May 31, 2017

Item 7900
CalPERS Supplemental Payment, Issue 34

LEGISLATIVE ANALYST'S OFFICE

Presented to:

Budget Conference Committee

Hon. Holly J. Mitchell, Chair

LAO
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Governor's May Revision Budget Proposal

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☑ ***Use Borrowed Money to Make One-Time Supplemental Payment to CalPERS.*** The administration proposes borrowing $6 billion from the state government funds in the Pooled Money Investment Account (PMIA) to make a one-time supplemental payment to reduce unfunded liabilities at CalPERS.

☑ ***Repay Loan Over Next Decade or So.*** Under the administration's plan, the state would pay interest on the loan based on a rate equal to a specific two-year U.S. Treasury index. The state would pay the full principal and interest of the loan by 2030.

- The General Fund would repay its portion of the loan using constitutionally required debt payments under Proposition 2 (including a $427 million repayment proposed in 2017-18).
- Special fund repayments would be apportioned by fund according to their pension payments.

Legislative Action

☑ **Assembly**

- Adopted the Governor's proposal.

☑ **Senate**

- Approved $427 million Proposition 2 supplemental payment to CalPERS in 2017-18.
- Did not approve PMIA loan proposal.

LAO Comments

- ☑ ***Fiscal Benefit to the State Is Likely, but Uncertainties Remain.*** The administration projects the loan would benefit the state by $11 billion over the long term. The amount of this benefit would depend on a variety of factors including: investment returns, interest rates, cash flow and external borrowing costs, internal borrowing costs, and the length of the loan.

- ☑ ***Administration Has Not Carefully Considered Implications of Proposal.*** The administration has completed few of the legal or quantitative analyses the Legislature should expect when receiving a request of this magnitude and complexity. For example, local governments often ask actuaries to report publicly on the probability that borrowing would generate net pension savings under a variety of investment scenarios.

- ☑ ***LAO Compromise.*** The Legislature could commit Proposition 2 funds in the budget to reduce the state's CalPERS pension liabilities in 2017-18 and consider the specifics of the PMIA loan at a later date after the administration has submitted additional analysis. Specifically, the Legislature could:

  - ***Adopt Budget Bill Language Requiring the Administration to Conduct Further Analysis of PMIA Loan.*** The Legislature could require the administration to conduct specific legal and quantitative analyses to better understand the risks and possible fiscal effects of the loan proposal. The Legislature could consider the administration's PMIA loan proposal after the administration has published its analyses.

  - ***"Pencil in" $427 Million Towards Proposition 2 Debt Payment.*** The budget could include a one-time $427 million Proposition 2 supplemental payment to CalPERS or any other state retirement system. If the Legislature later approves the PMIA loan, this $427 million could be applied to replay that loan.