



City of Brea

November 20, 2014

Dave Baker, Foreman
Orange County Grand Jury
700 Civic Center Drive West
Santa Ana, California 92701

Dear Mr. Baker,

Attached is the City of Brea's response to the Grand Jury's report, *Orange County City Pension Liabilities – Budget Transparency Critically Needed*.

Sincerely,

Terrie Stevens
Human Resources Manager

cc: Tim O'Donnell, City Manager

City Council

Brett Murdock
Mayor

Christine Marick
Mayor Pro Tem

Ron Garcia
Council Member

Roy Moore
Council Member

Marty Simonoff
Council Member

Findings

F.1. OC cities have large unfunded pension liabilities both in terms of absolute dollar value and on a per capita basis and as a percentage of city General Fund revenues.

I cannot speak to other OC cities unfunded pension liabilities. The respondent agrees with the finding as it applies to the City of Brea.

F.2. OC cities' unfunded pension liabilities have been increasing on a year over year basis over the past several years as a result of the 2007-2009 Great Recession and as key actuarial assumptions have been changed by CalPERS and OCERS.

I cannot speak to other OC cities unfunded pension liabilities. The respondent agrees with the finding as it applies to the City of Brea.

F.3. There are risks to OC cities of changes to key actuarial assumptions including revisions downward of expected returns on investment and the likely move by pension funds to using more realistic mortality assumptions, which would increase unfunded liabilities.

I cannot speak to other OC cities unfunded pension liabilities. The respondent agrees with the finding as it applies to the City of Brea.

F.4. Locating city budget information on a city web site is not always straightforward and prior year budgets are sometimes not posted by a city.

I cannot speak to other OC cities' website postings of their budgets. The respondent wholly disagrees as it applies to the City of Brea. City budget information is straightforward and prior year budgets are posted in our on-line archived documents.

F.5. City budgets posted online project revenues and expenditures for at most one or two years into the future and sometimes do not show prior year data.

I cannot speak to other OC cities website postings of their budgets. The respondent wholly disagrees as it applies to the City of Brea. The City of Brea posts revenue and expenditure projections for a five year period as well as prior year data.

F.6. City budgets often lack footnotes explaining key assumptions, risks, and unusual changes in budgeted amounts or revenues and expenditures.

I cannot speak to other OC cities budgets. The respondent wholly disagrees with the finding as they apply to the City of Brea. The City of Brea includes detailed information regarding key assumptions, risks and unusual changes in budgeted amounts.

F.7. City budgets sometimes do not provide trend data on the accumulation/drawdown of reserves and lack details on the city's plan for the size of its reserves or their intended uses.

I cannot speak to other OC cities website budget postings. The respondent wholly disagrees as it applies to the City of Brea. The City of Brea's budget includes the policy which indicates the minimum size of its reserve and intended uses. It also includes data over a five year period showing the accumulation/drawdown of reserves.

F.8. Cities can control most future expenditures by increasing or decreasing budgets for those expenditures as funds are available. However, increases to annual required contributions to their pension systems are imposed externally, change unpredictably, and when they occur, are ramped up over two to five years.

I cannot speak to this item for other OC cities. The respondent disagrees in part and agrees in part. Disagrees with the statement that Cities can just increase or decrease budgets when expenditure needs change and with the inference that since pension contributions are imposed externally that only they are difficult to deal with. The housing bust and subsequent recession dramatically changed public revenues and affected future expenditures. Those were external pressures that dramatically affected tax revenues and thereby budgets. There are options for handling unexpected revenue and expenditure decreases whether they are imposed by an internal or external force. Agree in that CalPERS has the ability to require increased contributions to pension plans.

F.9. City budgets posted online do not explicitly show the link between planned city pension expenditures and pension system actuarial reports and those reports' annual required contributions. Risks associated with predictions of future annual required pension contributions. Risks associated with predictions of future annual required pension contributions based on risk assessment data provided by their pension systems and/or based on their own analysis are not discussed.

I cannot speak to other OC cities website postings of their budgets. The respondent disagrees in part and agrees in part. Disagrees that the pension system actuarial reports are not provide online. The City has all actuarial reports in our online document archival system. Agrees that the City budget does not explicitly show the planned City pension expenditures and the annual required contributions.

F.10. Pension costs for New (Post-PEPRA) employees will be substantially lower than for Legacy employees, but only a small percentage of current employees, typically only a few percent of total employees, are New. Substantially reduced

pension costs for cities as a result of pension reform will not be realized for one or more decades.

I cannot speak to other OC cities pension costs or the affect of PEPRA changes to their budgets. The respondent agrees that it could be several years before a substantial reduction in pension costs are realized from the legislative changes enacted by PEPRA. The City of Brea however, implemented pension reform over two years before PEPRA was implemented, which required new hires to contribute 100% of the employee retirement contribution and created a lower, second tier, retirement formula for safety positions.

F.11. CalPERS Annual Valuation Reports for Miscellaneous and Safety City employees are available to the public online for a very small number of cities.

I cannot speak to other OC cities website postings of their budgets. As to the City of Brea, respondent wholly disagrees. The City of Brea does post the CalPERS Annual Valuation Report in its online document archival system.

F.12. OCERS provides pension plans for OCFA and OCSD employees, but there is no way to trace through publically available sources OCERS unfunded pension liabilities to the city budgets which outsource to OCFA and OCSD for fire and police services.

I cannot speak to this issue as the City of Brea has no involvement with OCFA, OCSD or OCERS.

RECOMMONDATIONS:

R.1. Each City should post its current and at least three most recent prior year budgets on the city's web site, and these budgets should be easily located. Each city's web site should have a search engine and a single search on the word "budget" should immediately link to the current budget.

The first recommendation cited in R.1. will not be implemented because it is not warranted. There has been little interest by members of the public in viewing past year budgets. For anyone interested in viewing older budgets, those documents are all listed in the on-line archival documents. The second recommendation in R.1. Has been in place for many years at the City of Brea. A search from the word "budget" will immediately link to the current budget on the City of Brea's website.

R.2. Each city's budget information should contain not only this year/next year budget projections, but should show at least five years of projected revenues and

expenditures. Projections should be at the same level of detail and use the same line item structure as information for the current budget.

The first recommendation cited in R.2. has been a practice of the City of Brea for many years. The second recommendation cited in R.2. will not be implemented because it is not reasonable. Developing an annual budget takes several months and involves many employees in each City department. To do five year projections with the same level of detail as the annual budget would be too onerous.

R.3. Each city's budget should show separate line items for predicted employee and predicted employer contributions for the city pension systems.

The recommendation will not be implemented because it is not warranted. Salary and benefit costs are delineated in the budget. There is no reason to separate the various components.

R.4. Each city's budget should provide trend data on the accumulation/drawdown of reserves and provide details on the city's policy for the size of its reserves and on the intended uses of such reserves. In particular any discussion of reserves should address possible use of reserves to accelerate amortization of unfunded pension liabilities.

The first part of R.4. has been in place in the City of Brea for many years. The five year projections show the accumulation and drawdown of reserves and the budget contains the City's policy for the size of its reserves and the intended uses. The second part of R.4. will not be implemented. Acceleration of payments towards the "unfunded" pension liability could result in financial losses with no benefit to the City. If for instance the City has a \$1 million future liability to CalPERS for its pensions and it is paid in advance and PERS investment returns are lower than expected we could lose the benefit of having had paid down the balance.

R.5. Each city using CalPERS for one or more of its pension plans should identify the names and dates of the CalPERS Annual Valuation Reports(s) which call out Annual Required Contributions (ARCs) for these plans and should provide a separate expenditure line item for predicted city catch-up contributions for the city pension systems based on these ARCs. A discussion of the risks associate with the CalPERS projections should also be provided by the city.

The recommendation will not be implemented because it is not warranted and is unreasonable. The CalPERS Annual Required Contributions are already listed on our website under "transparency". The City is not the appropriate one to determine and discuss associated risks with CalPERS projections.

R.7. Each city that has CalPERS as a provider for pensions should include a provision in their agreements with CalPERS that CalPERS will post their Annual Valuation Reports online.

The recommendation will not be implemented because it is not warranted. The City of Brea already posts the Annual Valuation Reports online.