

City of San José

**Current Status of Pension Systems and
Retirement Reform Ballot (Measure B)
Implementation Study Session**

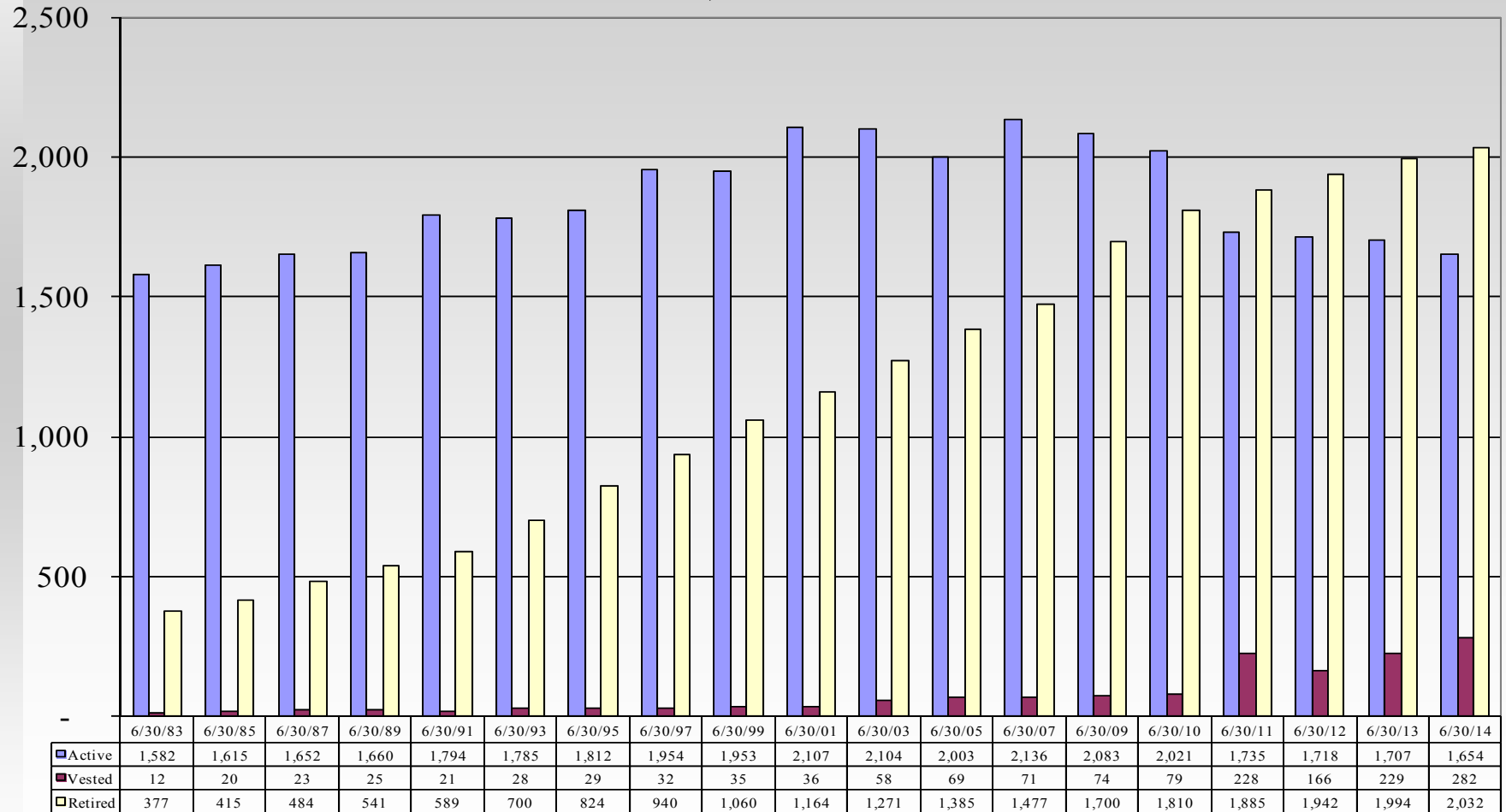
AGENDA

- Overview of How the Two Pension Systems Work
- Overview of Each Retirement Board's Governance Model
- Overview of Actuarial Valuations and Future Projections
- Background and History of the City's Two Retirement Systems
- Summary of Retirement Reform Ballot Measure (Measure B)
- Update on Measure B Implementation
- Comparison of Tier 1, Tier 2, and CalPERS Retirement Benefits
- Second Tier Costing

Police and Fire Department Retirement Plan Maturity

Summary of Demographic Information – Police and Fire

Participant Counts with separate bar each year
for actives, VTs & retirees



Plan Maturity – Police and Fire

- Three Measures of Maturity

- Percentage of Actuarial Liability belonging to Retirees

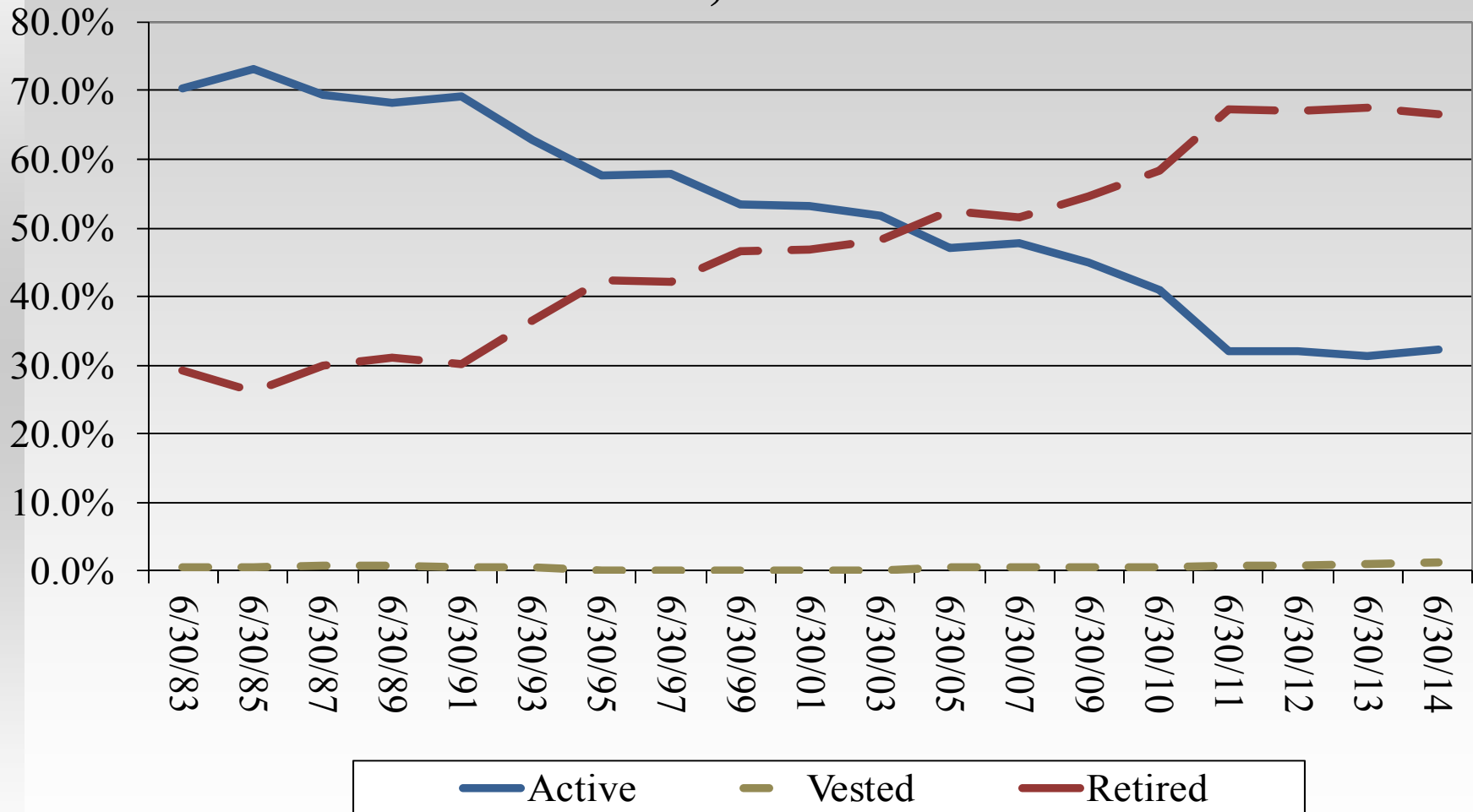
- **Liability Volatility Index** - Ratio of Actuarial Liability to Pensionable Wages

- **Asset Volatility Index** - Ratio of Market Value of Plan Assets to Pensionable Wages

- Note: Federated looks very similar to Police and Fire but slightly less volatile

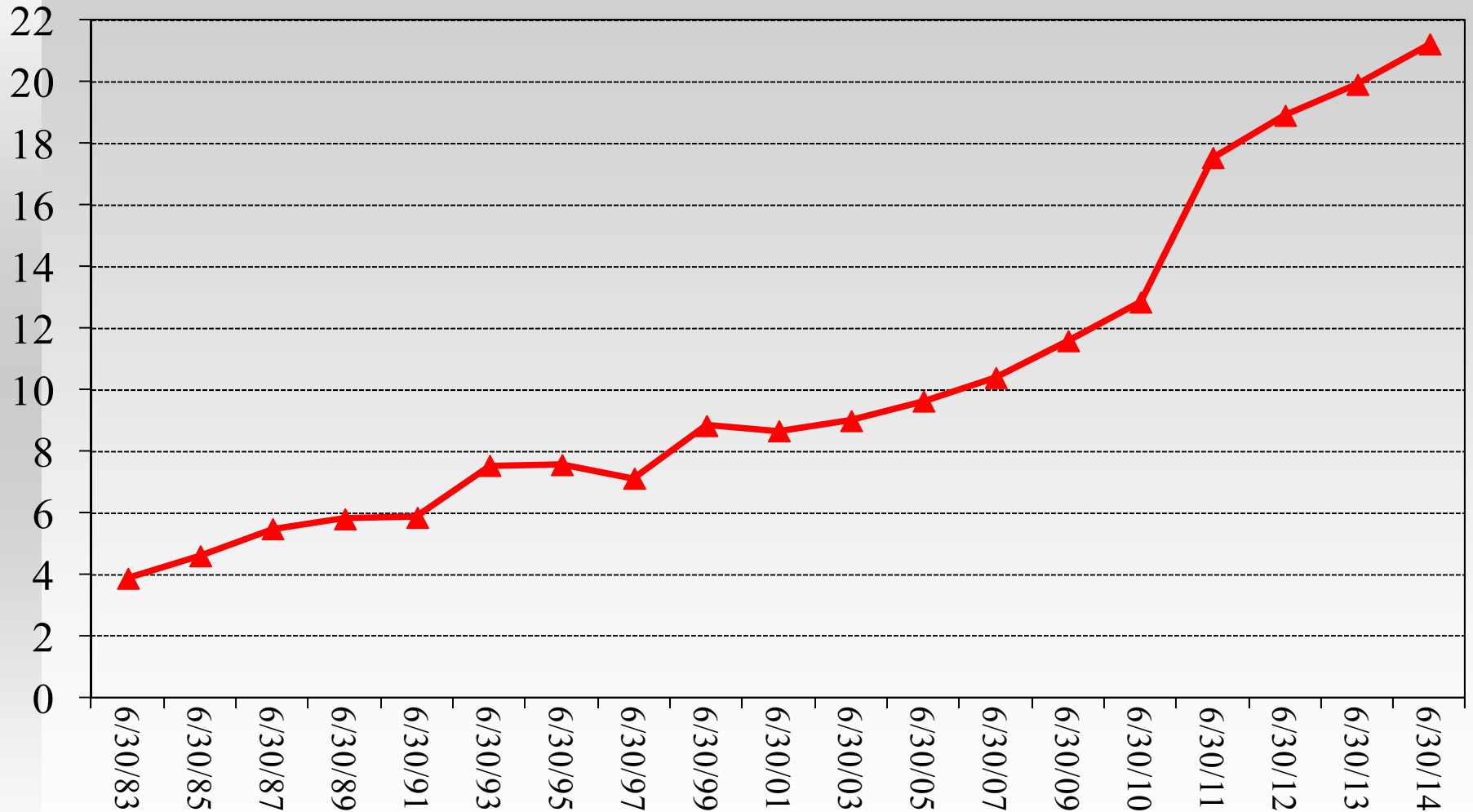
Plan Maturity – Police and Fire

**% of Total Police & Fire AAL line graph
with active, VTs and retirees**



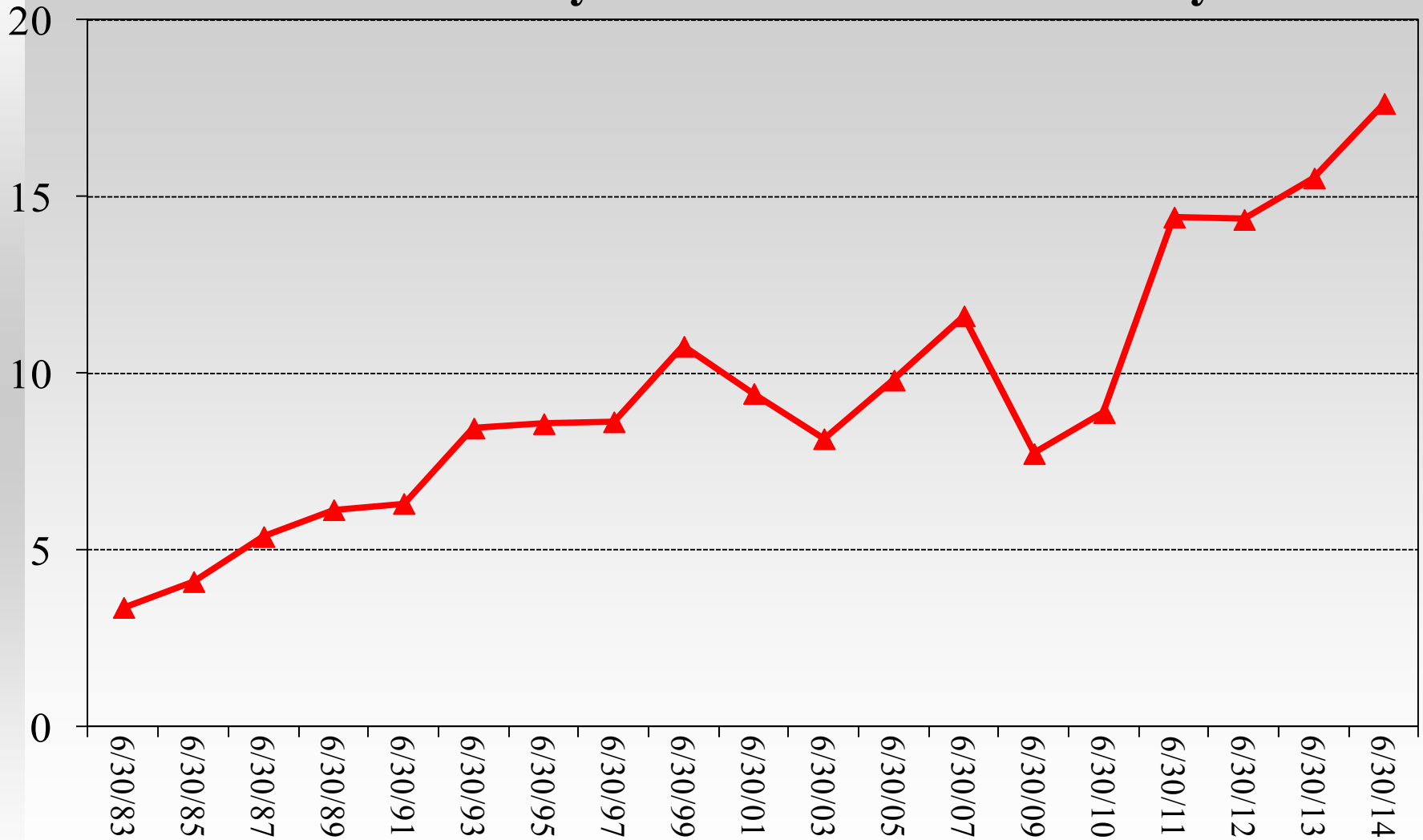
Plan Maturity – Police and Fire

Liability Volatility Index: Ratio of AAL to Payroll



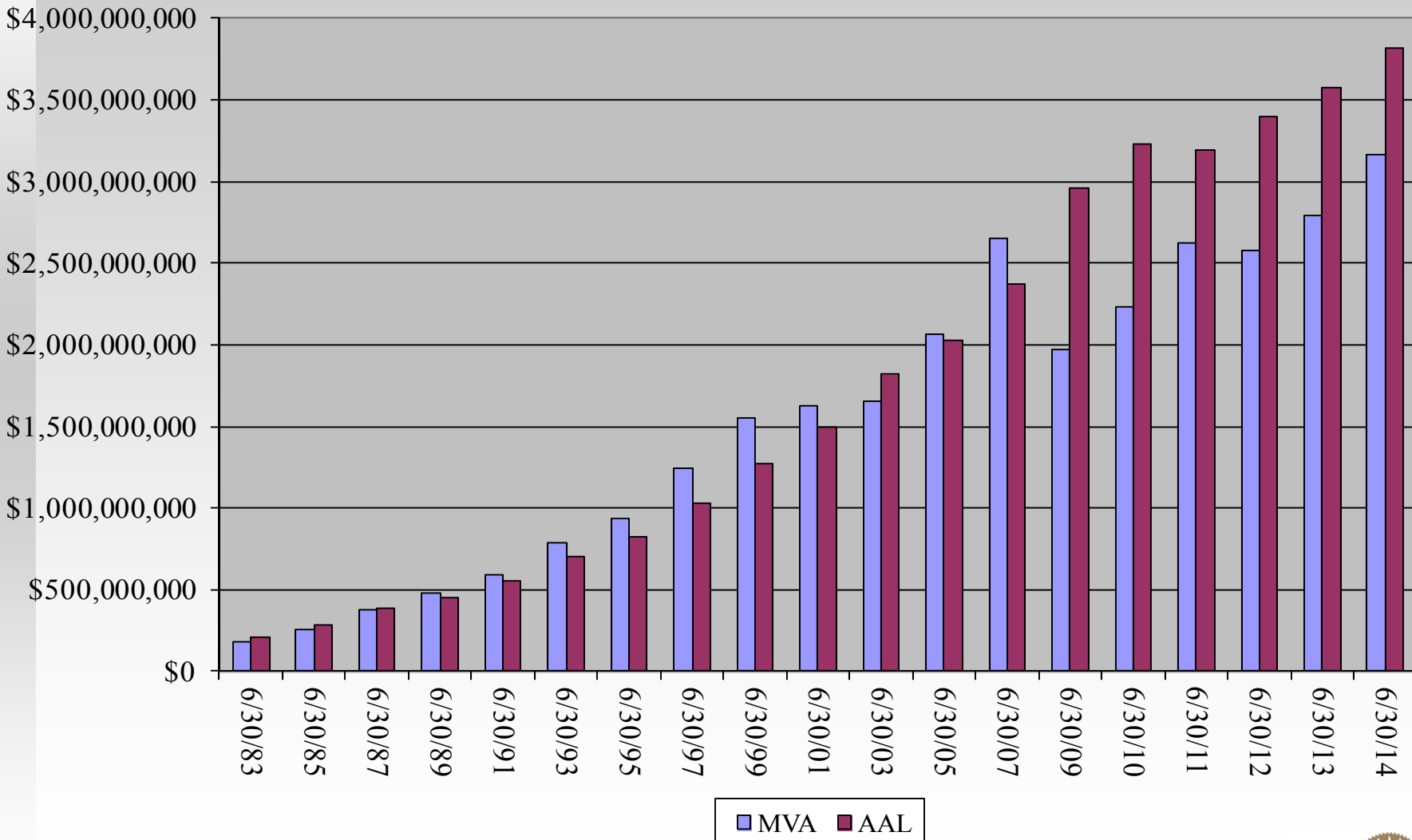
Plan Maturity – Police and Fire

Asset Volatility Index: Ratio of MVA to Payroll



Plan Funded Status – Police and Fire

Assets: AAL and MVA for each year



Plan Funded Status – Police and Fire

(Millions)

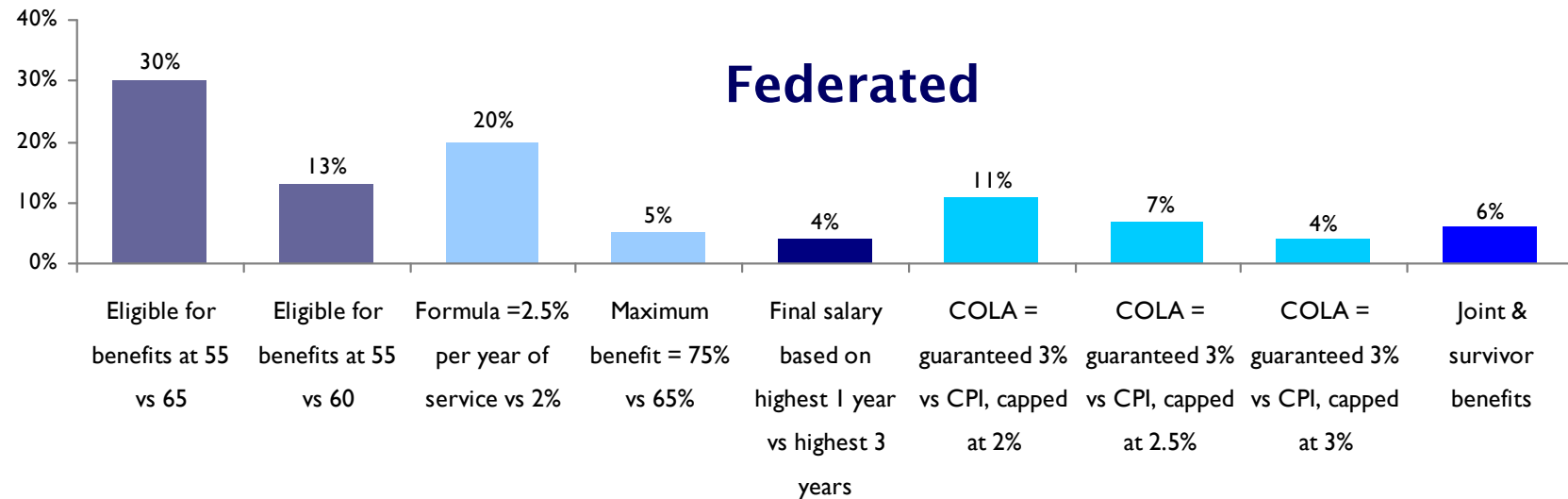
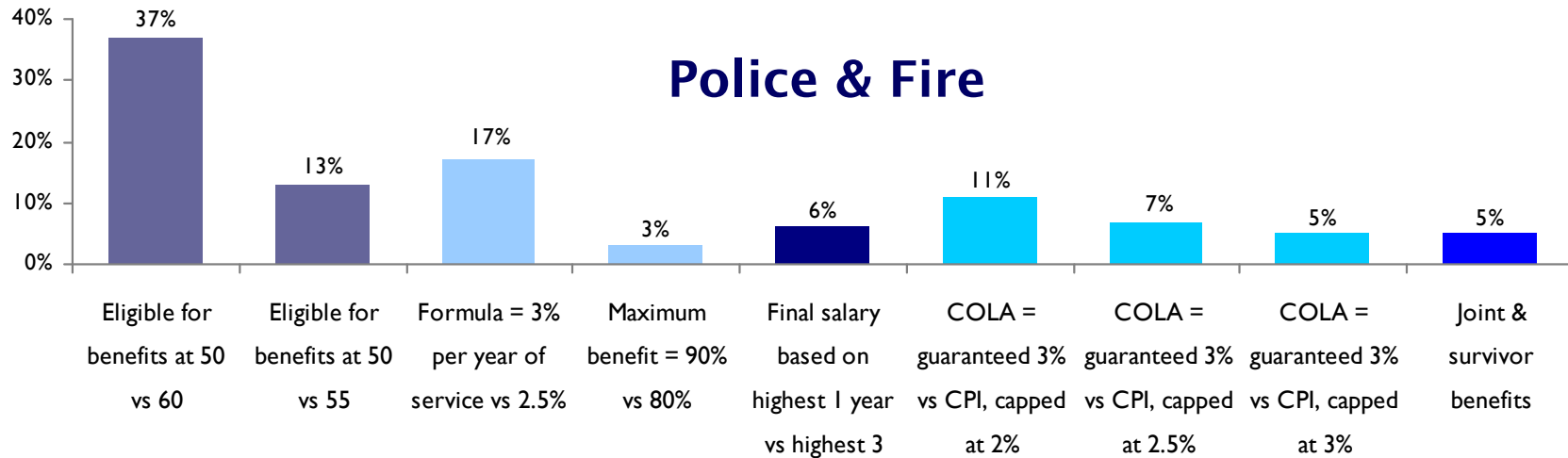
June 30	1983	1993	2003	2013	2014
■ Actuarial Accrued Liability	\$ 209.5	\$ 701.6	\$ 1,823.2	\$ 3,578.0	\$ 3,813.7
■ Market Value of Plan Assets	<u>182.2</u>	<u>785.2</u>	<u>1,651.2</u>	<u>2,789.5</u>	<u>3,168.2</u>
■ Unfunded Actuarial Accrued Liability	27.3	(83.6)	172.0	788.5	645.5
■ Pensionable Wages	53.7	92.8	202.2	184.6	188.2

Pension Sustainability Audit 2010

What Are The Primary Components Of The Benefits That Affect Normal Cost?

1. Retirement Age
2. Benefit Formula
3. Maximum Benefit
4. Final Salary Calculation
5. Cost-of-Living Adjustments (COLA)
6. Survivorship Benefits
7. Retiree Healthcare Benefits
8. Disability Retirements
9. Supplemental Benefits (SRBR)

2010 - Estimated Costs Attributable to Various Benefit Levels (Tier 1)



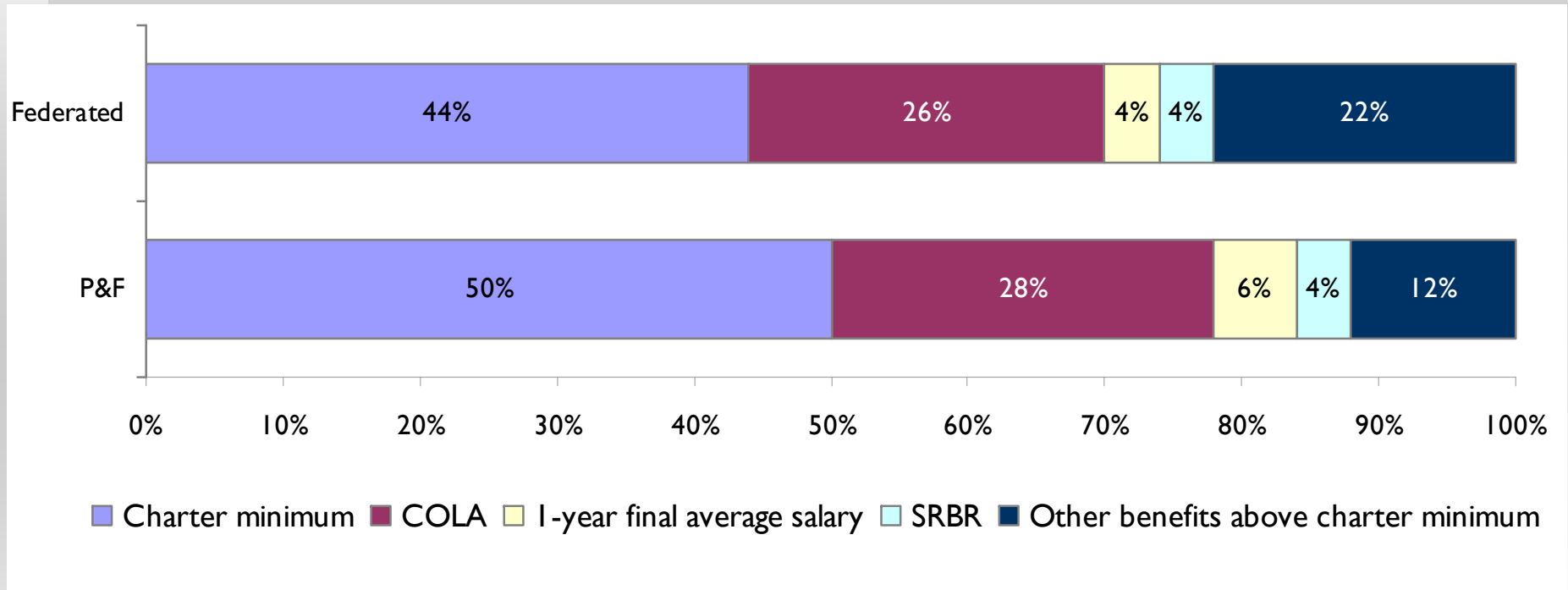
History of Federated Retirement Benefit Enhancements

- **Prior to 1975:** 2% for each year of service for first 20 years with additional 1.0-1.3% for additional years
- **1975:** maximum benefit 75% of final compensation; COLA established
- **1984:** Medical benefits added
- **1986:** SRBR established; dental benefits added.
- **1994:** Reciprocity with CalPERS established
- **2001:** Final compensation redefined as average compensation earnable for highest consecutive 12 months
- **2006:** COLA changed to guaranteed 3% annual adjustment

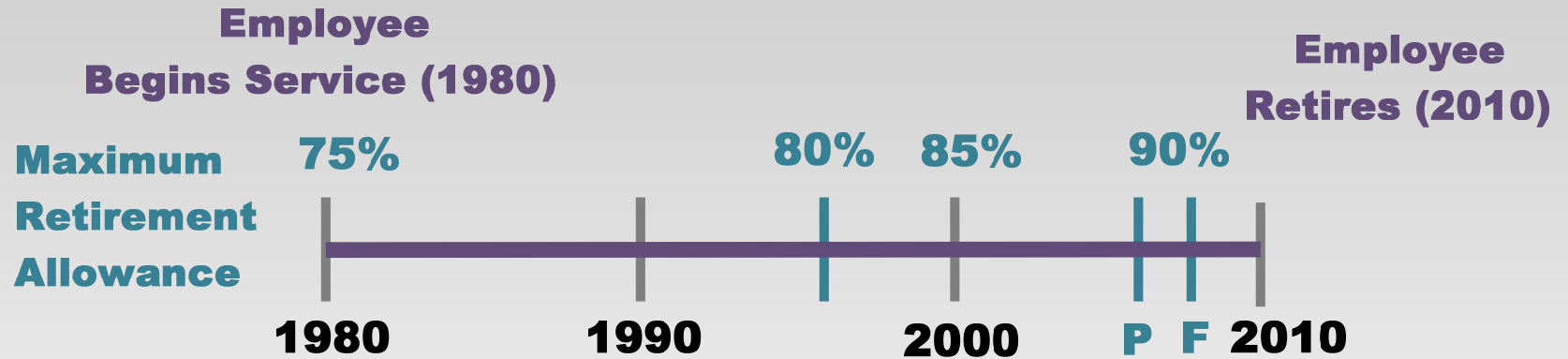
History of Police and Fire Retirement Benefit Enhancements

- **1961:** Benefit was 50% of final compensation (3 consecutive years)
- **1968:** Retirement age reduced to 50; maximum benefit 66.66%
- **1970:** COLA added; maximum benefit 75%
- **1984:** Medical benefits added
- **1986:** Dental benefits added
- **1994:** Reciprocity added
- **1998:** Maximum benefit 80% (awarded through binding interest arbitration—retroactive to February 1996)
- **2000:** Maximum benefit 85%
- **2002:** COLA changes to guaranteed 3%; SRBR began distributions
- **2006:** Maximum benefit 90% for Police
- **2008:** Maximum benefit 90% for Fire (awarded through binding interest arbitration)

2010 - Cost Components of the Tier 1 Plans



Retroactive Pension Benefit Enhancements Added to the Unfunded Liability

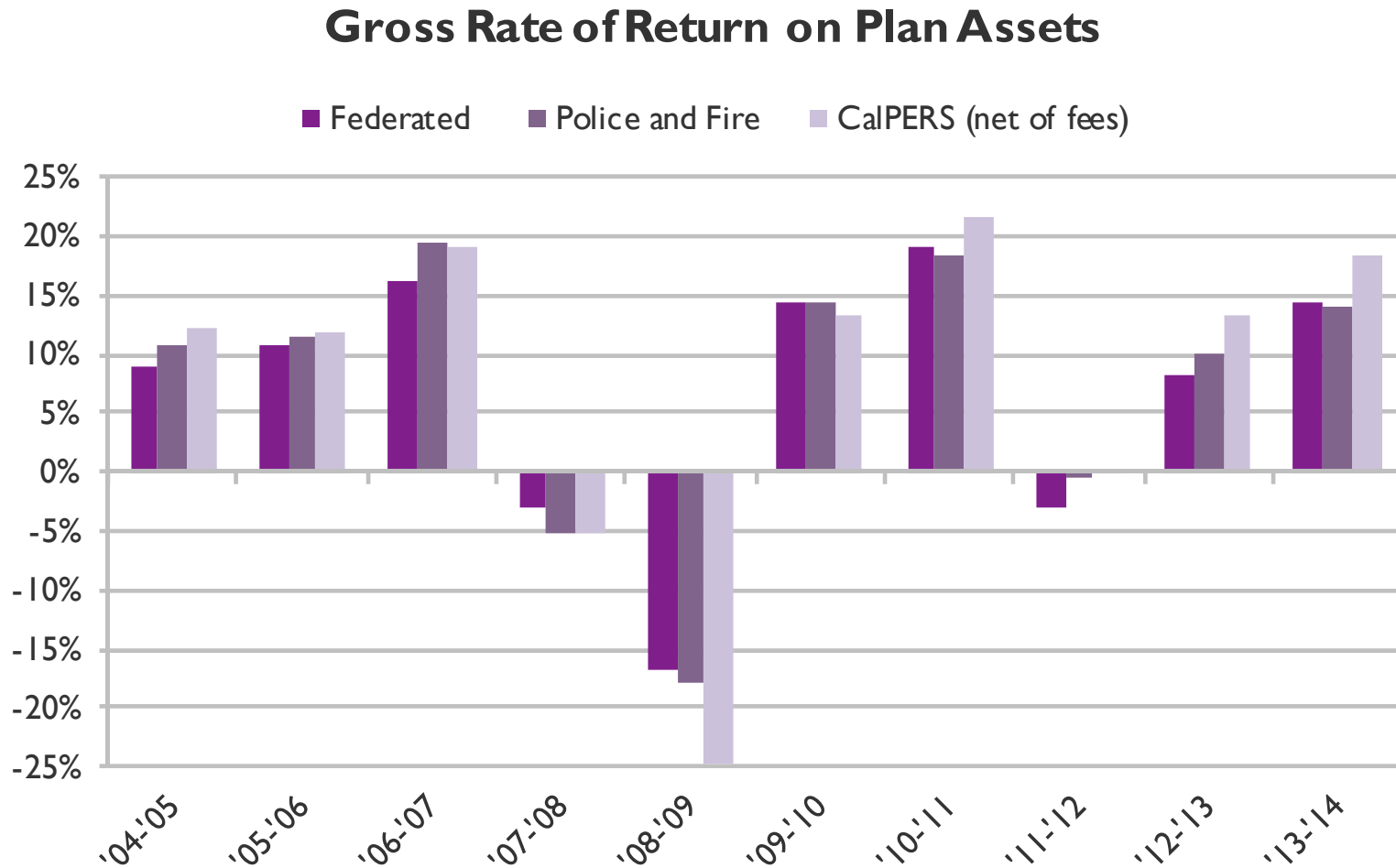


- Other changes
 - benefit formulas
 - retirement age
 - definition final compensation
 - survivorship benefits
 - guaranteed 3% COLA
 - supplemental retiree benefit

Actuarial Forecasts Did Not Hold True

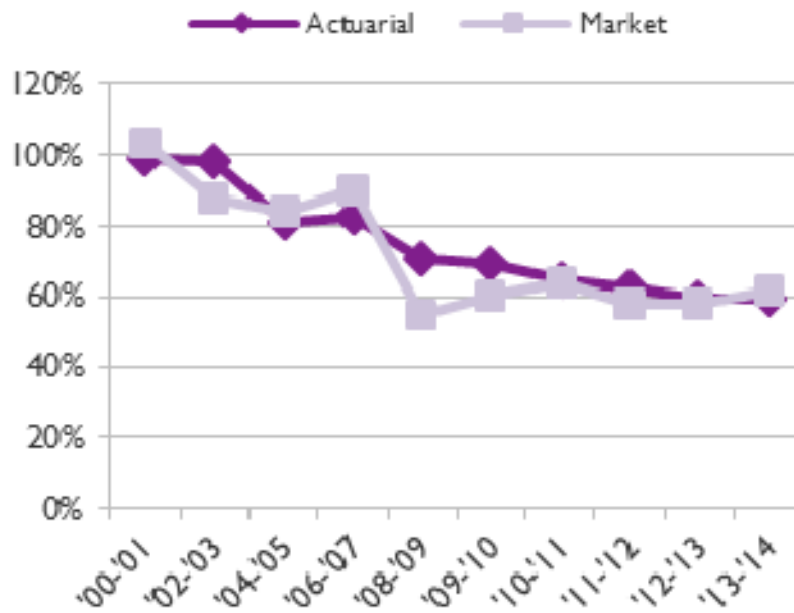
- The Retirement Board's actuaries build models with assumptions about future events to estimate liabilities and determine contribution rates
- For example, \$750 million added to the unfunded liability as of June 30, 2009
 - Assumed investment rate of return
 - Longer lives
 - Earlier and more retirements
 - Higher than expected salary increases

Investment Gains and Losses (Market Value of Assets)

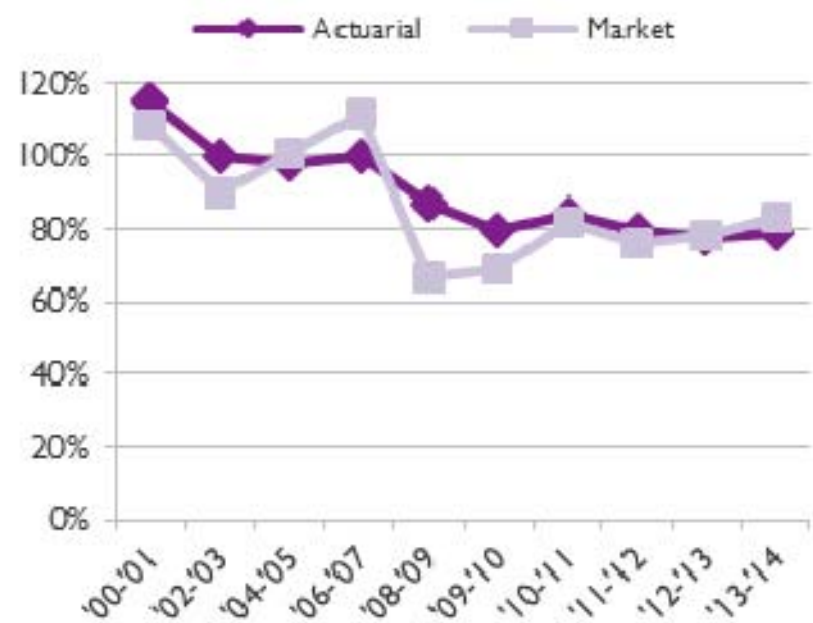


Funded Status Has Declined

**Federated Funded Status
(Pension only)**



**Police and Fire Funded Status
(Pension only)**



How Much Has Been Promised?

What do we owe?

\$7.1 billion accrued liability for pensions

\$1.4 billion accrued liability for retiree healthcare

\$8.5 billion

How much do we have?

\$5.2 billion held in trust for pensions

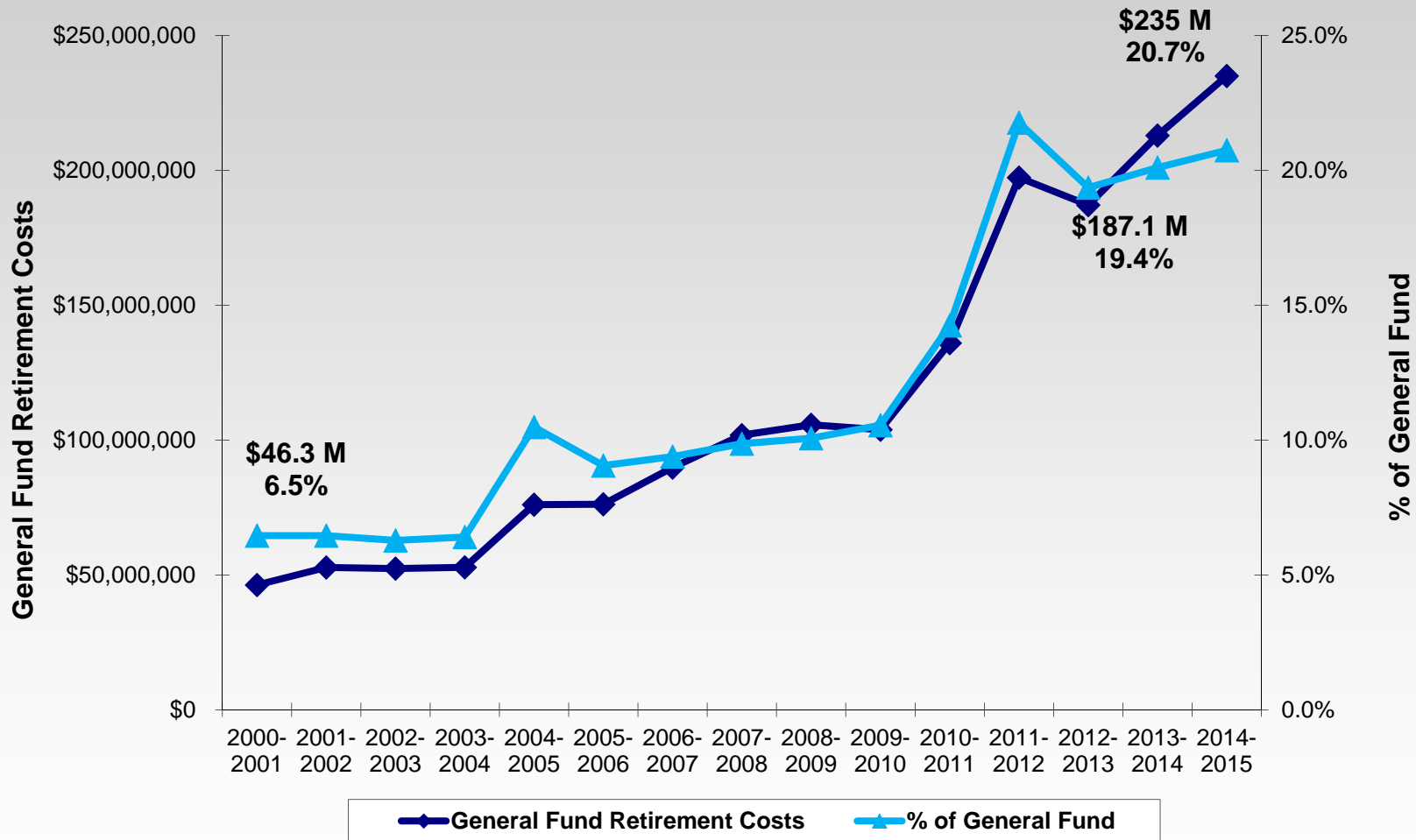
\$0.3 billion held in trust for retiree healthcare

\$5.5 billion

Source: 6/30/14 Actuarial Valuations and City of San Jose Comprehensive Annual Financial Report

City's Budgetary Situation and Fiscal Reform Plan

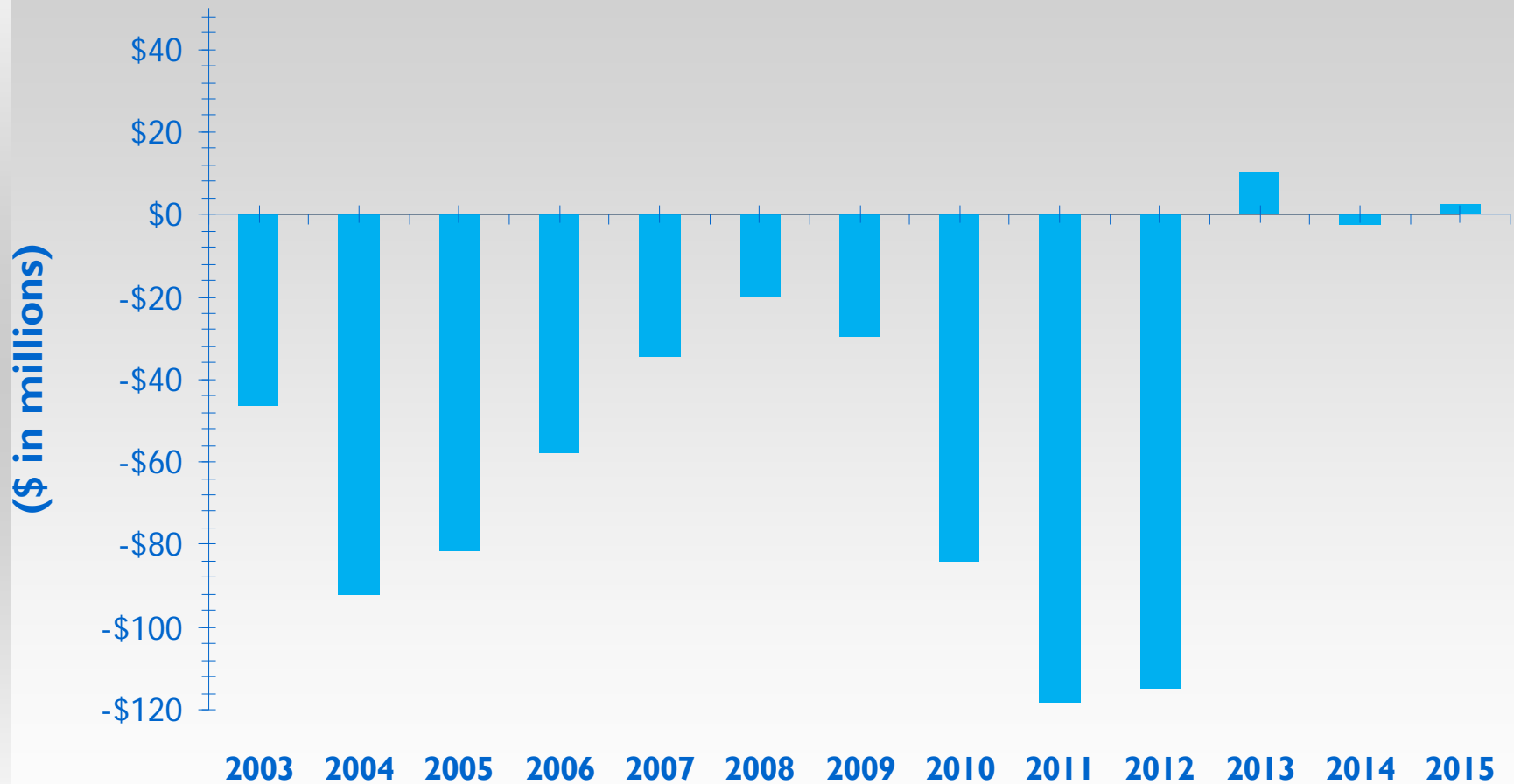
Escalating Retirement Costs



General Fund Structural Deficit Elimination Plan

- A decade of General Fund budget shortfalls (2002-2003 through 2011-2012) driven by two deep recessions and unsustainable cost structure
- Civic engagement and combination of three major strategies used to address shortfalls
- Significant service reductions in both public safety and non-public safety areas were unavoidable

\$670M in Cumulative Shortfalls Balanced



October 2011 - General Fund Shortfalls Expected to Continue into the Future

2012-2016 General Fund Forecast

(Based on Feb. 2011 Forecast, Updated for 2011-2012 Adopted Budget*)

(\$ in Millions)

	2012- 2013	2013- 2014	2014- 2015	2015- 2016	Total
Projected Annual Shortfall **	(\$78.2 - \$115)	(\$25.1)	(\$10.0)	(\$0.1)	(\$113.4 - \$150)

* Does not include: cost-of-living salary increases; additional impacts from future changes in actuarial assumptions or retirement benefit levels that could impact the City's required retirement contributions; unmet/deferred infrastructure and maintenance needs; Development Fee Programs; or one-time revenues/expenses. Assumes continued pre-payment of City's annual retirement contribution.

** Annual budget shortfall attributed to each fiscal year. Assumes shortfalls addressed with ongoing solutions. Any portion of the annual shortfall solved on a one-time basis would carry over to the following year. The 2012-2013 budget shortfall figure includes \$35 million from one-time solutions carried over from 2011-2012.

Fiscal Reform Plan

- Develop a plan to achieve \$216 million in General Fund savings in five years through cost reductions and/or new revenues
- Keep retirement costs at the Fiscal Year 2010-2011 level
- Restore/keep Police, Fire, libraries and community centers to the January 1, 2011, level
- Open the libraries, community centers, fire stations built or under construction and the police substation within five years

Fiscal Reform Plan - City Council

Direction

- Cost Savings From:
 - Reducing compensation for existing employees
 - Avoiding increases in retirement costs beyond the amounts paid for this fiscal year
 - Reforming workers' compensation and disability retirement systems
 - Reducing costs for sick leave payouts, vacation buybacks, and overtime pay
 - Modifying healthcare plans and cost sharing
 - Organizational changes and efficiencies

Measure B

Measure B - City Council Direction

- May 2011:
 - Place limits on retirement benefits for new employees
 - Place limits on retirement benefits for existing employees
 - Increases in COLA limited to the increase in the Bay Area CPI and not to exceed 1% per year
 - Place additional limitations on growth in retirement benefits if the fiscal and public safety emergency worsens
 - Implementation provisions
- June 2011:
 - Opt-in program for current employees

Seal Beach Bargaining

- “Seal Beach bargaining” refers to bargaining or negotiating over a proposed ballot measure prior to it being placed on a ballot for consideration by voters during an election. This is only done when a proposed ballot measure affects matters within the scope of representation, so not all ballot measures or all aspects of a particular ballot measure need to be bargained.

Measure B and Retirement Reform Negotiations and Mediation

- Engaged in bargaining for eight (8) months
- 45 negotiation meetings
- 25 mediation sessions (spanning 2 rounds of mediation)
- Seven (7) proposed ballot measures
- Ballot measure approved by Council on March 6, 2012

Ballot Measure Summary

- Established a Voluntary Election Program to opt into a lower level retirement benefit
- Current employees who chose not to opt-in subject to additional retirement contributions – 4% per year, max of 16%
- Tier 2 benefit maximums
 - Measure W eliminated benefit minimums
- Disability definition change, workers' compensation offset and medical expert panel
- Suspend COLA in fiscal emergency
- Eliminate SRBR- “13th paycheck”

Retirement Reform Negotiations

- Retirement reform changes made outside of ballot measure:
 - Medicare Parts A and B
 - Retirement benefits for new employees
 - Lowest cost healthcare plan
 - Healthcare cost sharing structure

Implementation of Measure B and Retirement Reform

- Elimination of SRBR
- Definition of disability applicable to Tier 2 employees
- Tier 2 for new employees based on Measure W and Measure B benefit maximums
- Stipulation for other provisions until July 2015
- Litigation in three arenas:
 - Sixth Appellate Court
 - Superior Court (Quo warranto)
 - PERB

Current Retirement Reform Cost Savings

Retirement Reform

Retirement Reform Estimate	GF Savings
Implemented	
SRBR Elimination	\$13 M
Retiree Healthcare Changes (lowest cost plan)	\$7 M
New Tier 2 Retirement Plans	\$5 M
<i>Subtotal Implemented</i>	<i>\$25 M</i>
Not Yet Implemented	
Tier 1 Employees (additional contributions/after 4 years)*	\$46 M
Disability (workers' compensation offset)*	3 M
<i>Subtotal Not Yet Implemented</i>	<i>\$49 M</i>
Total Retirement Reform Estimate	\$74 M

* Preliminary Estimates

Tier 1, Tier 2 and CALPERS Comparison

Average Pension Benefit - Federated

EXAMPLE

Retirement Tier	Average Salary	Years of Service	Accrual Rate	Pension Benefit
Federated Tier 1	\$75,842	30	2.5%	\$56,881.50
Federated Tier 2	\$75,842	30	2.0%	\$45,505.20

Average Pension Benefit – Police and Fire

EXAMPLE

Retirement Tier	Average Salary*	Years of Service	Accrual Rate	Pension Benefit
Police & Fire Tier 1	\$116,095	30	3.0%	\$104,485.50
Police & Fire Tier 2	\$116,095	30	2.0%	\$69,657

* *Base Pay Only*

PEPRA Formulas and Benefit Factors

- Miscellaneous 2@62, Max benefit 2.5@67

2% at Age 62 Benefit Formula Minimum Age for Retirement 52 Membership Date on or After January 1, 2013	
Age	Exact Year
52	1.000
53	1.100
54	1.200
55	1.300
56	1.400
57	1.500
58	1.600
59	1.700
60	1.800
61	1.900
62	2.000
63	2.100
64	2.200
65	2.300
66	2.400
67 or older	2.500

PEPRA Formulas and Benefit Factors

Safety Option 1: <i>2.5@57</i>		Safety Option 2: <i>2.7@57</i>																																					
<p>2.5% @ 57 Benefit Formula Minimum Age for Retirement 50 Membership date on or after January 1, 2013</p> <table border="1"> <thead> <tr> <th>Age</th> <th>Exact Year</th> </tr> </thead> <tbody> <tr><td>50</td><td>2.000</td></tr> <tr><td>51</td><td>2.071</td></tr> <tr><td>52</td><td>2.143</td></tr> <tr><td>53</td><td>2.214</td></tr> <tr><td>54</td><td>2.286</td></tr> <tr><td>55</td><td>2.357</td></tr> <tr><td>56</td><td>2.429</td></tr> <tr><td>57 or older</td><td>2.500</td></tr> </tbody> </table>		Age	Exact Year	50	2.000	51	2.071	52	2.143	53	2.214	54	2.286	55	2.357	56	2.429	57 or older	2.500	<p>2.7% @ 57 Benefit Formula Minimum Age for Retirement 50 Membership date on or after January 1, 2013</p> <table border="1"> <thead> <tr> <th>Age</th> <th>Exact Year</th> </tr> </thead> <tbody> <tr><td>50</td><td>2.000</td></tr> <tr><td>51</td><td>2.100</td></tr> <tr><td>52</td><td>2.200</td></tr> <tr><td>53</td><td>2.300</td></tr> <tr><td>54</td><td>2.400</td></tr> <tr><td>55</td><td>2.500</td></tr> <tr><td>56</td><td>2.600</td></tr> <tr><td>57 or older</td><td>2.700</td></tr> </tbody> </table>		Age	Exact Year	50	2.000	51	2.100	52	2.200	53	2.300	54	2.400	55	2.500	56	2.600	57 or older	2.700
Age	Exact Year																																						
50	2.000																																						
51	2.071																																						
52	2.143																																						
53	2.214																																						
54	2.286																																						
55	2.357																																						
56	2.429																																						
57 or older	2.500																																						
Age	Exact Year																																						
50	2.000																																						
51	2.100																																						
52	2.200																																						
53	2.300																																						
54	2.400																																						
55	2.500																																						
56	2.600																																						
57 or older	2.700																																						

Pension Benefit Comparison – Federated Retirement Plan

	Tier 1	Tier 2	CalPERS (PEPRA)
Max Benefit	75% (Status Quo)	65%	None
Accrual Rate	2.5% per year (Status Quo)	2.0% per year	2.0% per year at 62, 2.3% per year at 65, and 2.5% per year at 67
Age/Years of Service	55 w/ 5 yrs.; or 30 yrs at any age (Status Quo)	Age 65 w/5 yrs.	Age 52 w/5 yrs.
Final Average Salary Calculation	Highest 1 Year (Status Quo)	Highest 3 Years	Highest 3 Years
COLA	3% fixed (Status Quo)	Max 1.5% based on CPI	Depend on agency's contract
Cost Sharing	Current cost sharing of the Normal Cost is the City pays 8/11ths and the employee pays 3/11ths.	Costs will be shared 50/50 between the City and employees. City may, but is not required to contribute to a defined contribution plan if the total City contribution does not exceed 9%.	For public agencies, a new member's initial contribution rate will be at least 50% of the total normal cost rate or the current contribution rate of similarly situated employees, whichever is greater, except where it would cause an existing Memorandum of Understanding (MOU) to be impaired. Once the impaired MOU is amended, extended, renewed, or expires, the new requirements will apply.

Pension Benefit Comparison – Police and Fire Retirement Plan

	Tier 1	Tier 2	CalPERS (PEPRA)
Max Benefit	90% (Status Quo)	65%	None
Accrual Rate	2.5% - 4.0% depending on years of service (Status Quo)	2.0% per year	Option 1: 2.5% at Age 57 Option 2: 2.7 at Age 57
Age/Years of Service	50 w/ 25 yrs; 55 w/20 yrs; or 30 yrs at any age (Status Quo)	Age 60 w/10 yrs.	Age 50 w/10 yr
Final Average Salary Calculation	Highest 1 Year (Status Quo)	Highest 3 Years	Highest 3 Years
COLA	3% fixed (Status Quo)	Max 1.5% based on CPI	Depends on agency's contract
Cost Sharing	Current cost sharing of the Normal Cost is the City pays 8/11ths and the employee pays 3/11ths.	Costs will be shared 50/50 between the City and employees. City may, but is not required to contribute to a defined contribution plan if the total City contribution does not exceed 9%.	For public agencies, a new member's initial contribution rate will be at least 50% of the total normal cost rate or the current contribution rate of similarly situated employees, whichever is greater, except where it would cause an existing Memorandum of Understanding (MOU) to be impaired. Once the impaired MOU is amended, extended, renewed, or expires, the new requirements will apply.

Impact of Moving to CalPERS

- Short term differences:
 - Actuarial Assumptions
 - Actuarial Methods
 - Amortization Period
- Move to CalPERS for New Hires:
 - Has no impact on Unfunded Actuarial Accrued Liability

Measure B Disability Definition

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

1) an employee in the Federated City Employees’ Retirement System cannot perform any other jobs described in the City’s classification plan because of his or her medical condition(s); or

2) an employee in the Police and Fire Department Retirement Plan cannot perform any other jobs described in the City’s classification plan in the employee’s department 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.

What qualifies for a disability retirement?

San Jose Police and Fire (Measure B)	San Jose Federated (Measure B)	San Jose (Pre-Measure B)	CalPERS (PEPRA)
Employee cannot do the work they did before, <i>and</i>	Employee cannot do the work they did before, <i>and</i>	Employee cannot perform the duties of their position, <i>or</i>	Employee is unable to perform the usual duties of their job with their current employer
Employee cannot perform any other jobs in the City's classification plan in the Employee's Department	Employee cannot perform any other jobs in the City's classification plan	Employee cannot perform the duties of any other position in the same classification	
Employee's injury/illness has lasted or is expected to last at least 1 year, or result in death	Employee's injury/illness has lasted or is expected to last at least 1 year, or result in death	Employee's injury/illness is of permanent or extended and uncertain duration	
			Employee's injury/illness is expected to be permanent or last indefinitely

Costing of Second Tier Options

Federated Tier 2 Total Normal Cost Based on PEPRA

	Cheiron Federated Tier 2	Bartel Associates Estimate Alternative Tier 2
	6/30/13 Val.	2@62, Max 2.5@67
Normal Cost	11.04% (Employee and City)	13.2% (Employee and City)
Total Cost Difference (All Funds)	-	\$723K (City Only)

- Current benefit compared to CalPERS Public Employees' Pension Reform Act (PEPRA) benefit
- Alternative Tier 2 estimated based on 6/30/11 data & Tier 2 retirement rates
- Adjusted for 6/30/13 assumption & demographic changes
- If retroactive, creates an unfunded liability shared 50/50 between City and Tier 2 employees
- Cost difference based on FY14-15 Adopted budget, Cost to General Fund is \$409,253

Police Tier 2 Total Normal Cost Based on PEPRRA

	Police Cheiron Tier 2	Bartel Associates Estimate Alternative Police Tier 2	
	6/30/13 Val.	2.5% @ 57	2.7% @ 57
Normal Cost	21.60% (Employee and City)	27.7% (Employee and City)	28.4% (Employee and City)
Total Cost Difference (All Funds)	-	\$357K (City Only)	\$398K (City Only)

- Current benefit compared to CalPERS Public Employees' Pension Reform Act (PEPRA) benefit
- Alternative Tier 2 estimated based on 6/30/11 data & Tier 2 retirement rates
- Adjusted for 6/30/13 assumption & demographic changes
- If retroactive, creates an unfunded liability shared 50/50 between City and Tier 2 employees
- No costing for Fire Tier 2 since it was not yet effective
- Cost difference based on FY 14-15 Adopted Budget

Additional Federated Tier 2 Scenarios

	Federated Current Tier 2	Federated Scenario
Formula	2.0% at 65	2.0% at 62
Maximum Benefit	65%	65%
COLA	1.5% based on CPI	1.5% based on CPI
Ability to Retire at Any Age with 30 yrs	None	None
Final Average Salary	3 years	3 years
Normal Cost	11.04%	11.8%

Additional Police Tier 2 Scenarios

Fiscal Year 14-15	Current Police Tier 2	Police Scenario 1	Police Scenario 2	Police Scenario 3a	Police Scenario 3b	Police Scenario 4*
Formula	2% at 60	2% at 57	2% at 60	2% at 57	2% at 57	2.5% at 55
Maximum Benefit	65%	65%	75%	75%	65%	75%
COLA	1.5% based on CPI	1.5% based on CPI	1.5% based on CPI	2.0% based on CPI	2.0% based on CPI	2.0% based on CPI
Ability to Retire at Any Age with 30 yrs	None	None	None	None	Yes	Yes
Final Average Salary	3 years	3 years	3 years	3 years	3 years	3 years
Normal Cost	21.60%	23.0%	22.0%	24.3%	24.7%	28.6%*

* Fire Tier 2 not costed

Questions and Discussion