TO: BOARD OF SUPERVISORS

FROM: JOHN CULLEN, County Administrator

DATE: JUNE 24, 2008

SUBJECT: RESPONSE TO GRAND JURY REPORT NO. 0805, ENTITLED "THE SUPERVISORS CHIP AWAY AT THE COUNTY'S MOUNTAIN OF HEALTH BENEFIT DEBT"

Contra
Costa
County

SPECIFIC REQUEST(S) OR RECOMMENDATION(S) & BACKGROUND AND JUSTIFICATION

RECOMMENDATION:
APPROVE response to Grand Jury Report No. 0805, entitled "The Supervisors Chip Away at the County's Mountain of Health Benefit Debt" and DIRECT the Clerk of the Board to forward the response to the Superior Court no later than August 11, 2008.

BACKGROUND:
On May 12, 2008, the 2007/2008 Grand Jury filed the above-referenced report, which was reviewed by the Board of Supervisors and subsequently referred to the County Administrator who prepared the attached response that clearly specifies:

A. Whether a finding or recommendation is accepted or will be implemented;

B. If a recommendation is accepted, a statement as to who will be responsible for implementation and by what definite target date;

C. A delineation of the constraints if a recommendation is accepted but cannot be implemented within a six-month period; and

D. The reason for not accepting or adopting a finding or recommendation.

CONTINUED ON ATTACHMENT: YES SIGNATURE:

_____RECOMMENDATION OF COUNTY ADMINISTRATOR _____RECOMMENDATION OF BOARD COMMITTEE
_____APPROVE _____OTHER

SIGNATURE(S):

ACTION OF BOARD ON__________________________APPROVE AS RECOMMENDED ___________ OTHER ___________

VOTE OF SUPERVISORS

_____ UNANIMOUS (ABSENT__________________)

AYES:_____________________ NOES:____________________
ABSENT:__________________ ABSTAIN: ________________

CONTACT: LISA DRISCOLL (925) 335-1023

CC: PRESIDING JUDGE OF THE GRAND JURY
GRAND JURY FOREMAN
COUNTY ADMINISTRATOR
AUDITOR-CONTROLLER
TREASURER-TAX COLLECTOR

I HEREBY CERTIFY THAT THIS IS A TRUE AND CORRECT COPY OF AN ACTION TAKEN AND ENTERED ON THE MINUTES OF THE BOARD OF SUPERVISORS ON THE DATE SHOWN.

ATTESTED: June 24, 2008

JOHN CULLEN, CLERK OF THE BOARD OF SUPERVISORS AND COUNTY ADMINISTRATOR

BY ______________________________, DEPUTY

BOARD OF SUPERVISORS RESPONSE TO GRAND JURY REPORT NO. 0805: THE SUPERVISORS CHIP AWAY AT THE COUNTY'S MOUNTAIN OF HEALTH BENEFIT DEBT

FINDINGS

A. Defining the OPEB Problem

1. Governmental Accounting Standards Board Statement Number 45 ("GASB 45"), "Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions" (OPEB) sets an accounting standard analogous to the governmental pension accounting standard. This standard requires the calculation and disclosure of an unfunded liability for government employee retiree health care benefits similar to the method already in place for recognizing the cost of government employee pensions. Contra Costa County (County) has elected to embrace this standard.

   Response: *Agree.*

2. As of January 1, 2006, County's unfunded OPEB liability for the cost of providing health care benefits to its current and future retirees and their dependents over the course of their lifetimes was estimated by an independent actuarial consultant hired by the Board of Supervisors (Supervisors) to be $2.57 billion.

   Response: *Agree, with the clarification that the County's unfunded OPEB liability is for the 'accrued to date' cost of providing health care benefits.*

3. The 2006 actuarial study indicated that the structure and costs of the County's retiree health care benefits were not sustainable.

   Response: *Partially disagree. The 2006 actuarial study identified the liability and, correctly, made no comment regarding the County's ability to sustain the liability. The County, however, in its March 1, 2007 report did declare that 'The cost of the County's health care benefit is unsustainable'.*

4. According to a March 1, 2007 County OPEB Task Force report, as of January 1, 2006, the estimated unfunded OPEB liabilities for Alameda, Orange, Riverside, San Diego, and San Mateo counties were $613 million, $598 million, $257 million, $640 million, and $70 million respectively. These five counties have a combined OPEB liability of approximately $2.17 billion, which is less than the $2.57 billion estimate for Contra Costa alone.

   Response: *Agree.*

5. In 2008, the actuarial consultant updated the estimated unfunded OPEB liability. As of January 1, the revised estimate was $1.74 billion. The reduction results primarily from the use of new actuarial assumptions, and secondarily, from Supervisor action on May 6, 2008 to modify the health care benefits available to County employees that are not covered by a union labor contract; i.e., unrepresented employees. The $1.74 billion figure is more than the County's total annual

operating budget of approximately $1.2 billion for fiscal year 2007-08, and is still nearly equal to the combined health care benefit liabilities for Alameda, Orange, and San Diego Counties.

Response: *Partially disagree. The reduction results primarily from the Board of Supervisors' action to partially pre-fund our liability in the FY 2008/09 budget ($20 million), which allowed the use of a higher discount rate (6.32%). Of the $835 million reduction, over 82% or $687.5 million is due to partial pre-funding. The new valuation assumption changes and plan changes for non-represented employees both made smaller contributions to the liability savings after the larger discount rate savings due to planned pre-funding.*

6. According to County officials, the growth in the cost of health care benefits has and will continue to compromise the County's ability to provide public services since County general funds earmarked for services will have to be used to pay for increasingly costly employee and retiree health care benefits.

   Response: *Agree.*

7. As early as 1994, the Supervisors were briefed by administrative staff about the pending OPEB crisis, but took no action for more than a decade.

   Response: *The respondent is unable to verify Supervisor briefings from 1994.*

8. The OPEB liability results primarily from labor agreements in which retirees and their dependents receive the same increasingly costly health care benefits as active employees and their dependents. Other factors that contribute to the OPEB liability include longer life spans, earlier retirement ages, as well as medical costs and health insurance premiums that have escalated dramatically compared to overall inflation.

   Response: *Agree, with the clarification that the OPEB liability results from benefits not being fully funded on an annual basis (pre-funded the benefit rather than pay-go).*

9. The Supervisors have the authority and responsibility to establish the labor negotiation policy, to explain it clearly to the County's negotiating team, and to ensure that the negotiating team carries it out.

   Response: *Agree.*

10. There have been occasions in the past in which individual supervisors have had conversations with union leaders about matters being negotiated. Reportedly, these conversations have on occasion undermined the Supervisors' labor negotiation policy, causing a weakening of that body's resolve, resulting in labor contracts that were not fiscally prudent.

    Response: *Partially disagree. Individual supervisors have had conversations with union leaders about matters being negotiated; however these conversations, rather than undermining the negotiation policy have, on several occasions, encouraged union leaders to continue negotiating when they would have otherwise taken unproductive actions..*

11. The subject of the County's unfunded OPEB liability has been the topic of four previous Contra Costa County Grand Jury reports:

    • 2004: "Take Action Now to Reduce Costs of Retiree Health Insurance."

    • 2005: "Code Blue: County Health Care Costs."

    • 2006: "County Ignores Retiree Health Care Costs: The Financial Tidal Wave."

    • 2007: "Mayday, Mayday, Mayday! The County Drifts Ever Closer to the OPEB Rocks."

    Response: *Agree.*

12. The Governmental Accounting Standards Board recommends public agencies account for unfunded OPEB costs over the active service life of benefiting employees, rather than reporting current year OPEB costs for existing retirees.

    Response: *Agree.*

13. Currently, there is no universal County requirement for eligible retirees to enroll in Medicare Parts A (hospital coverage) and B (physician and ancillary medical coverage), and assign benefits to County sponsored health insurance carriers. When Medicare benefits are assigned to the County's health insurance carriers by retirees by means of a carrier-provided form, Medicare becomes the primary payer, leaving the County responsible only as a secondary payer. Currently, Medicare health benefits are not uniformly assigned to the County's health insurance carriers to help pay for the participants' medical care. This results in higher insurance premium costs for the County**.**

    Response: *Partially disagree. Medicare Part A is required by the Social Security Act for all individuals, including County retirees. Medicare Part A is automatic and requires no enrollment. Medicare Part B requires the retiree to enroll. Medicare is primary for retirees whether or not assigned, even if the retiree is only covered by Medicare Part A. Assignment of benefits to the carriers means that a retiree can use their Medicare card only for providers within their specific network. Non-assignment means the Medicare card can be used for both network and non-network providers. It is true that the County does not universally require the assignment of these benefits to the County's health insurance carriers.*

14. The County provides combined medical and dental benefits to approximately 8600 active employees, 5800 retirees, plus dependents and surviving spouses of retirees. Approximately 7400 (86%) of the active employees are represented by labor unions. The remaining 1200 (14%) are unrepresented.

    Response: *Agree.*

15. The County's $1.2 billion, fiscal year 2007-08 budget includes $130 million, 10.7% of the total budget, to pay health premium costs on a pay-as-you-go plan ($36 million for retirees and $94 million for active employees).

Response*: Agree.*

B. Addressing the OPEB Problem

16. On September 25, 2007, the Supervisors adopted a plan to finally begin addressing the County's unfunded OPEB liability. It included the following:

    - A Strategic Plan and timetable addressing the OPEB problem.
    - An Irrevocable Trust Account for pre-funding a portion of the County's OPEB liability.
    - An initial goal to pre-fund, i.e., deposit into the trust, 40% of the total OPEB liability over the course of the next 30 years. This amount represents only the costs of current retirees' health care costs during that period, not future retirees.
    - A pledge to deposit $588 million between fiscal years 2008-09 and 2022-23, 15 years, into the Irrevocable Trust Account.

    Response*: Disagree. The Board of Supervisors' took its first action to reduce the County's future OPEB liability on August 15, 2006. The CNA MOU adopted on that day included 'me too' language. The 'me too' language stated that 'the County agrees that eligibility requirements and implementation date for retiree health for employees covered by this MOU will be the same as agreed to by the majority of County employees'. On October 31, 2006 when they adopted a new fifteen year vesting requirement for the receipt of retiree health care for the majority of County employees, this change became part of the CNA MOU due to the 'me too' clause..*

    The Board's next action, on June 26, 2007 set a timetable for addressing the OPEB program, an initial pre-funding goal of 100% of the potential liability for the retiree population (currently 40% of the total liability), and pledged an allocation of resources ($588 million between fiscal years 2008-09 and 2022-23 and $100 million annually thereafter).

    The Board's next action, on September 25, 2007 approved the selection of an irrevocable trust structure (IRS Code Section 115). The January 15, 2008 Board action established the Irrevocable Trust Account.

17. Effective January 1, 2007, the County increased the eligibility requirement for retiree health care benefits. Since then, employees, other than deputy sheriffs and firefighters, must work for the County for 15 years. Previously, some new employees had become eligible for retiree health benefits after as little as one day on the job.

    Response*: Agree, with the clarification that the new tier excluded all employees covered by CalPERS health plans not just deputy sheriffs and firefighters.*

18. On January 15, 2008, the Supervisors established an Irrevocable Trust Account, under the provisions of Internal Revenue Code Section 115, to deposit future OPEB funds. The funds in such accounts may not be used for any other purpose than as directed in the trust document. The

trustees are: the County's Administrator, Auditor-Controller, Treasurer-Tax Collector, Director of Finance, and Health Services Department's Chief Financial Officer.

***Response**: Agree.*

19. The County Administrator has conducted information sessions covering the County's OPEB liability problems during which he answered employee and public questions.

***Response**: Agree.*

20. On January 23, 2008, the County Administrator presented a report to the County Health Care Coalition, a group that includes representatives of the various labor organizations. This report contained several benefit design change options that, if adopted, would have varying impacts on reducing the County's OPEB liability. The pros and cons, as well as the fiscal impact on the County's unfunded OPEB liability, were presented for each of the options.

***Response**: Agree.*

21. The January 23, 2008 report proposed changes to the health benefits available to retired unrepresented employees and their dependents. On May 6, 2008, the Supervisors approved the following changes for retired unrepresented employees and their dependants:

- Limit coverage to one County health plan for retired employees, and their dependents, regardless of a spouse or partner's County employee status; i.e., no dual County health coverage.
- Require retirees who become 65 on or after January 1, 2009 to enroll in Medicare Parts A&B.
- Beginning January 1, 2010, set the County health care insurance premium subsidy at the 2009 premium level.

***Response:** Agree, with the clarification that the January 23, 2008 presentation described several different options for liability reduction as a means of expressing the order of magnitude of the problem, it did not present any of the examples as proposed changes to the health benefits.*

22. The January 23, 2008 report proposed the establishment of a second benefit tier for newly hired unrepresented employees intended to limit the County's costs of providing health plan benefits to future retirees. On May 6, 2008, the Supervisors approved the following changes for unrepresented employees hired after January 1, 2009:

- Limit coverage to one County health plan for active or retired employees, and their dependents, regardless of spouse or partner County employee status; no dual County health coverage.
- Establish separate insurance rating pools for active and retired employees to allow for more accurate cost calculations for each group.

- Provide that upon retirement: a) the County would not contribute toward the cost of health care for employees that retire before the age of 65; and, b) the County would permit retirees to enroll in County health plans at their own expense until age 65, when employees are eligible to enroll in Medicare Parts A&B.

Response: *Partially disagree. The January 23, 2008 presentation described a possible second tier option that could reduce the County's future liability; it did not propose that the new tier be implemented as described. The May 6, 2008 Board Action established a new health care tier for unrepresented employees and officials hired, appointed, or elected* ***after December 31, 2008****. The separate rate pools are intended to eliminate one group subsidizing the actual costs of another group, not to more accurately calculate costs. Finally, upon retirement, these employees and officials will have access to County health plans, but no County premium subsidy will be paid for any health or dental plan before or after the age of 65. Retirees and eligible family members will participate at their own expense.*

23. The January 23, 2008 report proposed the establishment of a Benefit Design Task Force to develop a new health benefit program for the County. On May 6, 2008, the Supervisors approved:

- The establishment of a task force to deal with health care benefits for unrepresented employees. Members of the task force would include unrepresented employees and retirees, County subject matter experts, independent benefit design, actuary, and tax consultants.

- Setting specific achievement goals and parameters to recommend options for sound health care benefits within the County's budgetary limits.

- Setting specific target dates for completion of any re-design recommendations before 2010.

- Pursuing the means to assure portability of employee health coverage and access to health savings mechanisms for unrepresented County employees, retirees, and their dependents.

Response: *Agree, with the clarification that the January 23, 2008 presentation described how the establishment of a task force could be used to help to plan benefit design changes that counteract medical cost growth in order to preserve a balance between providing sound health care coverage for our employees and retirees and maintain vital county programs and services.*

24. The County Administrator implemented a hiring freeze effective February 1, 2008, subject to case-by-case exceptions only he and his chief deputies have the authority to grant.

Response: *Agree.*

25. On May 6, 2008, the Supervisors approved a fiscal year 2008-09 budget that directs $20 million to the OPEB trust.

Response: *Agree.*

26. The County has 39 labor contracts with 17 different employee organizations. Most of the contracts expire on September 30, 2008.

Response: *Agree.*

27. The County Human Resources Department's labor relations services unit coordinates the activities of both in-house staff and contracted labor consultants.

    Response: *Agree.*

C. The OPEB Problem Continues

28. In October 2007, the Supervisors approved a new contract with the United Professional Firefighters, Local 1230 that did not include any changes in health benefits.

    Response: *Agree.*

29. In December 2007, the Supervisors approved a new contract with the Costa County Deputy District Attorneys Association that did not include substantive changes in health benefits.

    Response: *Agree, with the clarification that the new contract eliminated dual coverage for Contra Costa County Deputy District Attorneys' Association employees.*

30. In April 2008, the Supervisors approved a new contract with the California Nurses Association that did not include substantive changes in health benefits.

    Response: *Agree, with the clarification that the new contract eliminated dual coverage for California Nursing Association employees not enrolled in dual coverage as of March 24, 2008.*

31. Based on 2008 estimates from the independent actuary hired by the Supervisors, the County will need to set aside $130 million per year, for 30 years, to pay down 40% of the OPEB liability. The Supervisor-approved 40% target level represents the estimated cost of the County's current retiree health care benefits, not the total amount required to also cover the health care benefit costs for all future retirees. Recent steps by the Supervisors, including the May 6, 2008 approval of the fiscal year 2008-09 budget, will reduce the liability over time. However, in the absence of any further action by the Supervisors to increase the target level, the gap between the required and planned contributions is estimated to be $54 million per year.

    Response: *Partially disagree. The $130 million annual funding gap to reach the County's 40% target was calculated by CAO staff, not the independent actuary. Additionally, the approved 40% funding target represents 100% of the estimated cost of the County's current retirees' health care benefits or 40% of the total amount required to cover the health care benefits costs for the County's current active and retired population.*

RECOMMENDATIONS

The 2007/08 Contra Costa County Grand Jury recommends that:

1. The Supervisors establish the County's labor negotiation policy, explain it clearly to its negotiating team, and see that the negotiating team carries it out.

   Response: *Has been implemented. The establishment and policy of labor negotiations has always been within the purview of the Board of Supervisors.*

2. The Supervisors refrain from individually communicating with labor leaders regarding any contract item being negotiated.

   Response: *Will not be implemented. There are policy and management reasons for elected officials to communicate with labor leaders on pending negotiations. Additionally, it is within the purview of each individual elected official to decide what they wish to communicate to labor leaders as long as (per the Brown Act) they do "not disclose confidential information that has been acquired by being present in a closed session … to a person not entitled to receive it, unless the legislative body authorizes disclosure of that confidential information." (Government Code, sec. 54963(a)).*

3. The Supervisors only approve labor contracts that are fiscally prudent and that reduce the County's unfunded OPEB liability.

   Response: *Will not be implemented because it is not reasonable to expect every labor contract to reduce the County's unfunded OPEB liability. Some labor contracts, IHSS for example, contain no provision for retiree health care and therefore have no impact on the County's unfunded OPEB liability; this recommendation would eliminate the Supervisors ability to approve labor contracts with these organizations. The Supervisors will continue to only approve labor contracts that are fiscally prudent.*

4. The Supervisors develop and implement a new health benefit program for County employees and retirees that will reduce the OPEB liability.

   Response: *This recommendation is in process. The County Administrator is working to form a task force to assist in the development of a new health benefit program for County employees and retirees. The work of the task force is then subject to negotiation with the affected unions, whose contracts are mostly scheduled to expire at the end of September, 2008.*

5. All Medicare eligible employees, retirees, and their dependants receiving health care benefits from the County be required to enroll in Medicare Parts A and B, and to assign their Medicare benefits to the County's authorized health insurance carriers.

   Response: *Will not be implemented because older retirees who have never enrolled in Medicare Part B would pay more in extra Medicare premiums than the benefit of their Medicare assignment would save. This recommendation is being pursued for future retirees.*

6. The Supervisors approve only County budgets that incorporate features of the approved OPEB funding strategy. These must include reductions and/or containment of employee and retiree health plan costs, program and service reductions, and redirecting funds into the OPEB irrevocable trust.

   Response: *The recommendation has been implemented in the FY 20008/09 budget. The FY 2008/09 budget includes $20 million in partial pre-funding which significantly impacted the County's OPEB liability and a fixed health care budget.*

7. Within six months of this report, the Supervisors develop a plan to incrementally increase the OPEB Irrevocable Trust funding from the current 40% target level to 85% over the course of the next 30 years.

   Response: *Will not be implemented because it is not currently warranted or reasonable to set an 85% funding target. An 85% funding target is higher than CCCERA's current funding level. The County's goal is to reduce the unfunded liability not attempt to fund it at its current level. Additionally, the County did not adopt a fixed 40% funding goal. The funding goal is based upon 100% of the liability for its current retirees. Over time, the combination of current resource redirection, new tiers for new hires, and a budget for health care costs will fully fund the County's liability.*