September 24, 2015

Honorable Glenda Sanders, Presiding Judge
Superior Court of California, County of Orange
700 Civic Center Drive West
Santa Ana, CA 92701


The City of Costa Mesa understands the significance of retiree healthcare obligations, and appreciates the Grand Jury’s work on this report. Please see the attached general comments and specific City responses to the findings and recommendations of the Grand Jury report.

If you have any questions or need additional information, please contact Steve Dunivent, Interim Finance Director at (714) 754-5243.

Sincerely yours,

[Signature]

STEPHEN M. MENSINGER
Mayor

cc: Orange County Grand Jury
    Council Members
    Tom Hatch, CEO
    Rick Francis, Assistant CEO
    Tamara Letourneau, Assistant CEO
    Steve Dunivent, Interim Finance Director

Attachment
City of Costa Mesa
Response to Grand Jury Report:
Unfunded Retiree Healthcare Obligations – A Problem for Public Agencies?
Issued June 29, 2015

GENERAL COMMENTS

The City of Costa Mesa administers a single-employer defined benefit plan which provides medical insurance benefits to eligible retirees and their spouses in accordance with various labor agreements (Other Post Employment Benefit, OPEB). The plan provides subsidized retiree health benefits for employees hired before January 1, 2004 who retire directly from the City with 10 years of City service. The City provides a contribution up to a percentage of the lesser of $500 per month or the premium for the most popular medical plan elected by the employees. The City currently provides this OPEB for 362 retired employees. In addition, there are 395 active employees that may one day qualify for retiree OPEB health benefits in the future assuming they meet plan eligibility requirements. This single-employer defined benefit plan was closed to new participants on December 31, 2003.

The contribution requirements of plan members and the City are established by City Council Policy 300-1 (effective date August 19, 2003), and may be amended by City Council. The contribution required to be made under City Council and labor agreement requirements is based on a pay-as-you-go basis (i.e., as medical insurance premiums become due). For fiscal year ended June 30, 2014, the City contributed $1,728,740 to the plan. The City has not established a trust for the purpose of holding assets accumulated for plan benefits.

FINDINGS

F.1. Aliso Viejo, Dana Point, Laguna Hills, and Villa Park were not in compliance with GASB Statement No. 45 regarding the authorization of a study to determine other post-employment benefit liabilities. Aliso Viejo, Dana Point, Laguna Hills, Laguna Woods, and Villa Park were not in compliance with the disclosure of post-employment benefits in the Notes Section of their Comprehensive Annual Financial Report for the FY2012-13.

Costa Mesa response not required.

F.2. Twenty-one out of the 32 agencies that provided June 30, 2013, data to the Grand Jury had not put aside funds in an irrevocable trust to help pay for the accrued actuarial liability of retiree healthcare costs in the future. This is an imprudent level of contribution.

Costa Mesa response: The City of Costa Mesa disagrees with this finding. While there are advantages to setting aside funds for future liabilities in a trust, such a funding mechanism is not currently a legal requirement, and comes with associated costs and restrictions. However, should a trust become a legal requirement in the future, the City of Costa Mesa will certainly comply. Until such time, Costa Mesa will continue to self-administer and fund its OPEB obligations on a pay-as-you-go basis pursuant
to City Council policy and as currently permitted by law.

F.3. Anaheim, Buena Park, County of Orange, Huntington Beach, Lake Forest, and Stanton were in compliance with the requirement to contribute a full 100% or more of their Annual Required Contribution in the FY 2012-13. The remaining 26 agencies were not in compliance.

Costa Mesa response: The City of Costa Mesa disagrees with this finding. As presented in its FY 2012-13 CAFR, Costa Mesa’s Annual OPEB Cost (AOPEBC) of $2,153,804 is an actuarial estimate of cost for FY 2012-13 determined in accordance with the parameters of GASB Statement No. 45, while Costa Mesa’s Actual Contributions (AC) of $1,727,148 represents the total actual OPEB payments made to retirees during FY 2012-13. To clarify, Costa Mesa paid 100% of its actual OPEB obligation, rather than just 80.2% as stated in Table 5 of this Grand Jury report. Viewed from this perspective, Costa Mesa’s total actual OPEB cost in FY 2012-13 was 80.2% of the actuarial estimate (AOPEBC) for that time period; i.e., the real cost was lower than the actuarial estimate.

The City of Costa Mesa has paid, and will continue to pay, 100% of its annual OPEB obligations on a pay-as-you-go basis pursuant to City Council policy and as currently permitted by law.

F.4. All agencies surveyed (except Anaheim) do not disclose retiree health benefits as part of employee compensation per GAAP standards.

Costa Mesa response: Costa Mesa disagrees partially with this finding. The Grand Jury stated on Page 15, Paragraph 1 of this report, “The OCGJ analyzed the compensation reports completed by the reviewed agencies to determine whether the agencies that had accrued actuarial liability of their OPEB costs had also disclosed earned retiree health benefits on their compensation reports for current employees. The analysis showed that only one agency, Anaheim, properly discloses retiree health benefits as part of employee compensation."

Anaheim does provide a column labeled RETIREMENT MEDICAL in its City Employee Positions and Compensation report posted on the city web page. However, Costa Mesa nor its outside auditors are aware of any GAAP or GASB standard compensation report requiring calculation and disclosure of individual retiree health benefits costs. Costa Mesa will continue its current financial reporting practices that are in full conformity with GASB 45 requirements.

RECOMMENDATIONS

R.1. The cities of Aliso Viejo, Dana Point, Laguna Hills, Villa Park, and Laguna Woods should measure and disclose their liability in accordance with Governmental Accounting Standards Board Statement No. 45. (F.1.)

Costa Mesa response not required.

R.2. The 21 agencies that have not contributed into an irrevocable trust fund to
finance their retiree health obligations should begin to put aside monies to fund this obligation and reduce their unfunded public liabilities (F.2.)

Costa Mesa response: The recommendation will not be implemented because it is not warranted. As stated in the response to Finding 2 above, Costa Mesa recognizes there are advantages to setting aside funds for future liabilities in a trust, but such a funding mechanism is not currently a legal requirement, and comes with associated costs and restrictions. Should a trust become a legal requirement in the future, the City of Costa Mesa will certainly comply. Until such time, Costa Mesa will continue to self-administer and fund its OPEB obligations on a pay-as-you-go basis pursuant to City Council policy and as currently permitted by law.

In February 2013, the Costa Mesa City Council established a Pension Oversight Committee composed of nine public members and the Mayor or Mayor’s designee to examine public employee pension-related matters with a focus on the following:

- Review annual and long-term pension and financial matters as they pertain to the City’s CalPERS retirement unfunded pension liability obligations;
- Ensure the City maintains adequate reserves and ratios per City Council guidelines;
- Review negotiated pension and compensation packages as they pertain to each employee bargaining unit;
- Evaluate and advise the City Council on annual changes to pension costs.

The Pension Oversight Committee is currently researching and evaluating various pension and retiree health funding mechanisms such as CalPERS California Employers’ Benefit Trust (CERBT) and private IRS Section 115 trust programs. To date, no committee recommendation has been made.

The Costa Mesa City Council is very much aware of the City’s retiree health obligations. Legal requirements and plans to address those obligations will be researched and evaluated.

R.3. The 26 agencies that are not recognizing the full amount of their Annual Required Contribution as expense in the current period and should comply with the requirement to do so. (F.3.)

Costa Mesa response: The recommendation has been implemented. As stated in the response to Finding 3 above, in its FY 2012-13 CAFR, Costa Mesa’s Annual OPEB Cost (AOPEBC) of $2,153,804 is an actuarial estimate of cost for FY 2012-13, while Costa Mesa’s Actual Contributions (AC) of $1,727,148 represents the total actual OPEB payments made to retirees during FY 2012-13. To clarify, Costa Mesa paid 100% of its actual OPEB obligation, rather than just 80.2% as stated in Table 5 of this Grand Jury report. Viewed from this perspective, Costa Mesa’s total actual OPEB cost in FY 2012-13 was 80.2% of
the actuarial estimate (AOPEBC) for that time period; i.e. the real cost was lower than the actuarial estimate.

The City of Costa Mesa has paid, and will continue to pay, 100% of its annual OPEB obligations on a pay-as-you-go basis pursuant to City Council policy and as currently permitted by law.

R.4. All agencies surveyed should recognize retiree health care benefits in employee compensation in conformity with GAAP. (F.4.)

Costa Mesa response: The recommendation has been implemented. GASB 45 requires local governments to report three figures related to OPEB: Annual Required Contribution (ARC); Annual OPEB Cost (AOC); and Net OPEB Obligation (NOO). All three of these figures are itemized and reported in Costa Mesa’s CAFR reports in the Notes Section. All Costa Mesa OPEB calculations are subjected to annual outside audits and are in full conformity with GASB 45 requirements. Additional calculations of healthcare benefits cost by employee are not currently a requirement.