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June 29, 2015

Board of Supervisors
County of Marin
3501 Civic Center Drive, Suite 329
San Rafael, CA 94903

**Re: Comments to Agenda Item 7 for Meeting on June 30, 2015 (Response to
2014/2015 Marin County Civil Grand Jury)**

Dear Board of Supervisors:

On behalf of Citizens for Sustainable Pension Plans (“CSPP”), I hereby request that you delay your response to the 2014/2015 Marin County Civil Grand Jury report entitled “Pension Enhancements: A Case of Government Code Violations and A Lack of Transparency” dated April 9, 2015 (“Grand Jury Report” or “Report”) until July 7, 2015, or later provided you obtain required authorization, to allow both you and concerned citizens more time to thoughtfully consider and comment upon the current draft of your response to the Grand Jury Report. To proceed otherwise will only compound the prejudice already suffered by the public in Marin County as a result of the events described in the Report.

For purposes of this letter, “BOS” shall refer to Board of Supervisors of the County of Marin, “County” shall refer to the County of Marin, and “MN memo” shall refer to the memorandum from the Meyers Nave dated June 24, 2015 to Mr. Matthew Hymel and Ms. Angela Nicholson. This letter incorporates by reference each and every document referenced herein, as well as all BOS meeting materials directly or indirectly related to increased retirement benefits, all County and MCERA financial reports, including budget and valuation reports, for the period from January 1, 2000 to June 30, 2015.

Following are points we request you consider before finalizing your decision on this matter:

- I. The BOS did not comply with the requirements of Government Code Section 7507¹ when authorizing retirement benefit increases described in the Grand Jury Report.**

¹ Unless otherwise noted, all section references herein are to the Government Code. Sections 31515.5 and 31516 both require compliance with Section 7507; therefore violations to Section 7507 described herein also refer to violations to Sections 31515.5 and 31516.

Government Code section 7507 (“Section 7507”) was adopted by the Legislature and signed into law in 1977. The legislative intent of Section 7507 is to protect taxpayers by avoiding unfunded liabilities resulting from increases in retirement benefits. (Enrolled Bill Report, Dept. of Finance, on Sen. Bill No. 439, September 15, 1977.) In order to avoid unfunded liabilities, Section 7507 includes specific requirements that must be followed before a local legislative body may authorize increases in retirement benefits. (See Sen. Russell, Chairman of Sen. Comm. On Pub. Employment and Retirement, letter to Gov. Brown on Sen. Bill No. 439, September 12, 1977.) As the Grand Jury correctly pointed out, the BOS did not follow these requirements when directly and indirectly authorizing pension increases.²

A. The BOS did not secure the services of an enrolled actuary or receive required actuarial statements and reports before authorizing all retirement benefit and salary increases referenced in the Grand Jury Report.

Section 7507 requires that the local legislative body, which in this case is the BOS, “secure the services of an enrolled actuary” to provide the “actuarial impact upon the future annual costs before authorizing increases in public retirement plan benefits.” (Gov. Code. § 7507.)

The MN memo acknowledges that the BOS did not secure the services of an enrolled actuary before each of the increases in public retirement plan benefits between 1999 and 2005 – this is a violation of Section 7507. Requiring the BOS secure the services of an enrolled actuary, and not just any department within the County, such as the HR Department, avoids conflicts of interests, promotes good governance, and ensures that the BOS is informed of the future annual costs of increases in pension benefits before they are approved, which also enables the individual Supervisors to properly execute their duty to their constituents who have been prejudiced by these failures.

In addition, the BOS could not have received relevant future annual cost information if, for example, the actuarial report was prepared years prior to approval of the increase or was based on a different plan than that applicable to the proposed increase. To determine the future annual cost of a pension benefit increase, the actuary reviews several factors at a certain point in time, such as number and age of employees, payroll information, contribution amounts, funding status, etc. These factors certainly change over time, and would have likely changed significantly over a six-year period described in the Grand Jury Report. In addition, because bargaining units received different benefits, these factors would be different for each bargaining unit, which is why the BOS should have received a separate report for each proposed increase. The MN memo does not mention or otherwise address these issues. Without a current actuarial report for each

² Section 23026 contains requirements similar to Section 7507 when authorizing salary and benefit increases, e.g., the BOS must receive an estimate from an enrolled actuary of the actuarial impact of each proposed salary or benefit increase, notice to the public must disclose the financial impact that the proposed salary or benefit change will have on the funding status of the applicable retirement plan, etc. Accordingly, violations to Section 7507 described herein shall also include violations to Section 23026. Section 23026 is likely how the Grand Jury determined the BOS approved 23 separate retirement enhancements between 2001 and 2005.

increase, including salary increases, it would have been impossible for the BOS to have made an informed decision on the future annual cost of each benefit increase. The BOS's failure to receive the future annual costs of retirement benefit increases before approving them violated Section 7507.

B. There is no evidence that the future annual costs of the increased benefits, including annual dollar increases and total dollar increases, were ever disclosed to the BOS.

Section 7507 requires that the actuarial report given to the BOS include the future annual costs, including annual dollar increases and total dollar increases. The MN memo only refers to a few percentages that may have been in a report obtained or prepared by the HR Department, but the MN memo doesn't explain why other future annual costs, including (without limitation) future annual costs based on retroactivity, were not provided to the BOS. (See, e.g., *California Statewide Law Enforcement Ass'n v. California Dept. of Personnel Admin.* (2011) 192 Cal.App.4th 1.)

Also, there has been no reference to the dollar amounts of the benefit increases. Dollar amounts are one form of future annual costs and are important for obvious reasons – the BOS is making a financial decision. Percentages only provide the variation from the cost of current plan benefits. The dollar costs of an increase are generally determined by multiplying the percentages by the then-current payroll amounts. Think about buying a car – would you buy a car if the only information you had was that the cost this year was 2% more than last year? Certainly not. You would ask what the cost was last year, so that you could calculate the total dollar cost of the new car. In this case, without having been provided all future annual costs of each applicable benefit increase, including the future annual dollar and total dollar increases, the BOS certainly was not informed as required by Section 7507.

C. All parties are in agreement that the public did not receive the future annual costs of pension benefit increases as required by Section 7507.

Section 7507 requires that the public be informed of the future annual costs of pension benefit increases at least two weeks before the adoption of any such benefit. MN agrees with the Grand Jury Report that this did not happen. We agree, too. And, we all agree that this was a violation of Section 7507.³

³ The MN memo's reference to "substantial compliance" with statutes that require the BOS/County to make public the future annual costs of retirement benefit increases is an admission that Sections 7507, 23026, etc., were in fact violated. Information hidden in an HR report does not meet the requirements of law. The law is not intended for the public to guess what might be stowed away somewhere in the County, so that they can lodge a public records request and wait 10 days for the information. The applicable law in this case required the BOS/County take affirmative steps to make public at a public meeting the required annual financial costs of the pension increase. Furthermore, without transparent language in the applicable meeting agendas, the 23 pension enhancements were effectively concealed from public view. The MN memo concedes this point. (See MN memo, p. 6.)

II. The requirements of Section 7507 are mandatory. Any conclusion to the contrary ignores the legislative intent of Section 7507.

The MN memo reaches the stunning conclusion that “shall” in Section 7507 means something other than mandatory. Not only is this supposition counter to the express terms of Section 14 and Marin County Code section 1.04.150 that both state ‘shall’ is mandatory, this conclusion is not supported by cases cited by MN.⁴

The MN memo cites to several cases that indicate:

- (i) if the failure to comply with the procedural requirement invalidates the purpose of the statute, the statute is mandatory (MN memo, p.15, citing *City of Santa Monica v. Gonzales* (2008) 43 Cal.4th 905),
- (ii) “if the procedure is essential to promote the statutory design, it is ‘mandatory’ and noncompliance has an invalidating effect (*Ibid.*, *Cal-Air Conditioning, Inc. v. Auburn Union School District* (1993) 21 Cal.App.4th 655, 673)

In light of the legislative intent of Section 7507, these cases and principles unequivocally support the conclusion that Section 7507 is mandatory.⁵

- A. Section 7507 is mandatory because the failure to make the future annual costs of the various benefit increases available to the public at a public meeting at least two weeks prior to the approval of each increase invalidated the purpose of Section 7507, as evidenced by skyrocketing unfunded liabilities since 2001.**

Here, the BOS/County’s failure to comply with the procedural requirements of Section 7507 invalidated the purpose of the law. Section 7507 protects against unfunded liabilities by

⁴ Please note that cited on page 19 of the MN memo is a case, namely *Edwards v. Steele* (1979) 25 Cal.3d 406, that was ordered not to be published by the California Supreme Court in October 1985. This effectively means the case has no precedential value.

⁵ The MN memo does not reference *Voters for Responsible Retirement v. Board of Supervisors* (1994) 8 Cal.4th 765 (“*Voters*”). In *Voters*, the Supreme Court stated that under Section 7507 the “local legislative body, before adopting increases in public retirement benefits for its employees, *must* obtain actuarial evaluations of future annual costs of the plan, and make that cost information public ‘at a public meeting at least two weeks prior to the adoption of any increases in public retirement plan benefits.’” (*Id.* at p.785, emphasis added.) The Supreme Court did not state that the requirements of Section 7507 were directory or optional or elective, it stated that the local legislative body *must* comply with Section 7507. Other courts have also indicated that Section 7507 is mandatory. (See, e.g., *Howard Jarvis Taxpayers’ Assn. v. Board of Supervisors* (1996) 41 Cal.App.4th 1363, 1375; *California Statewide Law Enforcement Ass’n v. California Dept. of Personnel Admin.* (2011) 192 Cal.App.4th 1, 18 (Gov. Code §7507 “necessarily includes the obligation to present the Legislature with a fiscal analysis of the cost of the agreement”).) No court has held that the requirements set forth in Section 7507 are optional.

requiring the future annual costs be made public at a public meeting two weeks prior to approval of any such pension increase.

Because this required information was not properly made public, the harm that Section 7507 was intended to protect occurred. Unfunded liabilities skyrocketed. For example, the County and District's unfunded liabilities were approximately \$10.9 million as of June 30, 2001; they were \$343 million as of June 30, 2013 – an increase of thirty times the amount just twelve years earlier. And this does not take into consideration that the County issued \$112.8 million in pension obligation bonds in 2003 to fund its pension liability, of which \$106 million was outstanding as of June 30, 2014.

The BOS response to F5 indicates this unfunded liability amount was \$217.8 million as of June 30, 2014. The BOS response, however, doesn't give the entire picture. The \$217.8 million in unfunded liabilities is based on a completely new valuation method; the unfunded liability amount would have been approximately \$371.3 million if the valuation method remained the same. (MCERA, Actuarial Valuation Report as of June 30, 2014, p.9.) When you add this to the pension obligation bonds, the County's unfunded liabilities on a constant valuation method would have increased from \$10.9 million on June 30, 2001 to over \$477 million as of the end of fiscal 2014. Further, the new market valuation method will increase volatility of the plan asset valuation, meaning unfunded liabilities and employer contribution rates could sharply increase again if the market declines.

In fact, in the County's stated on page vii of its Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2014 that:

Although investment earnings have been relatively strong in recent years, the Marin County Employees' Retirement Association (MCERA) Board is scheduled to discuss policy changes later this year which may have an adverse impact on the County's pension expenses. Changes to the discount rate, amortization schedules or mortality assumptions would increase the County's annual required contributions and, if significant, would require expenditure reductions to balance the budget. The impact of these changes is unlikely to be quantifiable until the end of the year.

The strain of unfunded liabilities has prejudiced and continues to prejudice the public and taxpayers in other ways, e.g., reduced workforce to provide public services, more fees/taxes, including Measure A, effort to require County Departments to recover costs by imposing fees or charges, increased Workers' Compensation liability, etc.

B. Because proper notice to the public is essential to the statutory design of Section 7507, failure to provide required notice invalidates any pension increase that failed to follow the procedural requirements of Section 7507.

As mentioned earlier, the MN memo states that non-compliance with mandatory procedural requirements invalidates any underlying action resulting from the non-compliance. We agree.

That is, because the requirements of Section 7507 are mandatory and the enhanced pension benefits described in the Grand Jury report were approved without complying with the procedural requirements of law, including (without limitation) the requirement to make public the future annual costs of the benefit increases at a public meeting at least two weeks before approving the increases, the respective pension benefit increases are void.

III. The pension increases violated the debt limitation in Article XVI, sec. 18 of the California Constitution.

Article XVI, section 18(a) of the California Constitution prohibits local government agencies, including counties and cities, from incurring “any indebtedness or liability in any manner for any purpose exceeding in any year the income and revenue provided for such year without the assent of two-thirds of the votes of the public entity voting at an election to be held for that purpose. Under this debt limitation, the “legislative body may not encumber the general funds of the [county] beyond the year’s income without first obtaining the consent of two-thirds of the electorate.” (*Starr v. City and County of San Francisco* (1977) 72 Cal.App.3d 164, 175.) Retirement benefits are subject to appropriation. (*San Francisco Taxpayers Assn. v. Board of Supervisors* (1992) 2 Cal.4th 571.) And, contracts that are beyond a municipality’s power are void. (*In re County of Orange* (C.D. Cal. 1998) 31 F.Supp.2d 768, 774.).

The significant increase in unfunded liabilities since 2001, as well as the County’s issuance of \$112 million in pension obligation bonds approximately one year after many of the pension increases were approved, is *prima facie* evidence that the Constitutional debt limit was violated.

IV. Pension benefits may be modified to maintain the integrity of a retirement system, even if the modification reduces benefits.

The MN memo does not mention that California courts have addressed the point of whether legally authorized pension benefit increases may be modified. Although the pension increases referred to in the Grand Jury report were clearly not authorized according to law, even if they had been, California courts have permitted the modification of pension benefits.

Pension benefits may be modified if it is critical to save the pension system. (See, e.g., *Kern v. Long Beach*, (1947) 29 Cal.2d 848, 854 (noting that legally authorized pension rights may be modified but not wholly destroyed and pointing to several cases where legally authorized vested pensions were modified, including a reduction from two-thirds to half of an

employee's salary); *Allen v. City of Long Beach* (1955) 45 Cal.2d 128, 131 (pension modifications that maintain the integrity of a pension system are reasonable.) And pension benefits that fail to satisfy the requirements of law may be repealed retroactively. (*California Statewide Law Enforcement Assn. v. California Dept. of Personnel Admin.* (2011) 192 Cal.App.4th 1.)

The pension benefit increases described in the Grand Jury Report clearly threaten the sustainability of the County's pension system. And, if they had been approved in accordance with law, modifications would help stabilize the retirement system, which would provide an advantage to all affected employees as well as the public.

V. Conclusion

The pension increases described in the Grand Jury Report were clearly approved in violation of Section 7507 (and other laws) are invalid as set forth above. We respectfully request that the BOS at a minimum take corrective action that is equitable to all parties – both the public and employees – affected by the failures to comply with the law. If the BOS is unwilling to implement a solution that is equitable to both the public, including taxpayers, and employees, we request that the BOS void the pension increases approved in violation of law.

This letter is written without prejudice to the rights of CSPP or any of its members, all of which rights are hereby expressly reserved.

Very truly yours,



Margaret L. Thum, Esq.