-Year Budget revisions.

FY 2015-16 Mid-Year Budget	Dollars (in thousands)	Positions
Approved FY 2015-16 Annual Budget		\$ 1,819,708
Additions to FY 2015-16 Annual Budget:		
Employee Compensation and Staff Benefits Rate Changes	\$ 4,557	
Water Conservation Projects	181	
Total Additions		4,738
SUBTOTAL		\$ 1,824,446
Reductions to FY 2015-16 Annual Budget:		
Board Member Election	\$ (1,123)	
Salary Savings due to Vacancies	(2,283)	
Third Party Administrator Fees: Self-Funded Health Program [\$-15.0M] Long Term Care [\$1.7M]	(13,259)	
Water Conservation Projects Grant Received from Department of General Services	(181)	
Total Reductions		(16,846)
Proposed FY 2015-16 Mid-Year Budget		\$ 1,807,600
Change from Annual Budget		(\$12,108)
Percent Change		(0.7%)

The following provides further details on the proposed changes in the FY 2015-16 Mid-Year Budget:

Employee Compensation and Staff Benefits Rate Changes (\$4.6 million increase)

Technical adjustments of \$4.6 million for the FY 2015-16 Mid-Year Budget reflect increased salary costs per collective bargaining agreements effective July 1, 2015 and rate increases to employee benefits which include retirement, health and dental coverage. The total cost for FY 2015-16 is \$9.3 million; of which \$4.7 million was anticipated and included in the 2015-16 Annual Budget. The remaining \$4.6 million is proposed in the Mid-Year Budget.

Water Conservation Projects (no net change)

CalPERS was awarded a Water Conservation Grant from the State Department of General Services, Office of Sustainability Drought Conservation Initiative, for the following two projects:

- The Emergency Operations Fixture Replacement project (\$6,300) will replace existing interior plumbing fixtures with low flow fixtures at the Emergency Operation Center.
- The Lincoln Plaza Water Filtration project (\$175,000) will add a filtration system to the existing storage system at CalPERS for non-potable recaptured water from cooling towers at Lincoln Plaza. The filtration system will allow an average of 1.8 million gallons annually of recaptured water to be used for irrigation, window washing and carpet cleaning applications.

This is cost neutral as the costs were not included in the budget, pending status of the grant.

B. FY 2015-16 Mid-Year Budget Revisions

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Board of Administration Retired Member Election (\$1.1 million decrease)

The 2015 Retired Member Election incumbent, Henry Jones, ran unopposed and therefore the Retired Member Election was not held. The term of office will be January 16, 2016, through January 15, 2020, in accordance with the Public Employees' Retirement Law.

Salary Savings due to Vacancies (\$2.3 million decrease)

To recognize the impact of vacancies on the cost of personnel services, an overall vacancy factor of 5.0 percent was applied during the annual process. This vacancy rate factor has been updated to 6.0 percent based on the year-to-date vacancy rate which is currently at 6.6 percent.

Third Party Administrator Fees (\$13.3 million decrease)

The costs are anticipated to be \$281.4 million, a decrease of \$13.3 million (4.5 percent) from \$294.6 million originally projected. This change is due to an anticipated Long Term Care Program fees increase of \$1.7 million, and an anticipated decrease to Self-Funded Health Program costs of \$15.0 million.

- Long Term Care Program fees are anticipated to increase to \$22.8 million, an increase of \$1.7 million (8.1 percent) from \$21.1 million originally projected. This change is due to a contract amendment to include additional service fees for open application, reorganization and revision of performance guarantees, website maintenance, and a Transitional Care Program Pilot.
- Self-Funded Health Program costs are anticipated to be \$254.6 million, a decrease of \$15.0 million (-5.6 percent) from \$269.6 million originally projected. This is due to the Board approval of the United Healthcare Medicare Advantage carrier in 2016 and therefore Blue Shield administrative fees for their Medicare Plans will no longer be applicable.

Third Party Administrator Fees

	FY 2015-16		
	Annual Budget	Mid-Year Adjustments	Proposed Mid-Year Budget
(in thousands)			
Health Program	\$ 256,669	\$ (14,192)	\$ 242,477
CVS/Caremark - PPO/HMO	12,966	(808)	12,158
Subtotal Health	269,635	(15,000)	254,635
Long Term Care Program	21,081	1,741	22,822
Total Health	290,716	(13,259)	277,457
Supplemental Income Plan	3,903	-	3,903
Total	\$ 294,619	\$ (13,259)	\$ 281,360

Investment Operating Costs (no net change)

Real estate appraisal costs are increasing by \$2.9 million because appraisals will now be completed on a quarterly basis instead of once a year to improve timeliness of real estate asset performance data. It is anticipated that this increase will be offset by reductions in investment related legal and consulting costs.

C. Budget Detail by Branch

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(in thousands)

Total Budget	FY 2015-16 Annual Budget	FY 2015-16 Mid Year Adjustments	Proposed FY 2015-16 Mid Year Budget	% Incr/(Decr) From Annual
Administrative and Investment Operating Costs				
Actuarial Office	\$ 8,248	\$ 53	\$ 8,301	0.6%
Benefit Programs Policy and Planning	29,646	130	29,776	0.4%
Customer Services and Support	102,081	654	102,734	0.6%
Executive Office	4,706	17	4,724	0.4%
Financial Office	26,191	169	26,359	0.6%
General Counsel	27,610	119	27,729	0.4%
Investment Office	150,721	378	151,099	0.3%
Communications and Stakeholder Relations	9,984	43	10,027	0.4%
Operations and Technology	137,020	(417)	136,603	-0.3%
Other (Includes state-wide pro-rata assessment)	30,298	4	30,303	0.0%
Subtotal	\$ 526,505	\$ 1,151	\$ 527,655	0.2%
Enterprise Projects Costs	37,508	-	37,508	-
Headquarters Building Costs	30,350	-	30,350	-
Investment External Management Fees	930,726	-	930,726	-
Third Party Administrator Fees	294,619	(13,259)	281,360	(4.5%)
CalPERS Total Budget	\$ 1,819,708	(\$12,108)	\$ 1,807,600	(0.7%)

D. Administrative Budget by Fund Source

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Administrative Operating Costs by Trust Fund

(in thousands)

Fund	FY 2014-15 Actual	FY 2015-16 Approved Annual Budget	FY 2015-16 Proposed Mid-Year Budget	Budget to Budget	
				\$ Change Incr / (Decr)	% Change Incr / (Decr)
Administrative Operating Costs					
Public Employees' Retirement Fund (PERF)	\$ 341,720	\$ 369,288	\$ 369,318	\$ 30	-
Public Employees' Contingency Reserve Fund (CRF)	27,168	27,564	27,926	362	1.3%
Public Employees' Health Care Fund (HCF)	22,955	33,630	33,886	256	0.8%
Long-Term Care Fund (LTCF)	4,000	4,249	4,209	(40)	(0.9%)
Annuitants' Health Care Coverage Fund (AHCCF)	2,025	2,527	2,744	217	8.6%
Deferred Compensation Fund (DCF)	1,514	1,682	1,822	140	8.3%
Judges' Retirement Fund (JRF)	1,124	1,250	1,336	86	6.9%
Judges' Retirement Fund II (JRF II)	1,242	1,367	1,441	74	5.4%
Legislators' Retirement Fund (LRF)	397	482	508	26	5.4%
Replacement Benefit Custodial Fund (RBF)	7	7	7	-	-
Subtotal	\$ 402,152	\$ 442,046	\$ 443,197	\$ 1,151	0.3%
Reimbursements ¹	1,604	1,500	1,500	-	-
Total CalPERS	\$ 403,756	\$ 443,546	\$ 444,697	\$ 1,151	0.3%

¹ Amounts received by CalPERS for services rendered. These reimbursements are actuarial valuations prepared for public agencies that qualify for reimbursement, cost of photocopies/postage related to the Public Records Act requests, annual employer conferences, and administrative assessments for employers' delinquent payroll.