CITIZENS FOR

SUSTAINABLE PENSION PLANS

A Non-Partisan Group of Marin Residents

Pension Roulette

A Comparative Analysis of the Pension and Retiree Benefits of Marin County and its Municipalities

Presented By
Citizens for Sustainable Pension Plans
September, 2013

Email: contact@marincountypensions.com
Website: marincountypensions.com

Notice

This report is published by Citizens for Sustainable Pension Plans (CSPP), a nonpartisan, volunteer group of concerned taxpayers who are residents of Marin County, California. The information in this report is not copyrighted and may be released, reproduced and quoted provided appropriate attribution is given to CSPP. The views expressed in the report are based on information in the public domain. CSPP has relied on such published data in good faith but takes no responsibility if the released data was incorrect as originally published. CSPP has provided an advance copy of this report to the relevant governmental units. It is our hope that this report furthers the current debate involving the sustainability of public sector pensions.

For information about CSPP:
contact@marincountypension.com
www.marincountypensions.com

Table of Contents

Executive Summary

Trillions of dollars in unfunded public employee pension and health care benefits are playing a leading role in a growing number of municipal bankruptcies and service insolvencies in towns and cities throughout the United States.

The cover story of Time Magazine's August 5, 2013 issue that reported on Detroit's fight for survival asks, "Is Your City Next?"

While every municipality in America should be acting responsibly by objectively looking at the short and long term implications of unfunded retiree benefits, few have done so and fewer have taken meaningful steps toward reform.

This report provides the first-of-its kind rating and assessment of the financial impacts of billions of dollars in unfunded retiree debt owed by the County of Marin and its towns and cities. It also compares retiree benefit data from a 2004-05 Marin Civil Grand Jury Report to current benefits to determine what, if anything, has been done over the last eight years to address this problem.

The report also provides an important additional perspective by comparing Marin's public employee retirement plans with an "average" private sector plan as well as a local and sustainable public plan in the city of Danville, California.

Report highlights:

- The health of a pension plan is usually measured by its funding ratio and the conventional wisdom is that a ratio of 80% or better is considered a healthy status. However, a comprehensive view of Retiree Debt (pension and retiree medical liabilities) shows that Marin County and its cities and towns fail to reach the 80% funding minimum using an optimistic 7.5% return on pension investments. (Page 29)

- In the most recent 12 year period CalPERS' cumulative average investment return has been only 4.8%. Assuming this more conservative 4.8% return on pension investments, the funding ratios for Marin County and its towns and cities collapse to 50% or worse. At this funding ratio, a government risks a financial "death spiral" if downturns in financial markets, actuarial forecasting errors, and/or investment risks further increase debt levels beyond the point of serviceability. At this point, a government entity is bankrupt. (Page 30)

- The total retiree debt for the County of Marin and its towns and cities is a staggering $1.2 billion, if 7.5% is used for pension investment returns and $2.3 billion if 4.8% is used. The average household's share of the debt for just the county plus his or her city or town is approximately $13,500 using a 7.5% pension investment return and $25,000 if 4.8% is used. These figures do not include unfunded retiree debt for other entities providing services including

sewer, water, mosquito abatement and more that are not studied in this report. (Pages 31-32)

- When Retiree Spending increases, government services are "crowded-out" of the municipality's budget which causes "Service Insolvency": cutbacks in services or increases in rates, fees and taxes. Chart 7 (below) shows Retiree Spending as a percentage of Governmental Activities Spending, compares to other benchmark towns and also shows which Marin local governments are seeking a tax increase. (Pages 36-37)

- Despite a clear warning about the implications of overly generous retiree benefit plans in a report by the 2005-06 Marin County Civil Grand Jury, over the last eight years there have been no "meaningful" pension reforms. In a few cases new lower cost pension tiers have been introduced, but these changes affect new employees only. Their positive impact will only be felt many years down the road, once a significant percentage of the total employees are members of the new tier. In other cases, pension changes are actually increasing pension costs. (Pages 16-17)

- A comparison of public and private sector pension plans demonstrates that public sector pensions are far more costly than "average" private sector pensions. Pension benefits offered by Marin County and its towns and cities are at least twice as valuable as an "average" private plan. Corte Madera, Fairfax, San Anselmo and San Rafael have benefits that are at least three times as valuable. (Pages 12-15)

- Pension debt can quickly grow to a dangerous size. In 2005, Sausalito's pension debt was $5,264,055. By June 30, 2011, Sausalito's total pension debt had exploded to <u>at least</u> $17,567,677. In 2003, the County of Marin issued Pension Obligation Bonds worth $112 Million to refinance all of its pension debt. As of June 30, 2012 the County still owed $110M on the bonds and had incurred an additional unfunded pension liability of $371M. In only nine years the County's total pension debt had increased by more than four times to $481 million. Both examples assume an optimistic 7.5% rate of return on pension investments. Using a more conservative assumed rate of return the calculated pension debt is much greater. (Page 23)

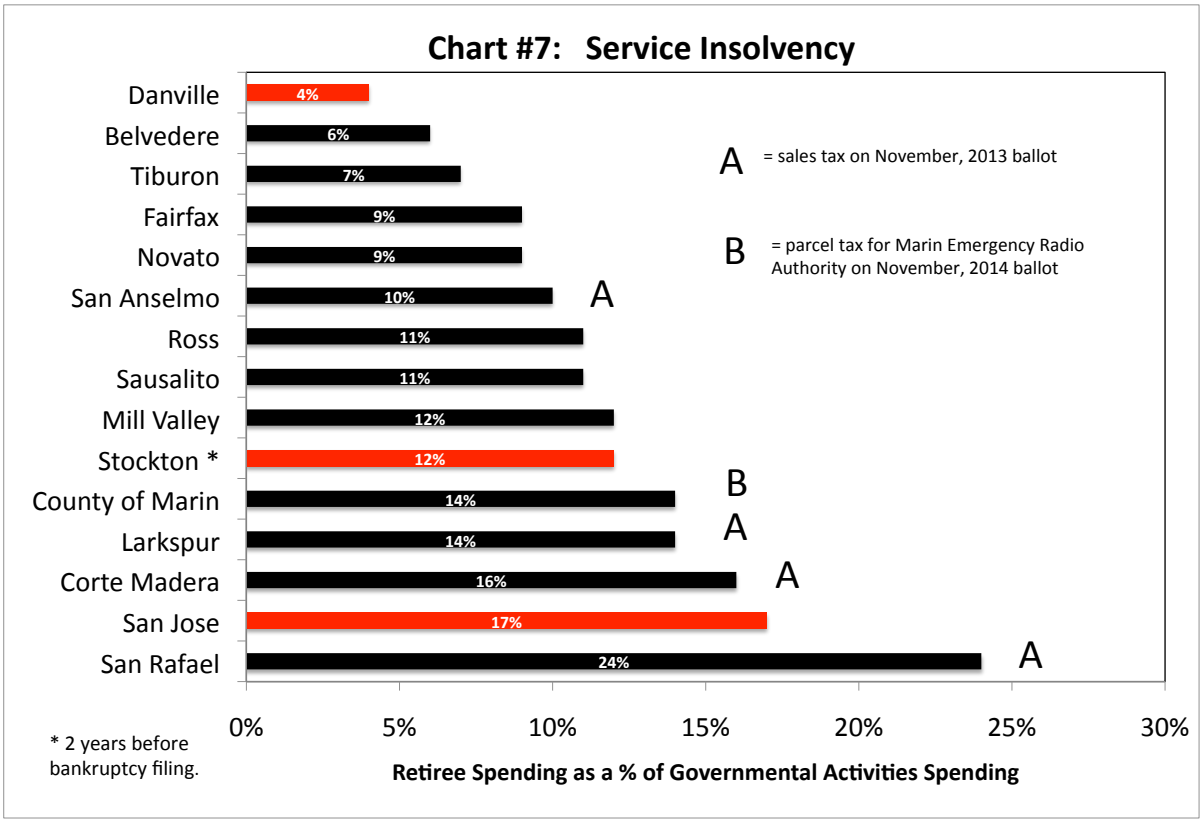


Chart #7: Service Insolvency
Danville
Belvedere
Tiburon
Fairfax
Novato
San Anselmo
Ross
Sausalito
Mill Valley
Stockton *
County of Marin
Larkspur
Corte Madera
San Jose
San Rafael
4%
6%
7%
9%
9%
10%
11%
11%
12%
12%
14%
14%
16%
17%
24%
A
= sales tax on November, 2013 ballot
B
= parcel tax for Marin Emergency Radio Authority on November, 2014 ballot
A
B
A
A
A
0%
5%
10%
15%
20%
25%
30%
* 2 years before bankruptcy filing.
Retiree Spending as a % of Governmental Activities Spending

Introduction

The amount and implications of between $1.2 billion and $2.3 billion in unfunded public employee retirement benefits for the County of Marin and its towns and cities is a serious problem that needs to be clearly understood by residents, politicians and public employees.

While Marin is not in the same position as Detroit, Vallejo, Stockton, San Bernardino and other cities and counties that are facing bankruptcy, the data in this report demonstrate that we are moving steadily down the same road that has led to their financial and service insolvencies.

The lack of understanding of the true gravity of an emerging tsunami of pension debt and a lack of resolve by political leaders to take meaningful action to address the problem has provided the impetus for this report.

Citizens for Sustainable Pension Plans, a nonpartisan group of Marin residents, was formed just in 2011 to bring attention to this serious problem and work with all stakeholders to develop solutions. The core group of CSPP includes two CPAs, an actuary, a pension plan expert, labor attorney, former Marin County Supervisor, several investment consultants and other financial professionals who together provide extensive knowledge and deep experience in addressing this problem. It is very likely that CSPP has more pension and financial experience than any government entity in Marin County.

Background

Marin's massive and unsustainable retiree benefit problem is not new, but today the emerging financial crisis is gaining more and more attention.

The 2004-2005 Marin County Civil Grand Jury published a report on the cost of retirement benefits for the County and its eleven cities and towns (Municipalities).[1] The report focused on retirement costs, with major emphasis on pensions and retiree healthcare. This GJ Report developed a framework for comparing the costs of public pensions to similar private sector pensions and concluded that the pensions provided by the Marin County and its Municipalities are "many times more generous than similar plans found in the private sector." The Report noted that these generous pensions were causing "financial stress" to the County and its Municipalities.

In 2012 Marin County Supervisor and Board President Steve Kinsey proposed that the County staff conduct an independent analysis of pension programs throughout

[1] "The Bloated Retirement Plans of Marin County, Its Cities and Towns". 2004-2005 Marin County Civil Grand Jury. May 9, 2005. Hereafter referred to as the GJ Report. The Grand Jury relied on actuarial reports of pension status as of June 30, 2003.

Marin to assess the risks to local government finances. He later reversed himself and declared this was no longer necessary, but gave no reason for this decision.

On June 3, 2013, the Marin Civil Grand Jury released a report called: "Marin's Retirement Health Care Benefits: The Money Isn't There". The Grand Jury's investigation into unfunded retiree health care benefits revealed that the 40 government entities (the County, cities and towns, special districts and school districts) that it surveyed have a collective liability of about $577 Million but have set aside only about $55 Million to fund these benefits.

Marin's enormous retiree debt has been widely reported by local media and important questions are being asked. Marin Independent Journal columnist Dick Spotswood wrote in early 2013:

> "Despite conflicting claims, progress is difficult without knowing which local governments are engaged in meaningful public employee pension reforms and which are full of hot air … Marinites need to find out which have made progress, the actual savings achieved, the remaining unfunded liability of each jurisdiction's public employee pension fund and the cost of their unfunded commitment for employee lifetime health care. Those who have accomplished little need to be spotlighted before November's municipal elections." [2]

This report follows a successful transparency effort by CSPP in July of 2013 to have financial data reflecting Marin County's unfunded liabilities for retiree benefits included with 2014 property tax bills.

---

[2] Dick Spotswood. "One Man's Way to Improve Civic Culture." Marin Independent Journal. December 30. 2012.

Report Objectives, Framework and Data Sources

This report has three overarching objectives and is divided into three parts:

PART ONE:

The report's first objective is to clearly establish the value and cost of pension benefits for Marin County and its towns and cities. In meeting this objective, the report provides an explanation of how pensions are calculated. We also include a comparison of the cost of public sector pension plans with that of an "average" private sector pension plan.

PART TWO:

The second objective is to compare current pension costs with pension cost data from the 2004-05 Marin County Civil Grand Jury Report in order to determine if significant changes (reforms) have occurred over the last eight years. In addition, the report gives two examples of the astonishing growth of pension debt which can occur in the absence of reform.

PART THREE:

The third objective is to measure and compare the financial stress on our local governments caused by retiree benefits. We then compare our local Marin County governments to the Town of Danville. Danville is one of a few cities in California with sustainable retiree benefit plans. [3]

Report Framework and Data Sources

To measure the costs of public pensions, this report uses the same analytical framework as the 2004-05 Grand Jury Report Report. This allows for direct comparability between pension costs in 2003 and 2011. The data is taken from official and reliable public sources. Specifically, we used the annual actuarial reports from the Marin County Employee's Retirement Association (MCERA) and the California Public Employees' Retirement System (CalPERS) for the fiscal year ending June 30, 2011.[4]

---

[3] We will not analyze retiree health benefits because that has recently been done. See: "Marin's Retirement Health Care Benefits: The Money Isn't There." 2012-2013 Marin County Civil Grand Jury. June 3, 2013.

[4] The employee pension plans of Marin County, the City of San Rafael and the Novato Fire Protection District are managed by MCERA. The plans of all other Marin cities and towns are managed by CalPERS. The June 30, 2011 actuarial reports are the latest available from CalPERS. We use the June 30, 2011 MCERA actuarial report for the sake of comparability.

To define and measure the financial stress caused by retiree benefits we developed objective and sound financial stress indicators, and then collected the following official and public information from the County and Municipalities:

1. The value of unfunded pension liabilities
2. The outstanding value of any “Side Funds” [debts] owed to CalPERS
3. The outstanding amount owed on any pension obligation bonds [POB)
4. The value of unfunded retiree health liabilities

PART ONE

Understanding the Value and Cost of Pension Benefits

Part One of our report provides an in-depth explanation of how pensions are valued and calculated. This information is critical to understanding the true cost of employee benefits as well as the immediate and long-term impacts of pension reforms.

How The Value of Pensions Are Measured – Benefit Richness

The central idea in the 2004-2005 Civil Grand Jury report was that pension benefits were unnecessarily generous and were causing "extreme stress" on local government finances. In this report we use the term "Benefit Richness" to describe the value of pension benefits.

To measure Benefit Richness the Grand Jury Report described four parameters, which together define public and private sector defined benefit pension plans. These four parameters are:

1. Benefit Factor – A percentage figure that is multiplied by the years of employee service.
2. Retirement Age – The age when an employee retires at full benefits.
3. Final Salary Years - The number of years of salary that are averaged to determine a final salary figure to use in a pension calculation.
4. Cost Of Living Adjustment (COLA) - The annual percentage increase in a pension.

Calculating Public Sector Defined Benefit Pensions

To use the standard formula for calculating an annual pension using these four parameters, the Benefit Factor is multiplied by the employee's years of service, and then this figure is multiplied by the final average salary. This annual pension is paid at the plan's retirement age and then the pension receives a COLA each year.

For example, a public employee who retires at 60 years old with full benefits after 30 years of service, a three-year average salary of $100,000, a Benefit Factor of 2% and a COLA of up to 2% will receive the following pension:

1). 2% x 30 = 60%
2). 60% x $100,000 = $60,000 Annual Pension
3). $60,000 x 2% = $1,200 Cost of Living Adjustment (paid 12 months after retirement, and then up to a 2% adjustment follow each additional year.)

Note: This employee would not receive any Social Security income.

Calculating Private Sector Defined Benefit Pensions

The Grand Jury consulted with pension actuaries and developed a model of an "average" or "typical" private sector defined benefit pension plan. Employees enrolled in these plans are usually also enrolled in Social Security. In terms of the four pension parameters above this "average" private sector plan is defined as:

1. Benefit Factor = 2.1% (including Social Security)
2. Retirement Age = 63
3. Final Salary Years = 5 (Average of last five years of salary)
4. Cost of Living Adjustment (COLA) = 0%

Under this "average" private sector plan an employee aged 63 retiring with full benefits after 30 years of service can retire with a pension income (including Social Security) equal to 2.1% x 30 = 63% of his last 5 years average pay but with no annual pension increase (except for the Social Security portion). An example follows in the next section.

Comparison of Public and Private Defined Benefit Plans

Public sector Defined Benefit pensions are more valuable than the "average" private sector Defined Benefit pension for four reasons: 1). The Benefit Factor is usually comparable or higher, 2). The retirement age is usually lower, 3). The number of years over which final salary is averaged is usually fewer, 4). A COLA is usually provided to the public sector.

It is self-evident that a larger Benefit Factor is more valuable than a smaller one. A pension with a 3% Benefit Factor is 42% more valuable than a pension with a 2.1% Benefit Factor (3% / 2.1% = 142%).

A pension with a younger retirement age at full benefits is more valuable than one with an older retirement age at full benefits because the retiree will have more years in which to collect pension income. In the public sector, retirement at full benefits is often possible at age 50 (safety employees) or 55 (miscellaneous employees.) In our "average" private sector plan, retirement at full benefits is possible only at age 63. The public worker, therefore, will receive more pension income than his private sector counterpart. The GJ Report argued that on a Net Present Value [NPV] basis, the lifetime value of a pension increases by about 7% for every additional year of retirement income.[5] So, a pension beginning at age 55 is 72% more valuable than an equal pension beginning eight years later at age 63.[6]

---

[5] Net Present Value is a standard financial tool for calculating the value in the present of a series of future cash flows, which have a known potential for earning investment income.

[6] 1.07^8 = 1.72.

A pension is also more valuable when the final average salary is calculated over fewer years (Final Salary Years). It is important to note that in almost all of the actuarial reports reviewed for this study the assumed average increase in salary was 3% per year.

Table 1 considers three workers: one private sector and two public sector workers. They all earn $66,637 in 2006, receive a 3% annual increase in their salaries, and are all earning $75,000 when they all retire in 2010 at full benefits. Based on our "average" private sector plan: The private sector worker's pension income is calculated on the average of his last five years of income. One of the two public sector worker's pensions is calculated on the average of the last three years, and the other public sector worker's pension is calculated on just the last year's income. Here are the results:

Table 1: Comparison Final Salary Years

<table>
<tr><th>Year</th><th>Salary For All Three Workers (+3% annual increases)</th><th>Final Average Salary Based on 5 Years (private sector worker)</th><th>Final Average Salary based on 3 Years (public sector worker 1)</th><th>Final Average Salary Based on 1 Year (public sector worker 2)</th></tr>
<tr><td>2006</td><td>$66,637</td><td rowspan="5">$70,756</td><td></td><td></td></tr>
<tr><td>2007</td><td>$68,636</td><td></td><td></td></tr>
<tr><td>2008</td><td>$70,695</td><td rowspan="3">$72,837</td><td></td></tr>
<tr><td>2009</td><td>$72,816</td><td></td></tr>
<tr><td>2010</td><td>$75,000</td><td>$75,000</td></tr>
</table>

Since pension income is a function of the calculated Final Average Salary, and Final Average Salary is greater with a shorter averaging period, it is obvious that the public sector worker's pension benefits will be greater than that of their private sector counterpart. A pension based on the average of the last three years of salary is about 3% more valuable and a pension based on the last year is about 6% more valuable than a pension based on the last five years.

A public sector pension with a COLA is more valuable than a private sector pension without a COLA due to the powerful effect of compounding interest. Even with a modest 1% COLA (i.e. 1% annual pension income increases) the public sector pension of a worker who retires at age 55 will increase by 35% over 30 years of projected retirement income. With a +2% COLA, the increase is 81% and for a +3% COLA the pension payment will have increase by +143%. See Table 2 on the following page.

Table 2: Impact of Cost of Living Adjustment on Pension

Annual Pension Income				
COLA	**COLA = 0%**	**COLA = 1%**	**COLA = 2%**	**COLA = 3%**
Pension at 55 years	$30,000	$30,000	$30,000	$30,000
Pension at 85 years	$30,000	$40,435	$54,341	$72,818
Pension Increase	+0%	+35%	+81%	+143%

Generally, the lifetime value of the typical public sector pension (retiring at age 55 with expected remaining life of 30 years) increases by about +9% for every percentage point of COLA attached to that pension.

It is critical to note when comparing public and private pensions that the combined effects of these pension parameters (Benefit Factor, Retirement Age, Final Salary Years, and COLA) are multiplicative and not additive. As noted above, comparing a public sector and an "average" private sector pension, a Benefit Factor of 3% for a public employee is 42% more valuable than one of 2.1% for a private employee, and retirement at age 55 is 72% more valuable as retirement at age 63. Astonishingly, a public pension which features both a 3% Benefit Factor and retirement at age 55 is 144% more valuable than the "average" private pension.[7] It is the multiplicative nature of the combined effects of these pension parameters which causes public sector pensions to be between two and three times as valuable as our "average" private sector pension as shown in Chart 1.

A Conservative Analysis

The analytical framework that we used to compare public sector pensions to an "average" private sector pension is conservative and arguably understates the relative "richness" of public sector pensions. There are three reasons for this.

First, most private sector employees do not receive pension benefits as generous as the "average" private sector pension used here. The GJ Report noted that in 2005 that only 40-50% of private sector employers (usually large employers) offered such plans; most offered less costly and less generous Cash Balance or Defined Contribution pension plans. Nevertheless, the GJ decided to use this "average" plan as a benchmark because they thought large private sector employers were the most comparable to local government employers.

Today, eight years after the GJ Report, even fewer private sector employers offer such plans. A recent research note from the Bureau of Labor Statistics reports that in the private sector the percentage of employers offering Defined Benefit pensions is 48% of very large employers (> 500 employees), 25% of large employers (100 – 499 employees) and only 10% of all employers. Viewed from the perspective of

[7] 142% x 172% = 244%

employees, 35% of private sector employees had Defined Benefit pensions in 1990, 20% in 2005 and only 18% in 2011.[8] In addition to the decrease in numbers of private sector employees covered by defined benefit pensions, many of the employees still covered have seen their benefit levels cut back due to reduction in level of benefits earned and/or complete curtailment of future benefit accruals.

Second, the value of a younger retirement age at full benefits is understated. As noted above, the GJ Report assumed that every year of earlier retirement at full benefits increases the lifetime value of that pension by about 7%. In retesting that assumption, we found that the factor is closer to 8%. Additionally, some actuaries believe that this factor should be increased to account for the value of dependent benefits that are typically found in public sector plans. For the sake of consistency, this report uses the same 7% factor used in the GJ Report.

Third, it is assumed that none of Marin's towns or cities offer Social Security coverage (benefits) to any of their employees. In fact, some Municipalities do offer this benefit to some of their employees and this increases both the "richness" and the cost of these pension packages.[9]

Chart 1 shows that pension benefits offered by Marin County and its towns and cities are at least twice as valuable as an "average" private plan. Corte Madera, Fairfax, San Anselmo and San Rafael have benefits that are more than three times as valuable.

[8] "The Last Private Industry Pension Plans." William Wiatrowsky. Monthly Labor Review (BLS). December, 2012.

[9] For example some employees of Fairfax, Larkspur, Ross and San Anselmo do receive Social Security coverage.

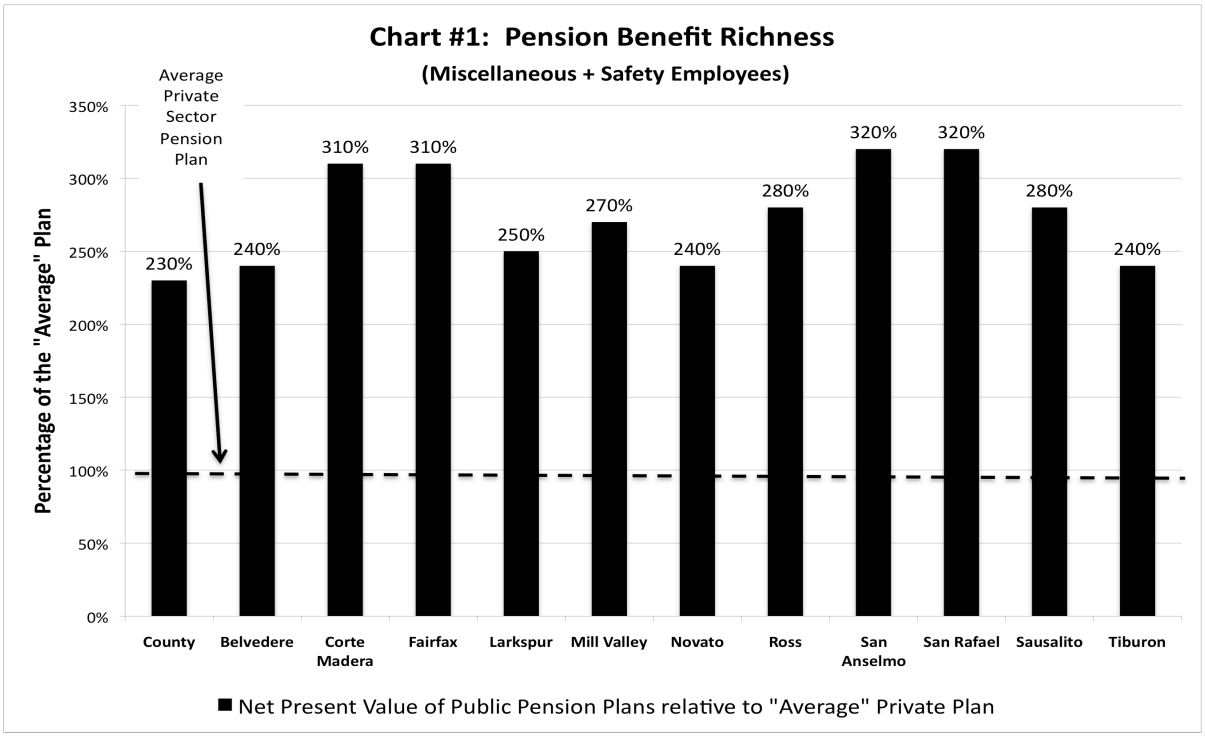


Chart #1: Pension Benefit Richness
(Miscellaneous + Safety Employees)
Average Private Sector Pension Plan
Percentage of the "Average" Plan
350%
300%
250%
200%
150%
100%
50%
0%
230%
240%
310%
310%
250%
270%
240%
280%
320%
320%
280%
240%
County
Belvedere
Corte Madera
Fairfax
Larkspur
Mill Valley
Novato
Ross
San Anselmo
San Rafael
Sausalito
Tiburon
Net Present Value of Public Pension Plans relative to "Average" Private Plan

PART TWO

Measuring Reform:
Comparing Current Pension Benefits to 2003 Benefits

In this part of the report we describe the pension plans of the County and 11 Municipalities using the analytical framework described in Part One. We review the summary pension plans descriptions from the Grand Jury Report (based on 2003 data), update these descriptions using 2011 data, and then compare the two. The objective is to discover how much change ("reform") has occurred during the study period.

The GJ Report included summary tables describing the pension parameters of Marin County and its Municipalities for both Miscellaneous workers (all except Safety) and Safety workers (Police and Fire). On the following pages we have reproduced these tables and provided new tables containing updated data, along with an analysis of changes.[10]

[10] The updated data come from the actuarial reports for June 30, 2011 from CalPERS and MCERA.

Table 3: **Miscellaneous Employee Plans (2003 data from the Grand Jury Report)**

Public Entity	Benefit Factor	Retirement Age	Final Salary Years	COLA
County	2.0%	55	3	2%
Belvedere	2.0%	55	1	2%
Corte Madera	2.0%	55	1	2%
Fairfax	2.5%	55	3	2%
Larkspur	2.0%	55	1	2%
Mill Valley	2.5%	55	1	2%
Novato	2.0%	55	1	2%
Ross	2.0%	55	3	2%
San Anselmo	2.7%	55	1	2%
San Rafael	2.7%	55	1	3%
Sausalito	2.5%	55	1	2%
Tiburon	2.0%	55	1	2%

Table 4: **Miscellaneous Employee Plans (2011 data from actuarial reports)**

Public Entity	Benefit Factor	Retirement Age	Final Salary Years	COLA
County	2.0%	55	3	2%
Belvedere	2.0%	55	1	2%
Corte Madera	**2.5% ***	55	1	2%
Fairfax	2.5%	55	3	2%
Larkspur	**2.5% ***	55	1	2%
Mill Valley	2.5%	55	1	2%
Novato	2.0%	55	1	2%
Ross	2.0%	55	3	2%
San Anselmo	**2.6% ***	55	1	2%
San Rafael	2.7%	55	1	3%
Sausalito	2.5%	55	1	2%
Tiburon	2.0%	55	1	2%

* Indicates value changed from 2003 to 2011.

Miscellaneous Employee Plan Analysis

A comparison of the two tables for Miscellaneous employees shows little change in pension parameters between 2003 and 2011; only three (3) values have changed:

For Corte Madera and Larkspur, the Benefit Factor increased from 2.0% to 2.5%. These increases were effective in July of 2005 (for Corte Madera) and in August of 2009 (for Larkspur), i.e. after the GJ Report.[11]

For San Anselmo the effective Benefit Factor decreased slightly from 2.7% to 2.6%. In February of 2007, following the release of the GJ Report, San Anselmo introduced a new tier of reduced pension benefits. This new Tier 2 reduced the Benefit Factor from 2.7% to 2.0% but applied only to new Miscellaneous employees. As of June 30, 2011 there were 129 employees assigned to the old pension tier and only 21 assigned to the new Tier 2. The weighted average puts the effective Benefit Factor at 2.6%. San Anselmo's experience illustrates how reforms that apply only prospectively to new employees are weak and will reduce costs very slowly.

Changes in pension parameters in Fairfax and Mill Valley are also examples of reforms with little impact in the near future. While both towns have recently introduced a second pension Tier that reduced Benefit Factors from 2.5% to 2.0%. But as of June 30, 2011 more than 97% of employees in both cities are in the first pension tier. These reforms left the effective Benefit Factor practically unchanged.

On the following page is the same comparison of the two tables for Safety employees.

[11] "Marin County Local Government Reform of Pensions and Other Post-Employment Benefits." Marin County Council of Mayors and Councilmembers. June 22, 2011, pages 31 and 34.

Table 5: Safety Employee Plans (2003 data from the Grand Jury Report)

Public Entity	Benefit Factor	Retirement Age	Final Salary Years	COLA
County	3.0%	50	3	2%
Belvedere	2.0%	50	3	2%
Corte Madera	3.0%	50	1	2%
Fairfax	3.0%	50	3	2%
Larkspur	3.0%	55	1	2%
Mill Valley	3.0%	55	3	2%
Novato	3.0%	55	1	2%
Ross	2.0%	50	1	2%
San Anselmo	3.0%	50	1	2%
San Rafael (Police/Fire)	3.0% / 2.0%	55 / 50	1 / 1	3% / 3%
Sausalito (Police/Fire)	3.0% / 3.0%	55 / 55	1 / 1	2% / 2%
Tiburon	3.0%	55	3	2%

Table 6: Safety Employee Plans (2011 data from actuarial reports)

Public Entity	Benefit Factor	Retirement Age	Final Salary Years	COLA
County	3.0%	**51 ***	**2.8 ***	**2.2% ***
Belvedere	2.0%	50	3	2%
Corte Madera	3.0%	**52 ***	1	2%
Fairfax	3.0%	50	3	2%
Larkspur	3.0%	55	1	2%
Mill Valley	3.0%	55	3	2%
Novato	3.0%	55	1	2%
Ross	**3.0% ***	**55 ***	1	2%
San Anselmo	3.0%	**51 ***	1	2%
San Rafael (Police/Fire)	3.0% / **3.0% ***	55 / **55 ***	1 / 1	3% / 3%
Sausalito (Police/Fire)	3.0% / 3.0%	55 / 55	1 / 1	2% / 2%
Tiburon	3.0%	55	3	2%

*Indicates value changed from 2003 to 2011.

1) The towns of Corte Madera and Larkspur in 2009 combined their police departments into the Twin Cities Police Authority. To retain comparability with the GJ Report the TCPA is allocated back to the Towns (based on household count) and their pension plan attributes combined (weighted by plan membership.)
2) The Sausalito Fire Department was annexed to the Southern Marin Fire Protection District on July 1, 2012 and after the date of CalPERS latest actuarial reports. So the status shown here is pre-annexation.

Safety Employee Plan Analysis

A comparison of the two tables for Safety employees also shows few changes between the 2003 and 2011 snapshots. The most interesting entity is Marin County where the following three offsetting changes net only a small reduction in the expected lifetime value of a safety pension for a Marin County safety worker:
1) A slight increase in Retirement Age (cost decrease)
2) An increase in the COLA (cost increase)
3) A small decrease in the Final Salary Years (cost increase).

Most of the County's Safety employees are assigned to pension Tier 2 or Tier 2B. The latter is a new tier implemented in 2005 (following the GJ Report), which reduced Retirement Age from 55 to 50 years (a cost increase). However, since the summary pension parameters reported here are averages weighted by the number of plan participants, the summary result is small off-setting changes. When evaluated on a Net Present Value basis, the net effect of these changes is a small reduction in plan cost.

The Town of *Corte Madera* shows an increase in Retirement Age from 50 to 52 years (a cost reduction). This is a consequence of the higher retirement age (55 years) for the Twin Cities Police Authority (TCPA) compared to Corte Madera's safety workers (50 years.) The police departments of Larkspur and Corte Madera were merged into the TCPA in 2009, after the GJ Report. To retain comparability with the GJ Report, the TCPA is allocated back to the towns (based on household count) and its pension plan attributes combined (weighted by plan membership). The Retirement Age increase associated with the creation of TCPA caused Corte Madera's weighted average Retirement Age for safety workers to increase. This reduces the expected lifetime value of the safety pension by about 13%.

The *Town of Ross* implemented a new pension formula for Safety workers effective June, 2003 (immediately after the data snapshot used by the GJ Report). Under this new formula, the Retirement Age increased to 55 years (a cost reduction) but the Benefit Factor increased to 3% (a cost increase). The net effect of these offsetting changes is a small increase in the expected lifetime cost of these pensions.

San Anselmo shows a small increase in Retirement Age from 50 to 51 years (a cost reduction). This is a consequence of a new Tier 2 pension formula implemented in 2007, which increased the Retirement Age from 50 to 55 years. However, 90% of the safety workers are assigned to Tier 1 (as of June 30, 2011). So the weighted Retirement Age increased by only one year with little impact on pension cost. This is another example of cost reductions lagging pension reform.

San Rafael shows offsetting changes for Fire Safety workers due to a new pension formula introduced in 2006 (following the GJ Report). The Benefit Factor increased from 2% to 3% (a cost increase) that was offset by an increase in Retirement Age from 50 to 55 years (cost decrease). The net effect of these changes increased the expected lifetime cost of the Fire Safety pensions.

In summary, we have updated the pension analysis of the 2004-2005 Civil Grand Jury and compared snapshots of summary pension data taken from 2003 and 2011. In a few cases new lower cost pension tiers have been introduced but these changes affect only new employees. The new tiers will meaningfully constrain costs only after a delay of years when a significant percentage of employees are members of the new tiers. In other cases, we have seen pension changes that increase pension costs. The pension plans of the County and the Municipalities remain two to three times more generous and costly as our "average" private sector plan.

Analysis

Dick Spotswood asked**:** "Which local governments are engaged in meaningful public employee pension reforms?" If "meaningful" means 'can take effect soon enough to avoid serious financial damage to the local government,' the answer is: *none of them.*

Pension reform needs to have effect soon because the existing pension debt is large and additional debt can be created in only a few years. Meaningful pension reform needs to have effect within 10 years. A reform plan with deferred pension benefits reductions and a 30 year time horizon is simply too risky. Changes expected to take place over 30 years can easily be repealed through collective bargaining before they have a chance to take effect. Even if not repealed, by the time reforms begin to constrain costs the accumulated pension debt could be crushing.[12] The following examples illustrate this point.

The Rapid Growth of Pension Debt

Effective July 1, 2005 the pension plans of Sausalito were terminated and employees of those plans were required by CalPERS to join new State-wide pension pools. The City was required at that time to pay off its unfunded pension liabilities either by paying cash or borrowing an equal amount from CalPERS. Sausalito chose the latter option and agreed to repay this "Side Fund" debt over 17 to 21 years. ~~A~~s of July 1, 2005 Sausalito's pension debt was $5,264,055.[13] By June 30, 2011 90% of the original Side Fund debt to CalPERS remained and new debt (unfunded liabilities)

[12] Existing reform plans all assume that the target investment Rate of Return of 7.5% per year will be achieved on average. This is a plausible but optimistic assumption. Even a miss of only 1 percentage point on the expected ROR can cause these plans to fail. This is especially true of mature plans with many retirees (like the County) because most of the plan income is expected to come from investments. The County's contribution rate (% of payroll) for pensions only was 26.5% in 2011 and expected to decrease to a more normal 12% by 2040 (with unfunded liabilities extinguished) but only with a 7.5% ROR. There is a large element of faith and hope in these reform plans. See: MCERA "Actuarial Review and Analysis as of June 30, 2011", page 11.

[13] Sausalito Annual Financial Report for FY 2005-2006, page 48.

had been created. Sausalito's total pension debt had exploded and was now at least $17,567,677.[14] In only 6 years the debt had more than tripled.

In 2003 the County of Marin issued Pension Obligation Bonds worth $112M to pay off its approximately $110M unfunded pension liability with MCERA. This made sense because MCERA was charging the County an annual interest rate of 8.25% on this debt and the County was able to borrow money at an average of 5.25%. In effect, the County was refinancing its debt and reducing the interest rate by 3 percentage points.[15] However, as of June 30, 2012 the County still owed $110M on the bonds and had incurred an additional unfunded pension liability of $371M.[16] So, in only nine years the County's total pension debt had more than quadrupled to $481 million.[17]

[14] This estimate is almost certainly too low. It assumes an "actuarial value of assets" [i.e. asset values averaged over several years] and a future Rate of Return (ROR) on investments of 7.5% per annum. A more plausible but still optimistic estimate uses the real market value of assets; by that measure Sausalito's pension debt was $23.7M. Using a plausible but conservative estimate based on a 4.8% ROR the debt could be as great as $47.9M. Sausalito could not service a debt of that size. See the CalPERS actuarial reports for Sausalito for June 30, 2011.
[15] Official Statement (prospectus) for "County of Marin, California Taxable Pension Obligation Bonds." May 6, 2003. See especially page F-3.
[16] Calculated using an actuarial value of assets and a target Rate of Return of 7.5% per annum.
[17] To be fair and to give credit, note in 2012 that Sausalito paid off about $2M of pension Side Fund debt and the County paid off $32M of pension unfunded liability (with expectations to make additional future payments.)

Part Three

Measuring, Rating and Comparing Financial Stress

In this part of the report we define five indicators of financial stress caused by pensions and other retiree benefits. We will use these five indicators to compare the County and the Municipalities to each other and also to the town of Danville. Danville is used as a benchmark because it has similar demographics to towns in Marin County and has a sustainable public employee pension plan.

The community of Danville, located in Contra Costa County, was founded in 1854 during the California Gold Rush but was not incorporated until 1982. Danville's population is 43,000: larger than most Marin towns but smaller than Novato (53,000) and San Rafael (58,000). Danville's median household income ($133,000) is about the same as Tiburon's ($136,000). It is a wealthy and medium-sized town that would not look out of place in Marin County.

Danville's retiree benefit programs are modest compared to those offered by Marin County and its Municipalities. Danville's pension benefit is a *defined contribution* plan through which the Town contributes for each employee 10% of pay and a 100% matching of employee contributions up to 5% of pay. Most employees make at least a 5% contribution, so the Town's effective pension contribution is about 15% of payroll. Danville's employees (like most of those in Marin County and its Municipalities) are not enrolled in Social Security.

Danville has a retiree medical benefit (OPEB), but pays almost nothing toward it. The Town used to be enrolled in a CalPERS retiree health plan but later dropped-out. There are a few retirees who still receive this benefit but only until they reach the age of Medicare eligibility. Consequently, today Danville is paying on average only $16 per month per retiree for medical benefits; practically zero.

Because Danville has no defined benefit pension and a very inexpensive OPEB plan, it has no pension or OPEB debt. A further consequence is that no portion of its current year spending is dedicated to servicing pension or OPEB debt.

Danville contracts out for its police and fire services. The Town contracts with the Contra Costs County Sheriff's Department for police services and with the San Ramon Valley Fire Protection District for fire services. The police and fire personnel serving Danville have pensions through their employers but Danville does not directly contribute to their pension or OPEB benefits.

Danville has no difficulty in recruiting and retaining good miscellaneous employees.[18] This is attributed to attractive salaries, benefits that are perceived to be good, a good work environment, and an excellent and experienced Town Manager. The miscellaneous employees of Danville have chosen not to unionize. Most of Danville's employees come from the private sector where it is unlikely that they have experience with defined benefit pensions.

Danville is a successful Bay Area town that does not offer a defined benefit pension or other significant post employment benefits (OPEB) to its employees. This shows that there is for our local governments a retirement benefit plan that can attract and retain good employees without causing financial stress.

Five Indicators of Financial Stress

We are now ready to explain the five indicators of financial stress that we will apply to Marin County, the Municipalities and to Danville. The table on the following page can be referenced as we present six comparison charts that measure the negative impact of these indicators on financial health.

[18] Per conversations by authors of this report with Denise Phoenix (Danville HR Manager) and with Candace Andersen (former Danville Mayor and now a Contra Costa County Supervisor).

Table 7: Indicators of Financial Stress		
Indicator	**Components**	**Explanation**
1) Earned Retiree Benefits Funding Ratio (% of benefits)	Pension benefits earned, Other Post Employment Benefits [OPEB] earned, POBs, Side Fund Debt, dedicated pension & OPEB assets.	This is the present value [PV] of pension & OPEB benefits earned to date by employees + POBs and Side Fund Debt, divided into dedicated assets. OPEB benefits are mostly retiree medical care. Following CalPERS we calculate the PV of future pension benefits 2 ways: with 7.5% & 4.82% assumed Rates of Return (or discount rates).
2) Retiree Debt ($ amount)	Unfunded Pension Liability	The difference between the PV of earned pension benefits and the Market Value of assets (savings) dedicated to paying those benefits. PV calculated with 7.5% & 4.82% discount rates.
	Pension Obligation Bonds (POBs)	Bonds issued to refinance unfunded pension liabilities at reduced interest rates.
	Pension Side Fund Debt	A pension debt owed to CalPERS for unfunded pension benefits.
	OPEB Unfunded Liability	The difference between the PV of earned OPEB benefits and the value of assets dedicated to paying those benefits. The County and Municipalities have not funded these benefits as earned, thereby creating a large debt.
3) Employer Contribution for Current Year Service (% of payroll)	Employer Normal Pension Cost	This is the Employer's annual pension contribution for the present value of pension benefit earned in the current year by Employees. It is expressed as a % of payroll.
4) Employer Contribution for Past Service (% of payroll)	Annual costs for Unfunded Pension Liabilities, POBs, Side Fund debt, and OPEB.	This is the sum of the Employer's annual costs to service Retiree Debt + OPEB pay-as-you-go cash payments. It is expressed as a % of payroll.
5) Retiree Spending ($ amount)	Sum of 3) + 4)	The Employer's total spending on Retiree benefits including contributions for both current and past Employee service. Expressed here as an absolute $ amount.

Indicator 1: Earned Retiree Benefits

We focus first on Earned Retiree Benefits. This is the Present Value [PV] of pension and OPEB benefits earned by employees to date.[19] The value of Earned Retiree Benefits can only be understood in relation to the value of assets (savings) dedicated to paying those benefits. If a government owes $1,000,000 of earned benefits and has $1,000,000 in dedicated assets to pay those benefits, then the Funding Ratio is 100% and there is no problem or financial stress. On the other hand, if a government owes $1,000,000 in benefits but has $500,000 in dedicated assets, then the funding ratio is only 50% and there is a major problem and significant financial stress.

To compare the value of dedicated assets to the future payments of retiree benefits, we must first calculate the value in the present [PV] of those future payments. The relative PV of those future benefit payments will depend on the investment Rate of Return [discount rate] on the pension fund's assets. Today, many if not most public pension plans assume a rate of return on investments of 7.5% to help fund future pension payments. If pension investment returns fall short of this assumed rate, then pension debt increases.

The discount rate that is used by municipalities and their pension funds for calculating the PV of earned benefits is a critical, necessary and now a very controversial assumption. Both CalPERS and MCERA assume a 7.5% discount rate. CalPERS reports that for the 23 years from 1990 to 2012 (years ending December 31) its cumulative average annual investment earnings rate was 8%.[20] This includes the boom years of 1990 – 2000 when returns were 11.5% and the bust years of 2001 – 2012 when the returns were only 4.8%. Whether the future pension investment Rate of Return [ROR] achieves the assumed rate of 7.5% (close to CalPERS' long term average) or achieves only 4.8% (the recent 12 year average) will have critical consequences for our County and Municipalities. At the lower rate, pension investments will earn far less income than planned and that deficit must be covered with more debt and greater contributions from our local governments. In this lower pension ROR scenario government pension contributions would have to increase by 40% to 70% above today's already elevated level. Since they are already struggling to pay pension contributions our local governments cannot tolerate another big increase. And the design of these public pension plans ensures that there is no limit to the amount of pension debt that can be incurred. Our local governments are playing "pension roulette" and cannot afford to lose.

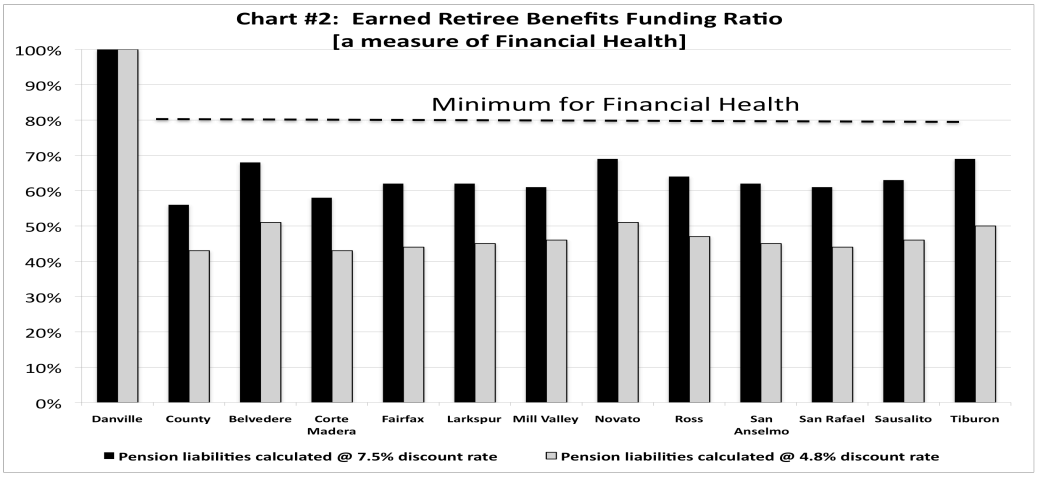
In its actuarial reports for June 30, 2011 CalPERS, which manages the pension funds of most municipalities in Marin, reported pension liabilities based on both a 7.5% and

[19] Present Value is a standard financial tool for calculating the value in the present of a series of future cash flows which have a known potential for earning investment income. It is very similar to the NPV calculation described in footnote 5.
[20] CalPERS "Facts at a Glance." March, 2013.

a 4.8% discount rate assumptions.[21] The County and San Rafael pensions are managed by the Marin County Employee Retirement Association (MCERA) and MCERA reports its pension liabilities using only a 7.5% discount rate assumption. In this report we have estimated the County and San Rafael pension liabilities assuming a 4.8% discount rate assumption.[22]

Chart #2 shows the "Earned Retiree Benefits Funding Ratio" (assets / liabilities) for Danville, Marin County and the Municipalities. Earned pension benefits are calculated two ways: with a 7.5% discount rate assumption (plausible but optimistic in today's economy) and a 4.8% discount rate assumption (plausible but conservative).

The health of a pension plans is usually measured by its funding ratio and the conventional wisdom is that a ratio of 80% or better is a healthy status. However, the conventional pension funding ratio ignores the additional and real costs of Pension Obligation Bonds (POBs), Side Fund debt owed to CalPERS and Other Post Retirement Benefit (OPEB) liabilities, which can be as large or larger than pension liabilities. Our report considers all pension and other liabilities pertaining to retiree benefits for a comprehensive and more accurate indicator of financial health.



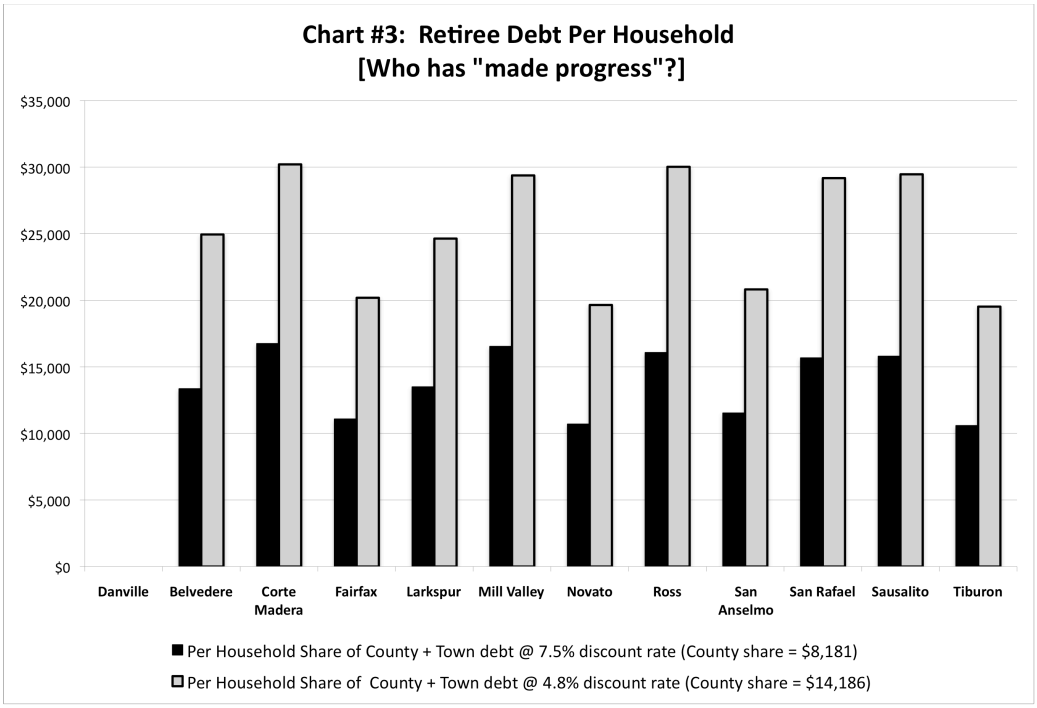
[21] CalPERS calls the latter a "Hypothetical Termination Liability" [HTL]. The HTL is a recalculation of the PV of earned pension benefits using a 4.82% discount rate and adding a 7% contingency factor for "unforeseen improvements in mortality" (retirees living longer and collecting more pension.) The HTL is the price at which any client government can terminate its pension plan and leave with CalPERS the responsibility for paying the earned pensions of its employees. The implied message here is that a 7.5% discount rate is extremely risky and far beyond CalPERS own risk tolerance.

[22] For the Municipalities that are CalPERS clients the ratio of pension liabilities calculated with a 4.8% compared to 7.5% discount rate is about 1.4. We have used this 1.4 factor in adjusting the numbers for the County and San Rafael.

The results are alarming. First, Danville scores a 100% funding ratio, which is the inevitable consequence of a well designed and sustainable defined contribution pension plan and practically no OPEB. Second, not one of the Marin's entities reaches the 80% funding threshold; only two (Novato and Tiburon) reach 70%. Third, when valuing pension liabilities with the more conservative 4.8% discount rate, the funding ratios for all Marin entities collapse to 50% or worse. At this funding ratio, a government risks a financial "death spiral" if downturns in financial markets, poor investment returns or actuarial errors further increase debt levels beyond the point of serviceability. At this point, a government is bankrupt.

Indicator 2: Retiree Debt

Next we focus on Retiree Debt, which is comprehensively defined to include all kinds of debt associated with retiree benefits: unfunded pension liabilities, Pension Obligation Bonds (POBs), Side Fund debt and unfunded OPEB. Chart #3 shows Retiree Debt per Household and compares the County and Municipalities to each other and to Danville. This chart addresses the question of which municipalities have "made progress" in controlling retiree debt.



For our study, we have reported the combined liabilities of the county and the towns. But every household in Marin is responsible not only for their town's retirement liabilities and the County's debt, but also for the other debts of the public entities that provide services (water, sewer, mosquito abatement, etc.). The average debt per Marin household (County and Towns) is about $13,500 using a 7.5% discount rate.

The results are surprising in that among the best and the worst performers in Marin are the wealthiest communities. Tiburon (a town which has aimed to control retiree debt) has the smallest retiree debt and Ross has almost the largest. Ross has both a

large unfunded pension liability and a large Side Fund debt to CalPERS. As shown, the town of Danville has zero Retiree Debt, which is a consequence of having a defined contribution pension plan and practically no OPEB liabilities.

Chart #3 reports the same combined Debt burden per household (the grey bar) for the County and Towns when pension liabilities are recalculated at a 4.8% discount rate (plausible but conservative.) With this assumption, the average debt increases to $25,000 per household. The table below provides the actual debt per town based on both a 7.5% return on pension investments and a more conservative 4.8% return.

Table 8: Retiree Debt Per Household

If you live in ------>		Belevedere	Corte Madera	Fairfax	Larkspur	Mill Valley	Novato	Ross	San Anselmo	San Rafael	Sausalito	Tiburon
And if pension liabilities are discounted @ 7.5% then …	Town Retiree Debt	$ 5,168	$ 8,560	$ 2,896	$ 5,309	$ 8,348	$ 2,513	$ 7,887	$ 3,346	$ 7,486	$ 7,610	$ 2,401
	County Retiree Debt	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181	$ 8,181
	Total Retiree Debt per household	$ 13,349	$ 16,741	$ 11,077	$ 13,490	$ 16,529	$ 10,694	$ 16,068	$ 11,527	$ 15,667	$ 15,791	$ 10,582
Or if pension liabilities are discounted @ 4.8% then …	Town Retiree Debt	$ 10,756	$ 16,020	$ 6,002	$ 10,447	$ 15,190	$ 5,459	$ 15,837	$ 6,630	$ 14,988	$ 15,274	$ 5,337
	County Retiree Debt	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186	$ 14,186
	Total Retiree Debt per household	$ 24,942	$ 30,206	$ 20,188	$ 24,633	$ 29,376	$ 19,645	$ 30,023	$ 20,816	$ 29,174	$ 29,460	$ 19,523

Chart #4 on the following page is another view of Retiree Debt but this time viewed as a percentage of a municipality's Total Debt. This is a measure of social inequity.[23]

Governmental debt is not necessarily a bad thing and debt is sometimes the best way to finance a public investment. Governments provide services and the idea of social equity suggests that those who benefit from services should pay for them. So, while fire protection services should be paid from current taxes because today's residents receive the benefits of these services, when a town invests in a new fire station, then it is fair to finance this investment with debt that is repaid by the current and future residents as both groups will benefit over the next 30 years of the fire station's useful life. In both cases there is a matching of beneficiaries and taxpayers.

Retiree Debt is a financial obligation for past services. It is the cost of obligations for services rendered in the past that should have been paid for in the past but were not. To require current and future residents to pay for public services provided in the past

[23] Total Debt is defined as Retiree Debt plus Non-Retiree Debt. The latter equals Total Liabilities (for governmental activities from the Statement of Net Assets) less any retiree debt reported on that Statement (i.e. pension obligation bonds and part of OPEB unfunded liability.)

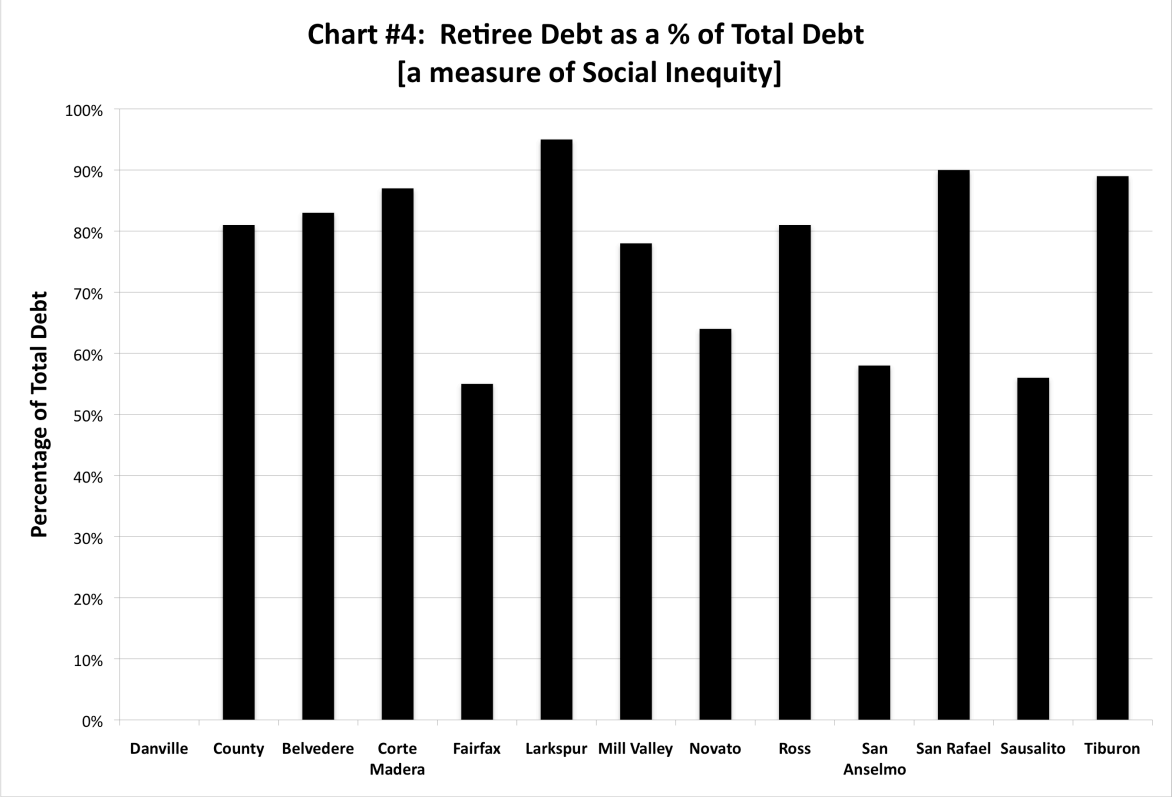
is not only unfair, it clearly demonstrates that a benefit plan is broken and needs to be repaired or replaced.

“Retiree Debt as a percentage of Total Debt” measures how much of a community’s existing debt—being serviced by current residents—is comprised of debt for past services rendered to past residents. This debt is a measure of social inequity.

The results indicated on Chart #4 are again alarming and cause for serious concern. For Marin County and all Marin towns, more than 50% of total debt is comprised of Retiree Debt. For Danville the ratio is 0% because this town has no Retiree Debt.

There are two aspects to this indicator: constraint and fairness. A high ratio of Retiree Debt to Total Debt will be constraining for some towns with high levels of overall debt. These towns already owe so much money they can’t borrow any more. Other towns with low overall debt levels will not be constrained from borrowing more but it will still be unfair to current residents if they are required to pay for debt incurred for past employee services.

Compare similarly sized Sausalito (population 7,000) and Tiburon (population 9,000). On the indicator of “Retiree Debt as a percentage of Total Debt,” Tiburon is more unfair (88%) than Sausalito (54%) but Sausalito’s liabilities for governmental activities ($26 million) are much greater than Tiburon’s ($2 million). Sausalito is more constrained by high levels of Retiree Debt. Tiburon is not so constrained but is still unfair.



Indicator 3: Employer Contributions for Current and Past Service

The next indicator we review is the amount of Employer Contributions for Current Year Service compared to the Employer Contribution for Past Service. The former measures the employer's (local government's) annual pension contribution for the value of pension benefits earned in the current year by employees, expressed as a percentage of payroll.[24] It is a measure of efficiency: other factors being equal (e.g. employee recruitment and retention) the smaller an employer's contribution for pension benefits the more efficient is that employer.

Chart #5 reports Employer Contribution for Current Year Service for Marin County, the Municipalities and Danville. The obvious and interesting result is there is so little variation between all entities. The values range from 10% to17% of payroll and there is no significant difference between the town of Danville and the Marin towns. The town with the largest payroll contribution is San Rafael at 17% but Danville is very close with 15%. Danville has a defined contribution pension plan and all of the other entities offer a defined benefit pension plan, yet there is little difference in their contribution rates for Current Year Service. The point here is that if the defined benefit pensions performed as planned then they would not be any more costly than a defined contribution plan. Unfortunately, the defined benefit pensions have not performed as planned. These defined benefit plans promise rich benefits predicated on optimistic investment returns and accurate actuarial assumptions. When those assumptions are too optimistic or when pension investments fail to meet target returns, employers must increase contributions to fund their pension plans.

Chart #6 "Employer Contribution for Current Year plus Past Service" is an update of Chart #5. It reports the same employer contribution for Current Year Service and then adds the contribution for Past Service. In Chart #6 there are significant differences between Danville and the Marin entities. Danville's total contribution remains unchanged at 15% of payroll; it has no Retiree Debt and no OPEB expenses so its contribution for Past Service is zero. For Marin County and towns the employer contribution for Current Year plus Past Service ranges from 17% to 64%.

Tiburon and Belvedere score well on this indicator with total employer contributions of 17% and 19% (respectively). San Rafael stands out with a contribution rate for Current Year plus Past Service of an astonishing 64% of payroll. This is obviously both inefficient and unfair. It is inefficient when a town pays a much higher portion of payroll for benefits than nearby towns competing in the same labor market. And it is unfair when a large part of the public payroll paid by current residents is dedicated to paying for services received by past residents.

[24] In actuarial terms, this is the pension "Normal Cost."

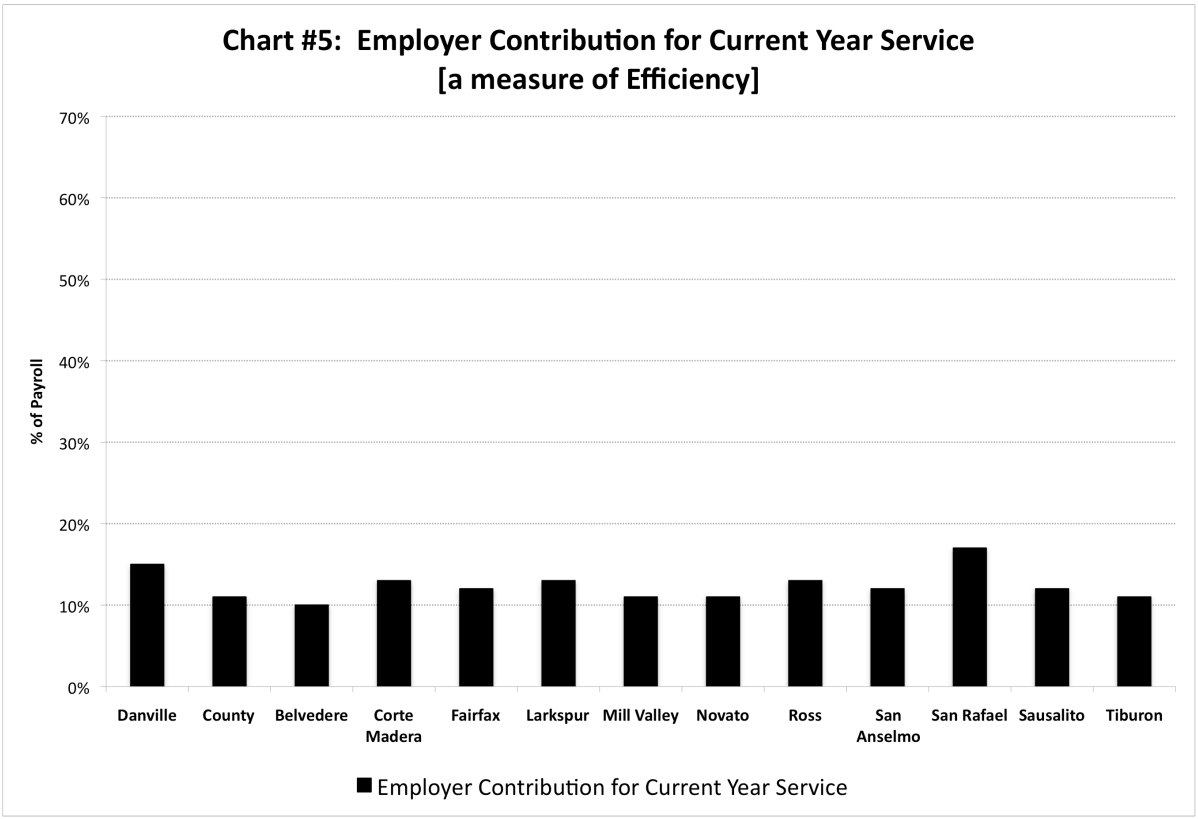


Chart #5: Employer Contribution for Current Year Service
[a measure of Efficiency]
70%
60%
50%
40%
30%
20%
10%
0%
% of Payroll
Danville
County
Belvedere
Corte Madera
Fairfax
Larkspur
Mill Valley
Novato
Ross
San Anselmo
San Rafael
Sausalito
Tiburon
Employer Contribution for Current Year Service

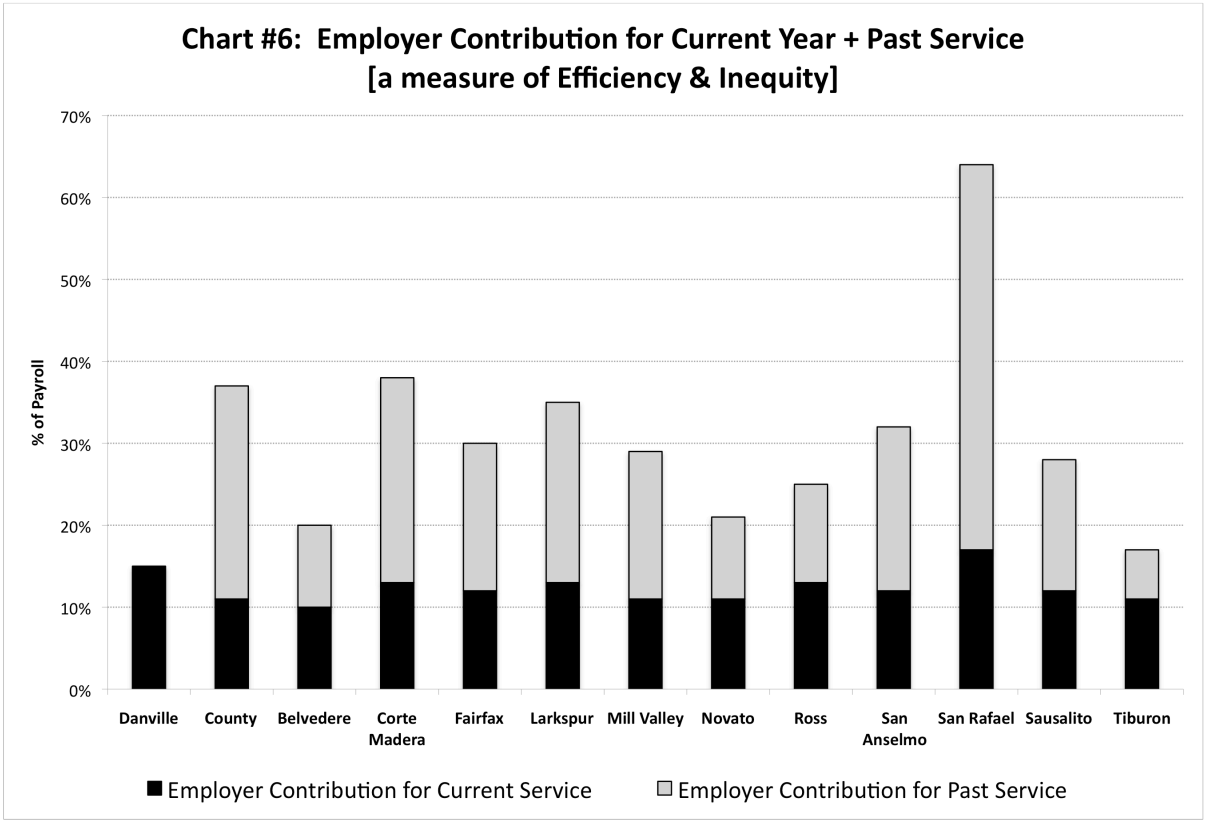


Chart #6: Employer Contribution for Current Year + Past Service
[a measure of Efficiency & Inequity]
70%
60%
50%
40%
30%
20%
10%
0%
% of Payroll
Danville
County
Belvedere
Corte Madera
Fairfax
Larkspur
Mill Valley
Novato
Ross
San Anselmo
San Rafael
Sausalito
Tiburon
Employer Contribution for Current Service
Employer Contribution for Past Service

Indicator 5: Retiree Spending as a Percentage of Governmental Activities Spending

Pensions and retiree benefits are complex subjects that are difficult to understand. In this report we relied on public information to define and measure the subject from different perspectives. We've looked at funding ratios, debt per household, debt as a portion of total debt and retiree spending as a percent of payroll. But too little funding or too much debt or too large a portion of payroll are finally just indicators and predictors of the big problem: too much of our government revenues are spent on retiree benefits leaving too little to be spent on everything else. "Service Insolvency" is the condition of a government that does not have sufficient money available to provide the basic services for which that government was created. A high level of retiree spending is a predictor of Service Insolvency. So the big question for residents of Marin is "What level of retiree spending causes Service Insolvency?"

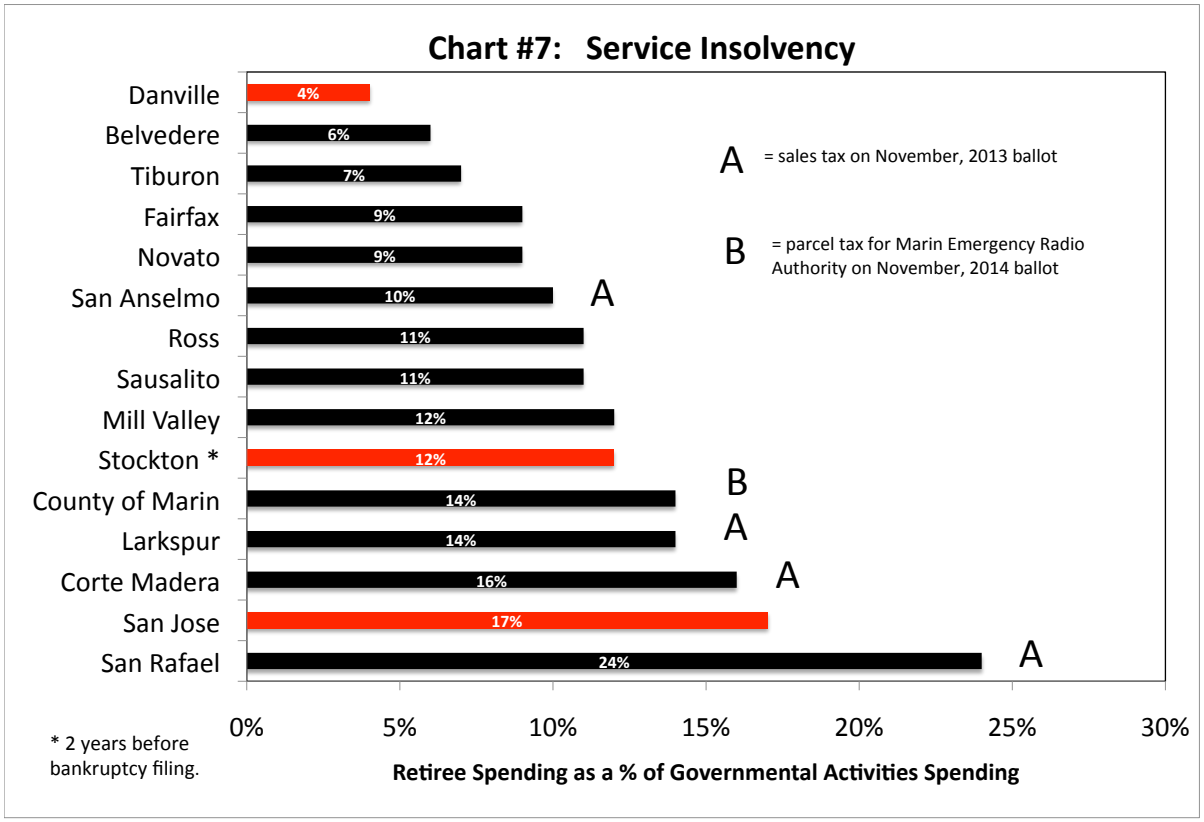
Chart #7 is our summary answer to that question. This chart ranks Danville, the County and the Municipalities based on the percentage of governmental activities spending that is dedicated to retiree benefits. The difference between best and worst is astonishing. Our benchmark Town of Danville dedicates just 4% of governmental spending to retiree benefits while San Rafael spends 24%. Only Belvedere and Tiburon come close to Danville. The remaining 10 local governments spend at least two times as much on retiree benefits.

In addition to Danville, Chart #7 includes two additional benchmark towns: Stockton and San Jose. The average retiree spending rate for Marin County and towns is 12%. The City of Stockton had a 12% retiree spending rate two years prior to its bankruptcy filing (in June 2012). So, a 12% retiree spending rate may not be comfortable or sustainable if a town faces unexpected financial challenges. The City of San Jose is famously at the forefront of pension reform. Last year 70% of its voters approved a referendum for pension reform intended to stop the rapid growth of retiree spending which was crowding-out basic government services. But this new pension reform law is tied-up in litigation and not yet implemented. San Jose's retiree spending increased to 17% in the fiscal year ending June 30, 2012. San Jose's retiree spending rate—which they find a crushing burden—is only slightly larger than Marin County and Larkspur (14%) and Corte Madera (16%). San Rafael leads them all with retiree spending equal to 24% of governmental spending.

Chart #7 also shows which entities are asking their residents to approve a tax increase. Four of the five local governments which will be asking their citizens to support increased taxes have Retiree Spending ratios close to or exceeding 15%.

The proposed tax increases are justified as necessary to fund police and fire services, road maintenance, and to replace a 15-year-old emergency radio system for the County. Additional revenues may be needed, but money for these most basic and important government services should already be available. If there is

insufficient money for basic services then other functions have been given a higher priority than basic services. Chart #7 makes it clear that in some communities retiree spending has a higher priority.



Concluding Statement and Call to Action

CSPP has long asserted that the reforms being undertaken in both our County and towns are neither meaningful nor sufficient. This report validates our opinion.

The Town of Danville, in Contra Costa County, has shown that it is possible to attract and retain qualified employees and to provide a high level of local government services without incurring the excessive expense, debt and risk of traditional public sector pension plans.

What is the next step? In Marin County, this is virtually the billion dollar question. To answer it, each and every resident needs to thoughtfully consider the following questions:

- Are our elected officials the “right people” at this time to deal with the crises and work to resolve them with meaningful pension reform?

- Do the challengers who wish to be elected in upcoming races have the courage and ability to work for change?

- Are we willing to push this debt onto the shoulders of our children and grandchildren in order to pay for services we receive today at the possible expense of future services for their generation?

- Do our elected officials today deserve our support when they ask for increases in taxes on November’s ballot, or is it time to send them a strong message that more taxes will not be forthcoming unless and until meaningful reform is adopted?

- Are we willing, as residents and taxpayers, to take the time from our busy lives to fully understand this pension crisis and hold people accountable for making the difficult changes necessary to preserve our way of life for future generations?

CSPP has given much time and consideration to possible solutions to this problem. Before addressing solutions, however, we felt that it was necessary to fully outline the problems facing our County and each of your hometowns. We have put months into this study, making sure our assertions are correct and verifiable.

It is our hope that both residents and our elected officials will acknowledge and accept the gravity of the situation, will agree on the same set of facts as outlined in this study, and will work together to implement solutions. It can be done – but it will require fortitude and willing participants.

Appendix: Financial Data Table

		Danville	Marin County	Belvedere	Corte Madera	Fairfax	Larkspur	Mill Valley
INPUTS	Present Value of Pension Benefits Earned (@ 7.5% discount rate)	$ -	$ 1,436,008,295	$ 13,703,450	$ 64,423,222	$ 21,559,367	$ 69,128,187	$ 97,657,538
	Present Value of Pension Benefits Earned (@ 4.8% discount rate)	$ -	$ 2,053,491,862	$ 18,889,005	$ 93,787,136	$ 31,691,262	$ 99,544,740	$ 139,866,610
	Pension Obligation Bonds (balance owed)	$ -	$ 110,185,000	$ -	$ -	$ -	$ -	$ 5,845,000
	Side Fund Debt (owed to CalPERS)	$ -	$ -	$ 989,692	$ 4,462,587	$ 2,095,133	$ 5,303,912	$ -
	Present Value of OPEB benefits earned	$ -	$ 382,720,000	$ 374,116	$ 11,829,000	$ 958,500	$ 7,493,551	$ 28,099,682
	Market Value of Assets (for pensions)	$ -	$ 1,087,619,409	$ 10,271,037	$ 46,984,258	$ 15,167,540	$ 50,497,393	$ 76,487,668
	Market Value of Assets (for OPEB)	$ -	$ -	$ -	$ 39,000	$ -	$ -	$ 3,617,703
	Non-Retiree Debt (Note 1)	$ 15,161,791	$ 199,963,448	$ 992,906	$ 4,870,035	$ 7,729,192	$ 1,683,528	$ 14,279,636
	Retiree Debt (pension @ 7.5% discount rate) (Note 2)	$ -	$ 841,293,886	$ 4,796,221	$ 33,691,550	$ 9,445,460	$ 31,428,258	$ 51,496,849
	Retiree Debt (pension @ 4.8% discount rate) (Note 2)	$ -	$ 1,458,777,453	$ 9,981,776	$ 63,055,464	$ 19,577,355	$ 61,844,811	$ 93,705,921
	Total Debt (pension @ 7.5% discount rate) (Note 3)	$ 15,161,791	$ 1,041,257,334	$ 5,789,127	$ 38,561,585	$ 17,174,652	$ 33,111,786	$ 65,776,485
	Household Count	15,175	102,832	928	3,936	3,262	5,920	6,169
	POB Debt Service Cost (Note 4)	$ -	$ 7,136,499	$ -	$ -	$ -	$ -	$ 643,376
	OPEB Actual Employer Contribution Made	$ -	$ 11,812,000	$ 14,809	$ 328,000	$ 10,977	$ 286,410	$ 951,023
	Employer Contribution for Current Year Service (Note 5)	$ 1,115,150	$ 19,188,425	$ 214,669	$ 866,156	$ 300,844	$ 973,867	$ 1,437,469
	Employer Contribution for Past Service (Note 6)	$ -	$ 46,243,381	$ 221,017	$ 1,607,738	$ 442,814	$ 1,719,900	$ 2,290,071
	Retiree Spending (Note 7)	$ 1,115,150	$ 65,431,806	$ 435,686	$ 2,473,893	$ 743,658	$ 2,693,768	$ 3,727,540
	Payroll	$ 7,434,332	$ 175,396,940	$ 2,205,429	$ 6,544,097	$ 2,451,104	$ 7,713,187	$ 12,604,399
	Governmental Activities Spending (Note 8)	$ 30,231,028	$ 461,103,484	$ 7,082,918	$ 15,167,254	$ 8,184,833	$ 18,920,650	$ 32,411,591
CALCULATIONS	Earned Retiree Benefits Funding Ratio (pension @ 7.5% discount rate)	100%	56%	68%	58%	62%	62%	61%
	Earned Retiree Benefits Funding Ratio (pension @ 4.8% discount rate)	100%	43%	51%	43%	44%	45%	46%
	Retiree Debt Per Household (pension @ 7.5% discount rate)	$ -	$ 8,181	$ 5,168	$ 8,560	$ 2,896	$ 5,309	$ 8,348
	Retiree Debt Per Household (pension @ 4.8% discount rate)	$ -	$ 14,186	$ 10,756	$ 16,020	$ 6,002	$ 10,447	$ 15,190
	Retiree Debt as a % of Total Debt (pension @ 7.5% discount rate)	0%	81%	83%	87%	55%	95%	78%
	Employer Contribution for Current Year Service (% of payroll)	15%	11%	10%	13%	12%	13%	11%
	Employer Contribution for Past Service (% of payroll)	0%	26%	10%	25%	18%	22%	18%
	Retiree Spending as a % of Governmental Activities Spending	4%	14%	6%	16%	9%	14%	12%

Appendix: Financial Data Table

		Novato	Ross	San Anselmo	San Rafael	Sausalito	Tiburon	County + Municipalities
INPUTS	Present Value of Pension Benefits Earned (@ 7.5% discount rate)	$ 144,085,710	$ 15,814,761	$ 39,413,596	$ 412,743,009	$ 71,699,175	$ 24,027,960	$ 2,410,264,270
	Present Value of Pension Benefits Earned (@ 4.8% discount rate)	$ 204,168,716	$ 22,334,187	$ 56,217,000	$ 590,222,503	$ 102,538,712	$ 34,624,384	$ 3,447,376,117
	Pension Obligation Bonds (balance owed)	$ 19,074,305	$ -	$ 3,583,000	$ 4,490,000	$ -	$ -	$ 143,177,305
	Side Fund Debt (owed to CalPERS)	$ 349,628	$ 1,585,618	$ -	$ -	$ 4,798,424	$ 668,742	$ 20,253,736
	Present Value of OPEB benefits earned	$ 2,786,000	$ 530,000	$ 1,941,900	$ 35,156,000	$ 6,888,060	$ 2,900,736	$ 481,677,545
	Market Value of Assets (for pensions)	$ 115,040,960	$ 11,463,185	$ 27,818,605	$ 264,399,742	$ 52,761,651	$ 18,936,200	$ 1,777,447,648
	Market Value of Assets (for OPEB)	$ -	$ -	$ -	$ 10,861,000	$ -	$ -	$ 14,517,703
	Non-Retiree Debt (Note 1)	$ 29,394,734	$ 1,494,133	$ 12,206,943	$ 20,364,969	$ 24,475,910	$ 1,060,172	$ 318,515,606
	Retiree Debt (pension @ 7.5% discount rate) (Note 2)	$ 51,254,683	$ 6,467,194	$ 17,119,891	$ 177,128,267	$ 30,624,008	$ 8,661,238	$ 1,263,407,505
	Retiree Debt (pension @ 4.8% discount rate) (Note 2)	$ 111,337,689	$ 12,986,620	$ 33,923,295	$ 354,607,761	$ 61,463,545	$ 19,257,662	$ 2,300,519,352
	Total Debt (pension @ 7.5% discount rate) (Note 3)	$ 80,649,417	$ 7,961,327	$ 29,326,834	$ 197,493,236	$ 55,099,918	$ 9,721,410	$ 1,581,923,111
	Household Count	20,396	820	5,117	23,660	4,024	3,608	$ 180,672
	POB Debt Service Cost (Note 4)	$ 1,065,732	$ -	$ 143,320	$ 276,512	$ -	$ -	$ 9,265,439
	OPEB Actual Employer Contribution Made	$ 62,634	$ 10,000	$ 75,701	$ 2,648,000	$ 159,678	$ 20,972	$ 16,380,204
	Employer Contribution for Current Year Service (Note 5)	$ 2,019,511	$ 348,710	$ 585,600	$ 5,257,239	$ 874,213	$ 392,470	$ 32,459,173
	Employer Contribution for Past Service (Note 6)	$ 1,842,783	$ 306,165	$ 955,638	$ 14,830,213	$ 1,125,910	$ 232,818	$ 71,818,448
	Retiree Spending (Note 7)	$ 3,862,294	$ 654,875	$ 1,541,238	$ 20,087,452	$ 2,000,123	$ 625,288	$ 104,277,621
	Payroll	$ 18,267,133	$ 2,642,800	$ 4,750,039	$ 31,692,289	$ 7,239,780	$ 3,700,251	$ 275,207,448
	Governmental Activities Spending (Note 8)	$ 41,905,926	$ 5,703,551	$ 15,053,414	$ 84,304,486	$ 17,697,216	$ 8,520,072	$ 716,055,395
CALCULATIONS	Earned Retiree Benefits Funding Ratio (pension @ 7.5% discount rate)	69%	64%	62%	61%	63%	69%	59%
	Earned Retiree Benefits Funding Ratio (pension @ 4.8% discount rate)	51%	47%	45%	44%	46%	50%	44%
	Retiree Debt Per Household (pension @ 7.5% discount rate)	$ 2,513	$ 7,887	$ 3,346	$ 7,486	$ 7,610	$ 2,401	$ 6,993
	Retiree Debt Per Household (pension @ 4.8% discount rate)	$ 5,459	$ 15,837	$ 6,630	$ 14,988	$ 15,274	$ 5,337	$ 12,733
	Retiree Debt as a % of Total Debt (pension @ 7.5% discount rate)	64%	81%	58%	90%	56%	89%	80%
	Employer Contribution for Current Year Service (% of payroll)	11%	13%	12%	17%	12%	11%	12%
	Employer Contribution for Past Service (% of payroll)	10%	12%	20%	47%	16%	6%	26%
	Retiree Spending as a % of Governmental Activities Spending	9%	11%	10%	24%	11%	7%	15%

Appendix: Financial Data Table

Notes:

Note 1. Non-Retiree Debt = Total Liabilities - (Net OPEB Obligations + POB debt). From the Statement of Net Assets. Note that Net OPEB Obligations & POB Debt are the only components of Retiree Debt that are reported on the Statement of Net Assets. The other components are hidden in the Notes to the financial statements.

Note 2. Retiree Debt = OPEB Unfunded Accrued Liability + Pension Side Fund Debt + POB Debt + Pension Unfunded Accrued Liability. (Pension UAL calculated @ either 7.5% or 4.8% discount rate). Note that only part of the OPEB UAL is reported on the Statement of Net Assets where it is called Net OPEB Obligations.

Note 3. Total Debt = Non-Retiree Debt + Retiree Debt (@ 7.5% discount rate). This parameter could also be calculated with the Pension UAL calculated @ a 4.8% discount rate but for the sake of simplicity we have not done that here.

Note 4. POB Debt Service Cost = POB Interest Expense + Repayment of Principal (for one year).

Note 5. Employer Contribution for Current Year Service = Pension "Normal Cost." This is the annual contribution that an employer must make to a pension plan that would completely fund this plan if investment return and actuarial assumptions were perfectly accurate.

Note 6. Employer Contribution for Past Service = (Employer Contributions for amortizing unfunded pension liabilities & Side Fund debt) + (POB Debt Service Costs) + (OPEB Actual Employer Contribution).

Note 7. Retiree Spending = (Employer Contribution for Current Year Service) + (Employer Contribution for Past Service).

Note 8. From the Statement of Activites.