TOWN OF PALM BEACH

Office of The Town Clerk

REPORT OF THE FINANCE AND TAXATION COMMITTEE MEETING HELD ON DECEMBER 16, 2008

I. CALL TO ORDER AND ROLL CALL

The Finance and Taxation Committee meeting was called to order at 9:30 a.m. in the Town Council Chambers. On roll call, Committee Chair Denis Coleman and Committee Member David Rosow were found to be in attendance. Others present for all or a portion of the meeting were: Town Manager Peter B. Elwell, Assistant Town Manager Sarah Hannah, Deputy Town Manager Tom Bradford, Finance Director Jane Struder, Town Council President Pro Tem Gail Coniglio, Town Council Member Susan Markin, Mayor Jack MacDonald, Public Works Director Paul Brazil, Parks and Recreation Director Jay Boodheshwar, Police Chief Michael Richter, Fire Chief Bill Amador, Human Resources Director William Crouse and Town Clerk Joanna Cunningham.

II. PLEDGE OF ALLEGIANCE

The Pledge of Allegiance was led by Chair Coleman.

III. APPROVAL OF AGENDA

The Agenda was approved as printed.

IV. PENSION DISCUSSION

1. Actuarial Items
   a. Overview of Actuarial Process
   b. Overview of Smoothing and Funding Process

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Mr. Brad Armstrong, Actuary from Gabriel Roeder Smith & Company presented a 42 slide Power Point presentation of actuarial items and described the actuarial process, the smoothing and funding process. This presentation is was included in the meeting backup packages. The most important component is to outline what the Town's objectives are with regard to pension plans. Mr. Armstrong indicated that they are:

- Key Measures of success
- Vary among stakeholders
- Attraction/retention/exit plan
- Funding progress
- Communication & periodic review
- Stay objective

Chairman Coleman asked staff to include in the next budget the Town Contribution Rates for general employees and Police and Fire employees listed as two separate line items. Member Rosow added he would like to see other ways to present the data and the dynamics explained better. Finance Director Struder indicated that she would make sure the presentation of this information is improved for next year.

The Committee thanked Mr. Armstrong for his detailed and informative report.

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After Mr. Armstrong's presentation, the Committee took a five minute break and resumed at 11:15am

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c. Report on Actuarial Study on Investment Assumption Options

Mr. Armstrong stated that it is his opinion, and that of the Boards he has spoken to, they are not recommending any changes in assumptions at this time.

Chairman Coleman cited a letter from Board Member Mr. Wilbur Ross, who was unable to attend the meeting this morning. Mr. Ross' opinion is that 8% is a reasonable rate of return.

d. Report on Actuarial Study on Other Actuarial Assumption Options

Member Rosow asked who establishes the assumptions. Town Manager Elwell indicated that the trustees recommend changes but the Town Council must vote and ratify the changes. The 8% return is the only item that has been looked at in recent years.

Member Rosow recommended the Pension Boards look at the other assumptions and report back to Town Council.

Carol Simmons, 201 Banyon Road, Chair of the Fire Fighters Pensions Board, offered to resign her position if the boards were to combine and would save the Town money. Discussion ensued regarding the potential cost savings of combining the Police and Fire Fighter Pension Boards. She said the savings would come from having one attorney, one accountant etc. Mr. Elwell provided the history regarding the division of the Town's unified retirement board into two and later into three boards.

George Frick, Palm Beach Police Department, and former Board member when the boards were combined. He indicated part of the reason for the split was due to differing views within Police and Fire Board Members. The Police Department voted to separate and an election would have to take place in order to combine the two boards.

Member Rosow stated that the idea of combining the two boards is a "no-brainer". The Town is guaranteeing benefits to its employees. There should not be a philosophical difference. Chairman Coleman agreed with Member Rosow and added that the Town needs to save money wherever possible.

Mike Hayes, Member of the Fire Fighter Pension Board for 6 years stated that he did not have a problem with combining the two boards, but it would take a formal vote from the Board.

The Committee recommended the topic of combining the Police Officer and Fire Fighter boards be referred back to those boards. This review should include consideration of pooling investments, if the concept of fully combining the boards is not favored. The boards should report their recommendations to the Finance and Taxation Committee at a future meeting.

Jim Karmen, 110 Seaspray Ave., Chairman of General Employee Benefits Board thanked the Committee for the meeting and he offered being open to the employees' ideas, reviewing various costs savings, and his Board is offering any assistance it may be able to provide.

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The Committee Recessed for a lunch break at 1:00 p.m. and resumed at 2:00 p.m.

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e. Impact of DROP Benefit on Town Pension Costs.

Mr. Armstong reported that the DROP program is cost neutral and may actually result in savings to the retirement funds.

2. Discussion of Defined Benefit Plans and Defined Contribution Plans

The following two items were heard after the five minute break at 11:15 a.m. due to the time constraints of Mr. Klausner and Mr. Garvey. Mr. Garvey presented first.

a. Presentation by Mr. Robert Klausner

Town Manager Elwell introduced Mr. Klausner, attorney for the Town of Palm Beach Police Officers Retirement System.

A memorandum from the Police Officers retirement Board was submitted in the back up materials outlining the characteristics, benefits and disadvantages of both Defined Benefit and Defined Contribution Plans.

Mr. Klausner began his presentation by responding to Member Rosow's question regarding the many benefits that government employees receive. The main question should be, What is the purpose of Municipal Government? Of all of the levels of government, municipal government is the one that touches residents most closely. The irony is that a government employee is the greatest bargain for the money.

Government employees are prohibited from making a profit and provide a service to the people. Residents want their garbage collected, to never be seen again. They want Police and Fire when they need them. They want running and clean water when they turn on the tap. Public Parks are beautiful. These are all services that are provided primarily by government entities. Government looks to create stability in its workforce. Defined contribution retirement creates portability among employees. It costs employers money to lose employees that they have spent months, even years training, only to go somewhere else that offers better benefits.

The Town should ensure, for the protection of citizens, that they have loyal, well-trained, experienced workforce that is dedicated to the welfare of the citizens that live in Palm Beach, instead of having employees looking for the better deal in the next City. That has been the trend in defined contribution plan entities- the employees leave when they find something better.

Mr. Klausner also cited examples of States, such as West Virginia, where the defined contribution plan was a disaster, and that state does not contribute into the Social Security System either. Teachers, for example, went to neighboring states to teach, and the school districts were unable to recruit new teachers.

It was his opinion that defined contributions are a risk.

With regard to DROP (Deferred Retirement Option Plans) plans, Mr. Klausner feels that they do save the Town money. From the time the employee participates, there is no more accrual in the pension system.

Mr. Klausner mentioned that the Town's Actuary is doing a very good job and is one of the best actuarial firms. Florida is a heavily regulated state for actuarial certainty. The Town of Palm Beach plans have progressed because of moderate risks. Mr. Klausner indicated he serves over 100 plans, and all are facing short term increased costs, but over time, they will have a stable workforce.

b. Presentation by Mr. Robert Garvey

Mr. Garvey, former Chairman of the General Employee's Retirement System, reiterated that he agrees with the discussion made by Mr. Armstrong that the Town's objectives are critical to achieve.

Mr. Garvey stated that many governments began to move away from defined benefit to defined contribution plans in the past ten years, but have found that the change does not necessarily save the entity money. He cited the City of Fort Lauderdale as one government entity that changed from a defined benefit to defined contribution. He indicated that the City has regretted doing that, as they have seen recruitment decrease, and employees leaving their employ to go to entities that still offer defined benefits. He also cited other states that had moved away from Defined Benefits such as Alaska and California but are now returning to defined benefit plans.

Mr. Garvey also indicated that retirement income security has surpassed race as the most important issue in the United States today. There are 60 million people entering into the retirement system in the next few years. In addition, defined contribution plans tend to cost between 50-100% more than maintaining defined benefit plans.

Member Rosow asked why governments tend to offer defined benefits while the private sector offers defined contributions. He indicated that he is asked this question quite often by residents who have managed companies and did not offer many of the retirement benefits that governments do. Mr. Garvey responded that volatility of the earnings that are impacted by the defined benefit plan, is the main reason companies moved to defined contributions. The voice of employees is less strong in the corporate world. The private sector offers many more entrepreneurial opportunities, such as stock options, partnerships and profit sharing.

Chairman Coleman suggested that perhaps people are attracted to different types of compensation.

Chairman Coleman thanked both Mr. Garvey and Mr. Klausner for coming.

c. General Discussion

Phillip Sweet, 423 Brazilian Ave., thanked the Committee for meeting and indicated it was very informative. He also commended staff on the Annual Financial report that was recently mailed to all residents. He expressed his concern that the Town could not permanently sustain the increase in cost benefits provided to employees.

Joel Brier, 13600 River Water Rd., a union representative of the fire department, made several comments regarding the shift from blue collar workers in the fire department to highly educated and trained individuals. He said there are no defined contribution plans in Palm Beach County government and employees do evaluate the entire benefit package when seeking employment. He was opposed to any change in the current benefit plans. Chairman Coleman indicated that this was not a meeting for decisions but an information session from the actuary and others.

Brad Armstrong commented that the reason government does have benefit plans, is that it helps to eliminate state subsidized programs later on.

Raymond Snow, 255 Monterey Road, speaking as a citizen and not as Chairman of the Police Retirement Pension Board, provided some insight into the colleges and universities. In that sector, there are two tiers with the professors and administrative staff covered under defined contribution plans and the laborers and maintenance staff are covered under a defined benefit plan. It was his understanding that this is how many universities operate today.

Mr. Klausner added that the increase in payroll costs is often objected to by residents. The bottom line is that the government is not in the manufacturing business. Government does not produce a product, they provide a service, and humans provide the service.

IV. HEALTH INSURANCE DISCUSSION

1. Stop Loss Levels

Mr. William Crouse, Human Resources Director announced that the Town has been self-insured since 1978. The Town purchases stop loss insurance to protect itself. There are two types of stop loss insurance that the Town purchases. The program has performed very well for the past thirty years.

Mr. Richard Schell, Area Vice President of Gallagher Bassett Services, has been working with the Town's medical insurance for 8 years. He gave a brief description in the meeting backup of the specific stop loss and the aggregate stop loss.

The specific stop loss is coverage for each employee on the plan. Currently there is a $65,000 deductible for each individuals employee, every plan year. If a claim is over $65,000, the re-insurer will come in and cover the claim up to $5 million dollar maximum benefit per person.

The other type of claim is in the Aggregate. There may be a year with high utilization. For those instances, the Town purchases aggregate re-insurance. There is a 25% re-insurance corridor added to whatever the insurer feels the deductible should be for the Town based on demographics and other factors.

Richard stated that the Town has been at the $65,000 level for several years and they are looking at increasing the deductible to either $75, 85 or 100K for next year. With that is some risk.

Member Rosow indicated he read Mr. Schell's memo and liked it and would like the Committee to recommend to Town Council to adopt a $100,000 deductible, realizing that there is some risk.

2. Status of Retirement Health Savings Plan

Town Manager Elwell informed the Committee that the staff is studying the varying plans and options. In January, all employees will have an opportunity to participate in discussions at a series of meetings to become educated about Medical Savings Plan. Development of the specific proposed plan will follow in February and March.

A proposal will be brought to the April 2009 Town Council meeting for approval.

V. UPDATE ON TOWN RESERVES

1. Overview of Town Reserves

Finance Director Struder indicated that the Committee was provided copies of the budget that described reserves and all the reserve policies that the Town has adopted since 2001. When rating agencies look at the Town, they look at debt ratio and the reserves. The Town currently has a AAA rating.

Member Rosow asked that in a AAA rating, the aggregate reserves are looked at, but there are also contingency reserves, which are approximately 2.5 million dollars. At the end of the year, the money from the contingency reserves that has not been spent go into each of the reserve accounts. He asked at what point is the Town "over reserved".

Chairman Coleman suggested going through each account in declining order for discussion. This would include the next two agenda items.

Health Fund - Chairman Coleman stated that there is 18.9 million. Finance Director Struder clarified that it was the health insurance trust. That money is put aside for retiree health insurance, post-employment benefits. That it is also an actuarial determined amount. Town Manager Elwell added that it is invested similar to the pension funds. Chairman Coleman asked if there is any contingency in that fund and there is not. Finance Director Struder also indicated that the trust is currently underfunded. It should be at 22 million dollars.

Town Manager Elwell clarified that the portion for this year's expenses in operating the health fund is 1.3 million. Finance Director Struder indicated that this amount pays for active employees and the OPEB Trust pays for the retiree health care expenses. In the operating health fund, there is a $500,000 contingency reserve, which is reserved out of overall fund balance for money that can be expended this year if there were to be a catastrophic incident.

Member Rosow wanted to discuss the OPEB further. He stated that are 270 employees that are retired. He asked why there was so much money in the fund. Town Manager Elwell stated it is for the retired employees but also takes into account the 400+ who will be retiring. Member Rosow then asked if Medicare is taken into account, and it is calculated into this figure, and the Town insurance would become secondary. Town Manager Elwell said yes.

Town Manager Elwell gave a brief history of the fund. Approximately 15 years ago, the Town began over funding what was necessary in the health program when it was all one fund. When this was in place for about 10 years, the municipal world had to comply with a new GASB ruling that post-retiree health insurance has to be pre-funded like pensions. Because the Town had already set aside 16-18 million in the fund, we are way ahead of the rest of the municipalities who started with nothing and are working their way up. The Town pension plans, and the OPEB Trust are 80-90% funded and most municipalities are at 0-10% funded for OPEB and struggling to find the money, especially in this economy.

Finance Director Struder indicated that the annual contribution, had we not funded it, would be 2.2-2.3 million instead of the 1.4 -1.6 that we are at now.

Member Rosow asked what the Town does to encourage healthier employees. Finance Director Struder commented that there is a clinic for all employees, the nurse handles lunchtime lectures on different topics, and there is a fitness center. Town Manager Elwell added that there are annual physicals for some employees, weight loss seminars, smoking cessation classes, etc.

Member Rosow thought that there are too many reserve funds in each category and that we may have too much money in the reserves. Town Manager Elwell explained the 25% threshold and that the Town tries to keep enough reserves for at least 3 months of operating expenses. Chairman Coleman asked if the Town has a policy or plan if the Island were to get hit with a Category 4 or 5 storm. If the Town were hit, the Town would not have enough reserves to make repairs. He is hesitant to use revenue bonds unless they are truly needed.

The Committee recommended that staff be directed to develop a catastrophe financial plan.

Next, the Committee discussed the Compensated Absence Fund. Town Manager Elwell stated that the fund is the same concept as the equipment replacement fund. The goal is to flatten out the fluctuations that would occur in the General Fund budget for the variations that can be planned for by having a formula. The fund allows for payouts of vacation and sick time to employees, which is a tiered benefit system. The older employees are compensated at a higher amount when they retire and vacation time when they terminate, while those hired more recently, although still compensated, do not receive the same percentage. This was a change that the Town Council implemented several years ago.

2. Equipment Replacement Fund

Town Manager Elwell explained that the same concept is used here as in the compensated absence fund for all of the rolling stock and computer equipment for the Town. He gave the example of the purchase of the aerial truck for the Fire Rescue Department. The Town would not have been able to absorb the one million dollar cost with the current economy, had this not been planned out. If the reserves had not been there, the Town would have had to borrow money for the purchase and pay it off over time. It relates primarily to larger purchases. Department Directors have been directed to be fiscally conscious, replace older vehicles with more fuel efficient and smaller ones, if possible, and staff is also monitored to make sure that they are not overspending. There is 11 million dollars in this fund.

The Committee recommended that staff re-evaluate the replacement costs each year to ensure proper long term funding of this program.

Member Rosow asked when it comes to purchasing new equipment, does staff look at purchasing an item that perhaps could replace several other pieces of machinery? Paul Brazil, Director of Public Works, stated that the example Member Rosow gave of the purchase of the vac truck was a very good one. That vehicle, although it cost over $300,000, has many more uses than just vacuuming sewage from pump stations. It also does many other smaller jobs such as spills, locates utility lines etc. On the other hand, there are pieces of equipment that are time-saving, but only perform one job.

Recreation Enterprise Fund - Finance Director Struder advised that the next four items on the Reserve Balances chart are Recreation Reserves. The 25% reserve of revenues is the amount currently in the fund. The Recreation Department has an equipment replacement fund, based on the same principles, the dock replacement fund was established when the marinas were rebuilt. There was debt being paid on those. The debt was paid off and it was decided to create a replacement fund to have the money available in the future for any dock replacement.

Chairman Coleman asked if that number is reviewed. Finance Director Struder advised that the number is locked.

The Committee recommended staff review this fund periodically to consider replacement costs. (Not necessarily every year).

The M & I reserve is a maintenance and improvement reserve that is collected by the people that play at the Par 3 Golf Course and it has been built up to help pay for improvements at the Par 3. That money can be used to offset the two million for the rehab of the golf course.

Member Rosow asked if there should be the same type of reserve fund for Tennis. It would benefit the people who play tennis. **The Committee recommended staff look into creating a Tennis M & I Reserve Fund.**

3. Risk Fund

Finance Director Struder explained that there is $5.9 Million in the Risk Fund. Of that, $2.5 million is the reserve for catastrophic exposures, which in the past has been used to pay for lawsuits, and used for hurricane expenses.

Chairman Coleman asked if it was possible to go to the voters to ask for standing authorization for general obligations to be only issued during emergencies. Town Manager Elwell responded that you could not as there are restricted windows of time after the voter approval to issue the debt, but he would be willing to look into it further.

Deputy Town Manager Tom Bradford explained that some of the expenditures from this fund are for lawsuits, judgments, replacement of streetlights if there is a hit and run etc.

Member Rosow requested that future budgets include more detailed information about reserves, including specific additions and reductions to each reserve fund. Chairman Coleman requested a breakdown of the line items for inter-fund transfers, as well. Member Rosow also suggested that the next Annual Financial Report of the Town better explain what the reserve balances are and why they are there.

Deputy Manager Bradford explained that the risk fund is partially self-insured, which is somewhat predictable, and for other things such as property, the Town is not. The items that could have catastrophic consequences such as property are not self-insured. There is an actuarial analysis every two years of the risk fund, relative to claims and the life of the claim. Using round numbers, with a 75% confidence level, the last study was in 2006 and it stated there needed to be $3 million dollars and there is currently $2.7 million in undesignated fund balance which is used to pay unrealized claims. The next study will be ready in the spring of 2009 and if it needs to be modified, it will come before Town Council. The concept of Average Annual Funding. Smoothing is something that the Council should think about doing for this particular fund once we think we are at a place where we can fund it without hurting the Town.

VI. REVIEW OF EXTRAORDINARY LONGEVITY BENEFIT

Member Rosow asked if the extraordinary longevity pay was added into the pension figures and Town Manager Elwell indicated that it was. Both Chairman Coleman and member Rosow agreed that this benefit is excessive.

Committee recommends to Town Council to eliminate the extraordinary longevity pay program.

VII. ANY OTHER MATTERS

There were none.

VIII. ADJOURNMENT

There being no further business, the Finance and Taxation Committee Meeting was adjourned at 3:00 p.m.

Denis P. Coleman
Committee Chair

David A. Rosow
Committee Member