



CITY OF LAGUNA HILLS

City Council

August 23, 2011

from judge

MAYOR
L. Allan Songstad, Jr.
MAYOR PRO TEMPORE
Melody Carruth

COUNCIL MEMBERS
Randal Bressette
Barbara Kogerman
Joel Lautenschleger

The Honorable Thomas J. Borris
Presiding Judge of the Superior Court
County of Orange
700 Civic Center Drive West
Santa Ana, CA 92701

Re: CPC Section 933(c) Response to Grand Jury Report Entitled, "Compensation Study of Orange County Cities" from the City of Laguna Hills

Dear Judge Borris:

As requested by the Orange County Grand Jury letter dated June 9, 2011, the City of Laguna Hills is responding to the findings and recommendations of the Grand Jury Report entitled, "Compensation Study of Orange County Cities." Specifically, the City of Laguna Hills is responding as directed to Findings F4, F6 and F7, and to Recommendations R1, R2 and R4.

Grand Jury Findings

F.4: Public disclosure of municipal compensation levels is widely inconsistent, ranging from good to non-existent.

Response:

The City agrees with the finding. There is no standardized format among public agencies for the reporting of compensation. Moreover, there is widespread opinion about what constitutes total compensation. The City of Laguna Hills provides appropriate disclosure of its employees' compensation on its website through a complete Public Officials Compensation Report of all elected officials and management employees. This report is required by Municipal Code Section 244-010 and must be updated annually by February 28 pursuant to Municipal Code Section 244-020.

F.6: The compensation of the City Manager and Assistant City Manager/Finance Director in the City of Laguna Hills exceeds levels in other comparably sized cities both inside and outside of Orange County.

Response:

The City wholly disagrees with this finding based in part on a comparison between the Grand Jury Report and the City's recently commissioned Compensation Study. The City's Compensation Study was conducted by Ralph Andersen & Associates, a reputable and professional consulting firm. The principal with Ralph Andersen & Associates that was assigned to conduct the study was Douglas Johnson, Vice-President. Mr. Johnson has over 24 years of consulting experience and is the firm's expert in job analysis, market comparability, compensation, benefits, and related matters. He has served as an expert witness in arbitration proceedings and mediation sessions on matters of compensation. In his career, Mr. Johnson has been involved with over 800 compensation related studies. The City's response is also based in part on the stated methodology and findings within the Grand Jury Report itself. The following are the more salient problems and fundamental flaws with the Grand Jury Report:

- 1) A valid compensation study begins with a definition of the labor market within which the City must compete. This includes identifying the group of agencies that the City competes with in terms of recruiting and retaining personnel. There are five important criteria utilized in identifying those agencies that comprise a city's labor market: historical practices, geographic proximity, employer size, nature of services provided and economic similarity. Unfortunately, the implication in the Grand Jury Report, and this particular finding, is that only population matters; even though the labor market in their report was all 34 cities in Orange County. By contrast, the City's professional compensation consultant pointed out in his report that establishing a universe of comparable employers involves a careful balancing of all five factors. Furthermore, an ideal market will include both larger and smaller employers, agencies located in higher and lower cost of living areas, and both local and regional employers. Therefore, whether or not the compensation levels in Laguna Hills exceed that of similar sized cities is irrelevant. Even the Grand Jury's Finding F.3 where they found that compensation of individual high-level positions bears no significant relationship to city population, belies the implication in this particular Finding F.6 that only population matters. With respect to cities outside of Orange County, it is not an accepted practice by professional compensation consultants to cherry pick other cities outside of an established labor market.

- 2) A valid compensation study includes an analysis of individual job descriptions to ensure that each position is being properly compared to comparable positions in the selected labor market. In its request for information from Orange County cities, the Grand Jury did not ask for any job descriptions. As a result, the Grand Jury incorrectly compared the Laguna Hills Assistant City Manager with Finance Directors in the County. While it is true that the Laguna Hills Assistant City Manager also serves as the City's designated Finance Director, he only spends about 15% -20% of his time on financial matters. If the Grand Jury had reviewed job descriptions, they would have found the City's Finance Manager most closely matches the typical duties of a Finance Director. Surprisingly, the Grand Jury had the requested data for the City's Finance Manager, but still failed to make the proper comparison, most likely because they didn't review any job descriptions. Therefore, all comments and findings made by the Grand Jury with respect to the Laguna Hills Assistant City Manager are invalid and without merit.
- 3) A valid compensation study makes salary comparisons at a specified control point. For a compensation study of all cities in Orange County, this should have been the top step in each salary range. The Grand Jury instead used actual base salary. As a result, differences in years of service and experience in a particular position were completely ignored by the Grand Jury. A reasonable person would expect that a City Manager that has 20 years of service in that position with one city would likely make more money than a new City Manager with only one to three years of service.
- 4) A valid compensation study recognizes and makes adjustments for the demonstrable differences between an age-banded and a composite health insurance rate environment. In an "age-banded" approach to charging health insurance premiums, the costs are lower for younger employees and higher for older employees. For example, under United Health Care's age-banded rates for 2011-12 for an HMO plan, the monthly premium for an employee and spouse is \$588.10 if the employee is 29 years of age or younger. For an employee that is 55-59 years of age, that same plan cost \$1,274.83 per month. If they were 65 and older, it would cost \$1,970.38 per month. In a "composite" rate environment, the health insurance premiums charged for each employee are the same amount regardless of age. In 2009, the City of Laguna Hills' health insurance premiums were structured according to the age-banded approach; therefore, the cost to provide health insurance to older employees and City Council members was significantly higher when compared to their counterparts in other cities whose premiums were based on a composite rate; even though the actual coverage was virtually identical. For the City of Laguna Hills, the more important issue was the bottom line or total cost for insuring all of its employees. The focus was not on the individual, but rather on the group. The

Grand Jury did not recognize this distinction and make adjustments that would be common in a professional compensation study. In Orange County, the vast majority of cities are in the PERS health program, which is a composite rate environment. As a result, the 2009 cost of benefits for the Laguna Hills City Manager, City Council and other employees is significantly skewed and effectively misrepresented by the Grand Jury Report.

- 5) A valid compensation study will look at total leave afforded employees annually (vacation, administrative, holiday, sick) and compare either the total number of days, or the cash value of the total days of leave based on salary. The Grand Jury Report's focus on vacation leave only included the cashed out value of vacation leave in compensation comparisons for a single year, 2009. This practice ignores the fact that in addition to cashing out accrued but unused vacation leave, employees may also take the time off which can negatively affect productivity, or may even require an employer to pay someone else to perform the individual's duties in their absence. In other cases, employees are allowed to let their leave hours accumulate without limitation over a period of years to be used or cashed out at a future date. The City of Laguna Hills places a limit on the amount of vacation leave that can be accumulated as a means of limiting future liabilities. The decision to include vacation buy-outs in compensation comparisons led to skewed data in the Grand Jury Report and overstated compensation levels for employees who happen to have cashed out vacation leave in 2009. In the City's professional Compensation Study, among the 17 selected comparator agencies, the total average annual leave time for City Managers is 53 days. The Laguna Hills City Manager has a total leave package of 54 days, which is in keeping with the market.
- 6) A valid compensation study will take into account the different retirement formulas in place among the surveyed cities. This is probably the most egregious flaw in the Grand Jury Report, which admits on page 2 of the report that, "This study does not include any analysis of benefits paid after retirement or pension plans." It is simply an unsound practice to compare compensation among cities that have varying levels of defined benefit pension plans without factoring in the present value difference between the various plans. In 2009, of the 34 cities in Orange County, 8 had a 2.7% at 55 formula, 10 had a 2.5% at 55 formula, 15 had a 2% at 55 formula and only one had a 2% at 60 formula. That one city was the City of Laguna Hills, which retained the reasonable and sustainable 2% at 60 formula when all others were enriching their defined benefit plans. In order to remain competitive, the City has offered a supplemental defined contribution plan. This is the very same approach that the State's Little Hoover Commission has recommended in its February 2011 report on public pension reform measures. The City also had a policy in place to pay employees 5% above the

County average of comparable positions. The City's professional Compensation Study found that the City on average was paying 1.5% above the City's comparator agency average in base salary. When the retirement impact from the differential retirement formulas was discounted to current dollars, the City was (-11.8%) below its comparator agencies. For the City Manager, the professional Compensation Study found that the Laguna Hills City Manager was 5.1% above the comparator agencies in base pay, but fell to (-1.7%) below the average when the retirement benefits were discounted to current dollars. The Grand Jury's methodology, which they acknowledge did not include the present value benefit of enriched contribution plans, nor did it include any Post-Employment Benefit Costs, has significantly skewed the data in its report to the detriment of all positions from Laguna Hills. It should not be lost on anyone that many cities are in the process of adopting second tiers for new employees that will offer them the same 2% at 60 formula provided by Laguna Hills to all of its full-time employees.

F.7: There is currently no disclosure of written employment contracts on the majority of cities' websites.

Response:

Since the City has not conducted an analysis of each city's website in Orange County, we are unable to agree or disagree, either wholly or in part, with this finding. With respect to the City of Laguna Hills, the City wholly disagrees with this finding. The City's prevailing Salary and Benefits Resolution is listed on the City's website and clearly states that the City has employment agreements with the City Manager and the Assistant City Manager. The City Manager's agreement has been available on the City's website and the Assistant City Manger's agreement was recently added.

Grand Jury Recommendations

R.1: Transparency – All cities in Orange County report their compensation information to the public on the Internet in an easily accessible manner. The Compensation Disclosure Model (Appendix 4) provides a sample as to the items that should be included in determining total compensation.

Response:

The recommendation has been implemented. The City already provides on its website a complete Public Officials Compensation Report of all elected officials and management employees. This report is required by Municipal Code Section 244-010 and must be updated annually by February 28 pursuant to Municipal Code Section 244-020. The

report is easily accessed through a permanent featured link on the City's home page. The City will not follow the sample provided by the Grand Jury since the City's current report is more detailed and comprehensive when compared to the Grand Jury Report sample.

R.2: Employment Contracts – Each city reveal any individual employment contracts in an easily accessible manner.

Response:

This recommendation has been implemented. Prior to the release of the Grand Jury Report, the City Manager's contract was easily accessible on the City's web site. The Assistant City Manager's employment agreement has been added.

R.4: Compensation Levels – The City of Laguna Hills conduct a compensation review of top officials.

Response:

This recommendation has been implemented. By action of the City Council, a comprehensive and professional compensation study was commissioned on February 22, 2011 of all full-time employees well prior to the release of the Grand Jury Report. The comprehensive compensation study by Ralph Andersen & Associates was completed and presented to the City Council at their July 8, 2011 City Council meeting.

Sincerely,



L. ALLAN SONGSTAD, JR.

Mayor