REED UNION SCHOOL DISTRICT

277 A Karen Way • Tiburon, CA 94920 • tel: 415.381.1112 • fax: 415.384.0890
www.reedschools.org

August 20, 2013

Nadine A. Mueller
Marin County Civil Grand Jury
3501 Civic Center Drive, Room 275
San Rafael, CA 94903

Dear Ms. Mueller:

This letter is Reed Union School District's response to the Marin County Civil Grand Jury's report titled "Marin's Retirement Health Care Benefits: The Money Isn't There", as requested by the Grand Jury.

GRAND JURY 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.*

The District currently has a minimum contingency reserve goal that is equal to the current-year differential between the district's Community Funded School revenue (property tax) and the state's revenue limit guarantee. The District's current reserves are in excess of $4.1M and could finance the Unfunded Actuarial Accrued Liability (UAAL) that is estimated at $3.04M.

Additionally, the District feels the need to maintain flexibility during this period of uncertainty surrounding the California state budget, appropriations to school districts, and the implementation of the Affordable Care Act and its impact on health benefits, associated costs, and employer responsibilities.

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.*

Cash flow issues coupled with the ability of the district to 'fund' the OPEB liability with ending fund balance are necessary considerations in a full exercise of fiduciary responsibility. While the pay-as-you-go amount does increase over the next several years, we expect that our funding levels will increase proportionately and provide the necessary resources to finance this 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.*

The amortization period allows the district to gradually phase in the cost of the liability that had been incurred prior to the adoption of GASB-45 and conforms to current accounting guidance for governmental entities.

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.*

The Reed Union School District has had a cap on retiree benefits since the 1990's. Currently retirees are divided into two separate benefit groups: Certificated and Classified. Certificated employees who are at least 55 years of age, retire from the district and are a member of the CalPERS health plan receive a monthly benefit of $355 for five years or until they reach the age of 65, there is no minimum length of employment required to receive this benefit. Classified employees who are at least 50 years of age, retire from the district and are a member of the CalPERS health plan receive a monthly benefit of $355 for five years no matter what age they are, they must have been employed with the district for a minimum of 10 years. Since the Reed Union School District participates in the CalPERS medical program the District is obligated to contribute toward the cost of retiree medical coverage for the retiree's lifetime or until CalPERS coverage is discontinued. To mitigate the District's cost of the CalPERS contribution, all employees hired after January 1, 2009, must meet minimum years of service to receive the contribution. Employees hired after January 1, 2009, who work less than 10 years must fund the CalPERS contribution, employees with 10 to 19 years of service must fund 50% of the CalPERS contribution and employees with 20 or more years of service will have 100% of the CalPERS contribution made by the district. However, if the District decides to switch health care plan providers and is no longer a member of the CalPERS health plan system those monthly costs would no longer be borne by the District. At any point in time the District may reevaluate its membership in the CalPERS health plan.

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.*

Benefits are subject to negotiations with the district's bargaining units and as such cannot be unilaterally changed. As noted above, the District has initiated years of service requirements to receive CalPERS contributions.

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 provided 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 those costs can know those costs.*

The District's actuarial study provides year-by-year pay-as-you-go estimates which does increase over time. However, at no time in the past 14 years has the pay-go amount exceeded .55% of expenditures and as noted above the District always has the option to reevaluate it membership in the CalPERS medical program.

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.*

Benefits are subject to negotiations with the district's bargaining units and, as such, cannot be unilaterally changed. The District has a five year limit on retiree benefits and as noted in F4 there is a vesting schedule for all employees hired after January 1, 2009.

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.

The district's annual audited financial statements provide full disclosure of the district's OPEB including the key assumptions used in the actuarial study. The audited financial statements are discussed and accepted at a public board meeting

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.

The District's contribution to retiree health benefit premiums is relatively minimal ($355 per month) as noted in F4 and limited by contract language. The on-going cost of the required CalPERS contribution can be reevaluated at any point in time and the District can cease membership in the CalPERS medical program.

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 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.

The District's actuary utilized a 4.5% discount rate to prepare our study and was based on then-current interest rates in place during the timeframe the study was prepared.

GRAND JURY RECOMMENDATIONS

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.

The District is not setting aside amounts in separate investment accounts as the OPEB liability has continued at a low .55% of expenditures over the last 14 years. The Governing Board will address this issue and determine if setting an amount to fund the retiree health care benefit is necessary.

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.

The amortization period allows the district to gradually phase in the cost of the liability that had been incurred prior to the adoption of GASB-45 and conforms to current accounting guidance for governmental entities.

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

The District has had retiree benefit caps since the 1990's' and has limited future costs as described in F4.

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

The Districts contracts with its bargaining units provide that employees must meet the requirements of their respective pension plans, either the State Teachers Retirement System or the Public Employees Retirement System in order to qualify for retiree health benefits.

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

Benefits are subject to negotiations with the district's bargaining unit and as such cannot be

unilaterally changed. After the five year district cap expires, retirees hired after January 1, 2009 must meet the vesting schedule years of service to receive the minimal contribution required by CalPERS.

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.

The District will post its actuarial study on its website.

If you have any questions please contact our Superintendent, Steven Herzog, at 415-381-1112 or our Business Manager John Frick at 415-383-1116 ext. 4101.

Sincerely,

Nancy O'Neill

Nancy O'Neill, President
Reed Union School District Board of Trustees