



CITY OF RANCHO SANTA MARGARITA

September 10, 2014

Mayor

Carol A. Gamble

Mayor Pro Tem

Bradley J. McGirr

Council Members

Steven Baric

L. Anthony Beall

Jesse Petrilla

City Manager

Jennifer Cervantez

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

Dear Judge Sanders:

The City of Rancho Santa Margarita has reviewed the Orange County Grand Jury Report entitled, "Orange County City Pension Liabilities – Budget Transparency Critically Needed." As requested, the City of Rancho Santa Margarita is responding to the findings and recommendations included with in the report.

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: Based on the data provided by the Grand Jury, the City of Rancho Santa Margarita generally 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: Based on the data provided by the Grand Jury, the City of Rancho Santa Margarita 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: Based on the data provided by the Grand Jury, the City of Rancho Santa Margarita agrees with this finding.



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.

Response: The City of Rancho Santa Margarita partially disagrees with the finding. The City lists the current fiscal year budget plus six prior fiscal year budgets on its web site.

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 of Rancho Santa Margarita partially disagrees with the finding. Each budget for the City of Rancho Santa Margarita identifies the current Fiscal year adopted budget, the prior fiscal years amended and year to date estimate, as well as three prior fiscal years actuals.

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

Response: The City of Rancho Santa Margarita partially disagrees with the finding. Rancho Santa Margarita addresses key assumptions, acknowledges risks, and identifies changes regarding budgeted revenues and expenditures in the transmittal letter that is included in the budget.

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 of Rancho Santa Margarita partially disagrees with the finding. The City's budget includes a Schedule of Fund Balance for all funds. This schedule identifies the beginning fund balance, revenue, expenditures, and ending fund balance. This schedule reflects this detail for the current adopted budget and the prior four fiscal years. The resolution that adopts the city budget identifies the amount of reserve funds to be allocated in the budget. This resolution is included in the Appendices section of the budget.

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 of Rancho Santa Margarita partially disagrees with the finding. There are many outside factors that impact the City's budget that we have no control over, for example, utility and water rate increases. The City of Rancho Santa Margarita adjusts budgeted expenditures based on internal changes as well as amounts determined by external sources.

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 disclosed.

Response: The City of Rancho Santa Margarita partially disagrees with the finding. The City of Rancho Santa Margarita discloses the required pension information in their Comprehensive Annual Financial Report (CAFR), but will identify more specific detail regarding unfunded pension liabilities in future CAFRs as that information becomes available through CalPERS.

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: Based on the data provided by the Grand Jury, the City of Rancho Santa Margarita agrees with this finding.

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 of Rancho Santa Margarita partially disagrees with this finding. CalPERS lists, under the employer publications section of their website, the valuations for all contract agencies, but only for the last several years.



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

Response: The City of Rancho Santa Margarita has no direct knowledge of this finding other than it being stated in the Grand Jury Report.

RECOMMENDATIONS:

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. (F.1) (F.4)

Response: The recommendation has already been implemented. Rancho Santa Margarita currently lists the current fiscal year budget plus six prior fiscal year budgets on its web site. The City's web site's search engine links to the current and prior year budgets using a single search on the word "budget".

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. (F.1) (F.2) (F.3) (F.5) (F.8) (F.10)

Response: This recommendation has not been implemented by the City of Rancho Santa Margarita. The City is reviewing the methodology and format for extended projections and will study their usefulness and accuracy.

R 3: Each city's budget should show separate line items for predicted employee and predicted employer contributions for the city pension systems. (F.8) (F.9)

Response: This recommendation has not been implemented. The City is studying the applicability of including this information in the budget document.



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. (F.7)

Response: This recommendation has not been implemented. Currently, during the public hearing process the City provides a 10 year General Fund Reserve Model based on current assumptions for both revenues and expenditures. However, any discussion of accelerating the amortization of unfunded pension liabilities would require a change to our reserve policy.

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 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. (F.1) (F.2) (F.8) (F.9)

Response: The recommendation has not been implemented. Government Accounting Standards Board (GASB) is formulating regulations on the reporting of pension contributions (GASB 68). All cities will be required to book these values in their CAFR.

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. (F.6) (F.12)

Response: This recommendation has not been implemented and inclusion into the City of Rancho Santa Margarita's budget will be based on information provided by OCSD. The City is a Structural Fire Fund City and part of a Joint Powers Agreement with OCFA. The nature of this agreement does not provide the financial information necessary to include these figures in the budget document.



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. (F.11)

Response: The City of Rancho Santa Margarita will consult with CalPERS to clarify if this option can be implemented.

Should you have any questions or need any additional information, please contact Stefanie Turner, Finance Director, at 949-635-1808 or via e-mail at sturner@cityofrsm.org.

Respectfully,

Carol A. Gamble
Mayor
City of Rancho Santa Margarita

Cc: Orange County Grand Jury
700 Civic Center West
Santa Ana, CA 92701