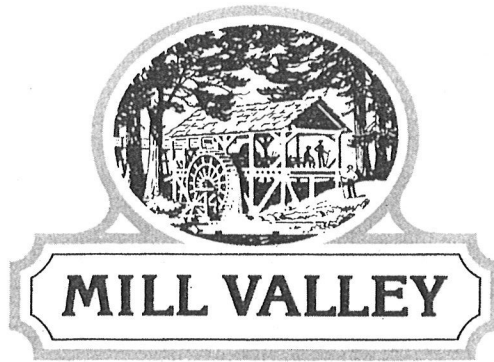


Andrew Berman
Mayor

Shawn Marshall
Vice Mayor

Stephanie Moulton-Peters
Councilmember



Kenneth R. Wachtel
Councilmember

Garry Lion
Councilmember

James C. McCann
City Manager

August 5, 2013

The Honorable Judge James Ritchie
Marin County Superior Court
P.O. Box 4988
San Rafael, CA 94913-4988

Dear Judge Ritchie:

The City of Mill Valley is in receipt of the Grand Jury Report – “Marin’s Retirement Health Care Benefits: The Money Isn’t There.” dated May 21, 2013. The City of Mill Valley recognizes the concerns surrounding the pensions and retiree health care benefits provided to public sector employees. The City Council has long-maintained a Core Value of “*Prudent fiscal policies and practices*” with respect to all aspects of municipal affairs. These fiscally conservative and responsible practices are evident in the City’s history regarding labor and compensation practices. The Council has taken aggressive steps over the years to contain and reduce the growth of labor costs in order to provide funding necessary to maintain service levels and to fund infrastructure repair and replacement and new community facilities.

The Grand Jury has requested a response to findings F1 through F10 and recommendations R1 through R6 of the report. These are as follows:

FINDINGS

The Grand Jury finds that:

Finding 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.

Response: We agree that many jurisdictions do not pre-fund future costs by making investments to cover promised benefits. However, it is not clear whether or not a particular jurisdiction’s funding practices and policies would jeopardize benefits being paid as it would vary based on their unique circumstances. The City of Mill Valley began setting aside funds using a Section 115 Integral Part Trust for the purpose of pre-funding retiree health costs nearly a decade ago and is currently exploring additional and alternative prefunding strategies. Additionally, the City Council has

approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

Finding 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.

Response: We agree that the “pay go” approach can lead to generation shifting of the payment responsibility. However, it is not clear whether or not a particular jurisdiction’s funding practices and policies would be inappropriate as it would vary based on their unique circumstances. The City of Mill Valley is working towards the full funding of our retiree health costs in order to avoid shifting retiree benefit costs unreasonably into the future. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

Finding 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: We agree that a longer amortization period reduces the annual cost of funding and defers costs but cannot pre-determine the appropriate amortization period length for other jurisdictions which should be based on their unique circumstances. As for Mill Valley, the City currently has 26 years remaining on its fixed (closed) amortization period.

Finding 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: We agree that benefits that are not capped provide less certainty to future costs. The City of Mill Valley has lengthened the service time required to qualify for this benefit and significantly reduced its retiree health care benefits going forward in order to reduce the amount and uncertainty of its future costs.

Finding 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.

Response: Health benefits continue to play a role in attracting and retaining employees. We disagree that benefits “appear to be unnecessary” because they are of greater or lesser importance based on an individual employee’s or applicant’s unique circumstances. As for Mill Valley, the City has enjoyed tremendous employee stability and has benefited from skills and institutional

knowledge from long-term employees which this benefit fosters. Retiree health benefits for new employees have been recently reduced and costs are shared between the employees and their employer.

Finding 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.

Response: The City of Mill Valley supports maximum transparency on both pension and OPEB-related issues. The City posts its OPEB actuarial reports on its website along with the City’s annual CalPERS pension actuarial reports.

Finding 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 City of Mill Valley does not have direct knowledge of the legal abilities and constraints of various health care systems that differ from our own system and retirement age is only one of many factors that should be considered in an appropriate benefit. As for Mill Valley, the City has lengthened the service time required to qualify for retiree medical benefits and the recent California Public Employees’ Pension Reform Act (PEPRA) has changed retirement ages which are used for retiree health eligibility. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

Finding 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.

Response: The City of Mill Valley supports maximum transparency on both pension and OPEB-related issues. The City posts its OPEB actuarial reports on its website along with the City’s annual CalPERS pension actuarial reports.

Finding 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 City of Mill Valley agrees that there is a wide range of benefits offered among the entities in the investigation and that individual jurisdictions are responsible for providing justifications to their citizens and customers. The City Council has long-maintained a Core Value of “*Prudent fiscal policies and practices*” with respect to all aspects of municipal affairs. These fiscally conservative and responsible practices are evident in the City’s history regarding labor and compensation practices. The Council has taken aggressive steps over the years to contain and

reduce the growth of labor costs in order to provide funding necessary to maintain service levels and to fund infrastructure repair and replacement and new community facilities.

Finding 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.

Response: The City has not researched the actuarial assumptions of other Marin local governments beyond what is contained in the Grand Jury report. Whether or not a particular jurisdiction's assumptions are appropriate would be based on their unique circumstances. As for Mill Valley, the City is partially funding our retiree health costs through the use of a Section 115 Integral Part Trust which invests the funds over a very long period of time using assumptions similar to a pension fund. The rate assumptions used in the City's OPEB actuarial valuations are consistent with the investment return targets used by the entity managing the investments. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

RECOMMENDATIONS:

The Grand Jury recommends that:

Recommendation 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 City of Mill Valley has already implemented this recommendation through the trust and the budgetary decisions of the City Council. The City initiated funding of our retiree health costs through the use of a Section 115 Integral Part Trust in 2005.

Recommendation 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.

Response: The City of Mill Valley currently has a remaining 26-year fixed (closed) period. The City will review the amortization period on a regular basis through each OPEB actuarial valuation as well as the study the City will undertake on additional and alternative prefunding alternatives.

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

Response: The City of Mill Valley has lengthened the service time required to qualify for this benefit and significantly reduced the benefit for new employees. The City will continue to review the benefit and negotiate further revisions as is determined to be appropriate. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

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

Response: Already implemented. The City of Mill Valley has lengthened the service time required to qualify for retiree medical benefits and the recent California Public Employees' Pension Reform Act (PEPRA) has changed retirement ages which are used for retiree health eligibility. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

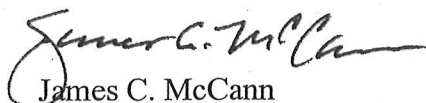
Recommendation R5. Require active employees to make a contribution towards the cost of their retiree health care benefit.

Response: Partially implemented. Most new employees receive a significantly reduced retiree health benefit and therefore must fund the remainder of the premium upon retirement. The City will continue to negotiate for this reduced benefit to be applicable to all employee groups. Additionally, the City Council has approved a resolution establishing a set of 10 guiding principles and practices including such issues as cost controls, benefit formulas, employee contributions, and reserve funding.

Recommendation 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: Already implemented. The City of Mill Valley supports maximum transparency on both pension and OPEB-related issues. The City posts its OPEB actuarial reports on its website along with the City's annual CalPERS pension actuarial reports and annual audited financial statements.

Sincerely,



James C. McCann
City Manager

CC: Rich Treadgold, Foreperson, Marin County Civil Grand Jury
Mill Valley City Council