San Diego Taxpayers Educational Foundation

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Brief Summary: An Analysis of Labor Costs at San Diego County Retail Water Agencies

Summary

This report is the last in a three-part series reviewing labor costs at water agencies operating within San Diego County and is part of a larger, ongoing examination of regional water issues being conducted by the San Diego Taxpayers Educational Foundation.

There are a number of agencies responsible for providing water directly to ratepayers in San Diego County. These include five water districts, three irrigation districts, eight municipal water districts, one public utility district, six cities and one federal agency (Camp Pendleton). Each of these 24 entities has a seat on the board of the San Diego County Water Authority, which sets water policy for the county as a whole.

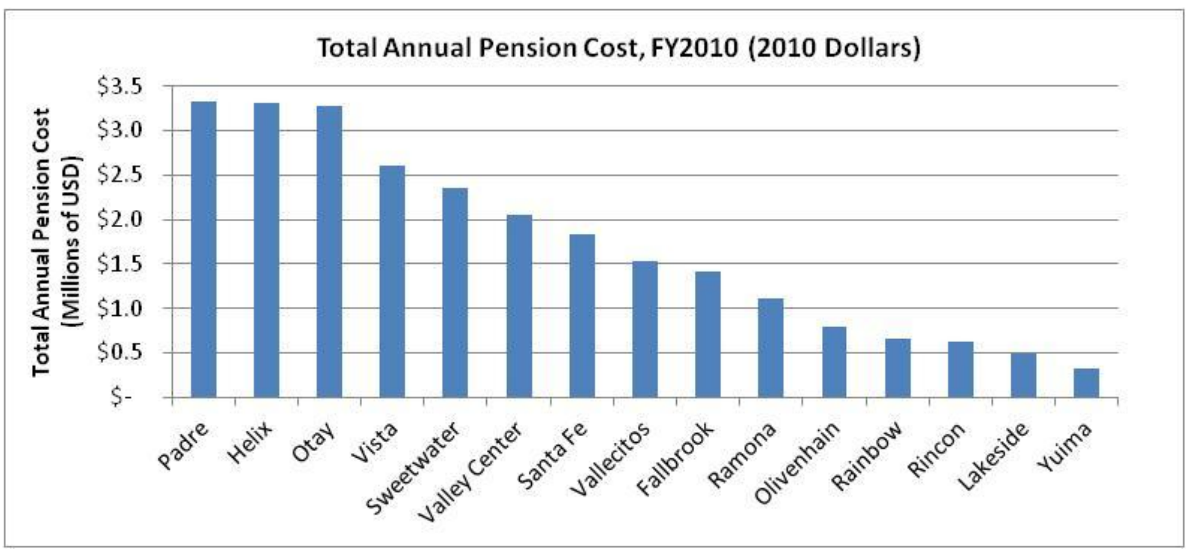
These water retailers are the means by which the water secured from the State Water Project and the Colorado River Aqueduct is distributed to actual customers (through water wholesalers such as the Metropolitan Water District and the County Water Authority). This analysis concentrates on the 15 independent water agencies within the county.[1]

Total Annual Pension Cost

The Total Annual Pension Cost is the combined yearly total of the Annual Required Contribution, the Employer Paid Member Contribution (EPMC), retiree healthcare costs, and miscellaneous pension costs.

Helix, Otay, and Padre Dam had the highest Total Annual Pension Cost, at more than $3 million each. Of note is the fact that the Vista Irrigation District, with far fewer employees, had a Total Annual Pension Cost of $2.6 million.

The EPMC (also referred to as the "pick-up") is a benefit whereby the employer pays the employee's required retirement contribution. Not only does this practice save employees from having to pay retirement costs out of pocket, but, if the employer reports the contribution as increased compensation, the amount is added to the final salary figure used to calculate retirement benefits, increasing pensions.



[1] This analysis focuses on independent agencies **as incomplete and/or unavailable** reporting from water agencies controlled by cities (Carlsbad Municipal Water District and San Dieguito Water District) and those that operate as part of a city's public works or utilities department (as is done in the cities of Del Mar, Escondido, Oceanside, Poway, and San Diego), **make comparisons difficult, if not impossible.**

Pension Contribution Rates			
District	Employer Pick-Up (EPMC)	Employee Pays	EPMC Counts Toward Retirement
Fallbrook	8%	0%	No
Helix	8%	0%	No
Lakeside	8%	0%	No
Olivenhain	5%	3%	No
Otay	7%	1%	No
Padre	7%	1%	No
Rainbow	7%	1%	No
Ramona	7%	1%	No
Rincon	7%	0%	Yes
Santa Fe	7%	1%	No
Sweetwater	7%	1%	Yes
Vallecitos	8%	0%	No
Valley Center	1.513%	6.487%	No
Vista	1.5%	3%	No
Yuima	8%	0%	No
Source: CAFRs, MOUs, CalPERS valuations, and direct communications			

<u>In Fiscal Year (FY) 2010, water districts spent more than $5.7 million subsidizing the employee's share of pension costs</u>. Six (6) water districts paid for the entire amount of the employee's pension costs.

Another common practice that further raises pension costs is to increase the retirement formula's benefit factor (a multiplier applied to each year of service: 2%, 2.5%, etc.). ***<u>All but one water district retroactively increased employee pension benefits by doing exactly this since FY 1999.</u>***

Total Annual Labor Cost

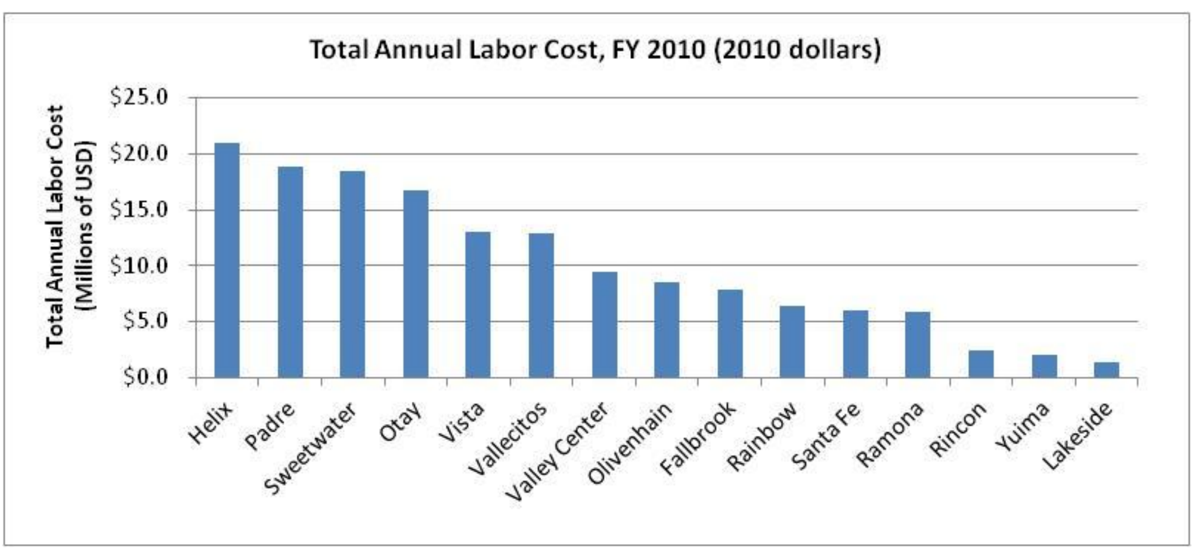
The Total Annual Labor Cost equals the total dollar amount for both salaries and benefits. That sum includes wages, annual pension and retiree healthcare contributions, unemployment insurance, medical insurance, FICA, and life/disability insurance, among other items.

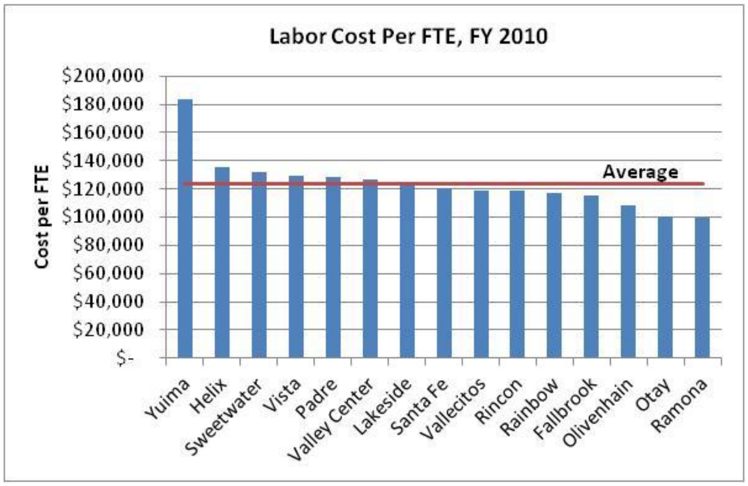
<u>A district-by-district analysis reveals significant double and even triple digit percentage increases in labor costs between FY 1999 and FY 2010 even after adjusting for inflation.</u>

Total Increase in Labor Costs, FY 1999-2010	
District	% Increase
Fallbrook	44%
Helix	63%
Lakeside	NA*
Olivenhain	66%
Otay	NA
Padre	85%
Rainbow	NA
Ramona	NA
Rincon	NA
Santa Fe	83%
Sweetwater	48%
Vallecitos	120%
Valley Center	70%
Vista	71%
Yuima	122%
****Data not available for FY 1999. Adjusted for inflation. Source: CAFRs, MOUs, CalPERS valuations, and direct communications***	

In FY 2010, the average cost per full-time employee was approximately $123,000.

<u>The labor cost per employee for Yuima, the smallest district with only 11 employees, was over $183,000</u>.





Pension Liability
To pay for the pension benefit, employers make contributions to CalPERS. The employer contribution rate is determined by actuaries and includes the normal cost plus a payment on the amortization of the Unfunded Actuarial Accrued Liability.

Pension Unfunded Liabilities, FY 2010 (2010 dollars)			
District	**FTE**	**UAAL**	**Funded Ratio**
Otay	166	$ 23,692,947	70.9%
Sweetwater	139	$ 19,206,008	73.3%
Padre	132	$ 17,746,712	75.2%
Helix	155	$ 15,636,522	82.5%
Source: CAFRs, MOUs, CalPERS valuations, and direct communications			

An unfunded liability is created when actual experience does not match actuarial assumptions. There are many reasons why an agency may have an unfunded liability. These include such factors as anemic investment returns and demographic changes. The funded ratio indicates how well a plan is funded (assets vs. accrued liabilities). It should be noted that ***<u>if CalPERS's forecasting is incorrect and retirement costs exceed a water district's ability to pay, the responsibility for paying the difference would fall on ratepayers</u>***.

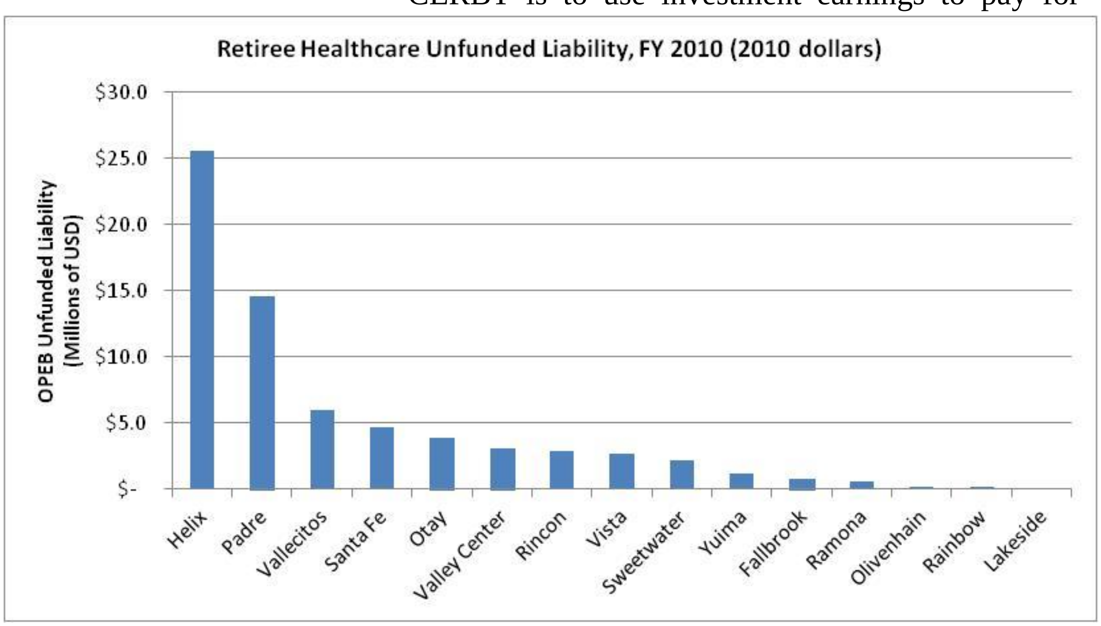
By FY 2010, the combined pension unfunded liability for the four largest districts (Helix, Otay, Padre, and Sweetwater) was over $76 million.

Retiree Healthcare Liability
While most of the discussion about outstanding obligations focuses on pensions, Other Post Employment Benefits, or OPEB, are gaining increased attention. In the case of the districts in this study, the OPEB refers exclusively to retiree healthcare benefits offered to employees who retire before they turn 65. These benefits usually extend to dependents and, in some cases, are provided beyond age 65. They may also be extended to former board members. As of FY 2010, every district provided this benefit to its employees.

<u>As of FY 2010, the county's water districts had a combined unfunded retiree healthcare liability of over $68 million</u>. At nearly $26 million, the Helix Water District's retiree healthcare liability made up more than one-third of that total.

Most public agencies have funded their OPEB obligation on a pay-as-you-go (paygo) basis. In other words, they pay for the benefit after employees retire rather than as the benefit is earned.

Some public agencies, including a number of local water districts, have begun to address their retiree healthcare costs by joining the California Employers' Retiree Benefit Trust Fund (CERBT), run by CalPERS. This trust fund allows public employers to pre-fund the future cost of their retiree health insurance benefits by investing in securities. Much like a traditional pension fund, the purpose of CERBT is to use investment earnings to pay for



retiree health benefits, thereby lowering future employer costs and unfunded liabilities.

OPEB Details			
District	**Paygo**	**CERBT**	**Annual OPEB Cost**
Fallbrook	Yes	No	$ 91,049
Helix	Yes	No	$ 2,510,000
Lakeside	No	Yes	$ 28,437
Olivenhain	Yes	No	$ 6,740
Otay	No	Yes	$ 455,122
Padre	No	Yes	$ 1,604,761
Rainbow	Yes	No	$ 26,850
Ramona	Yes	No	$ 82,794
Rincon	Yes	Yes	$ 255,932
Santa Fe	No	Yes	$ 633,242
Sweetwater	No	Yes	$ 244,000
Vallecitos	Yes	No	$ 802,051
Valley Center	No	Yes	$ 489,426
Vista	No	Yes	$ 302,281
Yuima	Yes	No	$ 128,105
Source: CAFRs, MOUs, CalPERS valuations, and direct communications			

While all of the districts in the county offered retiree healthcare benefits in FY 2010, only eight (8) had enrolled in the CERBT program.

Recommendations

The results of this analysis clearly show that, like many other public agencies, labor costs at San Diego County water districts, both annual and long-term, increased dramatically during the decade of the 2000s. This growth coincided with significant increases in employee pensions at almost every district examined. These increased pension expenses swell not only long-term obligations but the annual amounts employers pay to finance pensions. In addition, optional retiree healthcare benefits have added an unfunded liability at substantial annual costs to some districts.

The following actions are needed to curb labor costs at the county's water districts:

Pension Formula: All districts whose employees receive Social Security should reduce their pension benefit formula for new employees to 1.5% @ 65 (approved as a benefit formula option by CalPERS in 2011). Doing so will contribute greatly to reducing their long-term pension liabilities.

Eliminate EPMC: Throughout the period covered in this study, most districts have paid all or most of the amount that employees are required to contribute to help finance their retirements (usually seven or eight percent of salary, depending on the benefit formula). Eliminating the EPMC benefit would save districts hundreds of thousands of dollars annually.

Reform OPEB: Retired water district employees—and often their spouses—are also entitled to retiree healthcare benefits until they turn age 65 (and, in some cases, longer). This is an extremely generous benefit that further increases long-term liabilities. Districts that have not already done so should join CERBT or institute some other pre-funding mechanism, make employees pay the full costs of this benefit, or eliminate the benefit altogether.

Clarify Financial Reporting: While the districts' financial reporting is thorough, it fails, as does the reporting of most public agencies, to provide specific details about its labor costs, necessitating reports such as this one. Aggregate numbers, while helpful, do not give the public sufficient information. Such a level of detail is not required by law, but would allow ratepayers to better understand the public institutions that serve them and hold them accountable.

Unbundle City Water Departments: Because the cities of Carlsbad, Encinitas, Oceanside, Poway and San Diego combine the financial data relating to their respective water district or department with similar information for the city as a whole, it is virtually impossible to determine labor costs at the water agencies or departments serving their residents. This is a disservice to ratepayers who have a right to know the extent to which labor costs are influencing water rates.

Please refer to www.sdcta.org for the complete study and district-by-district analysis.

The San Diego Taxpayers Educational Foundation is a nonprofit public benefit corporation created to research government revenue and expenditure policies affecting taxpayers in San Diego County as well as other public policy issues having a direct bearing on county residents and businesses.