MEMO TO THE BOARD OF DIRECTORS

Subject: Agenda Item No. 6.10 Review and Approve Response to the Santa Cruz County Civil Grand Jury Report on Retirement Costs and Obligations in Santa Cruz County

2. Santa Cruz County Civil Grand Jury Response Packet
3. Soquel Creek Water District 2015 Ten Year Finance Plan
4. April 21, 2015 Finance Report

On June 11, 2015, the Santa Cruz County Civil Grand Jury released a report covering retirement costs and obligations in Santa Cruz County (Attachment 1). The Grand Jury investigated retirement costs of six jurisdictions in Santa Cruz County, including the cities of Capitola, Santa Cruz, Scotts Valley, Watsonville, the County of Santa Cruz, and the Soquel Creek Water District.

The report includes 2 findings and 2 recommendations for the District:

Findings
1. Continually rising retirement costs and obligations put funding of jurisdictions’ services and projects at risk.
2. A clear and complete statement of the total retirement costs and obligations has not been provided in the budget narrative for either the public or elected officials.

A third and final finding regarding enrollment in the CalPERS Retiree Benefit Trust Fund (CERBT) was not attributed to the District as we already participate in this program.

Recommendations
1. To prevent reduction in public services, each of the six public agencies studied in the report should increase, and make public, their efforts to manage and reduce retirement costs and obligations.
2. Each of the six public agencies should provide, in language understandable to the public, the totality of retirement obligations in their annual budget narratives beginning with the fiscal year 2015/16 budget.
The District was excluded from the third and final recommendation regarding enrollment in the CERBT as the District enrolled and began contributions to pre-fund OPEB in March of 2011.

California law PC § 933.05 requires that those responding to a Grand Jury report must provide a response for each individual finding and recommendation within a report, not a generalized response to the entire report (Attachment 2). Staff contacted the Grand Jury representative and was instructed that the Board should formulate a joint response, approve it by Motion, and return it. Responses by the governing body of any public entity are required within 90 days of the Grand Jury report’s publication.

The required format for formal responses to the Findings and Recommendations are outlined below:

Findings: Indicate Agree, Partially Disagree, or Disagree. An explanation of the reasons must be provided for any response other than Agree.

Recommendations:
1. Has been implemented. Provide summary of implemented action.
2. Has not yet been implemented but will be implemented in the future. Provide timeframe or estimated date of implementation.
3. Requires Further Analysis. Provide explanation of scope of analysis and timeframe not to exceed 6 months from date of publication of the Grand Jury Report.
4. Will not be implemented. Provide an explanation as to why the recommendation is unwarranted or unreasonable.

Staff has prepared a draft response to each finding and recommendation within the specified guidelines as follows:

Finding 1: Continually rising retirement costs and obligations put funding of jurisdictions' services and projects at risk.

___ AGREE
___ PARTIALLY DISAGREE - explain disputed portion below
___ DISAGREE - explain below

Response explanation (required for responses other than “Agree”):

The Soquel Creek Water District’s total Unfunded Liability (UL) for pension and OPEB as of June 30, 2013 was $9 million. Required employer contributions are estimated at $682,000 for the 2015/16 fiscal year and projected to rise over four more years before flattening out. If the District pays according to CalPERS amortization schedule, the pension UL costs would total $14.9 million over 30 years.
This is the first year that small employers in the mandated CalPERS risk pools have the ability to effectively manage their pension liabilities. The Fiscal Year 2015/16 Budget adopted by the Board on June 16, 2015 includes funding for accelerated payment of the UL. The smaller liability associated with the Second Tier plan will be paid off and the District intends to pay down the liability for the First Tier plan in ten years instead of thirty in order to achieve significant long term savings.

Retirement costs certainly contribute to the District’s financial pressures. However, as noted in the 2015 Ten-Year Finance Plan (Attachment 3), the District faces financial challenges on a number of fronts that combined, put significant upward pressure on future water rates. Future anticipated projects and costs include:

- $80 million (in escalated $) to develop a supplemental water supply project. New and ongoing annual maintenance costs to operate the project once it’s placed into service are estimated to be $1.3 million starting in 2022/23.

- $70 million (in escalated $) of water system capital needs in the current and next ten years, along with $1 million to $2 million each year for capital outlay, studies, and planning efforts.

- The District will be required to issue additional debt, which will increase debt service payments, in order to fund the supplemental supply project.

- $875,000 for Conservation Program expenses in 2015/16 increasing annually to $1.3 Million in 2024/25 depending upon the degree of implementation.

- $350,000 starting in 2017/18 in ongoing annual operational costs for hexavalent chromium treatment.

The District is currently operating in an environment of declining water sales and will need to raise rates to meet its financial obligations and ensure long term financial stability. Retirement costs must be acknowledged and properly managed but are not the District’s sole source of financial pressure. To state that these costs alone put services and projects at risk is not a fair and accurate assessment of the District’s overall financial outlook.

Finding 2: A clear and complete statement of the total retirement costs and obligations has not been provided in the budget narrative for either the public or elected officials.

AGREE

X PARTIALLY DISAGREE - explain disputed portion below

DISAGREE - explain below

Response explanation (required for responses other than “Agree”):
At the April 21, 2015 regular meeting of the Board of Directors, Staff presented an informational report on California Public Employees’ Retirement System (CalPERS) Risk Pool Changes (Attachment 4). The report provided an overview of the District’s retirement benefits under its contract with CalPERS and information regarding revisions to the risk pool that affect benefits costs. A clear and complete statement of pension retirement costs and obligations was presented. The report was intended to serve as a resource for the discussion and development of funding strategies during May’s budget discussions. Staff released the information ahead of the budget discussions to allow time for the Board (and public) to digest the information and formulate questions.

The 2015-16 Budget contains information regarding OPEB expenses, but does not address the unfunded liability.

More complete information regarding retirement costs and obligations (pensions and retiree health or OPEB) is appropriately located in the District’s annual audited financial statements.

**Recommendation 1:** To prevent reductions in public services, each of the six public agencies studied in this report should increase, and make public, their efforts to manage and reduce retirement costs and obligations.

_X_ HAS BEEN IMPLEMENTED

HAS NOT BEEN IMPLEMENTED BUT WILL BE IMPLEMENTED IN THE FUTURE - indicate timeframe below

REQUIRES FURTHER ANALYSIS - explain scope and timeframe below (not to exceed six months)

WILL NOT BE IMPLEMENTED - explain below

**Response summary, timeframe or explanation:**

The Soquel Creek Water District has a history of proactively managing, to the extent possible, its retirement costs and obligations. Actions taken to date include:

**Retirement**

- 2005: Negotiated a contract change to discontinue certain benefits to newly hired employees
- 2011: Paid off, eight years ahead of schedule, the CalPERS side fund which was accruing interest at 7.75%
- 2013: Negotiated a contract change to discontinue the Employer Payment of Member Contributions (EPMC)
- 2015: Adopted the Fiscal Year 2015-16 Budget which includes funding to pay off the unfunded liability for the Second Tier plan and to make a payment in excess of what is owed on the First Tier plan with the intention of paying down the unfunded liability in ten years instead of thirty years in order to achieve significant long term savings
Other Post Retirement Benefits (OPEB)
- 2011: Enrolled in the CalPERS Employers Retiree Benefit Trust Fund (CERBT) and began pre-funding retiree health benefits
- 2013: Negotiated a contract change whereby certain eligible retirees pay 10% of the health premium until they are eligible for Medicare. The District pays 100% of the Supplemental Medicare Premium
- 2013: Negotiated a contract change lengthening the number of years of District service AND the age requirement necessary to earn full retirement health benefits

District staff will continue to monitor retirement costs and obligations on an ongoing basis and seek ways in which to achieve savings and minimize the impact on District finances.

Recommendation 2: Each of the six public agencies studied in this report should provide, in language understandable to the public, the totality of retirement obligations in their annual budget narratives beginning with the fiscal year 2015/16 budget.

HAS BEEN IMPLEMENTED

HAS NOT BEEN IMPLEMENTED BUT WILL BE IMPLEMENTED IN THE FUTURE - indicate timeframe below

REQUIRES FURTHER ANALYSIS - explain scope and timeframe below (not to exceed six months)

WILL NOT BE IMPLEMENTED - explain below

Response summary, timeframe or explanation:

The District will include expanded language regarding retirement obligations in the annual budget narratives beginning with the Fiscal Year 2016-17 Budget. Additionally, the April 21, 2015 financial report on pensions (referenced above in Finding 2) will be posted as a supplementary budget document to the District’s website in the Transparency Center under Finance and Budgets. Staff will add information regarding the funded status of the plans to the report and make the document available on the website no later than July 30, 2015. The report will be updated annually.

As noted in the Grand Jury report, the District pre-funds Other Post-Employment Benefits (OPEB) through the California Employers’ Retiree Benefit Trust Program (CERBT). All plan participants are required to perform an actuarial valuation every two years. The District’s last actuarial report is as of June 30, 2013 and Staff has arranged for actuarial work to begin this summer. Once the study is complete; sometime in October, the results will be presented to the Board at a regularly scheduled public meeting. Staff will utilize the information in the 2015 actuarial report to develop a comprehensive OPEB report similar to the one on pensions that will also be updated annually and posted to the District’s website as a supplementary Budget document.
POSSIBLE BOARD ACTIONS

1. By MOTION, accept the draft response to the Santa Cruz County Civil Grand Jury Report on Retirement Costs and Obligations in Santa Cruz County and direct Staff to forward the completed response; OR

2. By MOTION, revise the draft response to the Santa Cruz County Civil Grand Jury Report on Retirement Costs and Obligations in Santa Cruz County and direct Staff to make changes as directed and forward the completed response.

By __________________________
Michelle Boisen
Financial and Business Services Manager