BUILD THE GOLD LINE TO MONTCLAIR

October 27, 2016

TO: Honorable Mayor and City Council

FROM: Edward C. Starr, City Manager

SUBJECT: CITY MANAGER'S WEEKLY REPORT: October 21-27, 2016

CITY MANAGER/ADMINISTRATIVE SERVICES DEPARTMENTS

- As more and more local government agencies struggle with meeting excessively high pension costs stemming from failures of the California Public Employee Pension System (CalPERS) to meet investment targets at a time when the stock market and real estate values are reaching all-time highs, the pension fund is sending a clear signal of its intent to crack down on employers unable to meet contribution obligations by threatening or acting to reduce retiree pensions. Case in point: Loyalton, a small Sierra County town, stopped making payments to CalPERS more than three years ago. In response, it is being reported that CalPERS is taking action to reduce pension payments for the town's four retirees—the proposed reductions would be in proportion to payments not made by the employer.

  Loyalton, a financially troubled town of approximately 780 residents, apparently stopped making payments to CalPERS in March 2013. The governing board unanimously determined that in order to avoid insolvency, the town could no longer make its CalPERS payments. For the present, the four Loyalton retirees continue receiving full pensions. To avoid imposing pension reductions, CalPERS reportedly issued a final demand letter in September 2016, directing the town to make a one-time lump sum payment of $1.66 million to fund the pensions of its four retirees—an amount more than the town's entire annual budget. If Loyalton fails to make the payment, the CalPERS board, at its November 2016 meeting, will be asked to declare the town in default, triggering pension cuts—a first for the state and perhaps the nation. One annuitant would see a pension cut from approximately $48,000 annually to $19,000.

Reductions to pension earnings appear to go against CalPERS' "protected status" message routinely told to public employees:

- ✓ Public pensions are bulletproof because cities seldom go bankrupt and states never do—in fact, several recent municipal bankruptcies have shown considerable light on the fallacy of this perspective, exposing CalPERS to both legal and public scrutiny, and raising awareness of the funding weakness of public employee pensions nationwide;

- ✓ Overtime, CalPERS retains high earning averages that keep pace with rising pension costs. Since the early 2000s, CalPERS' investment portfolio has been adversely impacted by a number of earning deficiencies, including its own failure to properly understand the full economic impact related to its advocacy for drastically improved retirement formulas;

- ✓ California has the nation's most protective pension laws and legal precedents (the "California Rule") and employers must fund pensions for the duration of an eligible employee's life, even if costs to the employer are unreasonably high or were severely underestimated at the outset (both of which characterize the CalPERS management of public pensions)—in fact, many public agencies are beginning to balk at the excessive pension costs triggered by CalPERS' poor performance record and recent court decisions are eroding the "bulletproof" status of the California Rule;

- ✓ In the event a contract agency does face insolvency, CalPERS, rather than reducing payments to annuitants, would pass on costs to the Fund's remaining participating agencies (CalPERS reportedly revealed this strategy during the City of San Bernardino bankruptcy. However, through its actions related to Loyalton, CalPERS is now indicating a shift from this perspective and will hold individual agencies and their respective retirees fully responsible for failed payments to the pension fund.

In recent years, California court decisions have eroded the bulletproof status of pension plans, building a stronger case for cities to exit CalPERS, reduce pension obligations, or otherwise reduce payments through bankruptcy actions. Loyalton has not filed for bankruptcy, but the town's finances are strained. According to a state controller's report for 2015, Loyalton had revenues of $1.17 million, expenditures of $1.68 million, liabilities of $6.16 million, assets of $11.1 million, and fund equity of $4.8 million.

Loyalton is not the only agency caught in CalPERS' funding crisis. Both the California Fairs Financing Authority and Niland Sanitary District received 30-day payment demand letters. Both agencies are inactive, but not yet terminated from CalPERS. If the Fairs Financing Authority and Niland Sanitary District fail to make payments, CalPERS staff will present the matter to the Board, also at the November meeting, asking that the Board terminate their contracts.

The Fairs authority would face a $9.4 million lump sum payment if terminated, according to its valuation report; it has 20 retirees, 14 transferred members, and 24 separated members. And, the Niland district would face a lump sum payment of $88,000 if terminated, as indicated in its CalPERS valuation report—it has 1 retiree, 1 transferred member, and 2 separated employees.

CalPERS' interaction with the town of Loyalton demonstrates that the pension promise may not be absolute. CalPERS is retreating from past claims that it would increase rates for other member agencies to keep retiree pensions whole if the parent agency fails to pay in to the pension fund.

What has brought about this change in CalPERS policy? In September 2016, the CalPERS board was told a new policy had been drafted to prioritize and speed up collections from member agencies. The actions against Loyalton and other agencies resulted from this policy change.

When a plan is terminated, CalPERS must pay the lifetime pensions with no more money coming in from employers and employees. In the past, CalPERS used its investment earnings forecast (currently set at 7.5 percent), to discount the debt for a terminated plan. Then in 2011, *CalPERS dropped* the terminated plan discount to a more realistic risk-free bond level (3.25 percent), causing debt and termination fees to soar. At the same time, CalPERS continues to maintain the fallacy that its annual earnings on investments remain at 7.5 percent for active plans. Last year (Fiscal Year 2015-16), CalPERS earned a meager 0.61 percent on investments. This failure to achieve the higher rate of earnings (7.5 percent) is what has imperiled CalPERS' fiscal status, causing the fund to raise rates on active plans to cover a massive unfunded liability.

According to CalPERS, terminated CalPERS plans go into a pool that paid $4.7 million to 716 retirees and beneficiaries from 93 plans in the fiscal year ending June 30, 2016. The Terminated Agency Pool was 261.9 percent funded as of June 30, 2014, due to the excessively high fees charged to cities placed in the pool.

CalPERS reportedly justifies a healthy surplus in the terminated pool to avoid a big bite if a large plan entered the pool. Allegedly, if the Terminated Agency Pool falls short, CalPERS would have to resort to using the funds of state and local government plans to cover the shortfall. The reasoning, however, is unsound. CalPERS assesses an extraordinarily high termination fee, which would require the terminated agency to more than pay for the cost of future pensions; furthermore, CalPERS is now demonstrating that it would reduce pension payments to annuitants as a means to reduce any fiscal impact on the Terminated Agency Pool. Also, a *report* prepared for the CalPERS board indicates that an underfunded plan that has not paid the termination fee can, after reasonable efforts to collect, enter the terminated pool with little or no cut in pensions if there is no impact on the Terminated Agency Pool's "actuarial soundness." However, the CalPERS Board can reject such qualified entries into the termination pool if it deems the agency's termination is voluntary or it ignored collection demands. CalPERS is also concerned with setting precedent and maintaining equality treatment of plans.

The CalPERS board did discuss attaching a lien on assets and revenue stream for agencies entering the Terminated Agency Pool, but such action would be harmful to a city financially distressed; further, lien efforts to attach revenues can typically be blocked in court, particularly when judicial decisions are eroding the sanctity of pension systems.

What triggered this pension crisis? In California, improved retirement benefits were granted in the early 2000s when CalPERS made the faulty assumption that investments would keep climbing and cover costs associated with improved plans. That flawed premise drove many cities, under increasing employee labor union pressure, to grant significantly richer plans, including the public safety 3 percent @ 50 formula, promising 90 percent of earnings at age 50 after 30 years of employment. But within one year, skyrocketing employer rates clearly established that the CalPERS Board was flat out wrong in ignoring critical signs that the fund could not effectively cope with the formula improvements. As a result, cities, including Montclair, have been struggling ever since with massive, annual employer rate increases.

To stop local governments and special districts from considering voluntary termination from CalPERS to escape excessively high employer rates, the pension fund annually reports to each of its 3,007 participating agencies how much they would have to continue contributing each year (voluntary termination fee) to pay off obligations. During the Stockton bankruptcy, a federal judge questioned the CalPERS voluntary termination fee that boosted Stockton’s pension debt or unfunded liability from $211 million to $1.6 billion, calling it a "poison pill" if the city tried to move to another pension provider.

Several small cities, including Pacific Grove, Villa Park and Canyon Lake, considered leaving CalPERS but ended the process after looking at the high poison pill–voluntary termination fee. For Montclair, the voluntary termination fee is approximately $450 million, or more than 15 times the City’s annual General Fund Budget.

Will the "California Rule" stand? The judicial tide appears to be turning against the sanctity of public employee pensions. An appeals court, in August, declared that public retirement plans are not immutable and could be reduced. The Court determined that the law merely requires governments to provide a reasonable pension. Effectively, the court ruled the Legislature can alter pension formulas for active members and reduce their anticipated retirement earnings.

Employees of the Marin County Employees’ Retirement Association appealed the ruling to the California Supreme Court, arguing the Public Employee Pension Reform Act of 2012 (PEPRA) violates the state Constitution because it denies the inclusion of certain pay components when calculating retirement earnings. The Court is now reviewing written arguments. The Court could agree to take the appeal, let the decision stand as precedent, or limit its effect. Proponents of the decision argue it is the means to reduce a massive state and local government pension shortfall now in the hundreds of billions of dollars. Because California has an outsized role in developing pension law, the Court’s decision will be watched by other states. A decision by the Court may come before the end of the current calendar year.

Some legal scholars, however, are not so quick to project a win for the lower court ruling. Standing in the way are decades of court decisions that shape and define the California Rule—decisions that guarantee government workers the pension in place the day they were hired—effectively treating pensions as contracts protected by the state Constitution. The California Rule, therefore, makes it difficult for states to reform pensions for classic members (those hired into the pension system before January 1, 2013).

Two cases that contributed directly to formulation of the California Rule are 1) Kern v. City of Long Beach (a firefighter who had contributed to his pension for 20 years sued because the city abolished pensions for all working employees 32 days before he was entitled to retire. The court acted to protect the employee's right to a pension), and 2) Allen v. City of Long Beach (the California Supreme Court ruled that any cutbacks in pensions for current employees must be offset by comparable new advantages).

At least 12 other states have adopted the California Rule, although with less strict adherence to its interpretation in California courts. The state argues that PEPRA does not violate the California Rule because it changes pension formulas only for employees hired on and after January 1, 2013; the formula for classic members can only be altered if it is neutral or advantageous to the employees.

As a result of the California Rule, local governments around the state are struggling to cover the growing cost of pensions; and because pensions cannot be legally reduced, the only real options remaining are reductions in personnel, restrictions on pay adjustments, and less costly pension plans for new hires.

Ironically, PEPRA may now provide the catalyst for change to the California Rule. Curiously, judges were largely exempted from PEPRA, perhaps predisposing them to take a harder look at the fiscal impact of public employee pensions, and they appear to be doing so.

- The California Department of Motor Vehicles (DMV) says it expects field offices around the state to soon be operating normally after what it calls a "catastrophic" computer failure.

  The outage, which began on Monday, affected hundreds of DMV offices across the state. Officials said the computers were not hacked or targeted by outside groups; instead the outage was the result of a hardware failure. IT technicians have worked around the clock to repair the hardware failure.

  Driver license and vehicle registration services were affected, but offices without computer services were still providing driving tests, making appointments for customers to return, helping with paperwork, and answering customers' questions.

The department says its offices should be operating normally by the end of the week and advises drivers to check www.dmv.ca.gov or call 1-800-777-0133 to see if their local field office was affected. The department's online services were not harmed.

- The Foothill Gold Line Construction Authority released two reports earlier this week that detail the amount of transit-oriented development (TOD) that has been built or is underway within a half-mile radius of a current or future Gold Line station, including the significant economic impact the corridor's development is bringing to the region.

  The reports, prepared by The Maxima Group and Beacon Economics, quantify the number of housing units, hotel rooms, and square feet of commercial space built along the corridor since the Gold Line's first segment opened for passenger service in 2003 and planning began for the extension from Pasadena to Montclair. They also highlight the direct, indirect, and on-going economic impact these projects have had on the region's economy.

  The studies found that $6.7 billion of private investment has already been made along this corridor since 2003 ($3.3 billion in the city of Pasadena alone); resulting in more than 12,500 new housing units, 3.6 million square feet of commercial space, and 1,400 hotel rooms being built within a half-mile radius of a Gold Line station. These projects have resulted in the creation of nearly 50,000 direct and indirect jobs during construction, 20,000 ongoing jobs for Los Angeles County workers, and $50 million in annual tax revenues to the county during the worst economic downturn since the Great Depression.

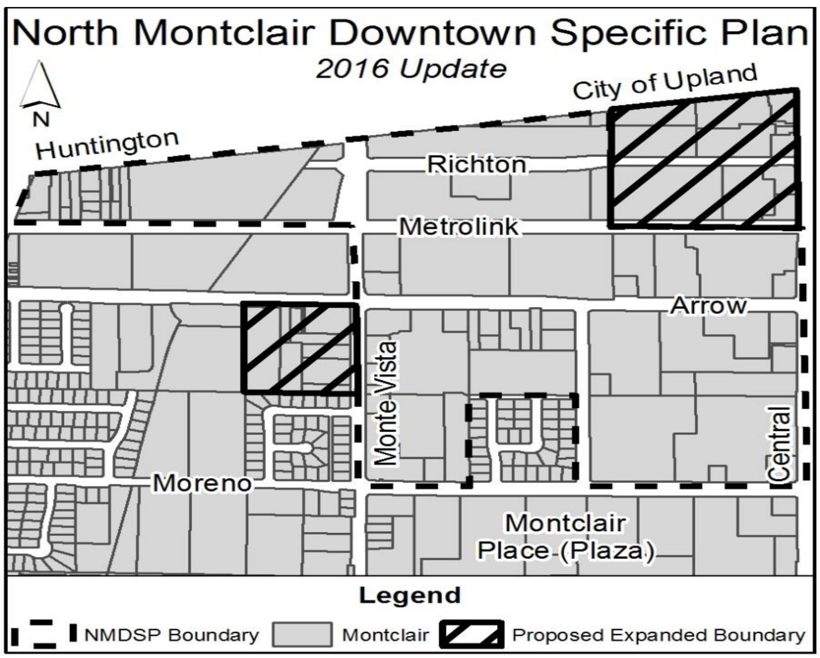
  The Maxima Group's report also measured the potential TOD that could take place along the Phase 2 corridor from Arcadia to Montclair looking forward, and found that a full build out of all the potential TOD projects would add 17,000 more housing units, 10 million additional square feet of commercial space, and 250 more hotel rooms to this transportation corridor in the future; generating $100 million more in annual tax revenues to Los Angeles County and creating tens of thousands of temporary jobs during construction and tens of thousands of more jobs with the on-going operation of businesses within these developments.

  I encourage you to review the TOD reports: (1) <u>Foothill Gold Line Transit Oriented Development Update</u>, by The Maxima Group and (2) <u>Economic and Fiscal Impacts of Transit Oriented Development at Gold Line Foothill Extension Pasadena Stations</u>, by Beacon Economics.

COMMUNITY DEVELOPMENT DEPARTMENT/ECONOMIC DEVELOPMENT

- On October 19, the City hosted a Scoping Hearing at City Hall related to the preparation of the Supplemental Environmental Impact Report for the North Montclair Downtown Specific Plan (NMDSP) Update project. Eight (8) members of the public attended the meeting where they were provided information on the project and the required environmental review process. After a presentation by City staff and consultant, attendees were able to ask questions and provide comments. Some of the questions were related to density, privacy, parking, wildlife, and adaptive reuse of existing buildings. These comments will be addressed in the Final Environmental Impact Report document to be released for public review and comment later this year.

The diagram, below, depicts the current NMDSP boundaries and the proposed areas of expansion



Further information on the project may be obtained by contacting City staff and/or by reviewing related documents available for public review and comment at: http://www.cityofmontclair.org/news/displaynews.asp?NewsID=532, the Montclair Library, and the Planning Division's public counter.

Scoping Comments Must be Received or Postmarked by November 1, 2016

Please send comments to:

City of Montclair
Community Development Department
5111 Benito Street
Montclair, CA 91763
Attention: Michael Diaz, City Planner
mdiaz@cityofmontclair.org

Please be sure to include your name, address, and phone number on all comments.

- On October 17, the City Council approved Tentative Tract Map 19713, involving proposal to convert an existing 28,128 square-foot, two-story, medical office building into 23 office condominiums—each unit to be sold separately and governed by an owner's association. The office unit sizes would range from 819 square feet to 1,670 square feet. The property is located on the north side of San Bernardino Street between Montclair Hospital and Montclair Royale Senior Housing complex.

Proposed exterior site improvements including landscaping and building facade upgrades as generally depicted on the attached drawings

4950 SAN BERNARDINO STREET
MONTCLAIR, CA 91763

PERSPECTIVE VIEW OF ENTIRE BUILDING

VIEW OF PROPOSED FRONT ENTRY

- Chipotle on Tuesday reported third-quarter earnings results that showed sales fell more than expected, about one year since outbreaks of E. coli and norovirus were linked to its food.

  The company said it earned $1.04 billion in revenue, according to Bloomberg. Diluted earnings per share fell to $0.27 from $4.59, including 29 cents related to the impairment charges at its ShopHouse Asian restaurants, and 23 cents due to the deferral of revenue from Chiptopia, its new rewards program.

  Analysts had forecast EPS of $1.56, although this may not be comparable to the reported figure of $0.27. They expected revenue totaling $1.09 billion.

  Comparable-store sales, at locations open for at least one year, fell 22 percent, more than analysts' forecast for a 19 percent decline.

  The disease outbreaks drove customers away from Chipotle and, in the first quarter, led to the company's first sales decline since it went public. Chipotle launched aggressive marketing campaigns and promotions to lure customers back.

  Chipotle anticipated that next year will be better. In 2017, it forecast that comparable restaurant sales will rise in the "high single-digits."

  For the full-year 2016, Chipotle expected that new restaurant openings would be at or above the high-end of its previously announced range of 220 to 235. It saw same-store sales declines in the "low single-digits" for the fourth quarter.

  The shares gained as much as 3 percent in after-hours trading before slipping. They were down 15 percent this year through the close of trading on Tuesday.

- New survey data from Morgan Stanley suggests Amazon's fashion business is quickly growing in popularity while eating into the market traditionally owned by big box retailers like Macy's and JC Penney.

  The survey, which polled 2,000 U.S. teens and adults, says 58 percent of the respondents shopped at Amazon in the past 6 months, making it the most popular apparel retailer in the country.

  Kohl's, JC Penney, and Macy's trailed by a wide margin, each receiving 37 percent, 33 percent, and 27 percent of the votes, respectively. The three retailers also saw the biggest declines in year-over-year purchasing activity.

  "These data points continue to support our thesis that Amazon is quickly gaining consumer traction in apparel at the expense of department stores and select specialty retailers," Morgan Stanley wrote in the note Tuesday.

  Morgan Stanley also forecasts Amazon will account for roughly 17 percent of the U.S. apparel market by 2020, selling $51 billion worth of clothing items per year.

HUMAN SERVICES DEPARTMENT

- Don’t miss out on the City’s Annual Children’s Halloween Party on Monday, October 31 from 5:30 p.m. to 8 p.m. in the Community Center. The party is free to children 12 and under, and parental supervision is required. Included will be a costume contest that begins at 6:45 p.m., prizes, games, refreshments, and lots of candy.

- Last Thursday evening, Council Member John Dutrey and I attended the City of Montclair Expanded Learning Program’s 17th Annual Lights on Afterschool celebration in the Community Center. This year’s theme was "The I’Mpossible Dream-Inventors: They Paved the Road to MY Future."

  Inventions that have made our lives easier were on display from each of the City’s 11 after-school program sites. There were also dance performances by students from El Camino, Mission, and Monte Vista Elementary Schools.

The Chief of Police was caught red-handed tinkering with the inventions

A highlight of the night was a visit and presentation from the famous American inventor, "Dr. Benjamin Franklin." Dr. Franklin spoke to the audience about life during the 18th Century and some of his inventions, like the Franklin stove, bifocals, and the glass harmonica. He then created electricity with a working electrostatic generator.

A big "thank you goes to the Lights on Afterschool committee, the Learning Coordinators, and staff for making our event a success.

Pictured from left: Senior Citizens Supervisor Ester Vargas Pipersky, City Manager Edward Starr, Police Chief Robert Avels, and Human Services Director Marcia Richter

POLICE DEPARTMENT

- On Monday, a swearing-in ceremony was held for Police Lieutenant Matthew Borra (promoted from Police Sergeant) and Police Sergeant Andrew Graziano (promoted from Police Officer). Their new classifications took effect on October 17. Congratulations!

Chief Avels is shown swearing-in Sgt. Andy Graziano and Lt. Matt Borra

ECS:spa

"Where there is no imagination there is no horror."

~ Sir Arthur Conan Doyle

OCTOBER 2016

31	Children's Halloween Party Community Center	5:30 p.m. - 8 p.m.

NOVEMBER 2016

1	City Manager's Staff Meeting City Hall Conference Room	9:00 a.m.
2	Community Action Committee Meeting Council Chambers	7:00 p.m.
6	Daylight Savings Time Ends	
7	City Council Workshop – The Ralph M. Brown Act Council Chambers	5:45 p.m.
7	City Council Meeting Council Chambers	7:00 p.m.
8	Election Day	
10	City Offices Closed in Observance of Veterans Day	
11	Veterans Day	
14	Planning Commission Meeting Council Chambers	7:00 p.m.
15	City Manager's Staff Meeting City Hall Conference Room	9:00 a.m.
16	Safety Committee Meeting City Hall Conference Room	10:30 a.m.
17	Public Works Committee Meeting City Hall Conference Room	4:00 p.m.
21	Real Estate Committee Meeting City Hall Conference Room	5:30 p.m.
21	Code Enforcement/Public Safety Committee Meeting City Hall Conference Room	6:15 p.m.
21	City Council Meeting Council Chambers	7:00 p.m.
24	City Offices Closed for Thanksgiving	
28	Planning Commission Meeting Council Chambers	7:00 p.m.