



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Councilmember  
Donald Rocha

**SUBJECT:** RETIREMENT REFORM

**DATE:** May 20, 2011

Approved

*Don Rocha*

Date

*5/20/11*

## INTRODUCTION

I offer this memorandum as an additional proposal to address the grave structural problems of our retirement system. I agree with some aspects of the memo authored by the Mayor, Vice Mayor and Councilmembers Herrera and Liccardo on this subject, and welcome their direct offer, as stated in their memo, to “engage constructively with alternative solutions.” In that spirit, I propose an alternative solution that I would like staff to analyze. My preference is to avoid as much legal risk and financial loss as possible. We have a potential opportunity for real and responsible fiscal reform and time is of the essence given our current budget situation. It is in our best interest to pursue policies that are most likely to succeed, and proposing government-by-formula charter amendments of the sort that have made California very difficult to govern is not a path I wish to see for the City of San Jose. Therefore, I propose that we adopt the City Manager’s Fiscal Reform plan, with the amendment that we direct staff to prepare both the alternative proposed in my colleague’s memo and the alternative I propose in this memo for side-by-side comparison at the Council’s June 21<sup>st</sup> meeting.

## RECOMMENDATION

Approve the City Manager’s Fiscal Reform Plan, with the amendment that staff be directed to bring back: (1) the proposal recommended in the May 13<sup>th</sup> memo issued by my colleagues and (2) my proposal, described below, for side-by-side consideration at the Council’s June 21<sup>st</sup> meeting.

### **1. First Tier Retirement Reform for Actives**

Direct the City Manager, in consultation with the Retirement Services Director, to design a 2<sup>nd</sup> tier opt-in proposal for the 2<sup>nd</sup> tier plan outlined in Recommendation 3. Such a plan should:

- a. Evaluate the full range of mechanisms by which the City can influence employees to opt into the 2<sup>nd</sup> tier.
- b. Make a proposal as to how 1<sup>st</sup> tier benefits would be treated when an employee opts into the 2<sup>nd</sup> tier.
- c. Make best efforts to gauge potential opt-in cost savings for the 2<sup>nd</sup> tier option discussed in Recommendation 3, similar to the analysis of opt-in cost savings provided in the staff presentation at the May 18<sup>th</sup> budget study session.
- d. Prioritize policy alternatives that minimize legal risk.

**2. First Tier Retirement Reform for Current and Future Retirees**

Direct the City Manager and City Attorney to develop a proposal for changes for current and future 1<sup>st</sup> tier retirees as follows:

- a. Bring forward an amendment to City ordinance that reduces the Cost of Living Adjustment (COLA) to a fixed 1.5% per year increase.
- b. Report back to Council as to whether, other than the COLA, there are benefit enhancements awarded to retirees after the date of retirement that could be rolled back in order to reduce pension costs.

**3. Second Tier Retirement System**

Direct the City Manager to develop cost estimates for 2<sup>nd</sup> tier defined benefit retirement plans. Cost estimates should be provided for both Federated and Police and Fire Retirement Plans based on the below defined benefit plan framework. For each plan, staff should develop two cost estimates, one assuming investment returns with a 50% likelihood of success, and one assuming 75%.

Benefit	Recommendation
Retirement Age	<u>Federated</u> : 62 <u>Public Safety</u> : 57
Early Retirement Reductions	Allow early retirement provided that the benefit does not exceed the actuarial value of full retirement.
Formula	<u>Federated</u> : 2% per year of service for 30 years, to a maximum of 60% of final salary <u>Public Safety</u> : 2½% per year of service for 30 years, to a maximum of 70% of final salary
COLA	Tied to Bay Area CPI and capped at 1.5%
City/Employee Share of Costs	50/50 split for 2 <sup>nd</sup> tier normal costs and unfunded liability
Final Salary	Final 3 year average
Health Care	Employees receive a fixed dollar amount for retiree healthcare costs based on how many years of service they have when they retire (as recommended by staff in the last paragraph of page 41 of MBA #1).
Service Credit	Change the definition of one year of service from 1739 pensionable hours to the number of hours typical Federated and typical Public Safety full time employees work per year.
Opt-in	Design an opt-in program for 1 <sup>st</sup> tier employees and make best efforts to analyze potential opt-in cost savings, as outlined in Recommendation 1.

#### 4. **Analysis of CALPERS Alternative**

Direct staff to contact CALPERS and bring back to the Council the various options available for a current member agency to opt into the CALPERS system with the associated costs and projected savings from the various options.

### **ANALYSIS**

#### **First Tier Reform for Actives**

I believe that an opt-in approach to 1<sup>st</sup> tier reform is a more certain path to budget savings than pursuing potentially vested 1<sup>st</sup> tier benefit reductions through a ballot measure and expected court challenge. It's impossible to know the outcome of a court case, but we do know that a ruling against the City would wipe out planned budget savings and put us back to square one. I'm not ready to gamble the City's future on a court battle. An opt-in system that gives employees incentives to choose the 2<sup>nd</sup> tier—as well as some disincentives to stay in the 1<sup>st</sup>—has the potential to deliver significant budget savings without a lengthy and costly legal dispute.

#### **First Tier Reform for Current and Future Retirees**

Unfortunately, in the case of 1<sup>st</sup> tier retirees, we don't have the opportunity to pursue an opt-in system. With no better option in front of us, I agree with my colleagues that we need to reduce the COLA, and in addition consider rolling back other benefits awarded after the date of retirement. Reducing the COLA isn't fair to retirees, I agree, but neither is reducing or eliminating services that the public has invested in and that have public health and safety implications. San Jose can continue to be a great city, but for that to happen, all of us must make some sacrifice—taxpayers, employees, and retirees alike.

I recommend we pursue a COLA change by ordinance instead of at the ballot. If the Council can accomplish the change on its own, I don't believe that we should spend money on an election, especially when we already have a mandate from the public for reform. If for some reason it is not possible to make this change by ordinance, I would support consideration of a ballot measure as suggested by my colleagues.

#### **Second Tier Option**

We have the opportunity, and I would argue the responsibility, to direct our staff to develop information on a range of viable options before choosing a course of action. At the May 18<sup>th</sup> study session, I made the case for consideration of multiple policy options before making a decision, and the City Manager offered this Council meeting as the venue to make that request. In that spirit, I propose directing staff to return with information on a defined benefit retirement system.

For the defined benefit system, I propose a list of plan criteria and request that staff cost out the proposal. In starting with plan design and working to cost, I'm reversing staff's usual approach of starting with cost and working towards plan design. This approach is intentional: only focusing on cost is just as one-dimensional as focusing only on benefits. As an employer, we must consider both—we need a plan we can afford, but also one that offers a livable retirement. Costing out reduced, but still reasonable benefits, will provide the Council with a useful data point to guide well-informed decision making.

I also ask that staff investigate the idea of opting into CALPERS. As a current member agency (Mayor and City Council are members of CALPERS) we should explore the potential savings of joining that retirement system.

### **Section C of My Colleagues' Memo**

As I hope I have shown in the above recommendations, I have made an honest attempt to incorporate recommendations made by my colleagues and craft a true compromise. However, I want to take a moment to voice my strongest possible disagreement with Section C of their memo. This section would implement government by formula in San Jose, preventing elected officials from making even the most basic decisions necessary to govern the City. The restrictions are referred to as temporary, but the language is written such that the temporary circumstance could persist for decades. The most concerning provision, item c, would prevent the Council from raising pay for members of any bargaining unit. Determining employee pay is one of the most basic functions of governance; if we give up that responsibility, we give up the job we were elected to perform. Successful representative democracy depends on publicly accountable elected officials who can exercise judgment under complex circumstances. Again, the State of California is a living example of the dysfunction that can result when we take away the ability of elected officials to govern basic functions and operations.

### **Conclusion**

We all recognize the unique position that we as elected officials find ourselves in. While balancing the needs of our residents with the need to value the employees who contribute to the service of those community needs, we have an opportunity to rebuild a broken system, and to do so with vision, dignity, and effective discourse. Fiscal reforms, if done correctly, will ensure that our City functions efficiently during any economic situation, good or bad. In my opinion, this option includes significant fiscal reform measures, and I appreciate the Mayor, fellow Councilmembers, and the City Manager for their leadership and commitment to this effort as priority number one for San Jose and its residents.

As policy makers we strive to make the best and most effective policies into realities for our community. I am concerned that if we limit the pool of options that we make those decisions from, we limit our ability to make a decision with all options considered. It is for that reason that I am asking us to bring forward an additional course of action as an option for Council consideration. The attached chart is provided as a convenient way of comparing my recommendations to the ones made in the May 13<sup>th</sup> memo.

# Reform Recommendations and Analysis

## 1<sup>st</sup> Tier Actives

Sec.	May 13 memo Recommendation	Sec.	Proposed Alternative
A	Attempt to alter or take away vested rights through a Charter amendment	1	Design opt-in system for existing employees to transition into the 2 <sup>nd</sup> tier system

## 1<sup>st</sup> Tier Retirees

Sec.	May 13 memo Recommendation	Sec.	Proposed Alternative
B3	COLA tied to CPI and capped at 1%	2	COLA fixed at 1.5%

## 2<sup>nd</sup> Tier

Benefit	Sec.	May 13 memo Recommendation	Sec	Proposed Alternative <small>(Note: for further study and cost analysis)</small>
Retirement Age	B1	Federated: 65 PS: 60	3	Federated: 62 PS: 57
Early Retirement Reductions	B1	Early retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.	3	Accept memo recommendation
Formula	B2	No level specified	3	Federated: 2% per year of service for 30 years, to a maximum of 60% of final salary Public Safety: 2 1/3% per year of service for 30 years, to a maximum of 70% of final salary
COLA	B3	Tier 2: No level specified Tier 1: Capped at 1% and tied to CPI	3	Tied to Bay Area CPI and capped at 1.5%

## Reform Recommendations and Analysis

Benefit	Sec.	May 13 memo Recommendation	Sec	Proposed Alternative <small>(Note: for further study and cost analysis)</small>
Share of Normal Costs	4E	50/50	3	50/50 split for 2 <sup>nd</sup> tier normal costs and unfunded liability
Pension Amount		No level specified	3	Final 3 year average
Health Care	B2	20 year vesting	3	Employees receive a fixed dollar amount for retiree healthcare costs based on how many years of service they have when they retire (as recommended by staff in the last paragraph of page 41 of MBA #1)
Service Credit	--	No level specified	3	Change the definition of one year of service from 1739 pensional hours to the number of hours typical Federated and typical Public Safety full time employees work per year.
Additional limitations	4a-e	Adopt Charter-level benefits for Tier 1 employees who have not opted into Tier 2 if the unfunded liability surpasses 6/30/10 levels	1	Pursue opt-in approach
Implementation Provisions	C	Require voter approval of increases in other benefits until essential services have been restored	--	Reject