

August 6, 2014

The Honorable Glenda Sanders
Presiding Judge, Orange County Superior Court
700 Civic Center Drive West
Santa Ana, CA 92701

RE: CITY OF TUSTIN'S RESPONSE TO ORANGE COUNTY GRAND JURY REPORT, "ORANGE COUNTY CITY PENSION LIABILITIES – BUDGET TRANSPARENCY CRITICALLY NEEDED"

Dear Judge Sanders:

We have reviewed the Orange County Grand Jury Report, "Orange County City Pension Liabilities – Budget Transparency Critically Needed", which was released on June 25, 2014. The City of Tustin's responses to the report's findings and recommendations are as follows:

GRAND JURY 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.

Response: The City agrees with this finding.

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.

Response: The City agrees with this finding.

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.

Response: The City agrees with this finding.

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

Response: The City agrees with this finding. While the City of Tustin makes its budget information easy to access on the City's website and publishes five years of past budget information, this may not be the case with every city in the county.

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.

Response: The City agrees with this finding. The City of Tustin does include at least two prior fiscal years in its budget document; however, this may not be true for all cities in the county.

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

Response: The City agrees with this finding.

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.

Response: The City agrees with this finding.

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.

Response: The City agrees with this finding.

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 based on risk assessment data provided by their pension systems and/or based on their own analysis are not discussed.

Response: The City agrees with this finding.

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.

Response: The City agrees with this finding. While over 11% of the City of Tustin's current full-time employees are in the new PEPRA retirement plans, substantial reductions to pension costs as a result of PEPRA will most likely not be realized for many years.

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.

Response: The City disagrees with this finding. For the last several years, CalPERS has published their Annual Valuation Reports for all member agencies on their website at www.calpers.ca.gov. Reports can be found by searching for "annual valuation report" or "actuarial report" from the CalPERS home page.

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

Response: The City disagrees with this finding. Under the terms of our agreement with OCFA, Tustin (and other cities that contract for services with OCFA) is not responsible for any unfunded pension liabilities associated with OCERS. Therefore, this information would not be included in our City's budget.

GRAND JURY RECOMMENDATIONS

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

Response: This recommendation has been implemented. For many years, the City has posted its current and recent prior year budgets on the City's website. The links to the City's budgets are accessible by accessing either the Finance Department's home page or the City's Transparency in Government page. Further, the budgets are immediately accessible through a single search on the search engine embedded into the City'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.

Response: The City's budget document includes revenues and expenditures for the two prior fiscal years, the current fiscal year and the projected fiscal year. The recommendation to include at least five years of projected revenues and expenditures at the same level of detail and use the same line item structure as information for the current budget will be implemented with the fiscal year 2015/2016 budget.

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

Response: This recommendation will be implemented. The City's budget currently reports separate line items for the City's contribution towards the employer share of pension costs as well as the City's contribution towards the employee share of pension costs. Since the City currently does not pay any of the employee's contribution the line item for each department is zero. The City's budget does not currently report the pension contributions paid directly by employees. In addition to paying the full employee contribution, most employees also pay 3% of the employer's contribution as cost sharing; therefore, the total amount budgeted for the employer's contribution is net of the 3% employee cost-sharing contribution. For fiscal year 2015/2016 the City's budget document will show separate line items for predicted employee and employer contributions so the reader will know how much the employees actually contribute and what the City contributes for pension costs.

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.

Response: This recommendation has been implemented.

R.5: Each city using CalPERS for one of more of its pension plans should identify the names and dates of the CalPERS Annual Valuation Report(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 associated with these CalPERS projections should also be provided by the city.

Response: The City will implement this recommendation for the fiscal year 2015/2016 budget.

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R.6: Each city which outsources fire or police services to OCFA and/or OCSD should require them to provide projections of future costs of service out at least five years into the future and require that these projected costs explicitly show the relationship of projected pension costs including amortization of unfunded liabilities. This level of pension cost information should be provided in budgeted expenditures for outsourced services. A discussion of the risks associated with these projections should also be provided by the agencies and incorporated in the city's budgets.

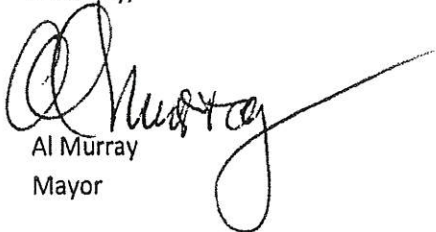
Response: A portion of this recommendation will be implemented, while another portion will not be implemented. The City currently outsources fire services to OCFA. We will provide projected costs of service at least five years into the future, beginning with the fiscal year 2015/2016 budget. Under the terms of our agreement with OCFA, Tustin (and other cities that contract for services with OCFA) is not responsible for any unfunded pension liabilities associated with OCERS, however, should OCFA provide the City with information regarding OCFA's unfunded liabilities, we can include this information in the City's budget.

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.

Response: This recommendation has been implemented. For the last several years, CalPERS has published their Annual Valuation Reports on their website at www.calpers.ca.gov. Reports can be found by searching for "annual valuation report" or "actuarial report" from the CalPERS home page.

The City thanks the members of the Grand Jury for their efforts in investigating this issue. If you have any questions regarding this letter, please feel free to contact Pamela Arends-King, Director of Finance/City Treasurer, at (714) 573-3061 or parends-king@tustinca.org.

Sincerely,



Al Murray
Mayor

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cc: Orange County Grand Jury
Jeffrey Parker, City Manager