



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Jennifer A. Maguire

SUBJECT: ANNUAL RETIREMENT COSTS
RECONCILIATION

DATE: May 24, 2012

Approved

Date

5/25/12

RECOMMENDATION

Direct the City Manager to annually complete a final reconciliation of the City's annual required retirement contributions to the Federated and Police and Fire Retirement Plans and bring forth the results of the reconciliation as part of the Annual Report in accordance with the City's fund balance policy as outlined in City Council Policy 1-18, Operating Budget and Capital Improvement, for the General Fund, and as appropriate for all other Special and Capital funds.

BACKGROUND AND ANALYSIS

Reconciliation of Annual Required Contribution for Retirement Costs

In 2011-2012, the Federated and Police and Fire Retirement Boards approved actions that changed the methodology for setting the City's Annual Required Contribution (ARC) to a minimum amount or the amount generated by a rate, if the City's actual pensionable payroll is projected to be higher than that included in the Boards' actuary report. The 2011-2012 Proposed Budget included funding to pay a minimum amount for retirement costs for both plans. As part of the approval of the 2011-2012 Mayor's June Budget Message and Adopted Budget, the City Council amended the city-wide position total which required a final reconciliation of the 2011-2012 City's ARC across all funds as part of the 2010-2011 Annual Report process. In October 2011, the City Council approved the 2010-2011 Annual Report, which set aside additional funding due to this reconciliation for the 2012-2013 Future Deficit Reserve.

In general, due to the new minimum ARC requirements, an annual retirement cost reconciliation after the Adopted Budget will be required annually in order to ensure that all City funds contain the correct contribution amounts that are required to be transferred to the Retirement Plans. The result of these reconciliations are proposed to be recommended to the City Council as part of the Annual Report process each fall in accordance with City Council Policy 1-18, Operating Budget and Capital Improvement, Section A.4, Fund Balance for the General Fund, and as appropriate for all other Special and Capital Funds. Based on the budget actions approved after the release of the Proposed Budget in any given year, the annual reconciliation could result in additional funding

needs to ensure the ARC is fully funded, no change in funding, or in savings to over 100 budgeted funds.

Supplemental Retiree Benefit Reserve

The Supplemental Retiree Benefit Reserve (SRBR) program in the Federated and Police and Fire Retirement Plans provides a supplemental "13th check" benefit to retirees under certain conditions as specified in the Municipal Code. The 13th check is in addition to the monthly pension payments, disability and survivor benefits, annual fixed cost of living adjustments, and retiree healthcare benefits eligible retirees receive.

In 1986, the City Council established the SRBR program in the Federated City Employees' Retirement System to allocate investment income earned by retirement fund assets that exceeds expected returns to that account. Such allocations as well as interest earnings in the SRBR program would fund new, or supplemental, benefits for retirees. In 2001, the City Council adopted an ordinance establishing an SRBR program within the Police and Fire Retirement Plan similar to the Federated Retirement System SRBR program except for the SRBR reserve off-set. If the City's contribution rate to the Police and Fire Retirement Plan, as determined by the Board's actuary during any actuarial valuation, will increase as a result of poor investment earnings in the retirement fund, the SRBR reserve offsets the City's contributions in an amount equal to ten percent of the City's increased contributions for the first twelve months following the increase in the contribution rates, but will not exceed five percent of the accrued balance in the SRBR reserve as of the date of the actuarial valuation. Since the City Council approved actions to suspend any distribution for the Federated and Police and Fire Retirement Plans on May 17, 2011, no distributions were made from the SRBR to Federated System as well as Police and Fire Retirement Plans' retirees in 2011-2012.

During the production of the 2012-2013 Proposed Operating Budget document, at the April 5, 2012 Police and Fire Retirement Plan Board (Board) meeting, the Board approved the final retirement rates, which included the SRBR offset. The SRBR offset resulted in a slight adjustment to the City's 2012-2013 Retirement Contribution rates for both the Police and Fire Retirement Plan. Based on the March 29, 2012 letter from Cheiron titled "City of San Jose Police and Fire Department Retirement Plan Supplemental Retiree Benefit Reserve as of June 30, 2011," these new rates and resulting amount differed from the rates received from Cheiron, the retirement boards' actuary in February 2012 and assumed in the 2012-2013 Proposed Operating Budget. Therefore, the resolution approving the final retirement rates by the Police and Fire Retirement Board for the City and employees effective June 24, 2012 reduces the City's 2012-2013 Annual Required Contribution (ARC) in the General Fund by approximately \$848,000 (\$541,499 reduction to the Police Retirement Plan and \$306,880 reduction to the Fire Retirement Plan) from approximately \$187.6 million assumed in the 2012-2013 Proposed Budget to approximately \$186.8 million.

Because there is significant uncertainty regarding the retirement contribution amounts that will be required for 2013-2014 (e.g., interest earnings assumptions, actual investment earnings realized as of June 30, 2012, and other economic or non-economic assumptions), this additional funding is

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recommended to be included as part of the Annual Report retirement reconciliation as discussed earlier in the memorandum.

COORDINATION

This memorandum has been coordinated with the Office of Employee Relations and the Retirement Department.



JENNIFER A. MAGUIRE
Budget Director