

**SENT VIA EMAIL**

June 7, 2012

Vera Todorov  
President  
Association of Legal Professionals (ALP)  
c/o City Attorney's Office  
200 E. Santa Clara Street  
San Jose, CA 95113

**RE: ALP's Public Records Act Request Dated May 25, 2012**

Dear Ms. Todorov:

The City is in receipt of ALP's Public Records Act (PRA) Request dated May 25, 2012. It is our understanding that ALP had received numerous documents related to retirement issues directly from the City's Public Records Manager, and that these may overlap with the information ALP is seeking via its May 25<sup>th</sup> PRA.

In any event, the City is unaware of any records responsive to ALP's first and second request for information and, even if these records were available, they may be subject to the Attorney-Client privilege. Regarding ALP's second request for information, however, please find enclosed the opinion from Meyers Nave dated March 5, 2012, which may provide further information; this opinion has also been posted online at:

- <http://www.sanjoseca.gov/employeeRelations/retirementreform/LegalOpinionRERevisedBallotMeasure.pdf>

As to ALP's third request for information, please find enclosed the presentation provided by the City on or about May 1, 2012, as well as the supplemental memo dated April 27, 2012, related to the estimated savings from the City's Last, Best and Final Offer on Healthcare, Medicare Part A and B, and Pension Benefits for New Employees. These documents are also available online at:

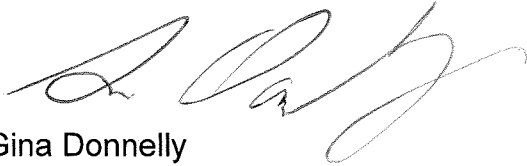
- **May 1, 2012 Council Presentation:**  
<http://www.sanjoseca.gov/employeeRelations/retirementreform/5.1.12OpenSessionItems3.3To3.12.pdf>

- **April 27, 2012 supplemental memo:**  
[http://www.sanjoseca.gov/clerk/Agenda/20120501/20120501\\_0303012.pdf](http://www.sanjoseca.gov/clerk/Agenda/20120501/20120501_0303012.pdf)

As to ALP's fourth request for information, the City is unclear regarding what ALP means by "new compensation;" we would appreciate clarification on what "new compensation" ALP is making reference. Furthermore, we would also appreciate clarification on what any potential "post employment benefits for *new* employees" ALP believes will have "possible impacts to *current* employees," and what those impacts may be.

We are reviewing ALP's other requests for information and will provide responses to ALP as the information becomes readily available.

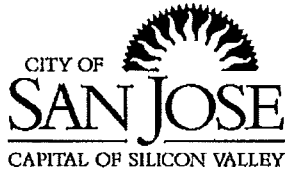
Sincerely,



Gina Donnelly  
Deputy Director of Employee Relations

c: Debra Figone, City Manager  
Richard Doyle, City Attorney

Enclosure



## Memorandum

**TO:** HONORABLE MAYOR  
AND CITY COUNCIL

**FROM:** Richard Doyle  
City Attorney

**SUBJECT:** Legal Opinion Related to the  
Revised Ballot Measure

**DATE:** March 5, 2012

Attached is a public legal opinion from Meyers Nave related to the Revised Ballot Measure recommended by the City Manager under item 3.5 for Council consideration on March 6, 2012. In the past several months the Council has received oral and written legal advice related to pension reform and proposals for ballot measures. That advice was provided to the Council as privileged attorney-client communications in closed session and is subject to the confidentiality of those sessions. The contents of that advice are confidential unless and until there is a decision to waive the privileged and confidential nature of the communications.

RICHARD DOYLE  
City Attorney

By 

Ed Moran  
Assistant City Attorney

cc: Debra Figone

MEMORANDUM

**DATE:** March 5, 2012  
**TO:** Richard Doyle, City Attorney  
**FROM:** Arthur A. Hartinger  
Linda M. Ross  
Jennifer L. Nock  
**RE:** Proposed Charter Amendment -- Sustainable Retirement Benefits and Compensation Act

I. INTRODUCTION

In December 2011, the San Jose City Council voted to place on the ballot a Charter Amendment that addresses City employee retirement benefits. The City Manager is recommending that the Council consider a revised ballot measure entitled the "Sustainable Retirement Benefits and Compensation Act" (the "Act"), dated February 21, 2012. You asked us to provide a summary of the legal authority relevant to the Charter Amendment.

Whenever an agency modifies retirement-related benefits, there are legal risks, particularly with respect to vested rights challenges. But as set forth below, we believe the Act overall is defensible against a potential legal challenge. We review key sections of the Act, and note that these sections involve different degrees of legal risk.<sup>1</sup>

We are aware that since the City published and circulated the first draft of the Act last summer, the City has made numerous amendments. As a result, subsequent versions eliminate or significantly reduce many of the legal risks identified in the first draft.

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<sup>1</sup> We note that this opinion does not encompass legal risks that may be brought related to bargaining obligations under the Meyers-Millias-Brown Act (MMBA), California Government Code section 3500, et seq. It is our understanding, however, that the City has met and conferred with City labor unions under the MMBA as required by law.



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The "Findings" for the Act state that the City's ability to provide its citizens with "Essential City Services" -- such as police and fire protection, street maintenance and libraries -- is threatened by budget cuts. The stated "Intent" of the Act is to "ensure the City can provide reasonable and sustainable post employment benefits while at the same time delivering Essential City Services."

The key provisions of the Act include: a requirement that employees receive adjusted compensation in the form of additional employee contributions towards their retirement systems' "unfunded liability" (Section 6); the creation of a new less expensive plan into which employees may voluntarily "opt in" (Section 7); the creation of a "Tier 2" hybrid plan for new employees (Section 8); authority to reduce COLA payments in the event of a fiscal emergency (Section 10); the elimination of the supplemental retiree benefit reserve (Section 11); and a "savings" clause that adjusts employee compensation in the event a court does not permit the increase in employee contribution rates pursuant to Section 6 (Section 14).

Below we provide legal background and then discuss each of these sections.

## II. LEGAL BACKGROUND

**Charter City.** San Jose is a Charter City. The California Constitution, section 5, subdivision (b)(4), gives charter cities "plenary authority to provide in their charters for the compensation of their employees." *Sonoma County Organization of Public Employees v. County of Sonoma*, 23 Cal. 3d 296, 317 (1979). The San Jose City Charter itself affirms the City's "power to make and enforce all laws and regulations in respect to municipal affairs ...." (Charter, Section 200 [General Powers].)

**Retirement Plans.** Whether to have a pension plan, and the level of benefits provided, is a municipal affair subject to the City's home rule authority. The San Jose Charter grants the City Council the authority to create and change retirement plans for City employees. "Subject to other provisions of this article, the Council may at any time, or from time to time, amend or otherwise change any retirement plan or plans or adopt or establish a new or different plan or plans for all or any officers or employees." (Section 1500 [Duty to Provide Retirement System]; *see also* Section 1503.)

The Charter provides for certain "Minimum Benefits" for employees. The Charter requires that employee contributions to their retirement plans "because of current service or current service benefits" (called "normal cost" contributions) be paid in a ratio of "three (3) for such officers and employees to eight (8) for the City." (Sections 1504(b); 1505(c).) But the Charter does not address the payment towards pension plan unfunded liabilities.

In 2010, the voters amended the Charter to authorize the Council to enact ordinances that exclude new employees from any existing retirement plan or retirement benefit. (Charter section 1501(b).)

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**Charter Revisions.** Under the home rule provisions of the state constitution, the “governing body . . . of a county or city may propose a charter or revision.” (Cal Const., Art. XI, Section 3(b).) Under this authority, the City Council is proposing an amendment to establish new Charter requirements in connection with employee compensation and retirement. The City Council has the authority to place an amendment on the ballot after the City conducts “meet and confer” with employee organizations. *Seal Beach Police Officers Assn. v. City of Seal Beach*, 36 Cal. 3d 591, 601 (1984).

**Vested Rights.** A retirement benefit is considered “vested” if the employees or retirees are deemed to have a legal right, protected under the Constitution, to receive that benefit. The enforceable legal right between the employer and employee generally stems from an official enactment – Charter, statute or ordinance – that sets the terms of the benefit the employer agrees to provide. *See International Association of Firefighters v. City of San Diego*, 34 Cal. 3d 292 (1983).

Before a Court will enforce a claimed contractual right there must be “clear” and “unmistakable” evidence that the public entity intended itself to be bound to provide the benefit. The California Supreme Court recently held that: “legislation in California may be said to create contractual rights when the statutory language or circumstances accompanying its passage ‘clearly... evince a legislative intent to create private rights of a contractual nature enforceable against the [governmental body].’” *Retired Employees Assn of Orange County, Inc. v. County of Orange*, 52 Cal. 4<sup>th</sup> 1171, 1187 (2011). [Emphasis added] Federal law similarly requires “clear and unmistakable” evidence that a governmental entity “intends to bind itself contractually.” *San Diego POA v. San Diego City Employees Retirement System*, 568 F.3d 725, 737 (9<sup>th</sup> Cir. 2009).

### III. LEGAL DISCUSSION

We discuss below the key provisions of the Act.

#### A. Current employees -- Reduction In Compensation In Form Of Increased Employee Contribution Rates (Section 6).

1. **Charter Amendment.** Beginning June 23, 2013, the Act requires that the compensation of current employees be adjusted to help defray the unfunded liabilities in their pension plans. To do so, the Act requires employee compensation to be reduced in increments of 4% of pensionable pay per year, up to a maximum of 16% of pensionable pay per year. But in any year, employees are not required to contribute more than 50% of the yearly cost to amortize pension plan unfunded liabilities. (Section 6(b).)

Under the Act, the adjustments in compensation will be treated as additional retirement contributions credited to employees’ retirement accounts. (Section 6(e).) The Act does not alter the existing 3/8 ratio that governs employee and City contributions towards the

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"normal cost" of pension plans. Rather, the Act addresses only the contributions required to amortize the "unfunded liability" of the plans.

2. **Legal Discussion.** There are arguments that this requirement does not implicate employees' vested rights. The City Charter never bound the City to pay the entire amount needed to defray the "unfunded liabilities" of the retirement systems, and the City's Municipal Code and past practices reflect this understanding. Thus, the voters may amend the Charter to legally require employees to share in that burden.

a. **Charter.** As explained above, the San Jose Charter reserves the City's right to create and amend the City's retirement plans. (Charter Sections 1500, 1503.) The Charter establishes employee and city ratios (3 to 8) that pertain to the contribution rates for "current service" otherwise known as "normal cost." But the Charter does not address the "unfunded liabilities" of the retirement systems. The Charter left that topic to the City Council to address in the Municipal Code and, as indicated above, reserved the right for the Council to make changes.

Based on the information we have seen to date, the City has asserted its authority -- in the Municipal Code and Memoranda of Agreement with City unions -- to require employees to pay towards the pension systems' unfunded liability.

b. **Municipal Code.** San Jose's Municipal Code and past practices specifically permit modification of employee contribution rates. These provisions and practices are evidence that San Jose did not intend to bind itself to pay the entire amount of pension system unfunded liabilities, but reserved the right to require employee participation in the form of additional employee contributions.

**Federated employees.** Section 3.28.200 of the 1975 Federated City Employees Plan permits the retirement board to fix and change rates of contribution for employees and the City "as it may determine reasonably necessary to provide the benefits provided for by this retirement plan." Other Code sections require employees to pay a "normal rate" of contribution (also called "normal cost") for current service (Part 6, Section 3.28.700, 3.28.710), and require the City to pay both a "regular current service rate" (again, also called "normal cost") and a "current service deficiency rate" of contribution. (Part 7, Section 3.28.850, 3.28.860.) Consistent with this latter Code section, the City has paid a contribution rate towards pension system unfunded liabilities.

But the Code not only requires employees to make contributions towards "normal cost," it also gives the City the authority to require employees to make additional retirement contributions. In 2010, the Code was amended to read: "Notwithstanding any other provisions of this Part 6 or of Chapter 3.44, members of this system shall make such additional retirement contributions as may be required by resolution adopted by the city council or by agreement with a recognized bargaining unit." (Section 3.28.755.)

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Moreover, the Code expressly gives the City an offset from its contribution obligations, as determined by the retirement system actuary, for "the additional employee retirement contributions made by employees under section 3.28.755 against the retirement contributions that the city would otherwise be required to make under this Part 7." (Section 3.28.955.)

**Safety employees.** The Municipal Code similarly permits the modification of the employee contribution rates required from safety employees through resolution, agreement or arbitration, as appropriate, and permits an offset against the City's own obligations. (Section 3.36.1520, Section 3.36.1525, see also 3.36.1560.)

Based on the above provisions, the Code provides authority for additional employee contributions, and specifically permits the application of those contributions against the City's obligations – such as contributions towards deficiencies in the retirement system.

As stated above, in 2010 the City Council enacted the Code sections authorizing additional employee contributions. In connection with their enactment, the City and some bargaining groups agreed that employees would make payments of additional employee retirement contributions towards the retirement systems' unfunded liabilities. But the Code does not require "agreement" to impose additional contribution rates; it also permits the City to do so by resolution, or through binding arbitration. These provisions codified the City's understanding that it had the authority to require additional employee contributions to defray the retirement systems' unfunded liabilities.

Based on the Charter, Municipal Code and the City's practices, San Jose has arguments that it never bound itself to limit employee contributions, but reserved the right to increase employee contributions, including to pay for unfunded liabilities. In that case, San Jose's employees had no reasonable expectation that their contribution rates could not be raised in order to share in the expense of unfunded liabilities. See *International Association of Firefighters v. City of San Diego*, 34 Cal.3d 292, 300-302 (1983) (no vested right to contribution rates when pension plan expressly provided for modification of contribution rates based on periodic actuarial investigations).

**c. Changes in compensation.** In addition to relying on the Charter and Municipal Code, the City reasonably may argue that the changes to employee contribution rates in fact are changes to employee compensation, over which it has plenary authority under the state constitution.

As explained above, San Jose has the constitutional authority to set employee compensation in its Charter. If the City had simply reduced compensation to afford additional payments into the retirement system, no vested right would be implicated. "It is well established that public employees have no vested rights to particular levels of compensation and salaries may be modified or reduced by the proper statutory authority."

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*San Diego POA v. San Diego City Employees Retirement System*, 568 F.3d 725, 738 (9th Cir. 2009), quoting *Tirapelle v. Davls*, 20 Cal. App. 4<sup>th</sup> 1317 (1993); see also *Butterworth v. Boyd*, 12 Cal. 2d 140, 150 (same).

Instead of reducing compensation, the proposed amendment permits employees to contribute additional amounts to the retirement system. This characterization is to the benefit of employees, because it prevents a reduction in the "final compensation" used to compute retirement allowances. Since there is no vested right to a particular level of compensation, there should be no vested right that prevents the City, in lieu of a decrease in compensation, from requiring additional employee contributions into the retirement system.

In summary, the City has reasonable arguments, based on the City's Charter and Municipal Code, and its practices, that the City never bound itself to completely subsidize the deficiencies of the retirement funds, and thus can require employees to share in that cost through higher employee contribution rates. Further, the City has an argument that its constitutional authority over employee compensation enables it to adjust compensation in the form of additional employee contributions towards unfunded liabilities.

We recognize, however, that aspects of these arguments are untested. City employees may contend that the City created the expectation, through its historical practices, that it would pay for all unfunded liabilities, despite the contrary provisions of the City Code and union agreements. And prior judicial decisions have held that the employee contribution rates at issue in those cases were vested rights. See e.g., *Allen v. City of Long Beach*, 45 Cal. 2d 128, 130-131 (1955); *Wisley v. City of San Diego*, 188 Cal. App. 2d 482, 485-487 (1961). These decisions did not address the particular arguments that will be made by the City, and we believe the courts will revisit this issue in light of the modern practice of bargaining and treating as interchangeable, wages, employee contribution rates and other benefits. But as in any case involving vested rights, there can be no certainty as to any judicial outcome in the event of a legal challenge.

#### **B. Current Employees - VEP (Section 7).**

Under the Act, employees who do not want their pay adjusted in the form of higher contribution rates may opt into a one time "Voluntary Election Program." In exchange for no reduction in pay, the VEP provides a different pension plan. The VEP reduces the accrual rate for future service (2% per year), raises the eligibility age for retirement over time (55 to 62 for miscellaneous, 50 to 57 for safety), limits cost of living adjustments to 1.5% of CPI, and requires "final compensation" to be determined by an average of three years pay instead of one, among other changes. (Section 7(b).)

The VEP is legally permissible on its face, as a voluntary alternative to payment of additional employee retirement contributions. Courts have enforced agreements by individual employees to give up existing benefits and select a new pension plan. See

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*Pasadena Police Officers Assn v. City of Pasadena*, 147 Cal. App 3d 695, 706-707 (retirees gave up fixed pension in exchange for city's promise to pay a pension that would rise or fall based on the cost of living index).

As demonstrated above, the City has arguments that it may require employees to pay additional retirement contributions. But if a Court invalidated this requirement, the Court might not hold employees who elected VEP to their VEP election

#### C. New Employees – Hybrid Plan (Section 8).

The Act requires the City to adopt a "Tier 2" retirement program for employees hired after the program is enacted. Under the Act, 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. (Section 8(a).)

This proposal plainly does not affect vested rights. A public entity may change the benefits offered to new employees, who have only the right to benefits conferred during employment. *Legislature v. Eu*, 54 Cal. 3d 492, 534 (1991); *Claypool v. Wilson*, 4 Cal App. 4<sup>th</sup> 646, 670 (1992).

In 2010, in accordance with this principle, the voters amended the City Charter to permit the City Council by ordinance to exclude new employees from any existing plan. (Charter section 1501(b).) The Act provides further guidance by setting the parameters for the modified plans to be offered to new employees.

#### D. Emergency Measures to Contain Cost of Living Adjustments (Section 10).

Under the Act, if the City Council "adopts a resolution declaring a fiscal and service level emergency, with a finding that it is necessary to suspend increases in cost of living payments to retirees," the City may temporarily suspend cost of living adjustments in whole or in part for up to five years. (Section 10(a).)

Even if a court determined that a change in the COLAs would impair vested rights, "a substantial impairment may be constitutional if it is 'reasonable and necessary to serve an important public purpose.'" *Valdes v. Cory*, 139 Cal. App. 3d 773, 790-791 (1983); *see also Sonoma County Organization of Public Employees v. County of Sonoma*, 23 Cal. 3d 296, 304 (1979).

In making this assessment, courts analyze whether the enactment: (1) serves to protect the basic interests of society; (2) has an emergency justification; (3) is appropriate for the emergency, and (4) is designed as a temporary measure, during which contract rights

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are only deferred. *Olson v. Cory*, 27 Cal. 3d 532, 539 (1980), citing *Sonoma County*, 23 Cal. 3d at 305-306 (1979).

Based on the above authority, it is legally permissible for the Act to grant this emergency authority to the City Council to reduce COLAs. Whether the Council's actions implicate vested rights or satisfy the above requirements cannot be determined until the time of the emergency enactment.

#### E. Supplemental Payments to Retirees (Section 11).

The Act discontinues the Supplemental Retiree Benefit Reserve and returns its assets to the appropriate retirement trust fund. Any supplemental payments to retirees may not be funded from plan assets.

The Supplemental Retiree Benefit Reserve ("SRBR") permits the allocation of excess investment income earned by retirement fund assets to an account to fund supplemental benefits for retirees. The City has changed the formula for distribution of benefits to retirees over the years. For example, in 2005, the City Council enacted Municipal Code Section 3.28.340(E), which stated that the Council, after consideration of the Board's recommendation "shall determine the distribution, *if any*, of the supplemental retiree benefit reserve to said persons." [Emphasis added.] Moreover, we are informed that the City has not always paid this benefit.

The language of the Municipal Code, quoted above, and the City's practices are evidence that retirees do not have a vested right to payments from the SRBR.

#### F. Savings Provision (Section 14).

Section 6(b) requires current employees, not enrolled in Tier 2, to have their compensation adjusted in the form of additional contributions to their retirement funds. Under Section 14, in the event Section 6(b) is determined to be "illegal, invalid or unenforceable as to Current Employees then to the maximum extent permitted by law, an equivalent amount of savings shall be obtained through pay reductions."

As explained above in the section on Legal Background, San Jose has the constitutional authority to set employee compensation in its Charter. And public employees "have no vested rights to particular levels of compensation and salaries may be modified or reduced by the proper statutory authority." *San Diego POA v. San Diego City Employees Retirement System*, 568 F.3d at 738. Although reduced compensation will affect an employee's "final compensation" for retirement purposes, "indirect effects on pension entitlements do not convert an otherwise unvested benefit into one that is constitutionally protected." *Id.*

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Therefore, there is authority to support the alternative of reducing pay in order to pay the unfunded liabilities of the pension system. The City has sound arguments in favor of voter authority to determine compensation, after meet and confer with employee organizations. But this is a developing area of the law and as we stated above, in any case involving vested rights, there can be no certainty as to any judicial outcome in the event of a challenge.

## V. CONCLUSION

The City has made numerous amendments since it published and circulated the first draft of the Act last summer. As a result, subsequent versions eliminate or significantly reduce many of the legal risks identified in the first draft.

We believe the Act in its present state is defensible against a potential legal challenge. But some sections involve a different degree of risk than others. We have reviewed each of these sections and identified the arguments in favor of their legality and the risk that a court may find that they violate employees' vested rights. The Act contains a severability provision. If a Court were to invalidate portions of the Act, this provision enables the City to still implement others.



**CITY COUNCIL OF THE  
CITY OF SAN JOSÉ**

**May 1, 2012**

Items 3.3, 3.4, 3.5, 3.6, 3.7, 3.8, 3.9,  
3.10, 3.11 & 3.12



- Current Employees
- Retirees
- Future Employees
- Taxpayers

## **Last, Best and Final Offers- April 16th**

- Pursuant to City Council direction, provided Last, Best, and Final Offers to bargaining units on April 16<sup>th</sup>
  - Healthcare- Lowest Priced Plan
  - Medicare Part A and B
  - Pension Benefits for New Employees (Federated)

# Healthcare – Lowest Priced Plan

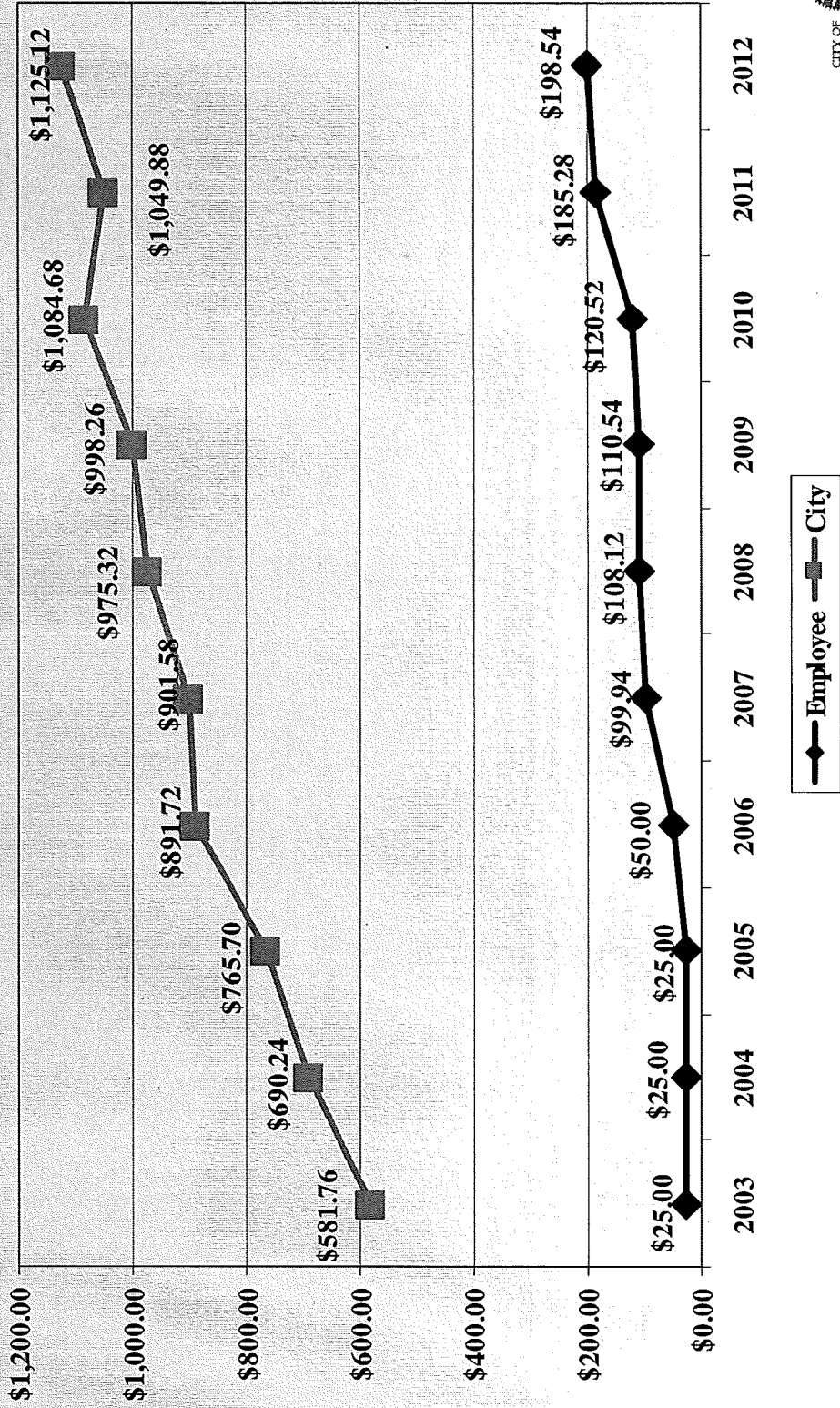




# Healthcare Premiums

- City of San Jose's premiums are blended—  
active employees and retirees
- Eligible retirees choose among plans offered to  
active employees
- Premium cost sharing and plan design affect  
costs

# Monthly Lowest Cost Healthcare Plan Premium History 2003-2012



# Healthcare Premiums Cost Sharing

## Active Employees

- 85% City/15% Employee of lowest priced plan (single or family)

## Retirees

- 100% of premiums paid for lowest priced plan (single or family) available to active employees (at 15 years of service)

# Active Employee & Retiree Healthcare Cost Comparison

<b>Active Employee Monthly Premium (85/15 LPP)</b>	
Single Coverage	\$79.72
Family Coverage	\$198.54

<b>Retiree Monthly Premium (100% LPP)</b>	
Single Coverage	\$0
Family Coverage	\$0



# Retiree Healthcare Liability and Funding Ratio

Retiree Healthcare Unfunded Liability and Funding Ratio		
	<i>Unfunded Actuarial Liability</i>	<i>Funding Ratio</i>
Federated	\$800.505 Million	14.00%
Police and Fire	\$596.764 Million	9.20%
<b>Total</b>	<b>\$1.397 Billion</b>	

# City/Active Employee Cost Sharing for Retiree Healthcare Funding

- Retiree Medical
  - Costs split 50%-50%
- Retiree Dental
  - Costs split approximately 75%-25%

# Historical & Projected Retiree Healthcare Contribution Rates (Federated)

Fiscal Year	Employee	City	Total
2008-2009	4.65%	5.25%	9.90%
2009-2010	5.07%	5.70%	10.77%
2010-2011	5.76%	6.41%	12.17%
2011-2012	6.51%	7.16%	13.67%
2012-2013	7.26%	7.91%	15.17%
2013-2014	15.50%	16.84%	32.34%

Source: Projections developed by Federated Retirement System's Actuary, Cheiron



# Projected Retiree Healthcare Contribution Rates at Full Funding (Police and Fire Plan)

Fiscal Year	City and Police Total Contribution	City and Fire Total Contribution
2012-2013	17.22%	12.72%
2013-2014	19.82%	15.32%
2014-2015	29.74%	17.92%
2015-2016	29.20%	20.52%
2016-2017	29.17%	31.07%

Source: Projections developed by Police and Fire Department Retirement System's Actuary, Cheiron





# **City's Proposed Changes to Healthcare**

## **Effective January 1, 2013:**

- Introduce a fourth healthcare plan option
  - “High Deductible Plan”
- Maintain 85/15 cost sharing for the lowest priced Non-Deductible HMO plan for active employees
  - Currently the Kaiser \$25 co-pay HMO plan

# Active Employees -Lowest Priced Plan

	Active Employees Cost: \$25 Co-Pay Plan Premiums	Active Employees Cost: High Deductible Plan Premiums
<b>Single Coverage</b>	<b>\$79.72/mo*</b>	<b>\$0*</b>
<b>Family Coverage</b>	<b>\$198.54/mo*</b>	<b>\$0*</b>

\*Based on rates for Calendar Year 2012. Calendar Year 2013 rates subject to increase.



# Retiree Healthcare-Lowest Priced Plan

	Current Retiree Costs	Retiree Costs – With High Deductible Implementation
Non-Medicare LPP (High Deductible)	N/A	\$0
Non-Medicare \$25 Co-pay	\$0	\$129.96/mo (single) \$323.62/mo (family)
Medicare Supplement LPP	\$0*	\$0*

\*Retirees enrolled in Medicare Part B (\$99.90-\$319.70/mo.) and Medicare Part D (\$0-\$66.40/mo.)





# Average Retiree Pension Non-Medicare Eligible (Under Age 65)

	Base	COLA	Total Pension	Average 2013 COLA	Average Years of Service
Federated City Employees' Retirement System	\$41,777	\$5,311	\$47,087	\$1,413	21.11
Police and Fire Department Retirement Plan	\$83,499	\$14,379	\$97,878	\$2,940	25.25

Note: Data includes all retirees under age 65 as of January 21, 2012





# Projected Retiree Healthcare Savings

Projected Savings		
	7.50% Earnings Assumption	6.75% Earnings Assumption
Federated	\$5.1M	\$5.4M
Police and Fire	\$5.7M	\$6.2M
<b>Total Projected Savings</b>	<b>\$10.8M</b>	<b>\$11.6M</b>

Source: Projected savings developed by City's Actuary, Bartel Associates LLC



# Medicare Part A and B

# Medicare Part A and B

- All eligible retirees are currently required to enroll in Medicare Part A and B
  - Retirees are provided a six (6) month window to enroll once becoming eligible
- Failing to enroll within the prescribed time frame will result in loss of Non-Medicare coverage
- Medical coverage will be restored upon enrollment in Medicare Part A and B
  - Coverage provided through Medicare and selected Medicare supplemental coverage offered by Retirement Services



# **2nd Tier Federated Pension Retirement Benefits**



# 2nd Tier Pension Retirement Benefit

Federated-Tier 2 New Employees	
Max Benefit	65%
Accrual Rate	2.0% per year
Age/Years of Service	Age 65 with 5 years of service
Final Average Salary Calculation	Highest 3 Years
COLA	Maximum of 1.5% based on CPI
Cost Sharing	50:50 (Normal and UAAL)
Disability	<p><i>Service:</i> 50% of pensionable pay</p> <p><i>Non-Service:</i> 2% per year, but not less than 20% and not greater than 50% of pensionable pay</p>
Survivorship	<p><i>Death before ret.</i> – If not vested, return of contributions; if vested, pension equivalent to what employee would have received</p> <p><i>Killed in line of duty</i> – 50% pension benefit</p> <p><i>Death after ret.</i> – Employee may elect to receive a lower pension to provide survivorship benefit</p>

# Estimated Pension Normal Cost for Tier 2

Federated-Estimated Total Pension Normal Cost			
	City Rate	Employee Rate	TOTAL
7.5% Earnings Assumption	6.9%	6.9%	13.8%
6.75% Earnings Assumption	7.95%	7.95%	15.9%

Source: Cost estimates developed by City's Actuary, Bartel Associates LLC



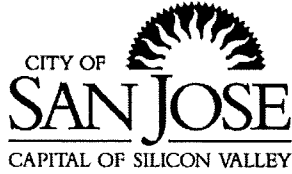
# Recommendation

- Approval of Items 3.3 – 3.12



# Conclusion





# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Debra Figone

**SUBJECT:** SUPPLEMENTAL INFORMATION    **DATE:** April 27, 2012  
**FOR ITEMS 3.3- 3.12**

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**SUPPLEMENTAL**

**REASON FOR SUPPLEMENTAL**

The reason for the supplemental memorandum is to provide additional information related to the savings that is estimated to be achieved with the changes to healthcare as outlined in the memoranda dated April 17, 2012, for the May 1, 2012, Council Agenda, Items 3.3-3.12.

**INFORMATION**

Attached is a letter from John Bartel of Bartel Associates, the City's consulting actuary, who has estimated the savings from the introduction of the lower cost healthcare plan.

<b>Projected City Savings</b>		
	<b>7.50% Earnings Assumption</b>	<b>6.75% Earnings Assumption</b>
Federated	\$5.1M	\$5.4M
Police and Fire	\$5.7M	\$6.2M
<b>Total Projected Savings</b>	<b>\$10.8M</b>	<b>\$11.6M</b>

It should be noted that these are estimates provided by the City's actuary and any revised retiree healthcare contribution rates will need to be determined by the Boards' actuary, Cheiron.

HONORABLE MAYOR AND CITY COUNCIL

April 27, 2012

**Subject: Supplemental Memorandum for Items 3.3-3.12 on May 1, 2012 Council Agenda**

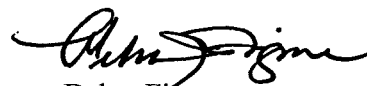
Page 2 of 2

These savings are important not only for the City, but for employees as well because retiree medical is shared 50/50. We are expecting an increase in retiree healthcare costs as projected by Cheiron, the Boards' actuary and these savings will help mitigate those increases. The attached letter from Bartel Associates indicates their estimate of the reduction in the contribution rate at full pre-funding with the introduction of a new lowest cost healthcare plan.

In addition, as noted in our memoranda dated April 17, 2012, the impact of the lowest cost plan will for the most part be for those retirees who are non-medicare eligible (below age 65). The average pension of retirees who are under age 65 is below.

	<b>Base</b>	<b>COLA</b>	<b>Total Pension</b>	<b>Average Years of Service</b>
<b>Federated City Employees' Retirement System</b>	\$41,777	\$5,311	\$47,087	21.11
<b>Police and Fire Department Retirement Plan</b>	\$83,499	\$14,379	\$97,878	25.25

It is important to note that we cannot assume that this is a retiree's only source of income as they could have other employment once they retired, and/or other pensions or defined contribution plans.



Debra Figone  
City Manager

For questions please contact Alex Gurza, Deputy City Manager, at (408) 535-8150.

Attachment



April 27, 2012

Debra Figone  
 City Manager  
 City of San Jose  
 200 East Santa Clara Street  
 San Jose, CA 95113

**Re: Impact of a High Deductible Medical Plan on the City's Retiree Health Care Plan Valuations**

Dear Ms. Figone:

For eligible Federated and Police & Fire retirees, the current retiree healthcare plans provide a benefit of 100% of the premium cost for the lowest priced medical plan available to active employees, currently the Kaiser \$25 Co-Pay Plan. (The Police & Fire plan also provides a reimbursement of the Medicare Part B premium, subject to the cap.) This letter provides the impact on the Federated and Police & Fire Retiree Health Care Plans' June 30, 2011 Actuarial Valuations if a high deductible medical plan, with premiums 24% lower than the Kaiser \$25 Co-Pay plan, had been available to active employees.

**Results**

Following is a comparison of the June 30, 2011 Actuarial Accrued Liability (AAL) and 2012/13 Contribution (before phase-in) for the current lowest priced plan (Kaiser \$25 Co-Pay) as compared to an estimate of what the results would have been if the lowest priced plan was a high deductible plan with 24% lower premiums than the Kaiser \$25 Co-Pay plan. The results are shown separately for Federated and Police & Fire, using the June 30, 2011 valuation funding discount rate assumption of 7.5% and an alternative lower funding discount rate assumption of 6.75%.

	Federated Employees			
	Current Plan Lowest Priced Plan = Kaiser \$25 Co-Pay Plan		Alternative Medical Plan Lowest Priced Plan = High Deductible Plan. (24% Lower Premiums)	
■ Discount Rate	<u>7.5%</u>	<u>6.75%</u>	<u>7.5%</u>	<u>6.75%</u>
■ AAL on 6/30/11 (\$millions)				
• Actives	\$379	\$435	\$332	\$381
• Inactives	<u>557</u>	<u>605</u>	<u>504</u>	<u>549</u>
• Total	936	1,040	836	930
■ Total Contribution 2012/13 (% of payroll, before phase-in)				
• Normal Cost	7.7%	9.4%	6.8%	8.3%
• UAAL Amortization	<u>22.5%</u>	<u>24.1%</u>	<u>19.3%</u>	<u>20.7%</u>
• Total Contribution	30.2%	33.4%	26.1%	29.0%
■ City Contribution 2012/13 (\$millions, before phase-in)	\$37.2	\$41.1	\$32.1	\$35.7
			<i>Savings: \$5.1</i>	<i>Savings: \$5.4</i>



	Police & Fire			
	Current Plan Lowest Priced Plan = Kaiser \$25 Co-Pay Plan		Alternative Medical Plan Lowest Priced Plan = High Deductible Plan (24% Lower Premiums)	
■ Discount Rate	<u>7.5%</u>	<u>6.75%</u>	<u>7.5%</u>	<u>6.75%</u>
■ AAL on 6/30/11 (\$millions)				
• Actives	\$295	\$327	\$249	\$277
• Inactives	<u>481</u>	<u>535</u>	<u>406</u>	<u>452</u>
• Total	776	862	655	729
■ Total Contribution 2012/13 (% of payroll, before phase-in)				
• Normal Cost	10.7%	13.0%	8.9%	10.8%
• UAAL Amortization	<u>23.9%</u>	<u>24.5%</u>	<u>19.9%</u>	<u>20.4%</u>
• Total Contribution	34.6%	37.5%	28.8%	31.2%
■ City Contribution 2012/13 (\$millions, before phase-in)	\$34.1	\$37.0	\$28.4	\$30.8
			<i>Savings: \$5.7</i>	<i>Savings: \$6.2</i>

The 2012/13 contributions shown in the tables above are contributions before phase-in, and include both explicit and implicit subsidies. They may not reflect actual contribution policy, but are shown that way for comparison purposes.

**Assumptions**

The results are based on the City's Federated and Police & Fire Retiree Health Care Plans' June 30, 2011 Actuarial Valuations, including benefits, actuarial methods and assumptions and valuation census data provided by the City. The only change assumed was the addition of a high deductible medical plan with a 24% lower premium cost than the current lowest cost plan available to active employees.

**Actuarial Certification**

As an Associate of the Society of Actuaries, a Fellow of the Conference of Consulting Actuaries and a member of the American Academy of Actuaries, I certify these results are consistent with generally accepted actuarial principles and practices. We based our results on the June 30, 2011 Actuarial Valuations of the City's Retiree Health Care Plans and the valuation census data provided by the City.

Please call me (650-377-1601) with any questions about this information.

Sincerely,

John E. Bartel  
 President

c: Alex Gurza, City of San Jose  
 Jennifer Schembri, City of San Jose