



# CITY OF COSTA MESA

CALIFORNIA 92628-1200

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FROM THE OFFICE OF MAYOR JAMES M. RIGHEIMER

September 11, 2014


Honorable Glenda Sanders, Presiding Judge  
Superior Court of California  
County of Orange

SUBJECT: Response to Grand Jury Report: Orange County City Pension Liabilities  
Budget Transparency Critically Needed

The City of Costa Mesa understands the significance of the pension liabilities issue and appreciates the Grand Jury's work on this report. The City has worked intentionally and diligently to provide the public with as much information on this topic as possible. Please see the attached general comments as well as the specific City responses to the findings and recommendations of the Grand Jury report.

If you have any questions or need additional information, please contact Steve Dunivent, Interim Finance Director at 714.754.5243.

Sincerely yours,



JAMES M. RIGHEIMER  
Mayor

cc: Council Members  
Tom Hatch, CEO  
Members of the Pension Oversight Committee  
Rick Francis, Assistant CEO  
Tamara Letourneau, Assistant CEO  
Lance Nakamoto, HR Manager

Attachment

City of Costa Mesa  
Response to Grand Jury Report:  
ORANGE COUNTY CITY PENSION LIABILITIES—Budget Transparency Critically Needed  
Issued June 25, 2014

GENERAL COMMENTS

The City of Costa Mesa understands the significance of the pension liabilities issue and appreciates the Grand Jury's work on this report. The pension liability issue is significant and complex and warrants more attention than can be accommodated in the City's annual budget document. That is why the City provides the public much more information on this issue in the form of the following:

- Comprehensive Annual Financial Reports (CAFR) notes contain information regarding pension plans, cost and liabilities.
- City's Transparency website > City Employee Pension Information displays tables of pension costs by employee group, contribution rate trends, and contains links to various reports and PERS annual valuation reports.
- The City's Pension Oversight Committee was established in April 2013 and meets twice monthly in open, public meetings to review pension commitments and obligations, study the causes of the unfunded liability, advise the City on reserves and other financial issues related to pension obligations, review compensation packages and evaluate potential changes to pension benefits and advise the City on their impact.
- Pension Oversight Committee website (<http://www.costamesaca.gov/index.aspx?page=1603>) includes this committee's agendas, minutes, PERS valuation reports, "Fast Facts" informational bulletins, reports and presentations and actions logs.

In summary, the City of Costa Mesa has worked intentionally and diligently to provide the public with as much information on this topic as possible. In addition, the City Finance Department is developing a five-year plan that will incorporate projections of increasing pension costs and an analysis of the City's ability to pay those and other costs.

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.

City response: Agrees with the 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.

City response: Agrees with the 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.

City response: Agrees with the 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.

City response: Disagrees wholly with the finding. Costa Mesa's budget information is readily available on the City's website ([www.costamesaca.gov](http://www.costamesaca.gov)) either by using the search function (typing in "budget") or going to the transparency page and clicking budget information (<http://www.costamesaca.gov/index.aspx?page=562>) or by clicking City Hall then Finance. The City's website contains seven years of budget 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.

City response: Disagrees partially with the finding. The City's budget shows two to three years of prior year data; ten years of prior year data for major revenue categories.

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

City response: Disagrees partially with the finding. The City's budget contains introductory sections and detailed major revenue account descriptions that explain 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.

City response: Disagrees partially with the finding. The City's budget introductory section includes a short discussion regarding reserves. The five-year financial plan currently in development will provide more information on 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.

City response: Disagrees partially with the finding. Specific increases to annual required retirement contributions are known at least nine months prior implementation due to the timing of the PERS valuation reports. General long-term increases to annual required retirement contributions are known due to the inclusion of rate projections for the next four years in the PERS valuation reports that are updated annually.

**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.

City response: Agrees with the finding. However, the City Council's budget study session handouts (<http://www.costamesaca.gov/ftp/council/agenda/2014/2014-05-13/SS-Attach-2.pdf>) included the rates used for the retirement expense calculation. The rates are from the actuarial reports.

**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.

City response: Agrees with the 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.

City response: Disagrees partially with the finding. The City of Costa Mesa provides two years of online valuation reports for its three main bargaining units. (<http://www.costamesaca.gov/index.aspx?page=1614>)

**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.

City response: Agrees with the finding.

#### 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)**

City response: The recommendation has been implemented. See response to **F.4** above.

**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)**

City response: The recommendation will not be implemented because it is not warranted. The City's budget is prepared in conformance to the California Society of Municipal Finance Officers and Government Finance Officers Association standards. Future year projections will be contained in the City's five-year financial plan.

**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)**

City response: The recommendation will not be implemented because it is not warranted. The budget book has not traditionally included the employee contributions as these are not a budgeted City expense. However the City Council's budget study session handouts (<http://www.costamesaca.gov/ftp/council/agenda/2014/2014-05-13/SS-Attach-2.pdf>) included the employee contributions for the budget year as well as the past four years.

The City's transparency website > employee compensation report also shows, for each employee, actual employee and employer contributions for the pension systems. (<http://www.costamesaca.gov/index.aspx?page=692>)

**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)**

City response: The recommendation has not yet been implemented, but will be implemented in the future. The City's five-year plan will include the reserve policy, reserve size and intended uses and possible use of reserves to accelerate amortization of the liabilities.

**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)**

City response: The recommendation has not yet been implemented, but will be implemented in the future. This information will be included in the City's five-year financial plan which is a more suitable document for this level of detail and discussion.

**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)**

City response not required.

**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)**

City response: The recommendation will not be implemented because it is not warranted. See the response to **F.11** above.