CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Office of the City Manager
EMPLOYEE RELATIONS

September 9, 2011

Yolanda Cruz
President
Municipal Employees' Federation, AFSCME Local 101
c/o Library Department
150 E. San Fernando Street
San Jose, CA 95112

LaVerne Washington
President
Confidential Employees' Organization, AFSCME Local 101
c/o City Attorney's Office
200 East Santa Clara Street
San Jose, CA 95113

RE: Revised Draft Proposed Ballot Measure

Dear Yolanda & LaVerne:

On July 6, 2011, the City provided MEF and CEO a copy of the draft proposed ballot measure that incorporates the relevant elements from the May 13th memo and City Manager's Fiscal Reform Plan, as approved by the City Council. Since then, in part based upon feedback and questions the City has received from some bargaining units, the City Council has provided additional direction regarding the draft proposed ballot measure. Enclosed please find the revised draft proposed ballot measure that incorporates the City Council direction.

The City is open to discussing any changes to the enclosed revised draft proposed ballot measure. Our last negotiation regarding this matter was held on August 3rd, and the City is open to scheduling additional meetings to discuss the revised draft proposed ballot measure, including any proposed changes that you may have. Please notify us as soon as possible if AFSCME would like to schedule additional meetings.

The City expressly reserves the right to propose other charter amendments pertaining to retirement issues, or to make changes to the attached draft ballot measure.

If you have any questions or concerns regarding this information, please do not hesitate to contact me.

Sincerely,

Gina Donnelly
Deputy Director of Employee Relations

c: Alex Gurza, Deputy City Manager
Charles Allen, Business Agent, AFSCME

Enclosure

DRAFT- September 9, 2011

PUBLIC EMPLOYEE PENSION PLAN AMENDMENTS - TO ENSURE FAIR AND SUSTAINABLE RETIREMENT BENEFITS WHILE PRESERVING ESSENTIAL CITY SERVICES

The Citizens of the City of San Jose do hereby enact the following amendments to the City Charter which may be referred to as: *"The Employee Fair Pay Act for Fiscal Sustainability."*

Section 1: FINDINGS

The following services are essential to the health, safety, quality of life and well-being of San Jose residents: police protection; fire protection; street maintenance; libraries; and community centers (hereafter "Essential City Services").

The City's ability to provide its citizens with Essential City Services has been and continues to be threatened by budget cuts caused mainly by the climbing costs of employee benefit programs, and exacerbated by the economic crisis. The employer cost of the City's retirement plans is expected to increase dramatically in the near future. In addition, the City's accrued unfunded liability for other post employment benefits – primarily health benefits – is similarly increasing. To adequately fund these costs, the City would be required to make dramatic cuts to Essential City Services.

These cuts to Essential City Services have already created a public service emergency in the current fiscal year, an emergency that is projected to worsen significantly in Fiscal Year 2012-2013 and beyond. Because the cost of retirement benefits is rising so rapidly, and current economic conditions and legal restrictions severely limit revenue growth, there is no

reasonable prospect that further critical reductions in Essential City Services can be avoided. By any measure, projected levels of services are unsustainable, and endanger the health, safety and well-being of the residents of San Jose.

Without the reasonable cost containment provided in this Act, the economic viability of the City, and hence, the City's employment benefit programs, will be placed at an imminent risk.

The City and its residents always intended that its pension and post employment benefit plans be fair, reasonable and subject to the City's ability to pay without jeopardizing City services. At the same time, the City is and must remain committed to preserving the health, safety and well-being of its residents.

By this Act, the voters find and declare that pension and other post-employment benefits must be adjusted in a manner that protects the City's viability and public safety, at the same time allowing for the continuation of fair post-employment benefits for its workers.

This Act is intended to strengthen the finances of the City to ensure the City's sustained ability to fund a reasonable level of benefits as contemplated at the time of the voters' initial adoption of the City's retirement programs. It is further designed to ensure that future retirement benefit increases be approved by the voters.

The voters hereby find that the facts and circumstances constitute an emergency within the meaning of the Meyers-Milias-Brown Act ("MMBA"), Government Code section 3504.5, and pursuant to the City's authority as a charter city under the California Constitution. *E.g.,* Cal. Const., Art XI, §5.

Section 2: INTENT

This Act is intended to ensure the City can provide reasonable and sustainable post employment benefits while at the same time delivering Essential City Services to the residents of San Jose.

The City reaffirms its plenary authority as a charter city to control and manage all compensation provided to its employees as a municipal affair under the California Constitution.

The City reaffirms its inherent right to act responsibly to preserve the health, welfare and well-being of its residents.

This Act is not intended to deprive any current or former employees of benefits earned for prior service as of the time of the Act's effective date; rather, the Act is intended to preserve earned benefits as of the effective date of the Act.

This Act is not intended to reduce the pension amounts received by any retiree, including any cost of living increases received by retirees, as of the effective date of the Act.

This Act is not intended to grant any vested rights to any post employment benefit. The City expressly retains its authority to amend, change or terminate any retirement or other post employment benefit program provided by the City.

Section 3. Reservation of Voter Authority

The voters expressly reserve the right to consider any change in matters related to pension and other post-employment benefits. The City Council shall have no authority to agree to any increase in pension and/or retiree healthcare benefits, except that the Council shall have the authority to adopt Tier 2 pension benefit plans within the limits set forth herein.

Section 4. Reservation of Rights to City Council

Subject to the limitations set forth in this Act, the City Council retains its authority to take all actions necessary to effectuate the terms of this measure, to ensure the preservation of the tax status of the plan, and to amend, change or repeal any retirement or other post employment benefit program subject to the terms of this measure.

Section 5. Current Employees

(a) "Current Employees" means employees of the City of San Jose as of the effective date of this Act and who are not covered under the Tier 2 Plan (section 7).

(b) Unless they opt into a lower cost plan as provided in the Voluntary Election Program ("VEP," described herein), all Current Employees will share 50% of the costs to amortize any pension unfunded liabilities, except for any pension unfunded liabilities that may exist due to Tier 2 benefits in the future.

(c) A Current Employee's share of the cost to amortize pension unfunded liabilities shall be 5% of pensionable pay starting June 24, 2012, and increased by 5% annually until the

employee's proportionate share of the cost reaches 50% of the pension unfunded liabilities, with each employee's share capped at 25% of the employee's pensionable pay.

(d) The starting date for an employee's compensation adjustment under this Section shall be June 24, 2012, regardless of whether the VEP has been implemented. If the VEP has not been implemented for any reason, the compensation adjustments shall apply to all Current Employees.

(e) Current Employees' share of the cost to amortize any unfunded liabilities shall be calculated separately for employees in the Police and Fire Department Retirement Plan and employees in the Federated City Employees' Retirement System.

(f) The City Council shall adopt by ordinance the procedure and formulae necessary to implement this Section.

Section 6: Voluntary Election Program ("VEP")

The City Manager shall propose, and the City Council shall adopt by ordinance to be effective not later than June 30, 2012, a Voluntary Election Program ("VEP") for all Current Employees who are members of the existing retirement plans of the City as of the effective date of this Act. The implementation of the VEP is contingent upon receipt of IRS approval. The VEP shall be designed to permit Current Employees to enroll in an alternative retirement program which, as described herein, shall preserve an employee's earned benefit accrual; the change in benefit accrual will apply only to the employee's future City service.

The VEP shall have the following features and limitations:

(a) The plan shall not deprive any Current Employee who chooses to enroll in the VEP of the accrual rate (e.g. 2.5%) earned and accrued for service prior to the VEP's effective date; thus, the benefit accrual rate earned and accrued by individual employees for prior service shall be preserved for payment at the time of retirement.

(b) On and after the effective date of the ordinance, pension benefits under the VEP shall prospectively accrue based on the following limitations:

(i) the accrual rate shall be 1.5% of "final compensation", hereinafter defined, per year of service for future years of service only.

(ii) the current age of eligibility for service retirement under the existing plan as approved by the City Council as of the effective date of the Act for all years of service shall increase by six months annually on July 1 of each year until the retirement age reaches the age of 60 for employees in the Police and Fire Department Retirement Plan and the age of 65 for employees in the Federated City Employees' Retirement System. Earlier retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.

(iii) The eligibility to retire at thirty (30) years of service regardless of age shall increase by 6 months annually.

(iv) cost of living adjustments shall be limited to the increase in the consumer price index, (San Jose – San Francisco – Oakland U.S. Bureau of Labor Statistics index, CPI-U, December to December), capped at 1% per fiscal year. The first COLA adjustment following the effective date of the Act will be prorated based on the number of remaining months in the year after retirement of the employee.

(v) "final compensation" shall mean the average salary of the three highest consecutive years preceding the date of retirement.

(c) The cost sharing for the VEP for current service or current service benefits ("Normal Cost") shall not exceed the ratio of 3 for employees and 8 for the City, as presently set forth in the Charter. Employees who opt into the VEP will not be responsible for the payment of any pension unfunded liabilities of the system or plan related to past service.

(d) Survivorship benefits for Current Employees who do not opt into the VEP will remain the same. For employees who opt into the VEP, survivorship benefits shall be the same as the survivorship benefits in Tier 2 (benefits for new employees, as described in Section 7.).

(e) VEP Disability Retirement Benefits.

(i) A service connected "disability" retirement benefit, as hereinafter defined, shall be as follows:

a. The employee or former employee shall receive an annual benefit based on 45% of annual

pensionable pay based on the average of the highest three consecutive years of service.

(ii) A non-service connected disability retirement benefit shall be as follows:

a. The employee or former employee shall receive 1.5% times years of City Service (minimum 20% and maximum of 37.5%) of annual pensionable pay based on the average of the highest three consecutive years of service. Employees shall not be eligible for a non-service connected disability retirement unless they have 5 years of service with the City.

(iii) Cost of Living Adjustment ("COLA") provisions will be the same as for the service retirement benefit in the VEP.

Section 7: Future Employees – Limitation on Retirement Benefits – Tier 2

To the extent not already enacted, the City Manager shall propose, and the City Council shall adopt by ordinance, to be effective not later than June 30, 2012, a retirement program for employees hired on or after the effective date of such ordinance. This retirement program – for new employees – may be referred to as "Tier 2."

The Tier 2 program shall be limited as follows:

(a) The maximum City contributions shall not be less than 6.2% nor greater than 9% of pensionable salary. In no event shall the City contribution to such plan exceed 50% of the cost

of the Tier 2 plan (both normal cost and unfunded liabilities). The program may be designed as a "hybrid plan" consisting of a combination of Social Security, a defined benefit plan and/or a defined contribution plan.

(b) For any defined benefit plan, the age of eligibility for payment of accrued service retirement benefits shall be 65, except for sworn police officers and firefighters, whose service retirement age shall be 60. Earlier retirement may be permitted with reduced payments that do not exceed the actuarial value of full retirement.

(c) For any defined benefit plan, cost of living adjustments shall be limited to the increase in the consumer price index (San Jose – San Francisco – Oakland U.S. Bureau of Labor Statistics index, CPI-U, December to December), capped at 1% per fiscal year. The first COLA adjustment will be prorated based on the number of months retired.

(d) For any defined benefit plan, the measuring period for determining "final compensation" shall be the average salary of the three highest consecutive years preceding the date of retirement.

(e) For any defined benefit plan, benefits shall accrue at a rate not to exceed 1.5% per year of service.

(f) Employees who leave or have left City service and are subsequently rehired or reinstated shall be placed into the second tier of benefits (Tier 2). Employees who have at least five (5) years of service credit in the Federated City Employees' Retirement System and at least ten (10) years of service credit in the Police and Fire Department Retirement Plan on the date of separation and who have not obtained a return of

contributions will have their benefit accrual rate preserved for the years of service prior to their leaving City service.

(g) Any plan adopted by the City Council is subject to termination or amendment in the Council's discretion. No plan shall create a vested right to any benefit.

Section 8: Disability Retirements

To receive any disability retirement benefit under any pension plan, City employees must be incapable of engaging in any gainful employment for the City, but not yet eligible to retire (in terms of age and years of service). The determination of qualification for a disability retirement shall be made regardless of whether there are other positions available at the time a determination is made.

(a) An employee is considered "disabled" for purposes of qualifying for a disability retirement, if all of the following is met:

(i) An employee cannot do work that they did before; **and**

(ii) It is determined that the employee cannot perform any other jobs described in the City's classification plan because of his or her medical condition(s); **and**

(iii). The employee's disability has lasted or is expected to last for at least one year or to result in death.

(b) Determinations of disability shall be made by an independent panel of medical experts, appointed by the City Council. The independent panel shall serve to make disability determinations for both plans. Employees and the City shall have a right of appeal to an administrative law judge.

Section 9: Reasonable Cost of Living Adjustments for Retirees

(a) The City Manager shall propose, and the City Council shall adopt by ordinance, a program of benefits applicable to all retirees (both current and future) as follows:

(i) Cost of living adjustments ("COLAs") shall be adjusted for all retirees, such that the COLAs are limited to the consumer price index, (San Jose – San Francisco – Oakland U.S. Bureau of Labor Statistics index, CPI-U, December to December), capped at 1% per fiscal year. The first COLA adjustment following the effective date of the Act will be prorated based on the number of remaining months in a year following the retirement of the employee.

(ii) Any supplemental payments shall not be funded from plan assets.

Section 10: Retiree Healthcare

(a) **Minimum Contributions.** Existing and new employees must contribute a minimum of 50% of the cost of retiree healthcare, including both normal cost and unfunded liabilities.

(b) **Reservation of Rights.** No retiree healthcare plan or benefit shall grant any vested right, as the City retains its power to amend, change or terminate any plan provision.

Section 11: Actuarial Soundness (for both pension and retiree healthcare plans)

(a) All plans adopted pursuant to the Act shall be subject to an actuarial analysis publicly disclosed before adoption by the City Council, and pursuant to an independent valuation using standards set by the Government Accounting Standards Board and the Actuarial Standards Board, as may be amended from time to time. The City Manager shall certify that any plans adopted pursuant to the Act: (i) are actuarially sound; (ii) minimize any risk to the City and its residents; and (iii) are prudent and reasonable in light of the economic climate. The employees covered under the plans must share in the investment, mortality, and other risks and expenses of the plans.

(b) All of the City's pension and retiree healthcare plans must be actuarially sound, with unfunded liabilities determined annually through an independent audit using standards set by the Government Accounting Standards Board and the Actuarial Standards Board. No benefit or expense may be paid from the plans without being actuarially funded and explicitly recognized in determining the annual City and employee contributions into the plans.

(c) In setting the actuarial assumptions for the plans, valuing the liabilities of the plans, and determining the

contributions required to fund the plans, the objectives of the City's retirement boards shall be to:

1) achieve and maintain full funding of the plans using at least a median economic planning scenario. The likelihood of favorable plan experience should be greater than the likelihood of unfavorable plan experience; and

2) ensure fair and equitable treatment for current and future plan members and taxpayers with respect to the costs of the plans, and minimize any intergenerational transfer of costs.

(d) When investing the assets of the plans, the objective of the City's retirement boards shall be to maximize the rate of return without undue risk of loss while having proper regard to:

1) the funding objectives and actuarial assumptions of the plans; and

2) the need to minimize the volatility of the plans' surplus or deficit and, by extension, the impact on the volatility of contributions required to be made by the City or employees.

Section 12: Safety Net Provisions

(a) Preservation of Essential City Services:

At any time that: (1) Essential City Services are not provided at or above the service levels of January 1, 2011; (2) any library, community center, fire station, or police station or substation built or under construction as of January 1, 2011, is not

operational due to a budget shortfall; or (3) any of the City's pension or retiree healthcare plans have unfunded liabilities calculated on a market value or actuarial value greater than those liabilities existing as of June 30, 2010, then the Mayor, the City Council, the City Manager and other officers of the City, or any arbitrator or board of arbitrators, shall be prohibited from making or approving any contract, memorandum, agreement, award, grant, decision, resolution, ordinance or other official or binding act that allows or requires the City to do any of the following, without prior approval by the voters: (i) pay for unused sick leave or unused vacation time, except as required by applicable state or federal law; (ii) increase compensation for members of bargaining units after contracts expire; (iii) give automatic step increases or other raises for time in the job that are not based on performance; (iv) use hours not actually worked in determining eligibility for overtime or for retirement benefits; (v) pay overtime to executive, professional, or administrative employees or to other employees who are exempt from overtime requirements under the Fair Labor Standards Act ("FLSA"), or who are otherwise exempt from the FLSA; (vi) pay workers' compensation benefits for disability on top of disability retirement benefits without an offset to eliminate duplication of benefits for the same cause of disability; (vii) pay workers' compensation benefits beyond what state or federal laws require; (viii) allow existing or former employees to grant workers' compensation or disability benefits for existing or former employees; (ix) calculate retirement benefits on any compensation other than actual base salary paid or years (2080 hours) actually worked for the City of San Jose, except as required by applicable state law; (x) make layoff or rehiring decisions without considering individual employee performance; (xi) pay for more than 50% of the increase in the cost of healthcare benefits.

The provisions in the event (3) is triggered are intended to apply only to those employees in the plan that has the unfunded liabilities. For the purposes of this measure, retiree healthcare plans for employees covered under the Federated City Employee's Retirement System and the Police and Fire Department Retirement Plan shall be treated separately.

(b) Unfunded Liabilities in Pension and Other Post Employment Benefit Programs

The City Manager shall propose, and the City Council shall adopt by ordinance, safety net provisions with the following minimum features:

(i) At any time City pension or retiree healthcare plans have unfunded liabilities based on market value or actuarial value for pension or retiree healthcare greater than those existing on June 30, 2010, bonuses, cost of living increases, or supplemental pension payments to retirees shall not be allowed, except upon prior approval of the voters.

(ii) The limitations shall be temporary and shall remain in effect until the unfunded liabilities based on market value or actuarial value have remained below the level of June 30, 2010 for three consecutive years.

Section 13: Savings and Severability

(a) This Act shall be harmonized and interpreted to be consistent with all federal and state laws, rules and regulations. If any ordinance adopted pursuant to the Act is held to be invalid, unconstitutional or otherwise unenforceable

by a final judgment, the matter shall be referred to the City Council for determination as to whether to amend the ordinance consistent with the judgment, or whether to determine the section severable and ineffective. This Act shall be broadly construed to achieve its stated purposes.

(b) In the event any section of this Act is determined to be illegal, invalid or unenforceable as to retirees, then all benefit enhancements or increases (including pension and other post employment benefits of any kind) granted to retirees since the date of their retirement shall be eliminated.

(c) In the event either Section 5, 6, or 9 (as that Section applies to Current Employees), of this Act is determined to be illegal, invalid or unenforceable as to Current Employees, then the Current Employees' share of the costs to amortize any unfunded liabilities shall be 50% of the plan covering the respective employees.

(d) The City Council shall adopt ordinances as appropriate to implement and effectuate the provisions of this Act.