HowardRice

Letter of Comment No. 46 File Reference: 34-E Date Received: 9/28/11

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September 22, 2011

Director of Research and Technical Activities Project No. E-34 Governmental Accounting Standards Board 401 Merritt 7, P.O. Box 5116 Norwalk, CT 06856-5116

Re: New Pension Proposals of the Government Accounting Standards Board

Dear Mr. Director and GASB Board Members:

On behalf of the Marin Citizens for Sustainable Pension Plans (CSPP), we submit these comments to the proposed revisions to GASB No. 27 (the "Proposal"). CSPP is a grassroots organization of taxpayers in Marin County, California, that includes a broad range of disciplines, such as accountants, realtors, certified financial analysts, attorneys, and community activists. Our primary focus is on the pension plans and post-retirement health benefit plans of Marin County. Our secondary focus is on the eleven cities of Marin.

1. <u>ENDORSEMENT</u>

CSPP strongly endorses the Proposal. We believe that the pension plans of most, if not all, of the local government bodies in the San Francisco Bay region are presently unsustainable. Equally important, and particularly relevant to the Proposal, the status of each plan is not transparent. Instead, the liabilities of the plans as well as their assumed rates of return are placed in footnotes in each entity's annual financial statements. The Proposal would change

¹The CSPP mission statement is:

[&]quot;To develop new pension and retiree healthcare benefit plans to replace those currently in effect, in order to offer immediate as well as long term relief to taxpayers and more sustainability for retirees. CSPP's proposals will be presented to the public and to the Marin County elected officials and will be pursued and implemented through either successful negotiations with the county or, if necessary, through ballot initiatives in order to put the solutions in the hands of the voters."

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this. Citizens would be able to see more clearly the gaps that threaten the ability of government to continue to provide services to future generations.

2. SALIENT POINTS

- Almost all local government pension plans in the Bay Area are underfunded. Marin County, considered one of the most affluent California counties, has a shortfall in its pension plan alone—without taking into account a yawning liability for postretirement health benefits—of more than \$370 million. Indeed, if a realistic rate of return is used, the unfunded liability would approach \$1 billion—this, even after the County in 2003 issued general obligations bonds raising \$102 million to apply to unfunded pension liabilities.
- Citizens desperately <u>need</u> disclosure of pension liabilities in the audited financial balance sheets, rather than having such information shunted off to footnotes, coated with opaque language. If citizens are lulled into failure to contribute sufficient funds today to fund future obligations adequately, future taxpayers will be forced to cover the present real costs plus interest. That means that future taxpayers will have less money to compensate their own public employees, fund education, build infrastructure and finance environmental protection. The Proposal would address this concern.
- Citizens as well as elected officials need faster and more precise reporting of pension expenses that generate unfunded liabilities. The Proposal would also address this need. By requiring various specific causes of unfunded pensions to be reported, many of which must be reported for the year in which they occur, the standard will have a significant impact. Availability of transparent and timely information will help shape better reasoned positions in collective bargaining negotiations between the government employer and the employees.
- Elected officials can recognize the potentially harmful effects nature of unfunded obligations more readily when they are disclosed in the audited balance sheets, and when such specific causes are included. The Proposal would require such disclosures.
- A former member of the California State Teachers Retirement System Board observed in July 2011 that bonds and cash, which generally constitute about 28% of most pension funds, can generally be expected to yield no more than 5%.² This means that pension funds, in order earn returns of 7.5 to 8% on the total assets (the amount necessary just to break even), must earn 10% (before fees and

²David Crane, Catching Up Is Hard To Do, S.F. Chronicle (July 29, 2011) A 14.

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expenses)on the remaining 72% of assets which are invested in equities. But a 10% return is almost 40% higher than equities earned in the 20th Century.³

We recognize that problems in pension plans cannot be remedied overnight.
Fortunately, the proposed changes give local governments ample time to put their plans in order. But actions must be initiated <u>now</u> to avoid much harsher steps down the line.

3. POTENTIAL ADDITIONS TO THE PROPOSED CHANGES

- The Proposal is confined to pension liabilities; it does not cover the equally daunting shortfalls in Other Post Employment Benefits (OPEB) such as healthcare. The latter benefits are currently funded only on a pay-as-you-go basis. As the average age of retirees increases and medical costs soar, these liabilities threaten to become the "900 pound gorilla" at the retirement funding table. We understand the Board decided not to include OPEB in the pension standards, and that such benefits and the focus of a separate GASB research project. GASB will provide a great service to local governments by developing standards for disclosing such liabilities.
- The new standards in the Proposal ought to address the phenomenon known as "Employer Paid Member Contributions" (EPMC). Here an employee-member's contribution is not in fact paid by the member, but by the employer. Because the EPMC is not part of the employee's take-home pay, reporting of salaries in the employer's budget becomes understated by that amount. Moreover, employer-paid benefits can be included as compensable earnings for purposes of calculating an employee's final retirement benefits, resulting in an increase in the employer's pension liability. This practice is not made clear at present in governmental financial statements; it should be.

4. REQUEST TO SPEAK

 The undersigned CSPP member, Denis Rice, requests the opportunity to address you on October 13, 2011, at your San Francisco hearing at the Sir Francis Drake Hotel. Mr. Rice is a former President of the Marin County Board of Supervisors and Mayor of Tiburon had served on a number of Bay Area public agencies. He is a

³Id. According to Warren Buffett, whose investment acumen probably exceeds that of most local governments, the average annual increase in the Dow for the entire 20th century was 5.3% compounded. Buffett says that for investments to earn that return in the 21st century would require the Dow to close at 2,000,000 on December 31, 2099. And to return 10% annually would require the Dow to reach about 2,400,000 by 2100. Accordingly, Buffett concludes those who believe these returns to be realistic "are apparently direct descendants of the queen in 'Alice in Wonderland,' who said: 'Why, sometimes I've believed as many as six impossible things before breakfast.'" Id.

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practicing attorney listed in Who's Who in the World who received the Lifetime Achievement Award from the California State Bar Business Law Section in 2009.

Thank you for your consideration.

Yours very truly,

Denis T. Rice on behalf of CSPP