City of San Diego

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CITY COUNCILMEMBER –DISTRICT 5

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MEMORANDUM

DATE: January 26, 2009

TO: Mayor Jerry Sanders
Budget and Finance Committee Chairman Tony Young

FROM: Councilmember Donna Frye Donna Frye
Councilmember Carl DeMaio Carl DeMaio

RE: Next Steps in Pension Reform To Address the City's Structural Budget Deficit

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In October we requested that the City Attorney examine a variety of possible pension reforms to determine which can legally be implemented. We appreciate the City Attorney's response confirming that a number of pension reform options do exist to help save taxpayers millions each year and achieve retirement security for city employees.

The news that additional pension reforms are still available could not come at a better time. The recently released calculation of the FY 2011 pension payment shows a spike in our annual payment to $231 million – or approximately 40% of city payroll. Without further reform and when including all costs associated with retirement benefits for city employees (e.g. SPSP, Offsets, Retiree Medical ARC, etc.) the cost tops $370 million annually – or over 65% of payroll.

While noting that "core" pension benefits are vested, the City Attorney has confirmed that several elements of city employee retirement packages are not vested, but rather, are "employment benefits" that can be modified subject to our employer obligations to faithfully negotiate with our labor unions.

More importantly, consistent with the recent Taylor decision, the City Attorney confirms that the manner in which pension benefits are granted (legislative intent, consistency with City Charter rules, etc.) is an important factor in determining whether a benefit is indeed "vested."

We suggest that the upcoming budget deliberations and future labor negotiations include the following pension reforms.

- **Finish Pension Reform for New Hires**

The city has made progress in establishing a new pension system for new hires for some classifications. However, the new pension system does not apply to all city employees. We believe the Mayor and City Council should finish the job of reforming pensions for new hires in all job classifications. Among the reforms we can legally implement through labor negotiations include raising retirement ages, more equitably distributing investment risk, and preventing "pension spiking" by moving to a three-year average of highest salary for pension calculations.

- **Compliance Review on "Substantially Equal" Cost Share for "Normal Retirement Allowances"**

In the January 21 opinion, The City Attorney notes:

> *The City and SDCERS should ensure, through a proper accounting, that the "substantially equal" requirement is being met for "normal retirement allowances." ...[t]he accounting should include review of disability retirement contributions and any amortization of unfunded liability being paid by the City, such as any unfunded liability as a result of recent stock market losses, to determine that contributions that are not "substantially equal" properly fit into the exception to the requirement as "financial liabilities accruing under any new retirement plan or revised retirement plan because of past service of employees."*

As our January 25th memorandum outlines, we are asking that the City Council receive a presentation by SDCERS on these calculations as soon as possible to ensure that the calculations and cost contributions from city employees have complied with the Charter's requirements.

- **Amending City Charter Section 143.1**

Charter section 143.1 currently states in part, that:

> *No ordinance amending the retirement system which affects the benefits of any employee under such retirement system shall be adopted without the approval of a majority vote of the members of said system.*

In a recently released opinion, the City attorney raises the procedural challenge presented by this Charter section.

On January 4, 2010, we issued a joint memorandum proposing an amendment to this Charter section. It is our understanding that this proposal will be considered at the next Rules Committee meeting.

With the City Attorney's opinion in hand also noting the obstacle presented by Section 143.1, we respectfully ask the Mayor and our colleagues to act on this procedural reform in time for future rounds of labor negotiations.

- **Eliminate Accrual of Pension Credits on Terminal Leave**

Several city employee groups still have "terminal leave" -- wherein city employees continue to accrue pension service credits after they retire – based on their vacation and personal leave payouts.

While progress has been made with some of the city's bargaining units, some employees are still able to accrue pension service credit after terminating city employment. As soon as possible, the city should ensure that this benefit is reformed to eliminate the accrual of pension service credits on terminal leave.

- **Cost Neutrality Study of the DROP Program**

The City Attorney's opinion notes that DROP is not a vested benefit – and that municipal code language should govern how this discretionary benefit is administered. The municipal code clearly calls for DROP to be "cost neutral." To determine whether DROP is indeed cost neutral, we have repeatedly requested that an actuarial study be conducted – and if DROP turns out to not be cost neutral, that appropriate reforms in this benefit be implemented to ensure compliance with the municipal code.

- **Negotiations on Employee Offsets and SPSP**

The FY 2010 Adopted Budget contained citywide costs of more than $30 million for employee pension contribution "pickup" and employer contributions for the Supplemental Pension and Savings Plan combined. Given that the city has successfully reduced costs associated with these benefits in prior negotiations, the city should explore potential cost savings associated with both items in future labor negotiations.

- **Continue to Explore Legal Options for Pension Reform**

We note that a number of pension reform questions raised by our offices have not been fully answered in the City Attorney's opinion. We intend to continue to canvass for ideas on how to legally reform our pension system and to seek city attorney review of those ideas.

Moreover, we are optimistic that additional reform avenues will be opened in the near future – as evidenced by the successful rulings obtained by the City Attorney in 2009 on DROP and Presidential Leave. These outcomes may apply to other pension benefits currently included in our retirement packages.

We look forward to working with our Council colleagues and the Mayor to advance pension reform – and achieve taxpayer savings and retirement security for our city employees.

CC: Honorable City Councilmembers
Andrea Tevlin, IBA