

TOWN OF FAIRFAX
STAFF REPORT
July 24, 2013

TO: Mayor and Town Council
FROM: Garrett Toy, Town Manager *GT*
SUBJECT: Discussion/Consideration of Response to Grand Jury Report "Marin's Retirement Health Care Benefits: The Money Isn't There"

RECOMMENDATION

Accept the Response to the Grand Jury Report

DISCUSSION

On May 22, 2013, the 2012/2013 Marin County Civil Grand Jury issued a report "Marin's Retirement Health Care Benefits: The Money Isn't There". Each of the 11 Marin City and Town Councils has been asked to respond to "All findings F1 through F10 and all recommendations, R1 through R6".

Responses were prepared by staff and reviewed by the Finance Committee on July 18, 2013.

FISCAL IMPACT

None

ATTACHMENTS

Response to Grand Jury Report
Grand Jury report

AGENDA ITEM # 12

RESPONSE TO GRAND JURY REPORT FORM

Report Title: *Marin's Retirement Health Care Benefits: The Money Isn't There*

Report Date: May 22, 2013

Public Release Date: June 3, 2013

Response by: Town of Fairfax

FINDINGS

- I (we) agree with the findings numbered: _____
- I (we) disagree wholly or partially with the findings numbered: F1- F10
(Attach a statement specifying any portions of the findings that are disputed; include an explanation of the reasons therefor.)

RECOMMENDATIONS

- Recommendations numbered R1, R5 have been implemented.
(Attach a summary describing the implemented actions.)
- Recommendations numbered R3, R6 have not yet been implemented, but will be implemented in the future.
(Attach a timeframe for the implementation.)
- Recommendations numbered _____ require further analysis.
(Attach an explanation and the scope and parameters of an analysis or study, and a timeframe for the matter to be prepared for discussion by the officer or director of the agency or department being investigated or reviewed, including the governing body of the public agency when applicable. This timeframe shall not exceed six months from the date of publication of the grand jury report.)
- Recommendations numbered R2, R4 will not be implemented because they are not warranted or are not reasonable.
(Attach an explanation.)

Date: _____ Signed: _____

Number of pages attached 5

Town of Fairfax

Response to the Grand Jury

On May 22, 2013, the 2012/2013 Marin County Civil Grand Jury issued a report "Marin's Retirement Health Care Benefits: The Money Isn't There". Each of the 11 Marin City and Town Councils has been asked to respond to "All findings F1 through F10 and all recommendations, R1 through R6".

Findings:

- F1. We find that many of Marin's local governments and special districts are failing to pre-fund future costs for retired employees by making investments to cover promised benefits for active employees. This jeopardizes the certainty that retiree health care benefits to current employees will be paid.

Response: The Town has addressed its responsibility for funding retiree health care benefits by prefunding future obligations through the PERS-run California Employers' Retiree Benefit Trust Fund (CERTB).

- F2. The Failure of the majority of entities studied in this investigation to begin an investment program to provide a portion of the needed funds to pay for retiree health care benefits leads to generation shifting of the payment responsibility. Thus it appears to be, at least unethical, and even a breach of fiduciary responsibility.

Response: We agree that it is financially responsible to fund health care liabilities through an investment program. The Town joined the CERTB program in 2010 and is making regular contributions to fund its future obligation.

- F3. The extreme 30-year amortization period used by most entities minimizes the annual cost of funding the liability gap and further defers to future generations the compensation owed to present employees who provide services to present taxpayers and customers. Shorter amortization periods should be required for reasons of equity and to ensure that the promised benefits will be provided.

Response: The Town is using a 30-year amortization as shown in our actuarial analysis of retiree health benefits. The Town's ability and willingness to prefund its future liability is based on its financial position each fiscal year.

- F4. By capping retiree health care benefits, the City of San Rafael has reasonable certainty as to what those costs are. Other entities studied here that promise to pay for future retiree health care with uncertain and likely rapidly increasing costs are accepting an unknown and potentially very costly risk.

Response: In recent employee negotiations, the Town discussed its desire to alter the retiree health care plan to cap benefits to the Medicare rate once that age had been reached. The response was made that such trade-offs have a cost - so while the Town may save future costs, there is a current cost which would be added which may or may not result in savings. We were successful in reducing the benefits for future hires.

- F5. Because a few Marin County cities and other entities studied provide very limited benefits yet still appear able to meet community service needs, and because providing such benefits are increasingly rare in the private sector, such benefits appear to be unnecessary for attracting and retaining employees. Accordingly, for active and newly hired employees, the benefits should be trimmed and costs should be shared between employees and their employer.

Response: being prepared and will be distributed at the meeting.

- F6. Marin entities using "Pay-Go" funding are paying only the current year health care benefits of those already retired. This ignores the reasonably known rising costs to cover future retirees who are already headed for retirement. Some actuarial valuation reports the Grand Jury studied provide those future "Pay-Go" estimates year-by-year, so they should be readily available from the actuary's valuations. Estimates of those annual costs for each of the next 10 years should be provided to the public so that those who will incur the costs can know those costs.

Response: The Town pays current qualifying retirees (AKA: "Go-Pay") and also makes contributions towards its future retiree health care obligation.

- F7. Employers studied for this report should include an age-60, or even later, date for retiree health care benefits to commence in future negotiations with employees and their representatives.

Response: The mean age of retirees in Fairfax is 63.2. The mean age of POA retirees is 59.3. It may not be a significant issue for the Town or result in significant savings to negotiate a higher retirement age. As previously noted, there is a cost in negotiating reduced benefits, both in the attractiveness of the plan and the cost required to gain concessions.

- F8. The results of retiree health care cost analyses are summarized if at all only in obscure notes to annual financial statements. The public is entitled to more readily accessible explanation of these costs because the public will bear those costs.

Response: The annual financial statement (the audit report) is available to all interested persons by request and on the Town website. It has an advantage that under GASB 45 there are required disclosures which make comparability of the data possible with other entities. We will include an exhibit discussing retiree health care projections in the annual budget document.

- F9. There is a wide range of retiree health care benefits offered among the entities studied in this investigation. No clear explanation for the range from minimal to extremely generous is readily available. Those entities that are promising relatively generous benefits should provide clear justifications to their citizens and customers.

Response: The Town has sought to provide employees a fair and competitive benefit in line with what was being provided by other agencies within the public sector and with regard to its budget constraints.

- F10. Most of the entities the Grand Jury investigated are using fairly reasonable discount rates of 4% - 5% per year to bring back to today in actuarial valuations the future annual costs of retiree health care benefits. However, some are using higher and higher questionable rate assumptions that are not justified by the investments (if any) that they have made to grow and fund the future benefits. The result is to understate the total funding needed today and in future years, to pay for those future benefits.

Response: The Town believes its actuarial study fairly shows its required contributions consistent with the return on investments.

Recommendations:

The Grand Jury recommends that each Marin County local government, special district and school district:

- R1. Begin setting aside in separate investment accounts, if it is not already doing so, each year's funds for amortizing its retiree health care benefits' UAAL, in addition to its "Pay-Go" funding of those benefits for present retirees.

Response: The Town began participating in a separate investment fund, CERTB, in 2010 meeting its obligation to prefund future obligations as well as paying current liabilities.

- R2. Begin a program to lower the amortization period for funding its retiree health care benefits UAAL from as much as 30 years presently, to approach (within 10 years), the commonly used 17-year amortization for retiree pension funding.

Response: The Town believes the current amortization period is appropriate to provide funding for liabilities within the constraints of its budget, and may choose to fund additional amounts as future opportunities arise.

- R3. Negotiate caps on the amounts it commits to pay existing and new employees for retiree health care benefits.

Response: The Town continues to negotiate changes to the program which reflect the increasing cost of health care and the need to provide fair benefits. Recent negotiations have focused in a separate lower tier for new employees. In addition the Town has capped its contribution to the Kaiser employee-only rate, which is not the most expensive health plan.

- R4. Negotiate a higher retirement age than the currently applicable age for the commencement of retiree health care benefits.

Response: It may not be a significant issue for the Town or result in significant savings to negotiate a higher retirement age since the mean age of retirees is higher than 60.

- R5. Require active employees to make a contribution towards the cost of their retiree health care benefit.

Response: Employees who retire before 20-25 years do make payments towards their health insurance because the Town pays only a percentage of the total cost.

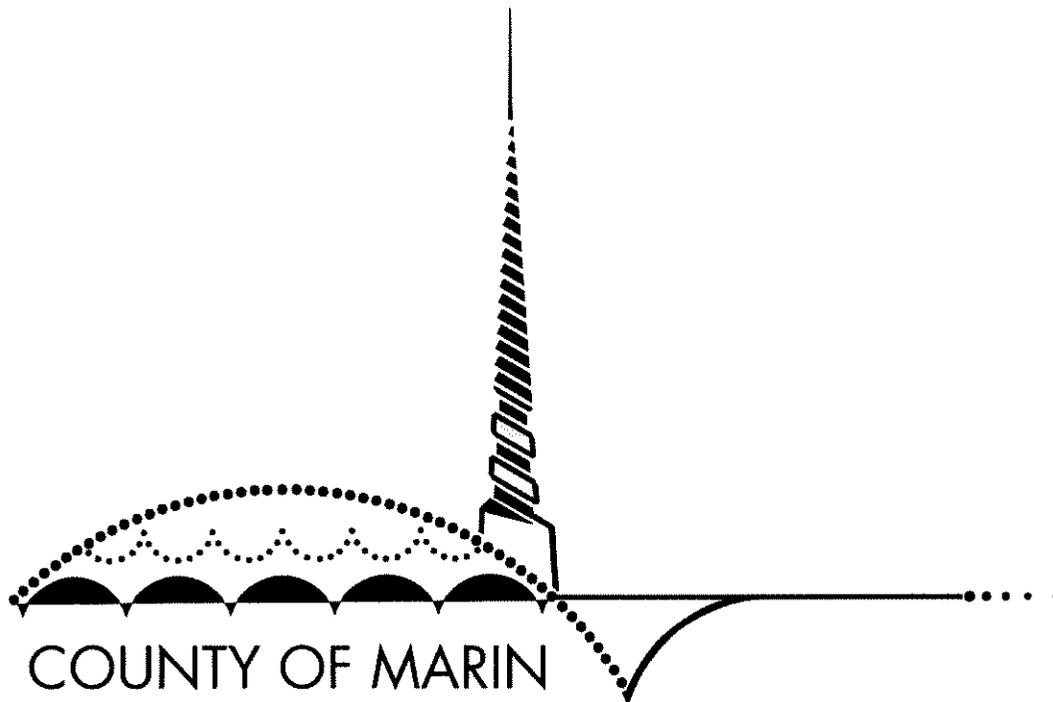
- R6. Place a link on its website to provide the latest actuarial valuation of its AAL, its UAAL, its consequent percent funded, its discount rate (annual percentage) used to determine these values, and a projection of outlays ("Pay-Go") for retiree health care benefits for each of the current and subsequent 10 years.

Response: The Town will put actuarial information and projections of costs based on the actuarial reports into the budget which will be available on the Town's webpage.

2012/2013 MARIN COUNTY CIVIL GRAND JURY

Marin's Retirement Health Care Benefits: The Money Isn't There

Report Date – May 22, 2013
Public Release Date – June 3, 2013





MARIN'S RETIREE HEALTH CARE BENEFITS: THE MONEY ISN'T THERE

SUMMARY

Much has been written about government pensions but there is another retirement benefit, retiree health care, which is large and mostly unfunded. Currently, most government entities pay for both retired and current employees on a "pay-as-you-go" or "Pay-Go" basis, meaning that the cost comes out of the current operating budget. Only the current year's medical insurance costs for retirees are paid under this approach. As more employees retire, this burden will eat into the funds needed to sustain the present level of service.

This Grand Jury investigated government entities' provisions to meet growing retiree medical health care costs for current employees and for those already retired. We reviewed the most recent actuarial valuations and financial statements that we were provided and found that with few (but important) exceptions, local Marin entities are failing to recognize a looming financial burden. This burden upon future generations of citizens (and customers, in the case of some special districts) will come about as a result of not implementing reduced retiree health care benefits, or from not funding them earlier (pre-funding), or both.

Our investigation discloses that the 40 government entities (the County, cities and towns, special districts and school districts) we surveyed have a collective liability of about \$577 Million but have set aside only about \$55 Million. Taxpayers and customers thus face future increased costs of \$522 Million or nearly 91% of the liability to pay for the benefits that have been promised but have not yet been provided for.

If each service provider put aside a portion of the anticipated future retirement health care costs, the money invested today will earn a return, thereby reducing payments that taxpayers and customers would be required to make in the future when retirees receive their promised health care benefits.

Of all the entities studied, the County has by far the largest unfunded liability for meeting retiree health care benefits. At the end of its 2011 Fiscal Year, the County was short about \$293 million (or about \$2,627 per county household).

Of the 40 entities the Grand Jury studied, only 12 have funded more than 5% of the liability presently owed for future benefits. Twenty-six of the forty have made no funding at all for those promised benefits.

This report includes information about the household liability for unfunded retiree health care benefits for all 40 entities studied, so that interested people can tally the amounts of their household's resultant liability.

Failure to invest now to cover retiree benefits that employees have already earned is ethically questionable, and jeopardizes the likelihood that the promised benefits can or even will be provided. If the benefits are to be provided by future large diversions of funds away from other services, then the public is entitled to an explanation.

Because the future payments will be so much larger than they are currently, employers are being less than honest with: 1) existing employees about the possibility of being unable to fund the benefits, and 2) taxpayers and Special District customers who will experience higher taxes and service rates, reduced future services, or both when the increasing annual payments must be made.

What this means in simple terms is that if the liability problem is not addressed within the next few years, each Marin County household will be assessed significant additional taxes or will see a dramatic reduction in services.

The Grand Jury recommends that each Marin County local government, special district and school district:

- Negotiate caps on the amounts it commits to pay existing and new employees for retiree health care benefits.
- If not already doing so, initiate annual funding of this benefit over and above the pay-as-you-go amount.
- Negotiate a higher initial retirement age than the currently applicable age for the commencement of retiree health care benefits.
- Require active employees to make contributions towards the cost of their retiree health care benefits.
- Lower the amortization period for funding its retiree health care benefits liabilities from as much as the present 30 years, to approach (within 10 years) the commonly used 17-year amortization period for retiree pension funding.
- Provide a link on its website to information listing the values of critical actuarial assumptions that determine the liability for funding retiree health care benefits.
- Include on its website the latest values for unfunded retiree health care liabilities, and the percentage of total retiree health care liabilities that has been funded.

BACKGROUND

Retiree Health Care Benefits Are Costly and the Costs are Rising

Because of widespread public coverage of concerns about public sector pensions, this Grand Jury determined to investigate the less prominently covered matter of other post-

employment benefits (OPEBs) offered in Marin to employees of local governments, special districts and school districts.

OPEBs are primarily health care payments and other related benefits promised to employees who meet specified periods of service and age at retirement. Although generally not as costly as promised pensions, retiree health care benefits costs can be substantial. They impose significant on-going government financial liabilities that, in fairness to future generations of taxpayers and customers served by special districts, should be paid for during today's employment, and not be left for payment during retirement at a cost to future taxpayers, customers and ratepayers.

A major difference between pensions and retiree health care benefits is that pension benefits have historically been paid from trust funds that receive periodic contributions and have the ability to generate investment earnings.

In contrast, the Grand Jury found that most Marin local government and other entities we studied manage their retiree health care plans by funding only current annual payments for those already retired under "Pay-Go" funding. That is, the plans commonly provide little or no contribution to fund the promised payments for present employees' benefits to be paid when they reach retirement, nor do they provide funds for the future health care benefits of those already retired. This failure to pre-fund places a burden on future taxpayers to pay for rising costs at the expense of other reduced services.

Like many California local governments, Marin County, cities and towns, school districts and many special districts promise employees retiree health care benefits. The Grand Jury found, however, that only a shrinking minority of private sector entities offer such retiree health care benefits. Those private-sector firms that do provide such retiree benefits increasingly cap or otherwise limit the benefits they promise to provide.¹

Health care costs continue to increase faster than general inflation, and this trend is forecast to continue. This is reflected in all of the actuarial valuation studies we reviewed. Additionally, retirees and their covered dependents are living longer.²

¹ For example, about ten years ago, Chevron decided to provide no more than a fixed total dollar amount annually to fund all retirees' health care costs, increasing that fixed dollar amount by no more than 4%/Year. This places a "cap" on what Chevron might incur to provide the benefits to retirees. Bank of America now provides retirees a flat \$100 per month, and both Wells Fargo and AAA stopped retiree health care benefits to new employees several years ago. General Electric Corp reports in its recent 2012 Annual Report to Shareowners that it will close its post-age-65 retiree medical plans to salaried and retired salaried employees who are not enrolled in the plan as of January 1, 2015. Those plans currently apply to 205,000 retirees and dependents. GE is essentially terminating those benefits as of 1/1/2015 for employees born after 1/1/1950.

² The Society of Actuaries issued a report in September, 2012 ("Mortality Improvement Scale BB Report") which concludes that longer life-spans than previously used should be reflected in actuarial studies in the future. This will increase the cost for retiree health care plan benefits above that for previous valuations such as those studied for this Grand Jury report. Marin County's demographics and life-styles also tend to result in still greater length-of-life compared to broader geographical-averages.

Further adding to future costs is the fact that the numbers of local government employees who will be entering retirement in the future are projected to exceed those now in retirement.

Accordingly, costs for Marin local government retiree health care benefits will increase substantially. Paying for these growing retiree health care costs will take increasing portions of current operating budgets. The public that will ultimately bear the costs generally does not readily understand this impact partly because of limited and somewhat hard-to-find financial disclosure. Most local government entities have only recently begun to disclose their retiree health care financial liabilities. The limited information provided is usually found only in relatively obscure notes to financial statements.

Information is Now Available that Wasn't Previously

Two recent Marin County Civil Grand Juries issued reports³ that included some focus on retiree health care benefits. The 2004-5 Grand Jury's report, "The Bloated Retirement Plans of Marin County, Its Cities and Towns (Revised)," primarily focused on pensions. It noted that criteria for estimating the future cost for retirees' health care benefits provided by local governments had not been generally determined. Therefore, it estimated that liability only for the County, and not for other Marin local governments or public entities.

The 2004-5 Grand Jury's report noted that guidelines calling for such retiree health care benefit calculations and for their public reporting had just been issued⁴ at the time of its report. Moreover, the new standards promulgated by the Governmental Accounting Standards Board (GASB) were not due to be implemented until Fiscal Years ending after June 2009.

The 2006-7 Marin Civil Grand Jury's report: "Retiree Health Care Costs: I Think I'm Gonna Be Sick," focused on whether retiree health care benefits were irrevocable legal obligations of local government. Page 5 of the report asks whether they are "...a vested right for active or retirement workers? Can they be taken away or changed?" Finding 12 of that Grand Jury's report concluded, among its other findings, that there is a potential conflict of interest for public employees who manage the retiree health care benefits they provide, because those public employees "...may be eligible to receive the health care benefits they manage." That Grand Jury, like the 2004-5 Grand Jury, also lacked any reported data about the extent of local-government-provided retiree health care costs and the capability to pay them.

The agency that issues accounting and financial reporting guidelines for local governments is the Governmental Accounting Standards Board (GASB). GASB issued its retiree health care cost reporting requirements in 2004 (GASB Statement 45 or GASB

³ The Bloated Retirement Plans of Marin County, Its Cities and Towns (Revised), May 9, 2005; RETIREE HEALTH CARE COSTS: I THINK I'M GONNA BE SICK, March 19, 2007.

⁴ Governmental Accounting Standards Board Statement No. 45. Accounting and Financial Reporting for Post-employment Benefits Other Than Pensions. June 2004.

45 - See Glossary), with implementation for entities like those in Marin generally to commence as of the 2009 Fiscal Year end. Thereafter, updated reports are required every 3 years for most Marin local governments and special districts and every 2 years for larger-employee jurisdictions like the County.

Because GASB 45 financial reporting standards have now taken effect, and thus, some data are now available for analysis, this Grand Jury decided to investigate Marin's County, towns and cities, some special districts and the largest school districts. For the entities studied, our investigation focused on understanding the:

- Likely future obligations to provide retiree health care benefits
- Likely funding approaches to pay for those benefits
- Potential impact on budgets and services from paying those benefits
- Efforts taken and planned to reduce the rising costs of those benefits

APPROACH

The Grand Jury reviewed the 2004-5 and the 2006-7 Grand Jury reports that concern Marin retiree health care benefits. We also reviewed the responses to those reports.

A more recent June 22, 2011 report by the Marin County Council of Mayors and Council Members, titled: "Marin County Local Government Reform of Pensions and Other Post-Employment Benefits," provided useful information, including some data on cities and towns' initial disclosure of financial liability for future retirees' health care benefits, pursuant to GASB 45 requirements.

We reviewed the retiree health care benefit accounting and financial standards now called for by the Governmental Accounting Standards Board. Specifically, we reviewed GASB 45, and various summaries and analyses of that Statement.

We researched and reviewed other California County Civil Grand Jury reports on retiree health care benefits. Local newspaper reports on the subject also provided useful perspective.

We reviewed various think-tank and academic research reports on the nation's retiree health care benefits' looming unfunded liabilities, and similarly focused governmental studies and reports. (See Bibliography for a partial listing.)

Our understanding also benefited from the recently released "Report for the State of California," valuing the liabilities for the State's retiree health care benefits as administered by the California Public Employees Retirement System (CalPERS) and the

California Department of Human Resources (CalHR).⁵ To understand the nomenclature and importance of terms reported in local government financial reports, we reviewed

those reports that now present GASB 45 required funding status, and related GASB 45 compliance.

Grand Jury representatives monitored the County's October 2, 2012 workshop at which County Administrative Office (CAO) personnel presented a proposal to pre-fund for the first time a small portion of the County's large (\$383 Million as of 7/1/2012) completely unfunded retiree health care liability.⁶ The proposal presented at the workshop was to fund both pensions and retiree health care with \$23 Million each, from available "one-time funds."

We also reviewed the subsequent CAO proposal to reduce that initially proposed retiree health care benefit pre-funding and instead, to reallocate the reduction to increase the pension-funding amount. Members of the Grand Jury monitored the Board of Supervisors' February 5, 2013 meeting at which the County's retiree health care pre-funding amount and mechanisms were authorized at \$14 Million rather than the original \$23 Million.

We reviewed the actuarial firm's reports for the County's retiree health care benefits.⁷ We followed this with two interviews with a representative of that firm.

We also reviewed the most recent report of the County's pension-benefit actuary.⁸ That report covers all of the entities that are part of the Marin County Employees' Retirement Association (MCERA). These include the County, the City of San Rafael, the Novato Fire Protection District, and some other local government entities.

Grand Jury members attended MCERA's October 2012 annual Investment Committee workshop. Our focus was to acquire further understanding of funding and actuarial issues, which have common application to pension and retiree health care benefit matters.

With an understanding of the issues, relevant financial reporting, and the mathematics of local government retiree health care benefit costs and funding matters, the Grand Jury prepared a list of data needed to evaluate Marin entities' steps to provide for the cost of those benefits. The resultant survey was sent to representatives of the County, its 11 cities

⁵ STATE OF CALIFORNIA RETIREE HEALTH BENEFITS PROGRAM, GASB NOS 43 AND 45 ACTUARIAL VALUATION REPORT AS OF JUNE 30, 2011. Gabriel Roeder Smith & Company, Consultants and Actuaries. February 21, 2013.

⁶ That workshop included discussion of a similar plan to further fund County Employee Pensions, which are funded at about the 75% level (or about 69% on a more complete basis that includes the County's Pension Obligation Bonds' outstanding principal of about \$108 Million).

⁷ County of Marin Retiree Healthcare Plan. Actuarial Valuation as of July 1, 2011. For Fiscal Years 2011/12 & 2012/13 GASB 45. January 2012. Bartel Associates, LLC.

⁸ Marin County Employees' Retirement Association. Actuarial Review and Analysis as of June 30, 2011. March 29, 2012. EFI Actuaries.

and towns and the now-separate Twin Cities Police Authority⁹, 14 county special districts, and the College of Marin and the 12 largest county school districts.

The survey responses and further follow-up data gave the Grand Jury information about how well local governments are prepared to fulfill the promised employees' health care benefits upon retirement.

The responses also disclosed that in the future most of the public entities surveyed will have a much higher number of retirees than those currently receiving retiree health care benefits, and money has not been adequately set aside to grow with time to fund those costs.

The data in the following exhibits are based on the latest GASB 45 actuarial valuations and the latest financial statements that we were provided.

The significant potential impact of an expanding eligible retiree population is illustrated in Exhibit 1. (The data for all of this report's exhibits have been provided by responses to survey requests from all 40 entities studied, their financial statements, budget statements, and responses to follow-up questions. The Grand Jury acknowledges and appreciates their cooperation).

Exhibit 1 shows, for example, that San Rafael Elementary School District has about 72 retirees now receiving health care benefits. But there are currently 335 employees who may eventually retire and become eligible for those benefits upon retirement. The future costs of such benefits, after allowing for reasonable assumptions of employees not continuing with the district to qualify for those benefits, will require substantial future outlays by the school district to fund those benefits. Actuarial calculations determine how much should be invested today in order to grow and pay for those future benefits. The higher the multiples in Exhibit 1, the higher the likely future cost and consequent need to invest today to pay for them.

⁹ Because other police departments are included in towns and cities, the spun-off Larkspur and Corte-Madera PDs were included with the towns, cities and county. Data were not available for the now 3-cities Central Marin Police Authority; San Anselmo's Police Department data were still included with the City of San Anselmo in the data used in our study.

Exhibit 1:

Many More Employees Will Move Into Retirement			
Marin County Local Governments, Special Districts and School Districts			
(Source: Retiree Health Care Actuarial Valuation Reports)			
	Actives	Retirees	Future Retirees Potential
	Count	Count	Multiple
Novato Sanitary District	20	24	0.83
Ross Valley Fire Department	28	29	0.97
Novato Fire Protection District	80	79	1.01
Town of Corte Madera	48	46	1.04
Southern Marin Fire Protection District	32	29	1.10
City of San Rafael	361	308	1.17
Kentfield Fire Protection District	13	11	1.18
Las Gallinas Valley Sanitary District	18	15	1.20
Central Marin Sanitary Agency	39	31	1.26
County of Marin	1813	1397	1.30
Twin Cities Police Department	42	32	1.31
City of Larkspur	54	39	1.38
Marin Municipal Water District	253	169	1.50
Tiburon Fire Protection District	24	15	1.60
North Marin Water District	53	32	1.66
City of Novato	209	124	1.69
Town of San Anselmo	53	30	1.77
City of Sausalito	82	37	2.22
San Rafael High School Dist	234	105	2.23
Marinwood Community Service District	22	9	2.44
Sanitary District #1 (Ross Valley)	23	9	2.56
Sewerage Agency of Southern Marin	13	5	2.60
Ross School District	45	17	2.65
Marin Sonoma Mosquito and Vector Control	35	13	2.69
Dixie School District	177	63	2.81
Ross Valley School District	205	65	3.15
City of Mill Valley	143	41	3.49
City of Belvedere	22	6	3.67
Town of Tiburon	35	9	3.89
Town of Fairfax	29	7	4.14
San Rafael Elementary School Dist	335	72	4.65
Larkspur-Corte Madera School District	33	7	4.71
Town of Ross	26	5	5.20
Reed School District	152	27	5.63
Mill Valley School District	287	41	7.00
Kentfield School District	99	10	9.90
Tamalpais Union High School District	406	34	11.94

For a further perspective, the Grand Jury looked at the most recent general budget outlays for the government entities surveyed and compared the amount of unfunded retiree health care liabilities to those budgets.

To provide an understandable measure of the unfunded liabilities we found, we developed a metric to tie the liabilities to those who ultimately should bear them. That is, we related the county and local government unfunded liabilities to the households served. (Household data are from the U.S. Commerce Department's Census Bureau statistics). We related the special district unfunded liabilities to the customers (generally households) they serve. We also related the school district unfunded liabilities to the households in their respective communities.

We note that these debts are additive, in that the recipients of county and local government services are often also customers of water districts, sewage-treatment, sanitation, and fire protection districts, and are local school district taxpayers. When accumulated this way, the magnitude of these debts is significant.

The per-household liabilities for each City/Town, Special District and School we surveyed are shown in Exhibits 2 – 4.

Exhibit 2:

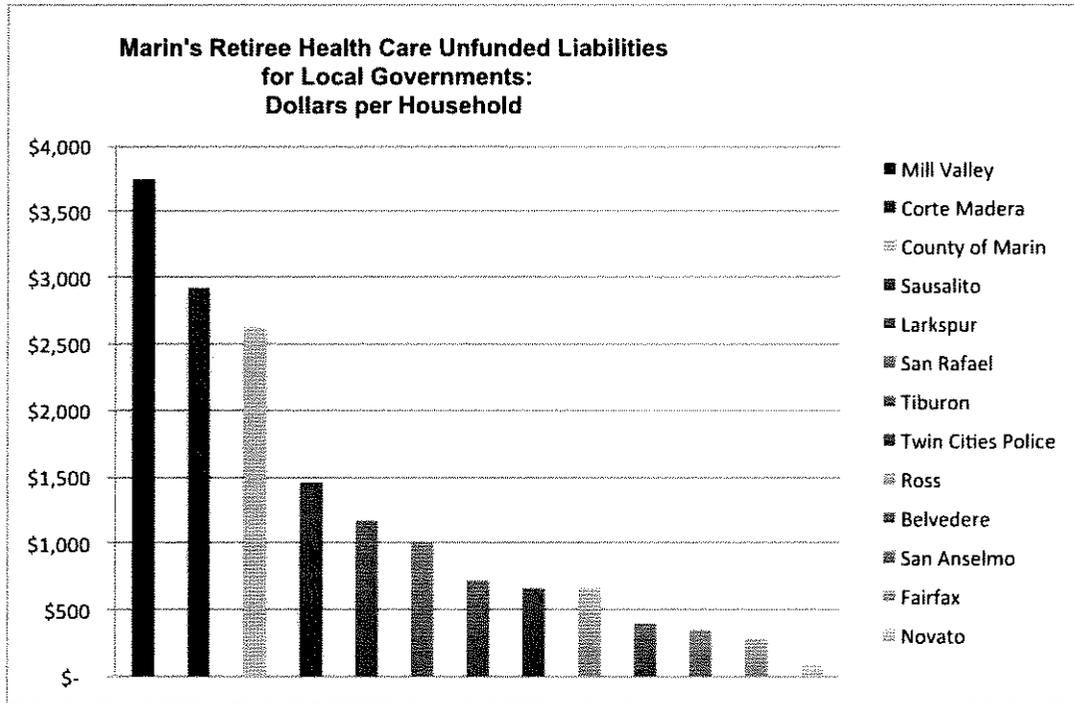


Exhibit 3

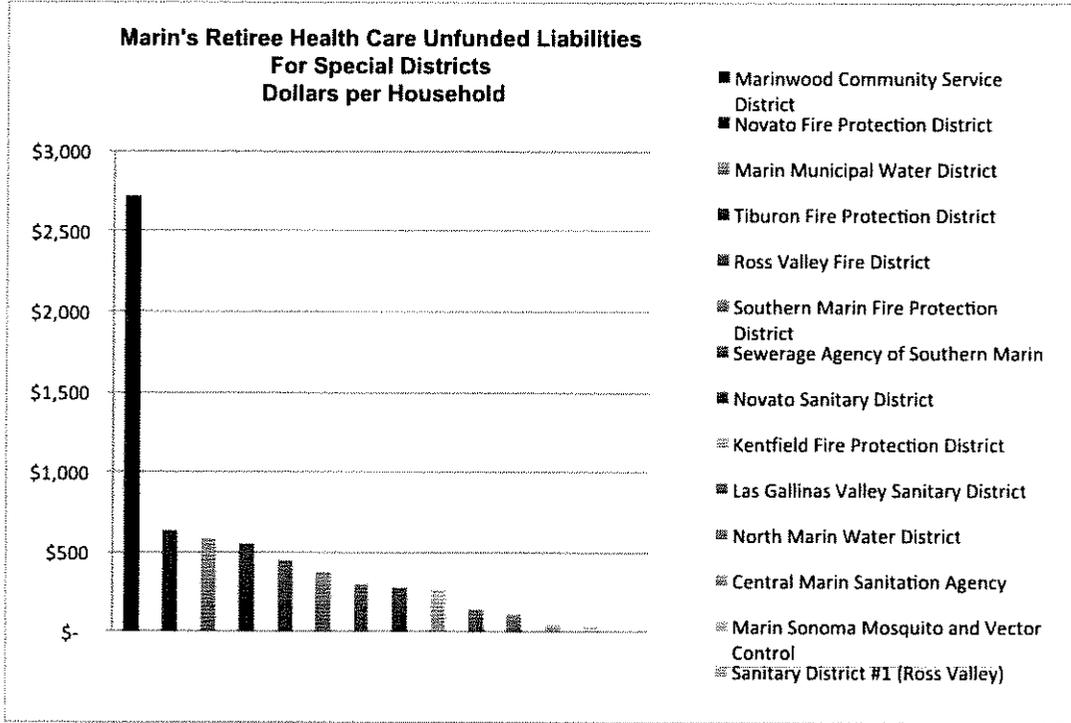


Exhibit 4

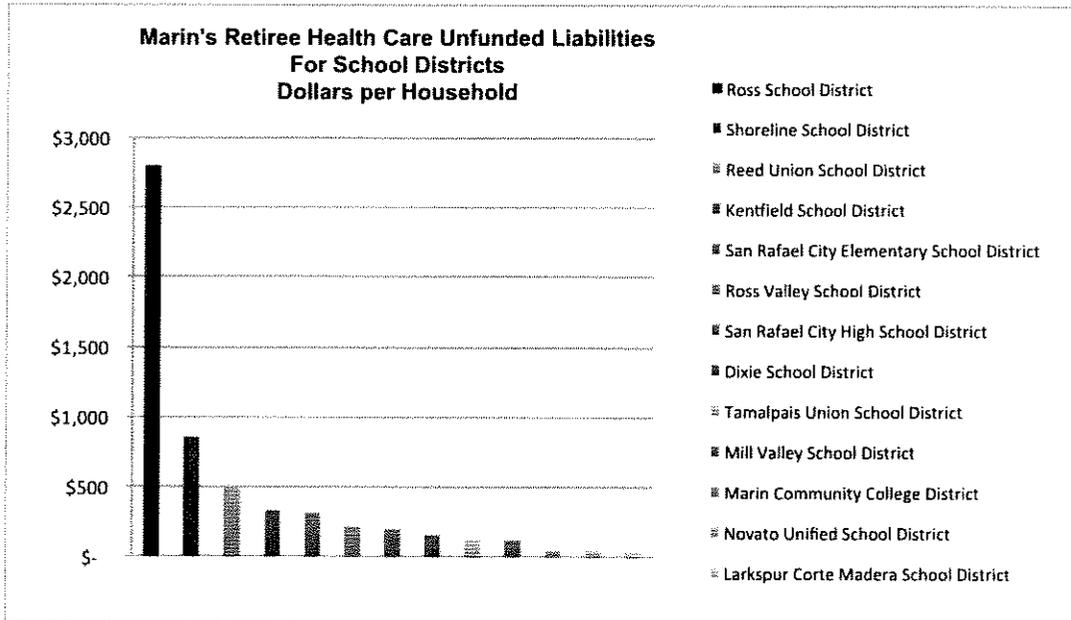
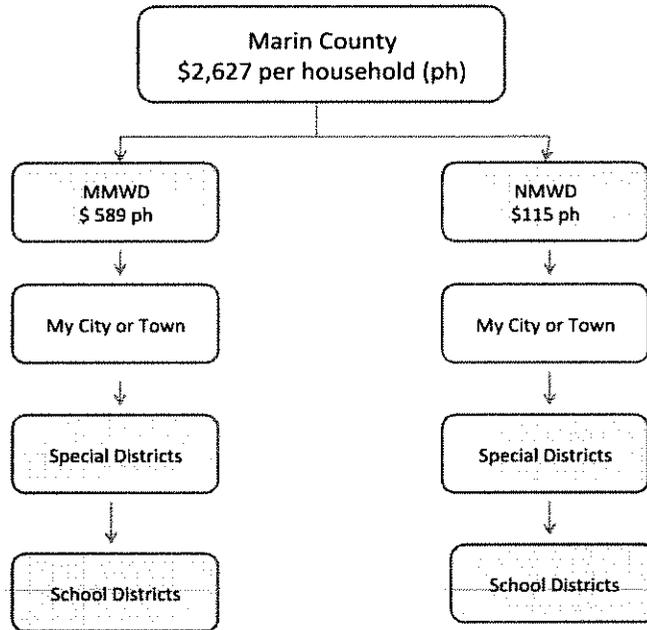


Exhibit 5 is an illustration of how these costs can be added up for a typical Marin household:

Exhibit 5:



To illustrate more fully, Appendix A presents the separate per-household costs of each entity we surveyed. This information can be used to determine the full impact each household will bear either by increased taxes or decreased services if this situation is not addressed.

DISCUSSION

What Has Been Promised?

The governments of Marin County, its 11 towns and cities, many of its Special Districts and its school districts all offer employees some form of retirement health care benefits. The benefits generally cover a portion, or even all of the cost of specified health care insurance, in some cases including spouses and dependents. They also often cover some of their dental care insurance. Such benefits are generally provided for the life of the retired employee and that of the spouse during that employee’s retirement, and often for the surviving spouse.

When covered retirees reach Medicare-eligibility age, the benefit costs generally decrease to reflect resultant reduced health care insurance costs, but the benefits continue thereafter, at the lower post-Medicare levels. Because of increasing life expectancy, funding needs today are very significant.

The stated justification for offering this retirement benefit is the need to attract and retain employees, and thus be competitive with other jurisdictions. Accordingly, it is considered a portion of compensation.

The Grand Jury notes, however, that private sector retiree health care coverage is increasingly rare, in contrast to the nearly 100% coverage provided by Marin's local governments, school districts and special districts. According to the Kaiser Family Foundation's Employer Health Benefits 2012 Annual Survey¹⁰, only 25% of U.S. firms with more than 200 employees that provided health care benefits for active employees, also offered retired employees health care benefits.

This most recent Kaiser finding of 25% coverage notes that the private sector continues to eliminate employee health care benefits: Kaiser reports that the benefit offering has declined to 25% from Kaiser's previous showing of 66% back in 1988, and 32% in 2005. The Kaiser Survey also reports that at only 25% coverage, these 200+ employee firms are "much more likely than small firms (3-199 workers) to offer retiree health care benefits." In contrast with these low coverage offerings by the private sector, the Survey notes that more than 77% of the more than 19 million employees of large U.S. state and local governments were eligible for retiree health care benefits, and that the percentage is even higher for smaller governments.

From the responses to our survey, we learned that there is a wide range of Marin local government retiree health care benefit offerings. The County, towns and cities tend to distinguish between eligibility and benefits for police and fire employees ("safety employees") on the one hand, and other general or miscellaneous employees. Benefits for the safety employees tend to be greater, and/or are earned earlier in employee careers and at a more rapid pace than for other employees. We note that this distinction is similar to that for local government retiree pension vesting and benefit amounts. Local governments historically have provided more generous retirement benefits, including earlier vesting for pensions, for safety employees than for non-safety employees.

We also learned that some Marin jurisdictions have modified their benefits depending upon when the employee's service commenced, and some are offering (or are considering to offer) greatly reduced or cost-shared benefits to more recently hired employees. We also note that some jurisdictions have placed limits ("caps") on the amounts they will pay, rather than agree to pay all or a fixed percentage of whatever the prevailing future health care costs might be under specified eligible programs retirees may select.

The trend has been to reduce promises for future retiree health care benefits for active employees, pursuant to collective bargaining negotiations where applicable, and concurrently to seek reductions for unrepresented employees.

¹⁰ Employer Health Benefits 2012 Annual Survey, Section 11: Retiree Health Benefits

Generous Benefits-City of Mill Valley

The City of Mill Valley is an example of a local government that provides generous retiree health care benefits. Pursuant to memoranda of understanding (MOUs) with represented employee unions and other resolutions, the City provides that "Full time employees of the Management, Technical, and Confidential group with 15 years of service and a PERS [California Public Employee Retirement System] retirement from the City shall be eligible for paid medical expense reimbursement for themselves and their spouse after retirement." And the City states that "*The maximum City contribution will be no more than the Kaiser employee + 1 rate.*" Moreover, the policy states "An employee who meets the above criteria shall qualify for medical coverage for the remainder of his/her life and that of his/her spouse."

For 2012, Mill Valley paid health care benefits of about \$1,168/month for a retiree and spouse under Kaiser's relevant HMO plan. This is about \$14,000 per year. (We note that when the retiree becomes eligible for Medicare, the City's payments decline, and for the same 2012 Kaiser-plan coverage, costs borne by the City drop to about \$570/month, or about \$7,000 per year, at 2012 rates.)

By contrast, Mill Valley School District teachers and staff recently agreed to cap their retiree health care benefits, which reduced the school district's liability by about one-third.

Marinwood Community Services District

The Marinwood Community Services District (MCSD) provides fire protection to approximately 1,750 houses in Marinwood and portions of Lucas Valley. It also provides and maintains the community's much-used swimming pool and related facilities. MCSD provides health care benefits to employees (the majority of whom are fire protection employees) and their spouses. The benefits are provided for those who retire at age 50 with only 5 years of service required for full eligibility. That relatively young eligibility age of 50 for full lifetime benefits for all employees is unique among the entities the Grand Jury studied. MCSD uses "Pay-Go" and thus only pays for retirees' health care benefits as the costs are incurred in retirement, with no funding for active employees' future post-employment health care benefits or for future years' benefits of those already retired.

To its credit, however, MCSD is taking steps to address the situation. According to the February 7, 2013 actuarial study of its retiree health care benefits, MCSD has lowered its benefit payments starting in Fiscal Year (FY) 2013 to no more than 90% of the CalPers Bay Area "pre-age 65" Kaiser premium rates for all fire and non-fire employees. And MCSD has set further step-downs (for fire-employees only) to 85% for FY 2014 and 80% for FY 2015.¹¹ MCSD has also increased the years of service required for employees

¹¹ Marinwood Community Services District Actuarial Valuation: July 2012. Nicolay Consultants.

hired after July 1, 2012 to earn full retiree health care benefits to 20 years from the 5-years for those hired before that date.

The impact of these changes will gradually reduce MCSD's very high liability from what it would have been absent these changes. But even with these changes, the liability per MCSD household (about \$2,750) is approximately 4 times that of any other Special District the Grand Jury surveyed. It is among the four highest liabilities per household of all entities the Grand Jury surveyed. And MCSD continues to fail to invest funds to pay for the benefits it has promised to present employees.

The Other End of the Range-City of Novato; Dixie School District

Some other Marin local governments offer similar or nearly as generous retiree health care benefits. But at the other end of the spectrum, retirees of the City of Novato received a monthly retirement health care benefit of about \$112 per month (\$1,314 per year) for 2012. This payment amount is the minimum prescribed by the California Public Employees System (CalPERS) pursuant to CalPERS' medical insurance through the Public Employees' Medical and Hospital Care Act (PEMHCA).¹² The Dixie School District also caps its qualified retirees' health care costs at approximately \$425/month for a five year period and thereafter, provides retirees a mere \$7.50/month towards their health care coverage costs.

Significant Movement to Control Costs-City of San Rafael

The Grand Jury noted a substantial favorable change in the City of San Rafael's reported OPEB liability in its most recent actuarial study report compared to the previous report. In follow-up discussions with the City, we learned that in 2009 the City negotiated caps on the amounts of retiree health care benefits that it would provide to present employees. The City also instituted programs that call for contributions by active employees, and negotiated reduced annual increases in benefits when those employees retire.

These changes are very significant: The cumulative effect is a reduction of approximately \$21 Million in the City's liability - a 37% reduction. This is equivalent to approximately \$900 per San Rafael household. San Rafael, unlike most of the entities we surveyed, funds its retiree health care liabilities and not just with a Pay-Go approach. Even though it has negotiated reduced retiree health care benefits, the City's more responsible approach to fund these costs will nonetheless burden its citizens. This is because those retiree health care fundings come at the expense of a corresponding reduction in other City services. The Grand Jury concludes that the City of San Rafael has taken important steps to reduce its future costs of retiree health care benefits. We also note that the City is among a small minority of Marin government entities that has addressed the issue.

In summary, the Grand Jury learned that retirees and those who will retire from Marin's local governments, special districts and school districts all receive or have been promised,

¹² PEMHCA is authorized by the California Government Code, commencing with Section 22751.

health care benefits from their pre-retirement employer. These are generally sizeable benefits. Their employers have not fully, or in most cases, not at all provided for their costs. We also learned that some employers offer substantially lower benefits, and yet are able to attract and retain employees.

Exhibit 6:

Future Retiree Health Care Costs: Funded Amounts and % Funded			
Marin County Local Governments, Special Districts and School Districts			
	Liability	Funded Amount	%
A: Entities With Some Funding---From High to Low %	Million \$	Million \$	Funded
City of San Rafael	\$ 35.16	\$ 10.86	30.9%
Tiburon Fire Protection District	\$ 3.10	\$ 0.83	26.7%
Town of Fairfax	\$ 1.28	\$ 0.25	19.8%
Marin Municipal Water District	\$ 44.77	\$ 8.67	19.4%
Tamalpais Union High School District	\$ 6.54	\$ 1.26	19.3%
Central Marin Sanitary Agency	\$ 3.55	\$ 0.68	19.1%
Kentfield Fire Protection District	\$ 2.39	\$ 0.39	16.2%
City of Mill Valley	\$ 28.10	\$ 3.62	12.9%
Las Gallinas Valley Sanitary District	\$ 2.15	\$ 0.27	12.5%
County of Marin	\$ 319.30	\$ 26.30	8.2%
Ross Valley Fire Department	\$ 5.12	\$ 0.31	6.1%
Novato Fire Protection District	\$ 17.71	\$ 0.95	5.4%
Southern Marin Fire Protection District	\$ 5.49	\$ 0.20	3.6%
Town of Corte Madera	\$ 11.83	\$ 0.04	0.3%
Totals	\$ 486.46	\$ 54.63	11.2%
B: Entities With Zero Funding---From High to Low Liabilities			
Marin Sonoma Mosquito and Vector Control	\$ 12.03	0.00	0.0%
City of Larkspur	\$ 7.49	0.00	0.0%
Twin Cities Police Authority	\$ 7.25	0.00	0.0%
City of Sausalito	\$ 6.63	0.00	0.0%
Novato Sanitary District	\$ 6.11	0.00	0.0%
Marin Community College District	\$ 5.69	0.00	0.0%
San Rafael Elementary School Dist	\$ 5.46	0.00	0.0%
San Rafael High School Dist	\$ 4.94	0.00	0.0%
Marinwood Community Service District	\$ 4.74	0.00	0.0%
Sewerage Agency of Southern Marin	\$ 4.11	0.00	0.0%
North Marin Water District	\$ 3.07	0.00	0.0%
Reed Union School District	\$ 3.04	0.00	0.0%
Town of Tiburon	\$ 2.90	0.00	0.0%
Mill Valley School District	\$ 2.16	0.00	0.0%
Ross School District	\$ 2.14	0.00	0.0%
Town of San Anselmo	\$ 1.94	0.00	0.0%
Ross Valley School District	\$ 1.84	0.00	0.0%
City of Novato	\$ 1.80	0.00	0.0%
Shoreline School District	\$ 1.80	0.00	0.0%
Kentfield School District	\$ 1.43	0.00	0.0%
Dixie School District	\$ 1.06	0.00	0.0%
Novato Unified School District	\$ 0.82	0.00	0.0%
Town of Ross	\$ 0.53	0.00	0.0%
City of Belvedere	\$ 0.37	0.00	0.0%
Sanitary District #1 (Ross Valley)	\$ 0.30	0.00	0.0%
Larkspur-Corte Madera School District	\$ 0.19	0.00	0.0%
Totals:	\$ 89.85	0.00	0.00
Totals---All 40 Entities Studied	\$ 576.31	\$ 54.63	9.5%

For further reference, Appendix B presents the Unfunded Actuarial Accrued Liability (UAAL) for each of the 40 entities studied.

What Do the Promises Cost?

Exhibit 6 provides a glimpse of the retiree health care benefit costs that Marin local governments and special districts bear. As stated above, the governments generally do not pay for the benefits that their employees have earned. Rather, most of the government entities the Grand Jury surveyed are paying only for the current year's health care premiums of those employees who have already retired and are receiving the benefits previously earned from their working days---Pay-Go funding.

By far the bigger retiree health care cost is that which governments have not paid; namely, the cost of benefits that have already been earned by existing, and usually much more numerous, active employees whose retirement is in the future. Governments using Pay-Go funding are also not funding payments beyond the current year for those who have already retired.

What Information is Now Reported?

These unpaid---yet already employee-earned---retiree health care benefits have recently come under the scrutiny of GASB, the accounting standards entity that sets financial reporting requirements for U.S. local governments. Probably better known by the general public is its sister entity for private sector accounting and financial reporting standards, the Financial Accounting Standards Board---FASB. Both issue what are known as Generally Accepted Accounting Principles (GAAP) required to be followed for financial reporting. Adherence to such common principles is essential for such purposes as receiving auditor verification of financial statement adequacy ("clean audits"), and rating agency evaluation of credit-worthiness vital for debt issuance and for determining the costs of such debt.

Because GASB 45 is now implemented, this Grand Jury was able to scrutinize conforming filings by Marin's governments for the first cycle. In some instances, we also had access to second cycle GASB 45 reports: Fiscal Year ending 2011 for the County and recent 2012 reports for some Cities, towns, schools and special districts.

In compliance with GASB 45, local governments must report in their financial statements: 1) Retiree health care accrued liabilities (Actuarial Accrued Liabilities, or AAL) for future benefits, 2) The amount of that AAL that has been funded by specifically ear-marked investments or by other assets, 3) The resultant unfunded portion (the unfunded AAL, or UAAL), 4) the interest rate used to calculate those values---analogous to the annual earnings rate that is assumed to grow invested funds to pay for the future benefits, and 5) The annual cost of currently paid benefits plus annual amortization of that AAL. This is named the Annual Required Contribution (ARC).

The last element above, the ARC payment, while named Annual Required Contribution is actually not required to be made, nor is it even enforced by any institution, regulatory

body, or accounting agency. *Understanding this is important!* The difference between this ARC and the smaller payments under "Pay-Go" is accounted for as an obligation (like debt) to be met in the future, but has generally not been funded with invested cash by most of the entities studied by the Grand Jury. And there is a further nuance: this is the liability calculated for obligations arising only since the implementation of GASB 45, not the higher obligation that would be calculated going back to the time when the employees started their employment and earning their future benefits.

With each passing year the time comes one year closer to when the retiree health care benefits must be paid. Consequently, this debt rises annually absent adequate funding, or absent any reductions in the promised benefit.

More details describing the mathematics of actuarial valuations and funding are shown in Appendix C. It presents information regarding the critical assumptions of discount (or funds earnings) rate and unfunded liability amortization periods.

Illustration: The County's Retiree Health Care Obligation

The County is Marin's largest local government entity. It presently provides health care benefits to about 1,400 retirees¹³ who average 71 years of age, and incurs an annual Pay-Go cost of about \$12 Million to do so. This is about \$8,600 per year per retiree and is capped at that amount for most employees, per negotiations with represented employee unions. In 2008, the County capped retiree health care costs at \$3,000 for new employees. The County has about 1,800 current employees that would be eligible for retiree health care benefits upon retirement. According to its actuary's latest report, approximately 1,100 are within ten years of retirement eligibility and could soon add greatly to the numbers in retirement. The County cited this looming issue in its April 2012 FY 2012-13 Budget Hearings, when it pointed out that:

The Department of Human Resources has identified that, over the next 5 years, 42% of the total workforce will be eligible to retire, but 24% will likely retire given current work patterns.¹⁴

At its March 2013 Budget Workshops for the next fiscal year, 2013-14, the County Administrator stated that the 42% retirement eligibility is now estimated to have increased to 50%. Either statistic---42%-50% eligible or 24% or so likely---suggests near-term swelling in retiree health care costs. This is because the ranks of those retired will grow and receive healthcare benefits, and those costs will likely not be offset by an equal reduction in health care costs for replacement active employees.

¹³ These Marin County retiree healthcare data were provided in the most recent biennial actuarial study by Bartel Associates, Inc: "County of Marin Retiree Healthcare Plan Actuarial Valuation as of July 1, 2011 For Fiscal Years 2011/12 & 2012/13 GASB 45." Dated January 2012.

¹⁴ According to the U.S. Census Bureau, the nation's over-65 year olds of about 40 million in 2010 is projected to grow to 54 million by 2030 and 70 million by 2050. Marin is likely to experience similar or even greater relative growth owing to life-style, present demographic and education factors.

The County's actuary, taking all of the probabilities and costs into account, estimated in its most recent (June 30, 2012) report that the County's retiree health care AAL as of July 1, 2011 was \$383 Million. At the time of the actuary's valuation, the County had set aside zero funds to defray any of those earned benefits. Accordingly, the County's UAAL was that same \$383 Million. With a population of about 250,000, that county liability alone is equivalent to about \$1,530 per county resident, or about \$3,430 per household.

Fortunately, the Board of Supervisors decided to begin funding for this liability. As a result, the County funded \$26.5 million in 2013 at an estimated investment rate of return of 5.5%, which was an increase over the prior estimate of 4.25%. When the County's actuary recently re-calculated the liability at this new higher discount rate and took the amount invested into account, the liability decreased to \$293 million, or a decrease of 24%.

For perspective, the County's \$293 Million retiree health care benefit UAAL is 79% of its Fiscal Year 2012-13 general budget---\$371.7 Million. As a percent of the general budget, the County's unfunded liability is among the highest for any of the county's 11 cities and towns¹⁵ and amounts to \$2,627 per household.

The County's retiree health care UAAL equals about 80% of the County's retiree pension plan \$370 million UAAL. However the County's unfunded retiree health care liability is far more alarming than the County's pension funding inadequacy. This is because the County's retiree health care liability is 92% unfunded after the initial investment. In contrast, its pension liability is about 25% unfunded.

To its credit, the County has recently recognized the dire straits of its retiree health care UAAL, and has begun what hopefully will become annual funding. However, the UAAL balance remains startlingly high. Funds spent to reduce the UAAL of retiree health care benefits are funds that will not be available for the services that county citizens would otherwise look to the county to provide. Absent reductions in the benefits already earned by employees and existing retirees, the result will be increasing pressures on the County to raise money from taxpayers.

Potential Impact on General Budgets if the Obligations are Paid For

Exhibits 2-4, and 6 above, show the deficiency in funding retiree health care benefits for all 40 entities studied. The unfunded amounts are thus the debt that has been incurred by taxpayers and special district customers for failure to fund those obligations.

For perspective, the Grand Jury compared the unpaid retiree health care liability of each entity studied, to its most recent general budget. The following exhibits present that information.

Exhibit 7:

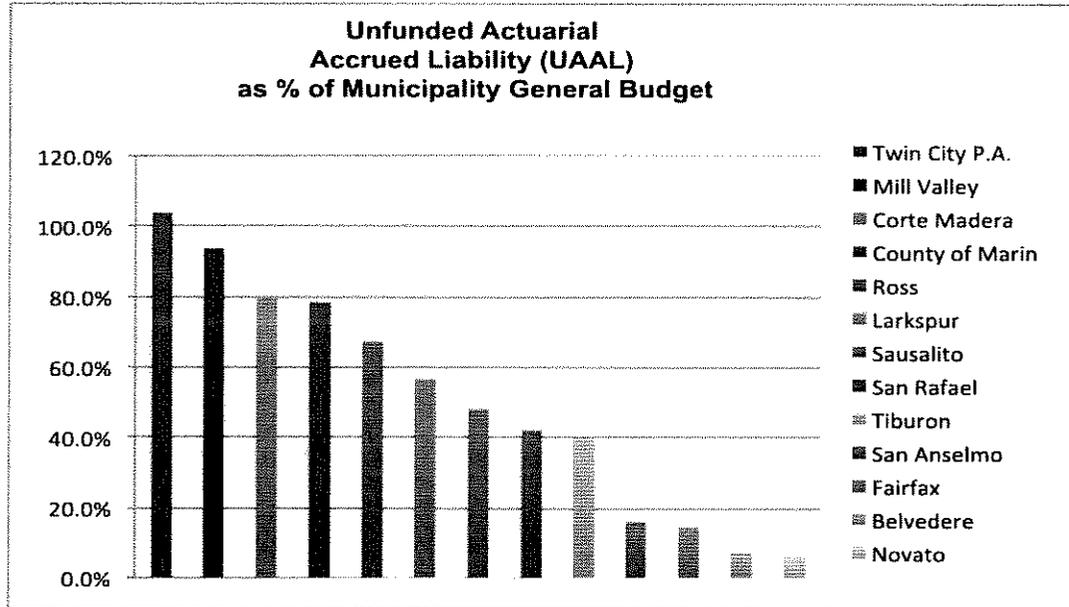


Exhibit 8:

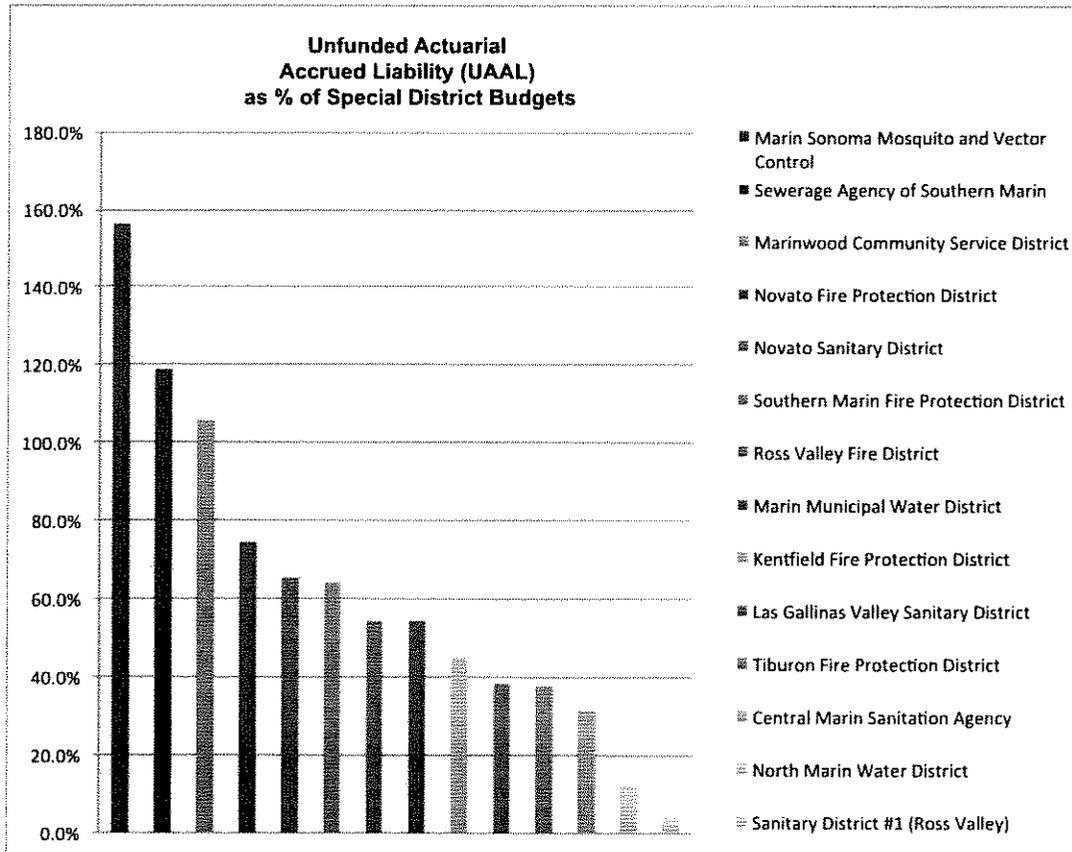
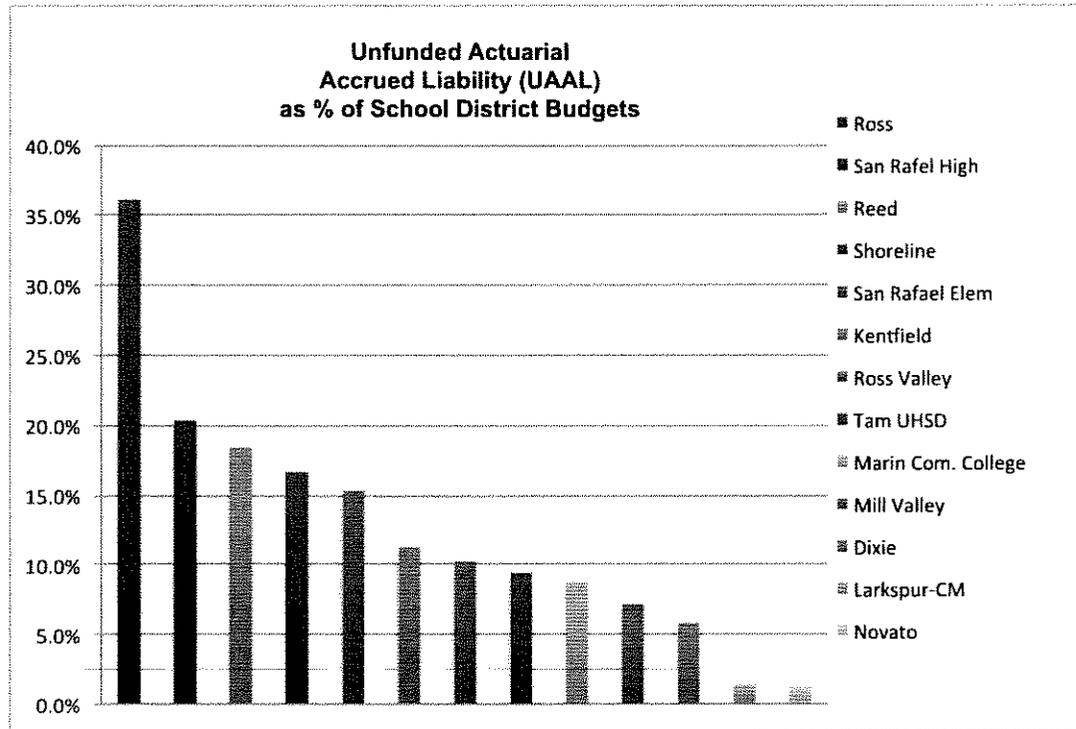


Exhibit 9:



As these Exhibits show, the unfunded retiree health care liabilities for many of Marin County's governments, Special Districts and school districts impose a significant impact on government services if and when funds are diverted to pay for what has been promised.

Solutions

Solutions will be painful, especially in the likely scenario of limited revenue growth, resistance to further taxation, and an economic outlook that appears to be less than robust. A combination of a reduction in promised retiree health care benefits, and accelerated funding to enhance monies available to pay those future benefits is necessary and prudent.

Timing is critical. Continuing with only Pay-Go funding will result in rising costs, primarily attributable to the influx of employees into retiree ranks. Necessary steps that should be taken by local governments are difficult. Among the painful actions needed are to greatly reduce (that is, cap) retiree healthcare benefits for newly hired employees and to require all employees to make contributions towards their retiree health care benefits.

FINDINGS

- F1. We find that many of Marin's local governments and special districts are failing to pre-fund future costs for retired employees by making investments to cover promised benefits for active employees. This jeopardizes the certainty that retiree health care benefits promised to current employees will be paid.
- F2. The failure of the majority of entities studied in this investigation to begin an investment program to provide a portion of the needed funds to pay for retiree health care benefits leads to generation shifting of the payment responsibility. Thus it appears to be, at the least unethical, and even a breach of fiduciary responsibility.
- F3. The extreme 30-year amortization period used by most entities minimizes the annual cost of funding the liability gap and further defers to future generations the compensation owed to present employees who provide services to present taxpayers and customers. Shorter amortization periods should be required for reasons of equity and to ensure that the promised benefits will be provided.
- F4. By capping retiree health care benefits, the City of San Rafael has reasonable certainty as to what those costs are. Other entities studied here that promise to pay for future retiree health care with uncertain and likely rapidly increasing costs are accepting an unknown and potentially very costly risk.
- F5. Because a few Marin County cities and other entities studied provide very limited benefits yet still appear able to meet community service needs, and because providing such benefits is increasingly rare in the private sector, such benefits appear to be unnecessary for attracting and retaining employees. Accordingly, for active and newly hired employees, the benefits should be trimmed and costs should be shared between the employees and their employer.
- F6. Marin entities using "Pay-Go" funding are paying only the current year health care benefits of those already retired. This ignores the reasonably known rising costs to cover future retirees who are already heading for retirement. Some actuarial valuation reports the Grand Jury studied provide those future "Pay-Go" estimates year-by-year, so they should be readily available from the actuary's valuations. Estimates of those annual costs for each of the next 10 years should be provided to the public so that those who will incur the costs can know those costs.
- F7. Employers studied for this report should include an age-60, or even later, date for retiree health care benefits to commence in future negotiations with employees and their representatives.
- F8. The results of retiree health care actuarial cost analyses are summarized if at all only in obscure notes to annual financial statements. The public is entitled to more readily accessible explanation of these costs because the public will bear those costs.
- F9. There is a wide range of retiree health care benefits offered among the entities studied in this investigation. No clear explanation for the range from minimal to

extremely generous is readily available. Those entities that are promising relatively generous benefits should provide clear justifications to their citizens and customers.

- F10. Most of the entities the Grand Jury investigated are using fairly reasonable discount rates of 4% - 5% per year to bring back to today in actuarial valuations the future annual costs of retiree health care benefits. However, some are using higher and highly questionable rate assumptions that are not justified by the investments (if any) that they have made to grow and fund the future benefits. The result is to understate the total funding needed today and in future years, to pay for those future benefits.

RECOMMENDATIONS

The Grand Jury recommends that each Marin County local government, special district and school district:

- R1. Begin setting aside in separate investment accounts, if it is not already doing so, each year's funds for amortizing its retiree health care benefits' UAAL, in addition to its "Pay-Go" funding of those benefits for present retirees.
- R2. Begin a program to lower the amortization period for funding its retiree health care benefits UAAL from as much as 30 years presently, to approach (within 10 years), the commonly used 17-year amortization period for retiree pension funding.
- R3. Negotiate caps on the amounts it commits to pay existing and new employees for retiree health care benefits.
- R4. Negotiate a higher retirement age than the currently applicable age for the commencement of retiree health care benefits.
- R5. Require active employees to make a contribution towards the cost of their retiree health care benefit.
- R6. Place a link on its website to provide the latest actuarial valuation of its AAL, its UAAL, its consequent percent funded, its discount rate (annual percentage) used to determine these values, and a projection of outlays ("Pay-Go") for retiree health care benefits for each of the current and subsequent 10 years.

REQUEST FOR RESPONSES

Pursuant to Penal code section 933.05, the Grand Jury requests responses as follows:

From the following individuals:

- Marin County Administrative Officer: **F3, F5, F7, F8, F9, R2 through R6.**

From the following governing bodies:

- County of Marin Board of Supervisors: **F3, F5, F7, F8, F9, R2 through R6.**

- Each of the 11 Marin City and Town Councils: City of Belvedere, Town of Corte Madera, City of Larkspur, City of Mill Valley, Town of Fairfax, City of Novato, Town of Ross, Town of San Anselmo, City of San Rafael, City of Sausalito, Town of Tiburon: **All Findings F1 through F10 and all recommendations, R1 through R6.**
- The Police Council Chair, Central Marin Police Authority: **All Findings F1 through F10 and all recommendations, R1 through R6.**
- The School Board President for each of the 12 surveyed Marin School Districts: Dixie School District, Kentfield School District, Larkspur School District, Mill Valley School District, Novato Unified School District, Reed Union School District, Ross School District, Ross Valley School District, San Rafael Elementary School District, San Rafael City High School District, Shoreline Unified School District, Tamalpais Union High School District: **All Findings F1 through F10 and all recommendations, R1 through R6.**
- President of the Marin Community College District Board of Trustees: **All Findings F1 through F10 and all recommendations, R1 through R6.**
- The Chairman or equivalent of the Board of Directors for each of the 14 surveyed special districts: Central Marin Sanitation Agency, Kentfield Fire Protection District, Las Gallinas Valley Sanitary District, Marin Municipal Water District, Marin-Sonoma Mosquito and Vector Control District, Marinwood Community Services District, North Marin Water District, Novato Fire Protection District, Novato Sanitary District, Ross Valley Fire Department, Sanitary District #1 (Ross Valley), Sewerage Agency of Southern Marin, Southern Marin Fire Protection District, Tiburon Fire Protection District : **All Findings F1 through F10 and all recommendations, R1 through R6.**

The governing bodies indicated above should be aware that the comment or response of the governing body must be conducted subject to the notice, agenda and open meeting requirements of the Brown Act. (GJ Text)

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Reports issued by the Civil Grand Jury do not identify individuals interviewed. Penal Code Section 929 requires that reports of the Grand Jury not contain the name of any person or facts leading to the identity of any person who provides information to the Civil Grand Jury.

GLOSSARY—

AAL--Actuarial Accrued Liability: The Actuarial Present Value of future benefits (such as retiree health care benefits) attributable to employees' (including retirees') past service.

Actuary: A professional skilled in the mathematical and statistical analysis of future probabilities for likely future event outcomes, and estimating the cost today of those future outcomes. Usually is a member of a society that has standards of proficiency and experience for certification of such expertise.

Amortization: The process of determining the payments to pay a loan or other obligation over a series of years with (usually) equal annual payments of interest and principal, such that at the end of the term the obligation has been fully repaid.

ARC or Actuarially Required Contribution: An employer's periodic required contribution to a defined benefit plan such as retiree health care benefits. It is usually determined annually. It includes payments actually made for existing retirees' benefits plus the current year's portion of an amortization of future obligations.

Discount Rate: The interest rate used in actuarial calculations to bring the estimated future costs of retiree health care benefits back to the present. It should be no more than the anticipated annual earnings rate for funds invested to pay for those future benefits.

GASB or Governmental Accounting Standards Board: The organization that sets standards of accounting and financial reporting for all U.S. local governments.

GASB Statement 45 or GASB 45: Issued in June 2004, this Statement established accounting and reporting standards for other post-employment benefits (that is, those post-employment benefits other than pensions) offered by state and local governments. Retiree health care benefits are the major, if not exclusive, non-pension benefit affected by this statement.

General Budget: The portion of the annual budget of local government entities that is of an on-going repetitive nature; essentially all expenditures other than those for capital projects and for debt service.

Implicit Subsidy: Actuarial valuations for some entities studied here calculate a separate component of the AAL, which is the value for retirees of having lower insurance costs because the retirees and active employees are combined for determining the cost of health care benefits for them as a single group. The retirees thus benefit from being in a risk pool that has more favorable medical care experience and thus, lower insurance rates than if the retirees were in a retirees-only risk group. It is possible that such an implicit subsidy may never have to be paid, but it is required to be included in the actuarial liability calculations.

Pay-Go or Pay-As-You-Go: The name given to the funding of only currently-paid benefits for retirees' health care, with no additional funding of earned but not yet payable benefits for both retirees and active employees.

Special District: A government entity common in California, that provides services in a territory that is not completely congruent with a government jurisdiction. Examples include water districts that provide service to all or portions of several cities, sewage-treatment plants that handle sewage from several local areas, incorporated or not, fire protection districts, etc.

UAAL or Unfunded Actuarial Accrued Liability: That portion of an entity's AAL for which no funding assets have been provided.

APPENDIX A

Dixie School District \$ 160 ph	+ School Districts Where I Live	Central Marin Sanitary District \$ 53 ph	+ Special Districts That Provide Services	Belvedere \$ 405 ph	+ My City or Town Where I Live	Marin County \$3,431 Per Household (ph)	HOW MUCH MIGHT I OWE CALCULATION TABLE
Kentfield School District \$ 332 ph		Kentfield Fire Protection District \$ 269 ph		Corte Madera \$ 2,928 ph			
Larkspur Corte Madera Schools District \$ 39 ph		Las Gallinas Valley Sanitary District \$ 141 ph		Fairfax \$ 286 ph			
Mill Valley School District \$ 128 ph		Marin Municipal Water District \$ 589 ph		Larkspur \$ 1,175 ph			
Marin Community College District \$ 51 ph		Marin Sonoma Mosq & Vec tor Control \$ 38 ph		Twin Cities Police Authority \$ 673 ph			
Novato Unified School District \$ 48 ph		Marinwood Community Service District \$ 2,720 ph		Mill Valley \$ 3,747 ph			
Reed Union School District \$ 494 ph		North Marin Water District \$ 115 ph		Novato \$ 85 ph			
Ross School District \$ 2798 ph		Novato Fire Protection District \$ 638 ph		Ross \$ 660 ph			
Ross Valley School District \$ 218 ph		Novato Sanitary District \$ 278 ph		San Rafael \$ 1,012			
San Rafael City Elementary School District \$ 324 ph		Ross Valley Fire District \$ 457 ph		San Anselmo \$ 350 ph			
San Rafael City High School District \$ 206 ph		Sanitary District 1 (Ross Valley) \$ 15 ph		Sausalito \$ 1,461 ph			
Shoreline School District \$ 856 ph		Southern Marin Fire Protection District \$ 375 ph		Tiburon \$ 721 ph			
Tamalpais Union School District \$129 ph		Sewerage Agency of Southern Marin \$ 298 ph					
		Tiburon Fire Protection District \$ 553 ph					

APPENDIX B

Total Unfunded Retiree Health Care		
	Cities and Town	UAAL \$mil
1	County of Marin	\$293.00
2	Mill Valley	\$24.48
3	San Rafael	\$24.30
	Corte	
4	Madera	\$11.79
5	Larkspur	\$7.49
6	Twin Cities Police Authority	\$7.25
7	Sausalito	\$6.63
8	Tiburon	\$2.90
9	San Anselmo	\$1.94
10	Novato	\$1.80
11	Fairfax	\$1.02
12	Ross	\$0.53
13	Belvedere	\$0.37
	Total	\$383.51
	Schools	
1	Marin Community College District	\$5.69
2	San Rafael City Elementary School District	\$5.46
3	Tamalpais Union School District	\$5.28
4	San Rafael City High School District	\$4.94
5	Reed Union School District	\$3.04
6	Mill Valley School District	\$2.16
7	Ross School District	\$2.14
8	Ross Valley School District	\$1.84
9	Shoreline School District	\$1.80
10	Kentfield School District	\$1.43
11	Dixie School District	\$1.06
12	Novato Unified School District	\$0.82
13	Larkspur Corte Madera School District	\$0.19
	Total	\$35.85
	Special Districts	
1	Marin Municipal Water District	\$36.10
2	Novato Fire Protection District	\$16.75
3	Marin Sonoma Mosquito and Vector Control	\$12.03
4	Novato Sanitary District	\$6.11
5	Southern Marin Fire Protection District	\$5.29
6	Ross Valley Fire District	\$4.80
7	Marinwood Community Service District	\$4.74
8	Sewerage Agency of Southern Marin	\$4.11
9	North Marin Water District	\$3.07
10	Central Marin Sanitation Agency	\$2.87
11	Tiburon Fire Protection District	\$2.27
12	Kentfield Fire Protection District	\$2.00
13	Las Gallinas Valley Sanitary District	\$1.88
14	Sanitary District #1 (Ross Valley)	\$0.30
	Total	\$102.33
40	Grand total	\$521.68

APPENDIX C

How are OPEB Liabilities Calculated?

Estimating the cost of employees' future retiree health care benefits that are earned today is complicated and involves calculations by experts known as actuaries. These calculations use estimates of the likelihood that existing employees will remain employed and will retire from the local government and receive the promised future health care benefit payments. How long such retirees will live in retirement and receive those benefits, and how those benefit costs will rise in the future, are also estimated. If spouses are covered, retiree spouse coverage, costs, and life span are also involved. Such calculations are made feasible by using computer models, and the techniques that actuaries use are fairly standardized in their application to entities subject to GASB Statement 45.

With the estimated costs of a local government's future retiree health care benefits thus determined, the actuary calculates the amount of money that would be required to be on hand today, to grow at an assumed annual compounded earnings rate over time to fully fund these future retiree benefits when they are to be paid. The assumed compound annual earnings rate (or its counterpart--discount rate to bring each future year's future costs back to the present) is a critical component of the actuary's calculations. Results, which are the liability today to fund those future costs, can vary greatly depending on the discount rate assumed.

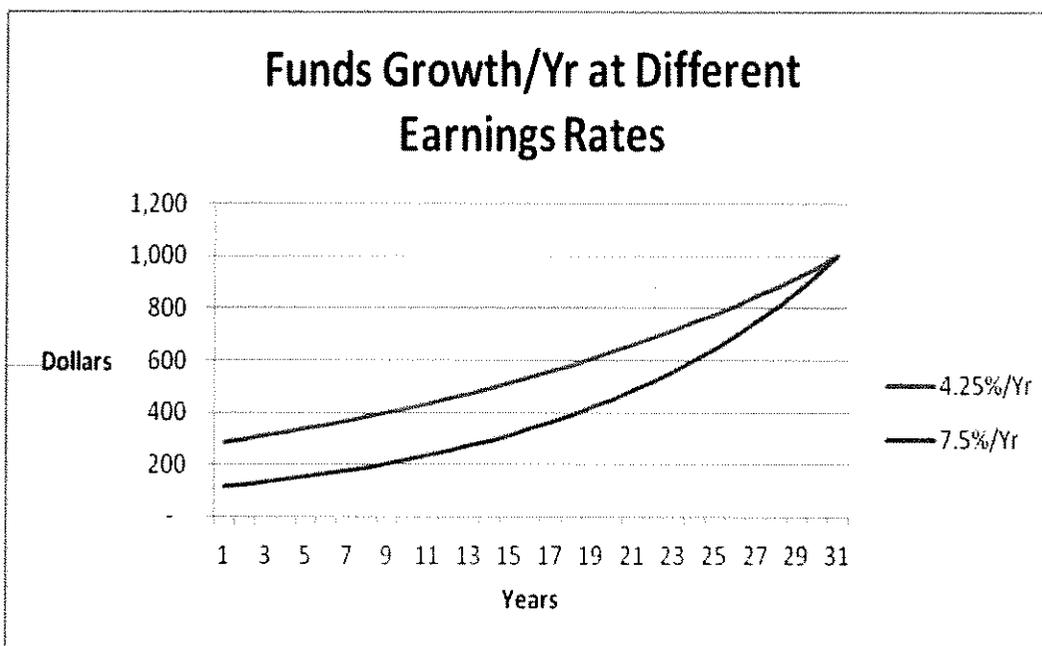
Generally, the assumed earnings or discount rate should have some realistic relationship to what the local government might earn on moneys it invests or better still, monies that it has invested for that purpose. But we found that overly optimistic assumptions (including unjustified high discount rates) are used by some entities in reporting their provisions to pay for retiree health care. This understates the amount of funds calculated as needed today to fund those future benefits.

The actuary's report determines the AAL by effectively discounting to the present each future year's nominal cost of retiree health care benefits to be borne by the local government entity. These annual future yearly costs, each discounted to the present, are accumulated and the total is the AAL. Thus, the AAL value is highly dependent upon the discount rate assumed.

The standard for recognizing pension liabilities costs includes a 17-year period for amortizing unpaid liabilities. In contrast, the standard for amortizing unpaid retiree health care benefit costs is as high as 30 years. The use of such a longer period (30 years versus 17 years) is to shift costs to future generations, and also understates the UAAL annual funding compared to a more reasonable and conservative funding period.

Interest Rate (or Discount Rate) and Amortization Period are Critical

For illustration, as the following chart shows, discounting \$1000 to be paid 30 years from now (an amortization period often used for retiree health care benefit liability cost calculations) at 4.25%, results in a value today of about \$287, but discounting it at a higher 7.5% results in a value today of only about \$114. Thus, if we assume that we need to accumulate \$1000 for payment 30 years from now, we would need to invest \$287 today if it would earn 4.25% compounded annually, but only \$114 if it would earn 7.5% compounded annually.)



Also, the period of time assumed to accumulate \$1,000 greatly affects the amount of money that needs to be invested today, to grow and reach that \$1,000. The following table shows the results of these assumptions. Using a 30-year period to grow investments rather than only a 17-year period for example requires a much smaller investment today to grow to the same future amount.

The table below indicates that an investment today of only \$114 would be needed under the most optimistic assumptions, compared to \$493 in the most conservative case. This could lead to an overly optimistic conclusion that only 23% (\$114 divided by \$493) need be set-aside today to reach a future 30-years obligation compared to a more conservative amount to grow and reach that objective.

Even using the 4.25% assumed growth rate but still a high 30-year amortization results in setting-aside today only 58% (\$287/\$493) of what would be required to reach that objective in 17 years.

Our review discloses that the actuary calculations for the entities studied generally are using amortization periods closer to 30 years (and even the full 30-years for some entities) than 17 years, and interest rates in the 4% -to 5% range----but some entities are still using as high as 7.5%, with no such investments to justify rates higher than 4%.

Effect of Interest Rate and Amortization Period on Investments to reach \$1000	
	Initial Investment
<u>30-Year Amortization</u>	
\$ Invested today to reach \$1000 in 30 Years	
At 4.25%/Year	\$287
At 7.5%/Year	\$114
<u>17-Year Amortization</u>	
\$ Invested today to reach \$1000 in 17 Years	
At 4.25%/Year	\$493
At 7.5%/Year	\$293
<u>4.25%/Year Interest Rate</u>	
\$ Invested today to reach \$1000	
In 17 Years	\$493
In 30 Years	\$287
<u>7.5%/Year Interest rate</u>	
\$ Invested today to reach \$1000	
In 17 Years	\$293
In 30 Years	\$114