

SUPPLEMENTAL

COUNCIL AGENDA: 06-19-07
ITEM: 3.4



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Les White

SUBJECT: RETIREMENT ENHANCEMENTS

DATE: June 18, 2007

SUPPLEMENTAL MEMORANDUM

Reason for Supplemental

The Association of Retired San Jose Police Officers & Firefighters submitted a letter dated June 14, 2007 (attached), regarding the request for benefit enhancements that is on the June 19th City Council agenda. The letter indicates that the Association has made revisions to their requests for benefit enhancements resulting in a revised cost estimate.

The purpose of this supplemental memorandum is to ensure that the entire City Council has the information provided by the Association and the Administration's response.

Recommendation

- (a) Acceptance of the Administration's recommendation to NOT approve the benefit enhancements requested by the Association of Retired San Jose Police Officers and Firefighters (Police and Fire Retirees).
- (b) Acceptance of the Administration's recommendation to NOT approve the benefit enhancements requested by the San Jose Retired Employees Association (Federated Retirees).

Background

Both the Association of Retired San Jose Police Officers & Firefighters and the San Jose Federated Retired Employees Association have made requests for benefit enhancements. The item was originally on the May 22nd City Council agenda and was deferred to June 19th. A copy of the initial Council memo is attached and includes a description of the specific benefit enhancement requests.

Analysis

The Association of Retired San Jose Police Officers & Firefighters indicates that they have dropped their request to provide after-retirement spouses with survivorship pensions. The two remaining benefits are as follows:

1. Provide medical and dental benefits for after-retirement spouses.

The estimated on-going annual cost of this benefit is .029% of payroll, which is approximately \$63,371 per year.

2. Provide surviving spouse with medical insurances at no-cost and provide full reimbursement for Medicare Part B premiums.

The estimated on-going annual cost of this benefit is .08% of payroll, which is approximately \$174,817 per year.

The total estimated on-going annual cost of these two benefits is .109% of payroll, which is approximately **\$238,188 per year**.

The Association contends that a "credit" in the amount of \$227,262 or 0.104% of payroll, should be applied to reduce the cost of the benefit enhancement requests. The Association states that after applying the \$227,262 "credit," the ongoing annual cost of providing their amended benefit enhancements would be \$10,926 per year or 0.005% of payroll.

This "credit" is referenced in the Retirement Board's actuarial report, and the Department of Retirement Services has indicated that this "credit" would be applied regardless of the implementation of any benefit enhancement. Therefore, the "credit" should not be applied to the cost of the requested benefit. The estimated **ongoing annual** cost of providing these benefit enhancements would be \$238,188 or 0.109% of payroll.

The City's defined benefit retirement plans provide a certain level of benefits regardless of investment returns or the amount contributed by employees. The plans experience actuarial gains and losses based on many factors. Any actuarial gain (or "credit") should not be relied upon to fund additional benefits since the benefit enhancements result in ongoing costs regardless of whether or not the plan experiences actuarial losses in the future.

The rising cost of the City's retirement plans is a significant concern. In 2000, the City's contribution rate was 16.09% of pensionable compensation for the Federated City Employees' Retirement System and 15.70% for the Police and Fire Department

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Retirement Plan. Currently, the City's contribution rates are 21.98% for Federated, 28.51% for Police and 25.22% for Fire. This represents an increase of approximately 37%, 82%, and 61%, respectively. (Retirement benefit increases for sworn Fire personnel are subject to the pending arbitration.)

In addition to the cost of the pension benefits, the cost of retiree health care in both retirement plans has been estimated to be as high as \$1.4 billion. Given this context and that the particular benefit enhancements are not common benefits provided by comparable pension plans, the Administration does not recommend approving any of the benefit enhancement requests. As indicated in the initial Council memo, if the Council were to approve these requests, they would only apply to current retirees and would not apply to any current employee that has not yet retired. Extending these benefits to future retirees would further increase the costs.



LES WHITE
City Manager

For questions please contact me at (408) 535-8111.

Attachments



June 14, 2007

Hon. Chuck Reed
200 E. Santa Clara Street
San Jose, CA 95113

Dear Mayor Reed:

At our request, the Police and Fire Retirement Board contracted for an actuarial study to be conducted that resulted in the discovery of an unanticipated annual gain to the retirement plan of \$227,000. These dollars could be utilized to significantly offset the costs of providing benefits to surviving spouses who are struggling to make ends meet and are trying to live out their lives with dignity.

In the attached report, the SEGAL company conducted a detailed actuarial analysis to determine the cost of our proposal. Their analysis discovered an inaccuracy in the methodology used to calculate the cost of survivorship benefits, creating a "credit" for the City in the amount of 0.104% of payroll, or \$227,262 per year.¹

Based on this credit and the difficult budget situation the City is in, we are officially amending our request to the City Council to:

- 1. Drop our request to provide "after retirement" spouses with survivorship pensions. This would reduce the cost of our request by \$478,561;²**
- 2. Provide medical and dental benefits for "after retirement" spouses; and³**
- 3. Provide surviving spouses with medical insurance at no cost and provide full reimbursement of Medicare Part B premiums.⁴**

The estimated cost of our revised proposal, based on the SEGAL analysis is \$238,188. Therefore, by applying the \$227,262 credit towards this benefit, a funding gap of only \$10,926 exists. It is important to point out that the yearly \$227,262 credit to the retirement plan does not belong to the City's General Fund, thus applying the credit towards our proposal has zero General Fund budget impact.

¹ SEGAL Letter, Pg. 3, shown in table as "Actuarial gain from revision of automatic continuance indicator" estimated at -0.10% of payroll and -0.004% of payroll for a total of -0.014% of payroll or \$227,262 credit to the Fund.

² City Manager's Memorandum, May 2, 2007, page 4.

³ SEGAL Letter, pg. 3 calculated as both City and Employee's share of Medical & Dental Plans. Cost, estimated at 0.029% of payroll or \$63,371.

⁴ SEGAL Letter, pg. 5 calculated as both City and Employee's share of cost, estimated at 0.08% of payroll or \$174,817.

Our proposal aims to provide basic health insurance protections to surviving spouses, including those survivors who were married after an employee's retirement. Current survivors face rising health care premiums after their spouse passes away and their survivorship pension is reduced by roughly 50%. In the case of "after retirement" spouses, once the retiree passes away, their health and dental insurance, and pension benefits are immediately cut, forcing them to grapple with an average of \$500 per month in health care premiums just to remain covered.

These are catastrophic circumstances for these widows, many of whom cared for our former police officers and fire fighters through trying conditions, such as cancer, post-traumatic stress, and other disabilities. The result of their sacrifices is that they are on the brink of financial disaster. We would like to help them live out their final years in dignity.

On behalf of the 2,000 members of our association, thank you in advance for your consideration of our proposal. We look forward to discussing this in more detail. Please feel free to contact me at (408) 833-4291 to answer any questions.

Sincerely,

Jack Salois
Director



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Les White

SUBJECT: RETIREMENT ENHANCEMENTS

DATE: May 2, 2007

COUNCIL DISTRICT: City-Wide
SNI AREA: N/A

RECOMMENDATION

Accept the Administration's recommendation not to approve the benefit enhancements requested by the Association of Retired San Jose Police Officers and Firefighters (Police and Fire Retirees) and the San Jose Retired Employees Association (Federated Retirees).

OUTCOME

The City Council will have an opportunity to review and consider the benefit enhancements requested by the Police and Fire Retirees and the Federated Retirees.

EXECUTIVE SUMMARY

Both the Police and Fire Retirees and the Federated Retirees have requested several benefit enhancements. The first enhancement requested by the Police and Fire Retirees would be to change the definition of surviving spouse to include those individuals who married after retirement. The second requested enhancement is to provide surviving spouses with medical insurance at no cost, including full reimbursement of Medicare Part B premiums. The Federated Retirees have requested an enhancement to provide current Federated retirees with reimbursement for Medicare Part B premiums.

Due to the City's current financial situation, GASB liability estimated at \$1.4 billion, and continuing increases in health care costs, the Administration does not recommend approving any of the requests for enhancements submitted by the retiree associations.

The table below details the annual cost of providing these benefits enhancements to *current retirees only*:

Annual Cost of Providing the Requested Benefit Enhancements		
Benefit Enhancements	Federated	Police and Fire
Expand the Definition of Surviving Spouse	N/A	\$479K
Provide Medical Insurance at No Cost	N/A	\$175K
Provide Reimbursement of Medicare Part B Premiums	\$754K	N/A
TOTAL ONGOING ANNUAL COST *	\$754K (.30% of Payroll)	\$654K (0.299% of Payroll)

* NOTE: The annual cost is based on the 2006-2007 payroll figures.

BACKGROUND

Generally, retirees receive those benefits that are in effect at the time of retirement unless the City Council decides to enhance benefits for persons who have already retired. When a benefit enhancement is being considered for current employees during the negotiations with the bargaining units, a request is normally made that the Retirement Boards' actuary also provide the additional cost of extending the benefit to existing retirees. After the negotiations, the City Council can then consider enhancing benefits for existing retirees.

Although the City is not obligated to make changes to retirement benefits for existing retirees, the City Council can approve changes that apply only to current retirees. In 1998, the City Council established an administrative process for representatives from the Retiree Associations to meet with the City Manager and communicate issues and concerns. If issues are raised that are within the scope of the meet and confer process, these issues could be addressed with the bargaining groups and costs could be obtained from the actuaries. By utilizing this established process, the City has a better understanding of the total costs to the Retirement System and the resulting impacts on the General Fund.

The City provides two defined benefit plans, one covering police officers and firefighters and the other covering all other full-time employees. Both plans provide retirement, disability, survivorship and health benefits. Both the Police and Fire Retirees and the Federated Retirees have recently made a request for several benefit enhancements for current retirees. Initially the Police and Fire Retirees requested a third benefit to provide full reimbursement of Medicare Part B Premiums for retirees as well as surviving spouses that had an annual cost of \$1.22M. However, the Police and Fire Retirees have elected not to pursue this request.

In accordance with the established administrative process with the Retired Employee Associations, two separate meetings were scheduled with representatives from each Retiree Association. Both Associations requested that the Retirement Plans be amended to provide additional benefits to retired members who qualify.

Association of Retired San Jose Police Officers and Firefighters

- Change the definition of survivor to include those individuals who married after retirement, which would result in the City providing medical, dental and survivor benefits for spouses of retirees regardless of whether the retiree was married to the spouse at the time of retirement.
- Provide surviving spouses with medical insurance at no cost and provide full reimbursement of Medicare Part B premiums for surviving spouses.

San Jose Federated Retired Employees Association

- Provide current retirees with reimbursement for Medicare Part B.

These requests come at a time when the City is faced with increased retirement and health care costs for both active and retired employees. In addition, the City will need to make a decision on its GASB liability for retiree health, as required by accounting standards; as well as explore options to maintain or reduce retirement and health care costs. As the City decides how to address these increasing costs, it was explained to representatives from each retiree association that a recommendation to approve these enhanced benefits will not be made.

ANALYSIS

The Association of Retired San Jose Police Officers and Firefighters has requested a change to the definition of surviving spouse to include those individuals who married after retirement. This change would result in the City providing medical, dental and survivor benefits for spouses of retirees regardless of whether the retiree was married to the spouse at the time of retirement. In addition, the Police and Fire Retirees Association has also requested that surviving spouses be provided with medical insurance at no cost, including reimbursement for Medicare Part B premiums. The Federated Retirees Association has requested that the City provide current Federated retirees with reimbursement for Medicare Part B premiums.

Changing the definition of a surviving spouse

Although the Police and Fire Retirement Plan currently does not extend survivorship benefits to a spouse acquired after the member retires as a matter of right, the plan does include an option whereby survivorship benefits can be provided. Section 3.36.1468 of the San Jose Municipal Code provides that a retiree who marries after retirement may elect an optional settlement to reduce the retiree's monthly allowance to provide a lifetime benefit to the surviving spouse upon the retiree's death.

The request to change the definition of surviving spouse would only apply to existing retirees and would not apply to future retirees, because changes for future retirees are negotiated by the Police Officers' Association (POA) and/or International Association of Fire Fighters (IAFF, Local 230). Providing this benefit enhancement only to current retirees would result in these retirees receiving a benefit that future retirees will not receive. Employees who retire on or

before the effective date would receive this benefit enhancement, but anyone who retires the very next day or thereafter would not.

It would be more appropriate for the requested benefit enhancements first to be negotiated between the City and the POA and IAFF, Local 230 for active employees. According to the established communication process with the Retiree Associations, the Retiree Association would meet with the City Manager or the Manager's designee on recommended benefit enhancements for retirees prior to negotiations with the POA and/or IAFF, Local 230. These benefit enhancements could then be proposed during negotiations. If an agreement were reached on a particular benefit enhancement during the negotiation process, it would only apply to current employees and would not extend to persons already retired. However, the City Council could then decide to extend the benefit enhancement to persons who are already retired. To determine the cost of extending a benefit to retirees, a request would be made to the Retirement Board's actuary to complete an actuarial analysis to determine the additional cost of extending such benefit to existing retirees. This process provides continuity in the benefit enhancements for all retirees and prevents any gap in coverage between current retirees and future retirees.

Although retirees are requesting this additional benefit, research shows that none of the comparable agencies the City uses for its surveys (the top ten largest cities in California as well as the Bay Area cities with populations of 100,000 or more) provide this benefit. Some of the agencies surveyed do provide a survivorship benefit to spouses of retirees married after retirement, however, like the City of San Jose, these agencies require that the retirees take an actuarial reduction in their monthly benefit. Some counties in California provide survivorship benefits in the case of marriage after retirement, but they require a minimum retirement age and specific length of marriage. However, these agencies are not comparable jurisdictions surveyed by the City of San Jose.

The Police and Fire Retirement Plan's actuary, The Segal Company, completed an actuarial analysis on this benefit and determined that the ongoing annual cost of this benefit for current retirees would be approximately \$478,561 or 0.219% of payroll. This only includes the cost of providing the enhancement to current spouses of retirees who were married after retirement, which is currently 39 individuals. The cost analysis does not anticipate the cost of any additional beneficiaries yet to be identified by the system or any new beneficiaries who may become eligible by marrying a retiree in the future.

Provide surviving spouses with medical insurance at no cost and provide reimbursement of Medicare Part B premiums for current surviving spouses

The second request submitted by the Police and Fire Retirees includes a request to provide surviving spouses with medical insurance at no cost, which includes full reimbursement of Medicare Part B premiums for surviving spouses. Currently, medical and dental benefits are extended to a surviving spouse if the retiree had at least 15 years of service and the retiree and spouse were married at the time of retirement. Premiums for health insurance are divided between the retiree and the Retirement Plan. The portion of the premium paid by the Retirement Plan is equivalent to 100% of the premium for the lowest priced plan available to active City employees; the retiree or surviving spouse pays the difference between that

amount and the premium for the health plan selected by the retiree. At age 65, a retiree or surviving spouse is required to enroll in Medicare Part A and B. Once enrolled in Medicare the premiums for medical plans are reduced because they are subsidized by Medicare Part A. The difference between the Medicare reduced premium and the Retirement Plan's contribution may be applied toward reimbursement of Medicare Part B premiums.

For example, a surviving spouse over the age of 65 enrolls in Blue Shield Medicare HMO. The monthly premium for Blue Shield Medicare HMO is \$301.21. The Retirement Plan's monthly contribution, based on the lowest priced plan is \$399.28. Pursuant to Section 3.36.1920 of the San Jose Municipal Code, the Plan will reimburse members, former members and survivors for the amounts paid for Medicare Part B coverage as long as the total payment does not exceed the cost of the lowest priced plan. Therefore, the members can receive a reimbursement of up to \$98.07 per month for the Medicare Part B premium. The current cost of Medicare Part B coverage is a minimum of \$93.50 per month.

The City provides a variety of medical plans for retirees and surviving spouses to choose from based on their needs or preferences. The 100% of the cost of the lowest priced plan that is paid by the Retirement Plan exceeds the health benefits provided to active employees, because active employees currently pay 10% of the premium cost up to a maximum dollar amount (maximum employee contribution varies by bargaining group). Providing these benefit enhancements only to current retirees as has been requested would create a gap in coverage between current retirees and future retirees.

The Police and Fire Department Retirement Plan's actuary completed an actuarial analysis to determine the estimated cost of providing medical insurance at no cost, which includes full reimbursement of Medicare Part B premiums for surviving spouses. The ongoing annual cost of this enhancement would be \$174,816 or 0.08% of payroll. The annual combined cost of changing the definition of surviving spouses and providing medical insurance at no cost, including full reimbursement of Medicare Part B premiums would total \$653,377 or 0.299% of payroll.

The Police and Fire Retirees have suggested that the estimated annual cost of providing these benefits can be paid for with the Police and Fire Retirement Fund's \$25 million "savings" for the fiscal year 2006-2007. However, the referenced \$25 million is not "savings." The \$25 million difference is the result of the City's projected contribution rate not increasing as much as was previously forecasted. If the City were to spend the \$25 million in "savings", the City's structural budget deficit would be \$25 million more than it otherwise would be.

Provide current Federated retirees with reimbursement for Medicare Part B

The request submitted by the Federated Retirees asks that retirees be provided with reimbursement of Medicare Part B premiums. Currently, members of the Police and Fire Department Retirement Plan who have retired receive such reimbursement subject to certain limitations, pursuant to Section 3.36.1920 of the San Jose Municipal Code.

The Federated Retirement Board requested that its actuary, Gabriel Roeder Smith & Company (GRS), conduct an actuarial study. The purpose of this study was to determine the cost and

increase in the annual required contribution if this benefit enhancement were provided to current retirees only. GRS also completed an actuarial analysis to determine the cost of providing this benefit to both current and future retirees. According to the report provided by GRS on December 7, 2006, if this benefit enhancement were provided to current retirees only, the estimated ongoing annual cost would be \$753,535 or 0.3% of payroll. If this benefit were extended to both current and future retirees the estimated annual ongoing cost would be \$1,619,638 or 0.6% of payroll.

Conclusion

Given the City's current fiscal situation, the estimated GASB liability of approximately \$1.4 billion, increasing health care costs, and the City's focus on implementing cost containment measures, it is recommended that these benefits not be approved.

PUBLIC OUTREACH/INTEREST

The purpose of this section is to describe discussions that have occurred with the public, stakeholders, community groups and/or other governmental agencies. Staff is asked to use the following checklist to determine if items are to be considered items of "Significant Public Interest", thus requiring additional notification per the matrix below. Please note the outreach that was done.

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

These modes of notification should only supplement outreach efforts that are undertaken or are planned to be undertaken. Additional outreach should be noted as a result of the determination that the item was of "Significant Public Interest".

Public Outreach does not apply to this item; however, this memorandum will be placed on the City website for the May 22, 2007 Council Agenda.

COORDINATION

This report was coordinated with the Department of Retirement Services, Human Resources Department, and the City Attorney's Office.

COST SUMMARY/IMPLICATIONS

Providing these benefit enhancements to current retirees has significant ongoing annual cost implications to the City. The following chart summarizes the costs for providing the benefits requested by both of these retiree associations.

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TOTAL ONGOING ANNUAL COST *	\$754K (.30% of Payroll)	\$654K (0.299% of Payroll)

* NOTE: The annual cost is based on the 2006-2007 payroll figures.

CEQA

Not a project.



Les White
City Manager

For questions please contact Alex Gurza, Director of Employee Relations at 535-8155.