



September 22, 2014

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

Re: City of La Palma Response to 2013-2014 Orange County  
Grand Jury Report "*Orange County City Pension Liabilities –  
Budget Transparency Critically Needed*"

Dear Judge Sanders:

The City of La Palma has reviewed the 2013-2014 Orange County Grand Jury Report, "*Orange County City Pension Liabilities – Budget Transparency Critically Needed*," which was made public on June 25, 2014. As requested by the Grand Jury and in accordance with California Penal Code §933 and §933.05, this letter constitutes the City of La Palma's response to the findings and recommendations contained in the report.

The City of La Palma agrees with the importance of addressing long-term pension liabilities and is proud of its past actions to address this issue. As the City is in a pool, it is currently unable to address its unfunded pension liability entirely; however, in 2009, the City paid the \$3.8 million unfunded liability created by enhanced retirement benefits granted in 2003 (commonly referred to as a side fund). This saved the City \$1.1 million in interest payments and reduced its ongoing operating expenditures by roughly \$500,000 per year. And, the City was one of the first Orange County cities to institute lower tiers of retirement for both safety and non-sworn members in 2011.

**Findings:**

**Finding F-1:** Finding F-1 states, "*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 of La Palma Response to Finding F-1:** The City of La Palma **agrees** with the finding, which is why in 2009 the City paid, in its entirety, the \$3.8 million unfunded liability in the CalPERS

side fund; and has long been a vocal advocate to find a method for CalPERS pooled agencies to pay off the remainder of their unfunded liabilities.

**Finding F-2:** Finding F-2 states, *“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 of La Palma Response to Finding F-2:** The City of La Palma **agrees** with the finding, which is why it paid off its CalPERS side fund unfunded liability in 2009; and in 2011 was one of the first Orange County cities to institute lower tiers of retirement for both newly hired safety and non-sworn members.

**Finding F-3:** Finding F-3 states, *“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 of La Palma Response to Finding F-3:** The City of La Palma **agrees** with the finding. These assumption changes are necessary to ensure that the CalPERS retirement system remains stable and able to provide the benefits that have been promised and that the cost of those benefits is transparent to the City, its residents, and its employees.

**Finding F-4:** Finding F-4 states, *“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 of La Palma Response to Finding F-4:** The City of La Palma **wholly disagrees** with this finding as it relates to itself. The City has eight years of budgets posted on its website and the information is easily accessible by clicking on a “Quick Link” on the front page of the website, by using the search feature, or by accessing the documents through the Finance Department page.

**Finding F-5:** Finding F-5 states, *“City budgets posted online project revenues and expenditures for at most one or two years into the futures and sometimes do not show prior year data.”*

**City of La Palma Response to Finding F-5:** The City of La Palma **partially disagrees** with this finding as it relates to itself. the City’s budget document shows the projected data for the immediate past year and accurate data for the preceding three years and as part of the City’s budget process, a ten-year Sustainable Financial Plan—including revenues, ongoing and capital expenditures, and reserve balances—is updated and analyzed.

**Finding F-6:** Finding F-6 states, *“City budgets often lack footnotes explaining key assumptions, risks, and unusual changes in budgeted amounts or revenues and expenditures.”*

**City of La Palma Response to Finding F-6:** The City of La Palma **wholly disagrees** with this finding as it relates to itself. The City of La Palma budget document includes an in depth analysis of key assumptions, risks, and unusual changes in the economy, budgeted amounts, revenues, and expenditures as part of the City Manager’s budget message.

**Finding F-7:** Finding F-7 states, *“City budgets sometimes do not provide trend data on the accumulations/drawdown of reserves and lack details on the city’s plan for the size of its reserves or their intended uses.”*

**City of La Palma Response to Finding F-7:** The City of La Palma **partially disagrees** with this finding as it relates to itself. While the documents are not currently in the budget document, La Palma has a Sustainable Financial Plan, which is updated annually as well as a separate Reserve Policy, both of which are available on its website for public review.

**Finding F-8:** Finding F-8 states, *“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 of La Palma Response to Finding F-8:** The City of La Palma **agrees** with this finding. Although increases to annual required contributions are imposed externally, the City took steps to reduce its obligations by instituting a second tier retirement program for all employees hired after July 1, 2011. The City incorporates CalPERS long term projections into its ten year Sustainable Financial Plan and through prudent fiscal management is prepared to adjust to future uncertainties.

**Finding F-9:** Finding F-9 states, *“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 of La Palma Response to Finding F-9:** The City of La Palma **agrees** with this finding. However, the City’s Sustainable Financial Plan incorporates CalPERS long-term rate projections along with projected staffing expenditures over a ten-year period and is used as a budget planning document. The City’s Comprehensive Annual Financial Report (CAFR) provides extensive information about all aspects of the City’s financial condition, including pension plans. The Budget Message also includes information about pension information as warranted. Additionally, three years of the City’s CalPERS Annual Valuation reports are available on the CalPERS website.

**Finding F-10:** Finding F-10 states, *“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 of La Palma Response to Finding F-10:** The City of La Palma **agrees** with this finding. While the benefit of reduced pension costs will not be seen for a decade, these changes will contribute toward the City’s long-term sustainability.

**Finding F-11:** Finding F-11 states, *“CalPERS Annual Valuation Reports for Miscellaneous and Safety City employees are available to the public online for a very small number of cities.”*

**City of La Palma Response to Finding F-11:** The City of La Palma **wholly disagrees** with this finding as it relates to itself. Three years of La Palma's Safety and Miscellaneous Actuarial Valuations are available on the CalPERS website at <https://www.calpers.ca.gov/index.jsp?bc=/about/forms-pubs/calpers-reports/actuarial-reports/browse-results.xml&strCatId=2&q=la-palma-city>.

**Finding F-12:** Finding F-12 states, "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 of La Palma Response to Finding F-1:** The City of La Palma **wholly disagrees** with this finding as it relates to itself. La Palma is a Structural Fire Fund (SFF) member of the Orange County Fire Authority (OCFA) which means that the City's "contribution" to the OCFA is made directly through property taxes paid to the Orange County Treasurer-Tax Collector; therefore, monies are neither budgeted or allocated by the City of La Palma. Additionally, pursuant to the OCFA Joint Powers Agreement (Article VI, Section 3 which states that "Except as otherwise provided herein, the debts, liabilities and obligations of the Authority shall be the debts, liabilities and obligations of the Authority alone and not the parties to the Agreement;" the liabilities of the OCFA are not the liabilities of La Palma. Further, OCFA's legal counsel opined in June 2014 that under the law and the Joint Powers Agreement, member agencies do not have liability for OCFA's pension obligations.

### **Recommendations:**

The City of La Palma notes that the Orange County Grand Jury report indicates that there are 8 recommendations, but only 7 are listed. Therefore, the City shall respond to the 7 listed recommendations.

**Recommendation R-1:** Recommendation R-1 states, "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 of La Palma Response to Recommendation R-1:** The recommendation has been **implemented**. This has been the City's practice for many years and it currently has eight years of budgets posted on the website. This information is easily accessible by clicking on a "Quick Link" on the front page of the website, by using the search feature, or by accessing through the Finance Department page.

**Recommendation R-2:** Recommendation R-2 states, "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 of La Palma Response to Recommendation R-2:** The recommendation **will not be implemented** because it is not reasonable or feasible. While the City updates its ten-year

Sustainable Financial Plan as part of the budgeting process, it is not completed at the same detail level as the current fiscal year budget. In order to complete a five year projection at the same level of detail would add a tremendous amount of work to the budget process in turn increasing costs. Further, the five year projections would be extremely challenging and not necessarily meaningful as financial information changes from year to year. The City's Sustainable Financial Plan is available for review at <http://www.cityoflapalma.org/DocumentCenter/View/4606> and in Fiscal Year 2015-16, the City will include it as an Appendix to the Budget document.

**Recommendation R-3:** Recommendation R-3 states, *"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 of La Palma Response to Recommendation R-3:** The recommendation has been **partially implemented – no further implementation will take place** because it is not warranted. In 2011, the City negotiated with its employees to assume the full employee share of CalPERS pension costs. These costs were phased in between July 1, 2011, and July 1, 2013, and as such La Palma employees now pay the employee portion of CalPERS contributions and that amount is not shown in the budget as an expense. Employer pension costs are shown as a single line item in the Employee Benefits budget, with that figure being allocated back to Department budgets along with other benefits.

**Recommendation R-4:** Recommendation R-4 states, *"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 liabilities."* [(F.7)]

**City of La Palma Response to Recommendation R-4:** The recommendation has **not yet been implemented**, but will be implemented in the Fiscal Year 2015-16 Budget. The City has a separate Reserve Policy that details each reserve fund, its use, and its target balance. The City also has a Sustainable Financial Plan that requires that 6.4% of the City's General Fund revenues be transferred for one time needs, such as capital projects, for non-recurring and generally non-capital needs - including contributions towards unfunded liabilities, and transfers to other reserves (as needed). The needs of various funds are taken into account as part of the budgeting process, including the annual update to the Sustainable Financial Plan. The City's Reserve Policy is available for review at <http://www.cityoflapalma.org/documentcenter/view/4784>. The City's Sustainable Financial Plan is available for review at <http://www.cityoflapalma.org/DocumentCenter/View/4606>. Both documents will be included as an Appendix to the Budget document in 2015-2016. Additionally, the City is currently in a CalPERS Risk Pool and does not have the ability to pay down its unfunded pension liability. It paid off its \$3.8 million side fund unfunded liability in 2009.

**Recommendation R-5:** Recommendation R-5 states, *"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 of La Palma Response to Recommendation R-5:** The recommendation has **not yet been implemented**, but will be partially implemented in the Fiscal Year 2015-2016 Budget. It is important to note that three years of La Palma’s Safety and Miscellaneous Actuarial Valuations are currently available on the CalPERS website at <https://www.calpers.ca.gov/index.jsp?bc=/about/forms-pubs/calpers-reports/actuarial-reports/browse-results.xml&strCatId=2&q=la-palma-city>. The City will also provide a link to said documents as part of its Employee Compensation page within 90 days of this response. The City’s Comprehensive Annual Financial Report includes extensive information on the City’s pension plans, as required by governmental accounting standards. Trend information for the CalPERS Annual Valuation Reports and risk information associated with projections provided by CalPERS will be implemented in the next budget cycle. However, until the City has the ability to actually pay down its unfunded pension liability, no expenditure lines will be included in its budget document.

**Recommendation R-6:** Recommendation R-6 states, *“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 the 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 of La Palma Response to Recommendation R-6:** The recommendation **will not be implemented** because it is not warranted. La Palma is a Structural Fire Fund (SFF) member of the Orange County Fire Authority (OCFA) which means that the City’s “contribution” to the OCFA is made directly through property taxes paid to the Orange County Treasurer-Tax Collector; therefore, monies are neither budgeted or allocated by the City of La Palma. Additionally, pursuant to the OCFA Joint Powers Agreement (Article VI, Section 3 which states that “Except as otherwise provided herein, the debts, liabilities and obligations of the Authority shall be the debts, liabilities and obligations of the Authority alone and not the parties to the Agreement;” the liabilities of the OCFA are not the liabilities of La Palma. Further, OCFA’s legal counsel opined in June 2014 that under the law and the Joint Powers Agreement, member agencies do not have liability for OCFA’s pension obligations.

**Recommendation R-7:** Recommendation R-7 states, *“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 of La Palma Response to Recommendation R-7:** The recommendation **will not be implemented** because it is not warranted. Three years of La Palma’s Safety and Miscellaneous Actuarial Valuations are currently available on the CalPERS website at <https://www.calpers.ca.gov/index.jsp?bc=/about/forms-pubs/calpers-reports/actuarial-reports/browse-results.xml&strCatId=2&q=la-palma-city>.

The City would like to thank the Orange County Grand Jury for its efforts in researching these issues and for giving the City an opportunity to respond to its findings and recommendations. Should you have any questions regarding the City's responses, please contact Laurie Murray, Administrative Services Director, at (714) 690-3338.

Sincerely,



Steve Shanahan  
Mayor

c: City Council  
City Manager  
City Attorney  
Orange County Grand Jury