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November 29, 2012

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*VIA E-Mail and US Mail*

Christopher E. Platten  
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**Re: New Employee Retirement  
City of San Jose and IAFF Local 230**

Dear Chris:

We are in receipt of your letter dated October 4, 2012. Notably, the second tier was a component of retirement reform negotiations between the City and the San Jose Fire Fighters, IAFF Local 230 (Local 230), which began in fiscal year 2010-11. Per the framework signed by Local 230 in June 2011, Local 230 and the City mutually agreed to “*negotiate concurrently* on the issues of retirement reform and related ballot measure(s). Negotiation of retirement reform shall include pension and retiree healthcare benefits for current *and future employees.*” The framework also specifically provided that Local 230 and the City agreed that, “(i)f the parties are unable to reach an agreement on retirement reform and/or related ballot measure(s) by October 31, 2011, the parties shall proceed to impasse.” Pursuant to this framework, IAFF Local 230 and the City engaged in negotiations from June 2011 through October 2011. Thereafter, the parties engaged in mediation over the second tier in November 2011, and again in January and February 2012.

The City provided Local 230 with specific proposals for the second tier on September 15, 2011; October 24, 2011; February 10, 2012 (in mediation); and again on September 12, 2012 (this final proposal was substantively identical to the one provided in February).

Questions about the second tier should have been presented to the City during the negotiations, or at least during the two rounds of mediation the parties engaged in between October of 2011 and June of 2012. While the City is happy to answer to Local 230’s questions regarding the second tier retirement benefits, the parties remain at impasse over the second tier retirement benefit and Local 230’s refusal to agree to move this matter forward to interest arbitration is in violation of the City Charter.



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Nevertheless, in order to best facilitate resolution of this matter, please find below information responsive to the questions raised in your October 4<sup>th</sup> letter. Some of the questions you raised can be found in the proposal provided to IAFF Local 230 on February 10, 2012 and September 12, 2012, and which represents the *maximum* benefit levels permissible under the Charter as amended by Measure B.

***1. Please provide copies of all prior City proposals limited to the issue of second tier retirement benefits and not to any charter amendment.***

The proposals provided to IAFF Local 230 regarding second tier retirement benefits for new employees may be found on the City's website:

<http://www.sanjoseca.gov/index.aspx?nid=3174>

***2. Does the City contend that the parties are prohibited by Measure B from negotiating retirement benefits other than the second tier pension benefits other than those set forth in Measure B? If so, please explain.***

As previously noted, the City's proposal to Local 230 during mediation on February 10, 2012 and again on September 12, 2012 reflect the maximum benefit levels permissible under the Charter as amended by Measure B. While the Union is free to propose a higher level of benefits, voter approval of those benefits would be required before they could be implemented.

***3. Does the City contend that an interest arbitrator under Charter Section 1111 is not empowered to award a second tier pension benefits other those provided for in Measure B? If so, please explain.***

As previously noted, the City's proposal to Local 230 during mediation on February 10<sup>th</sup> and again on September 12<sup>th</sup> reflect the maximum benefit levels permissible under the Charter as amended by Measure B. Because the right of the City Council to place a measure on the ballot is placed solely in the hands of the City Council, an arbitrator could not require the Council to place a measure on the ballot seeking a higher level of benefits.

***4. Does the City contend that it has a "reservation" of existing rights to alter second tier pension plans at any time? If this is the case, does it believe that it can alter the provisions regarding age, future accruals, vesting period, medical benefits, calculation of benefits based on final average salary, or all of the above?***

The Reservation of Rights language provides notice to any new employee that if they accept employment with the City, any provision of the retirement plan is subject to modification. It should be noted, however, that the City has never



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taken the position that benefits which have already been earned and accrued (e.g., prior years of service) may be altered after the service is rendered; otherwise the City will look at the reservation of rights on a case by case basis.

**5. *Does the City contend that under Measure B it must negotiate benefits with a “reservation” of rights to alter those benefits at any point in time?***

As stated above, the Reservation of Rights language provides notice to any new employee that if they accept employment with the City, any provision of the retirement plan is subject to modification. The City Council’s authority to negotiate benefits is subject to this Charter requirement.

**6. *Measure B does not define the vesting period. How many years will be required for a new employee to vest under the City’s proposal?***

As provided in the City’s proposal to Local 230 during mediation on February 10<sup>th</sup> and again on September 12<sup>th</sup>, employees in the second tier are eligible to retire “after earning ten (10) years of retirement service credit,” in addition to the age requirement. This is consistent with Measure B as well as the vesting period for current “Tier 1” employees in the Police & Fire Department Retirement Plan, who are required to have ten (10) years of service to be eligible to leave their contributions in the plan.

**7. *Does the City contend that under Measure B “final compensation” may not be defined by the bargaining parties? If so, please explain.***

As specifically defined by Measure B, final compensation for employees in the second tier “shall mean the average annual earned pay of the highest three consecutive years of service. Final compensation shall be base pay only, excluding premium pays or other additional compensation.” As noted above, while the Union remains free to propose a higher level of benefit, any increase would require voter approval.

**8. *Does the City contend that the amortization period to be used for second tier pension benefits is beyond the scope of bargaining? If so, please explain.***

Any amortization period will be determined and set by the independent Police & Fire Department Retirement Plan Board consistent with the City Charter and any applicable laws or regulations. Since neither the City nor Local 230 can exercise control over the amortization period, it is outside the scope of representation.

**9. *Does the City propose to credit employee accounts for amounts paid into the plan for purposes of unfunded actuary accrued liability?***



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Second tier employee contributions are expected to be treated similar to contributions made by current “Tier 1” employees and are subject to withdrawal, return and redeposit in the same manner as any other employee contributions.

***10. Does the City contend that employees who separate from City employment may not receive a refund of both normal and unfunded liability contributions? If so, please explain.***

Second tier employee contributions are expected to be treated similar to contributions made by current “Tier 1” employees and are subject to withdrawal, return and redeposit in the same manner as any other employee contributions.

***11. Does the City contend that the interest rate used to calculate moneys paid to separating an employee is beyond the scope of negotiation? If so, please explain.***

Any interest rate will be determined and set by the independent Police & Fire Department Retirement Plan Board consistent with the City Charter and any applicable laws or regulations. Since neither the City nor Local 230 can exercise control over the amortization period, it is outside the scope of representation.

***12. Does the City contend that it is beyond the scope of bargaining to negotiate an annual cap on unfunded liability amounts an employee or the City is required to make? If so, please explain.***

Measure B states: “If the City provides a defined benefit plan, the City’s cost of such plan shall not exceed 50% of the total cost of the Tier 2 defined benefit plan (both normal cost and unfunded liabilities).” As noted above, while the Union remains free to propose a higher level of benefit, any increase would require voter approval.

***13. Does the City contend that it is beyond the scope of bargaining to negotiate “smoothing” period regarding recognition of gains and losses for the second tier pension benefits? If so, please explain.***

Any “smoothing” period will be determined and set by the independent Police & Fire Department Retirement Plan Board consistent with the City Charter and any applicable laws or regulations. Since neither the City nor Local 230 can exercise control over the amortization period, it is outside the scope of representation.



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***14. Does the City contend that participants in a second tier pension plan may be prohibited from individually opting into social security coverage? If so, please explain.***

New hires will be required to participate in the pension plan which meets the requirements so that entry into Social Security is not required. We are not aware of any option available to an individual employee to opt out of the pension plan or to individually opt into Social Security coverage.

***15. Does the City contend that deferred vested participants in the pension plan will, upon re-employment with the City, have all prior service time converted to benefit formulas under any second tier pension plan? If so, please explain.***

Employees will maintain the benefit formula of 2.5% per year for their prior years of service. Upon choosing to reemploy with the City, the employee will be in the second tier and will be entitled to those benefits under the second tier for the period following their re-employment.

***16. Does the City contend that investment gains can only be used to reduce the required City contribution rate and not an employee participant? If so, please explain.***

Should the plan ever become over 100% funded, amounts over full funding of the plan may be used to reduce contribution rates.

***17. Does the City possess a qualification letter from the Internal Revenue Service concerning its proposal or the provisions for a second tier pension benefit under Measure B? If so, please provide a copy.***

The City has a qualified determination letter from the IRS for the Federated City Employees' Retirement System. The City is awaiting the favorable determination letter from the IRS for the current Police and Fire Department Retirement Plan. We do not have a public legal opinion regarding the provision mentioned in your question.

***18. Does the City contend that its proposed second tier benefits constitute a tax qualified plan as required by the Internal Revenue Service? If so, please provide any documents so stating.***

The City believes the Tier 2 provisions meet IRS requirements.



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***19. Is the City aware of any limit under law on the amount an employee can contribute pre-tax into a pension fund should the employee's share of unfunded liability consume more than 25% of the income? If so, please provide any relevant documents.***

Based on information from our outside tax advisor, this answer is with respect to a governmental defined benefit plan only. It does not cover a defined contribution plan or a 457 deferred compensation plan. With respect to mandatory pre-tax employee contributions – which are essentially treated as employer contributions – there is no IRS defined benefit plan contribution limit; the total employer contributions and employee pre-tax mandatory contributions can be whatever is necessary to fund the benefit under the plan. The benefit payable to each participant in the plan is subject to the applicable Code Section 415(b) limit (the 2012 dollar limit is \$200,000, but that is reduced for different forms of benefit, different retiree ages, etc.).

***20. Does the City contend that under Measure B second tier participants must contribute for half of the current and unfunded actuary accrued liability of retiree health care inclusive of medical and dental benefits? If so, please explain.***

There is currently no second tier related to retiree healthcare.

***21. What minimum level of retiree health care benefits will second tier employees be guaranteed under the City's proposal?***

There is currently no second tier related to retiree healthcare.

***22. Will second tier pension benefit participants contributions for retiree health care be on a pre-tax basis? If so, please provide any documents establishing that fact.***

There is currently no second tier related to retiree healthcare.

***23. Does the City contend that the second tier pension benefit plan will have reciprocity with benefits under pension plans in effect throughout the state of California with CalPERS and 1937 Act plans? If so, will second tier pension benefit participants have reciprocity with the new AB 340 Public Safety Plan of 2.7% at age 57?***

As provided in the City's proposal to the Local 230 during mediation on February 10<sup>th</sup> and again on September 12<sup>th</sup>, employees in the second tier "shall be eligible for the benefits under the reciprocal agreement with CalPERS that are in effect at the time of the employee's retirement."



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Negotiations between the City and the Local 230 have been ongoing for over a year and both sides have had ample opportunity to discuss the details of a second tier retirement benefit. Despite the best efforts of both sides, we have not yet come to any agreement on this matter. Per the framework mutually agreed upon in June 2011, the parties reached impasse on this issue on October 31, 2011, and we remain at impasse. As previously indicated, the City's current proposal represents the maximum benefits allowed under Measure B. Accordingly, we do not believe that there should be any reason to delay the selection of a neutral and the scheduling of arbitration.

Sincerely,

Charles Sakai

cc (via e-mail only): Alex Gurza, Deputy City Manager  
Nora Frimann, Assistant City Attorney  
Jennifer Schembri, Assistant to the City Manager