Controlling the County's Escalating Retirement Costs

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Issue

What can San Mateo County do to control the impact of escalating retirement costs on the County budget?

Summary

In fiscal 2005-06 San Mateo County contributed $78 million to its retirement fund.[1] By fiscal 2011-12 the County's retirement costs almost doubled to $150 million because of the market downturn in 2008-2009.[2] In fiscal 2013-14 the required County contribution will increase again, by an estimated $13 million. That is basically because on May 22, 2012 the San Mateo County Employees Retirement Association (SamCERA), which manages the County's retirement fund, lowered the future assumed rate of return on assets from 7.75% to 7.5%.

What can the County do to control escalating retirement costs? The Grand Jury believes that meaningful cost reductions need to come from negotiating an increase in employee contributions to the retirement fund, negotiating more limited pension entitlements for future employees and reducing the number of County employees by eliminating or outsourcing services. The choices will be difficult, but must be made now.

Background

SamCERA and Its Impact on Retirement Benefits

All permanent San Mateo County employees are members of the San Mateo County Employees Retirement Association (SamCERA). SamCERA exists "…to serve as Loyal Fiduciary for its members, retirees and beneficiaries and as a prudent administrator of the retirement system."[3] SamCERA was created in 1944 and is governed by Sections 31450-31485.10 of the California Government Code, known as the County Employees Retirement Law of 1937 (the 1937 Act), as amended over the years. It is governed by a Board of Retirement consisting of nine trustees. Four are appointed by the Board of Supervisors, two are elected from the general membership of SamCERA, one is elected from the safety membership, one is elected from the retired membership, and the County Treasurer/Tax Collector is the ninth trustee.

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[1] http://www.co.sanmateo.ca.us/bos.dir/Budget/recommend2008/county/B-32.pdf. Note: these are costs to the County only, and do not include the employee contribution.
[2] http://www.co.sanmateo.ca.us/Attachments/SMC/pdfs/Articles/Budget/2009-11-05_memo_FY2010-11_retirement.pdf
[3] http://www.samcera.org/mission.html

SamCERA operates 10 different retirement plans. Within each plan there are multiple tiers based on a member's bargaining unit, years of service and date of hire. Each tier has different employee contribution and cost sharing requirements. These have been negotiated with the County's nine employee unions within the specifications of the 1937 Act. The County has established at least one new plan by having the State Legislature modify the 1937 Act. Most recently, new tiers have been added which reduce retirement benefit levels for new hires.

As of June 30, 2011 the County had 5,245 active employees enrolled in SamCERA, 4,147 retired members and 1,190 vested terminated members. In addition to pension benefits, all qualified pensioners and active employees, except safety members, have paid into and will receive Social Security.

SamCERA is basically sustained by the return on its investment assets and by the contributions made to its fund by the employer (the County) and its active employees. The employer and member contribution rates are based on recommendations made by an independent actuary and adopted by SamCERA's Board of Retirement.

The County is ***required by the 1937 ACT to contribute the amounts necessary*** to fund the estimated benefits accruing to SamCERA members that are not otherwise funded by member contributions or expected investment earnings.

SamCERA's Unfunded Actuarial Accrued Liability. SamCERA's unfunded liability is the difference between the Plan's expected benefit payments and the Plan's current assets over time. On June 30, 2011 SamCERA's actuarial accrued liability for future benefit payments was $3.2 billion, the projected actuarial valuation of current assets was $2.4 billion and the difference or unfunded liability was $842 million. Another measure is called the "funded ratio" (assets divided by liabilities). The funded ratio on June 30, 2011 was 74.1%.

Section 31453.5 of the 1937 Act requires that the unfunded liability be funded over a maximum of 30 years. The SamCERA Board Of Retirement has adopted a policy it finds more prudent to fund the unfunded liability over 15 years. Like most pension funds, SamCERA employs an actuarial tool called "smoothing" to phase in the impact of market gains and losses over time so that its client, the County, can anticipate and plan for changes in the required contribution rates.

SamCERA's Assumed Actuarial Rate of Return. Actuarial assumptions are the actuary's estimate of the plan's ability to pay future benefits. One of the key assumptions is the assumed rate of return on the plan's investments. As of May 2012, SamCERA's assumption is that it can earn an average of 7.5% on its investments over any 15 consecutive year period. This represents a decrease of 0.25% from the previous assumption and will require higher annual contributions from the County to SamCERA, effective July 1, 2013. That will, in turn, add to the County's budget deficit unless offset by equivalent revenues or expense reductions. The assumed rate of return for fiscal 2012-13 will remain at 7.75% because the contribution rates for that fiscal year were established in January 2012. SamCERA also lowered its assumed wage-inflation rate from 4% to 3.5%, which has a mitigating effect on contribution increases.

Retirement Benefits and Their Impact on the County's Budget

How will SamCERA's assumption of a lower rate of return on assets affect the County's budget? In 2011, the recently retired County Controller, wrote the following;[4]

> It has been estimated that for every ¼% decline in the discount rate [SamCERA's assumed rate of return] used to compute the County's future pension liability, the County would incur a 3% increase in its employer contributions (as a percent of the County's payroll) using a 15-year amortization period. If the County were to meet its obligation of this new calculation, it would represent a staggering reduction of discretionary resources.

Using the former County Controller's example, the reduction of the assumed rate of return from 7.75% to 7.50% (the 0.25% decline), the County's *additional c*ontribution, would be approximately $13 million assuming $435 million in salaries.[5] As the Controller noted, unless the Board of Supervisors elected to increase the deficit, which is already projected at $32 million for fiscal 2012-13, this could cause a reduction in services equal, for example, to the Department of Child Support Services which had a general fund allocation of about $12 million in fiscal 2011-12.[6]

Evan Storm and Joe Nation of the ***Stanford Institute for Economic Policy Research*** (SIEPR) recently studied pension rates in California counties.[7] They wrote:

> Recent SIEPR reports on California's statewide pension systems have covered some of the debate surrounding the correct assumed investment rate of return. This report will not argue for any particular assumption but will show the effects on pension costs, including required contributions, under different assumed investment rates of return:
> - 5.0 percent, similar to relatively "risk-free" municipal bond yields
> - 6.2 percent, based on a blended 20th-century portfolio of equities and fixed income
> - 7.1 percent, based on roughly the 50th percentile of pension system earnings over the past 30 years
> - 7.75 percent, the most common expected rate used by California independent pension systems.

Table 1 below is supplied by Storm and Nation to show how the effects on San Mateo County's pension costs would affect the County's required contribution to the Pension Fund.

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[4] http://www.c.sanmateo.ca.us/Attachments/controller/Files/CAFR/2011CAFRprintable.pdf
[5] http://www.co.sanmateo.ca.us/Attachments/cmo/pdfs/smc_recommended_budget_fy_2011-12.pdf, ,B29
[6] http://www.co.sanmateo.ca.us/Attachments/cmo/pdfs/smc_recommended_budget_fy_2011-12.pdf p.3-2
[7] More Pension Math, Evan Storm, Joe Nation, February, 21 2012 p. 4 http://siepr.stanford.edu/system/files/shared/pubs/papers/pdf/Nation_More_Pension_v09.pdf,

Table 1
2012 San Mateo County Pension Contributions, Share of Total Expenditures Under Different Investment Return Assumptions:[8]

Assumed Rate of Return	2012 Required Pension Contribution
7.75%	$158.1 million
7.10%	$188.9 million
6.20%	$231.4 million
5.00%	$288.0 million

Even at the previously assumed 7.75% rate of return, the "Employer"[9] contribution to SamCERA has been increasing, as Table 2 below demonstrates.[10]

Table 2
"Employer" Contributions to SamCERA (Fiscal Years July 1-June 30)

2006		$ 78 million
2007		100 million
2008		105 million
2009		106 million
2010		106 million
2011		150 million
2012		146 million*
Grand Jury Estimate	2013	159 million**

*decrease in contributions reflects decrease in number of employees
** based on a revised rate of return of 7.5% and the former County Controller's estimate that every ¼% decline in the discount rate (assumed rate of return) used to compute the County's future pension liability, the County would incur a 3% increase in its employer contributions (as a percent of $435 million in salaries).

Referencing Table 2: In fiscal year 2006-07, the required employer contribution rate increased by $22 million. The increase basically resulted from: (1) a change in actuarial valuation methodology used for deferred membership and (2) a decrease in the assumed rate of return on investments from 8% to 7.75%.[11] The increase from approximately $100 million in fiscal year 2009-10 to $150 million in fiscal year 2010-11 was needed to restore SamCERA's asset base, because SamCERA lost 22.5% of its asset base during the market downturn of 2008-09. The reduction in contributions in fiscal year 2010-11 from $150 million to $146 million was achieved by a reduction in the number of County employees.

[8] *Ibid.* p. 47
[9] Does not include "employer pickup" show in Table 3 below.
[10] http://www.samcera.org/pdf/2011valuation.pdf Exhibit 14, p.44. The 2012 figure supplied by County staff.
[11] Information supplied by SamCERA.

The estimated increase of County contributions beginning July 1, 2013 is due to a decrease in the assumed rate of return from 7.75% to 7.5%. SamCERA projects that increases as a percent of salary will continue through 2022. *(See* Appendix A.) The change in the assumed rate of return will also increase the employee contribution. For example, an employee making $65,000 a year may have to contribute $108 more per year.[12]

Other Factors that Affect Required County Contributions

Retroactive Increases. The County's past agreements with unions included a pension increase that was retroactive for active employees hired on or before 2003, and another for active employees hired on or before 2005. These retroactive increases were enacted by the Board of Supervisors and awarded employees an increase in pensions for prior service for which no funds were set aside. Also driving up the cost of pensions are unanticipated increases in the life expectancy of retirees.[13]

Employer Pickup. Whereas the 1937 Act requires employees and employers to make contributions to SamCERA (called the "employee share" and "employer share" respectively), the County also pays a portion of the employee share. This is known as the "employer pickup." The County pays a portion of the employee's scheduled contribution to SamCERA for employees classified as management, attorneys and confidential. (Confidential employees are those who hold positions requiring access to confidential information, especially regarding employer-employee relations.) In addition, the County pays a portion of the employee contribution after 10 years of service for all the remaining employees. The cost to the County for the employer pickup for fiscal 2011-2012 was $6.4 million.[14]

The actual employee payments and the County contributions for fiscal year 2010-11 are shown in Table 3. The employer contribution share, including pickup, is 78 percent.

Table 3
2010-11 County Contributions to SamCERA Showing Employer Pickup

	Without Pickup	Pickup	With Pickup
Employer Share	$150 million	$6 million	$156 million
Employee Share	$49 million	$(6 million)	$ 43 million
Total	$199 million	none	$199 million
Employer Share	75%		78%
Employee Share	25%		22%
Total	100%		100%

[12] SamCERA valuation preview, May 22, 2012, p. 13
[13] Supplied by SamCERA staff.
[14] Employer Pickup Information was provided by the San Mateo County Human Resources Department..

Salaries. Increasing salaries (which include step increases)[15] help to drive up retirement costs. Table 4 shows that recent salaries on which pensions are based have been increasing a few percent per year since 2007. However, these average salary increases do not account for the most recent 2010-11 jump in retirement costs. In 2011, the average annual salary for general employees in San Mateo County was $79,188. If public safety and probation officers are included, the average annual salary was $82,464. [16]

Table 4
Average Annual Salaries Of County Employees 2007-2011
(Excluding Safety and Probation)[17]

2007	$72,648
2008	74,532
2009	77,616
2010	78,828
2011	79,188

The average annual salary increase may in part reflect the changing mix of employees in the employment pool. The Grand Jury was told that County employees have not received base salary increases in the last 3 years.

Retirement and Other Benefits as a Percent of Salary. The cost of total benefits for County employees is increasing in absolute dollars and as percent of payroll as Table 5 below demonstrates: [18]

Table 5
Benefits as a Percent of Salary[19]

	Adopted 2007-2008		Adopted 2009-2010		Adopted 2010-2011	
	Amount	%	Amount	%	Amount	%
Regular Salaries	439,211,768	100.00%	456,532,392	100.00%	442,293,384	100.00%
Retirement	105,988,910	24.13%	107,582,914	23.57%	148,809,269	33.64%
Health Benefits	56,596,849	12.89%	75,687,802	16.58%	76,794,632	17.36%
Statutory Compensation	40,945,837	9.32%	43,075,704	9.44%	41,892,830	9.47%
Other Benefits	5,967,424	1.36%	3,669,343	0.80%	3,322,970	0.75%
Total Benefits	**209,499,020**	**47.70%**	**230,015,763**	**50.38%**	**270,819,701**	**61.23%**

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[15] Step Increases are automatic salary increases associated with time, grade classification, or movement within a grade.
[16] http://www.samcera.org/pdf/2011CAFR.pdf pp110
[17] http://www.samcera.org/pdf/2011CAFR.pdf, pp110-111
[18] Supplied by County staff.
[19] Budget figures may vary slightly between tables because some are *adopted*, some are *actual,* some were supplied from budgetary *All Funds,* and some from the *General Fund*.

With the exception of safety members, employees will also receive Social Security benefits. The employer's portion of Social Security (FICA) paid by the County is part of the *statutory compensation* in Table 5. (Note that several counties organized under the 1937 Act do not participate in Social Security.[20]) Net, San Mateo County currently pays 61 cents in benefits for every dollar it pays in salary.

For nine years beginning in 2013, County contributions to retirement are projected by SamCERA to increase to between 35% and 40% of salaries. Consequently, the total amount of benefits as a percent of salary will increase from 61% to 68% barring other changes. In 2022, funding for retirement is projected to decrease. [21] (*See,* Appendix A for the projected year-by-year change in pension benefits as a percent of employee salary.)

Decreases in the Number of Active SamCERA Members (*i.e.*, County Employees). On June 21, 2011, then County Manager David Boesch reported to the Board of Supervisors that "the total [SamCERA] contribution has been reduced by approximately $5.3 million with the net elimination of 208 positions in the FY 2011-12 Recommended Budget, which includes 52 positions eliminated during FY 2010-11." [22] The full reduction was not achieved because 12 of the jobs were restored.[23]

The number of County employees since 2007 is shown in Table 6.[24] Note the decreases since 2009.

Table 6
Number of Active County Employees

Year	2007	2008	2009	2010	2011
Total members	5,514	5,475	5,524	5,327	5,227*

*Projected.

Referring to Table 2 above, one can see that the recent decrease in the number of employees has resulted in an approximate $4 million dollar decrease in the County's required retirement contribution in 2012. Additional employee reductions will come from ending the County's operation of the Burlingame Long-Term Care Facility.

[20] See Footnote 7, Appendix, throughout
[21] SamCERA valuation preview, May 22, 2012, p. 12.
[22] http://www.co.sanmateo.ca.us/bos.dir/BosAgendas/agendas2011/Agenda20110621/20110621_m_10.html
[23] http://www.co.sanmateo.ca.us/Attachments/cmo/pdfs/Budget%20&%20Performance/SeptemberRevisions_2011.pdf,
[24] http://www.samcera.org/pdf/2011CAFR.pdf, p.111

Toward Pension-Cost Reductions
The Grand Jury learned during its investigation that the County has done the following to reduce pension costs:

1. Obtained concessions from some unions during contract negotiations for their members to pay a larger portion of the employee contribution to SamCERA. For example, the California Nurses Association agreed that their members would forego 25% of the cost-of-living-adjustment increases, post retirement.
2. Developed plans to reduce the employer pick up for non-union employees. The Grand Jury understands that starting September 2012, the employer pick up will be reduced from 75% to 50% of the employee contribution for employees not covered by union contracts and, over the next several years, the employer pickup for this group will be eliminated.
3. For new employees, reduced the existing pension benefits and increased the age at which they can be taken.
4. Based final retirement benefits on an average of the last two or three years of salary, rather on than on the last year alone.
5. Reduced the number of County employees through staffing efficiencies, by not filling vacant positions, or by eliminating or outsourcing services.

The 1937 Act limits the changes that can be made without amending the Act. For example, increasing the retirement age for existing employees, capping benefits, or instituting a hybrid plan with employee contribution to a 401K would require legislative amendments. In the words of the Little Hoover Commission 2011 report, the pension problem

> …**cannot be solved without addressing the pension liabilities of current employees.** The state and local governments need the authority to restructure future, unearned retirement benefits for their employees The Legislature should pass legislation giving this explicit authority to state and local government agencies." [Emphasis supplied].[25]

Pension reform ballot measures passed in San Jose and San Diego on June 5, 2012 will be tested in the courts. Depending on the rulings, some local jurisdictions may be empowered to make changes to current employee pension contracts going forward (without affecting pensions already earned).

Investigation

This report was compiled from data from numerous sources including:

- Interviews with representatives from SamCERA, the County Controller's Office, the County Human Resource Department and the County Manager's Office

[25] Little Hoover Commission, Public Pensions For Retirement Security, Feb,2011, p.V http://www.lhc.ca.gov/studies/204/Executive%20Summary204.pdf

- Review of June 30, 2011 SamCERA Actuarial Valuation and CAFRs
- Review of San Mateo County Budgets
- Attending a SamCERA Board meeting
- Review of articles and staff reports

Findings

The San Mateo County Civil Grand Jury finds that:

1. All permanent San Mateo County employees are members of the San Mateo County Employees' Retirement Association (SamCERA).

2. SamCERA was created in 1944 and is governed by the provisions of the County Employees' Retirement Law of 1937 as amended over the years.

3. SamCERA operates 10 different retirement plans. Within each plan there are multiple tiers based on a member's bargaining unit and date of hire. Each tier has different employee contribution and cost sharing requirements. These have been negotiated with the County's nine employee unions.

4. As of June 30, 2011, SamCERA had an unfunded liability of approximately $842 million. As of that same date, SamCERA was estimated to be 74.1% funded.

5. On May 22, 2012, SamCERA lowered the assumed annual rate of return for its invested assets from 7.75% to 7.5%, effective July 1, 2013.

6. County contributions to SamCERA have been increasing per Table 2. In fiscal year 2005-06, the County contributed a total of $78 million to SamCERA. In fiscal year 2006-07 there was a $22 million increase in the County contributions. In fiscal year 2010-11, County employer contributions jumped by $45 million to $150 million.

7. For fiscal year 2013-14, the Grand Jury estimates that the required County contribution will increase again by approximately $13 million (assuming $435 million in salaries) unless salaries and/or number of employees are reduced, or other solutions are found.

8. Factors determining County contribution levels include past and future investment returns and losses on SamCERA's investment assets, salary levels, employer pickups, the total number of County employees, union agreements, and limits imposed by State statutes.

9. For 2010, per Table 3, the County paid 78% of the combined employer-employee share of contributions to SamCERA.

10. Pensions are partly based on salaries. However, salary increases do not account for the near doubling in pension costs since 2006. In fiscal year 2010-11, the average annual salary for non-safety employees in San Mateo County was $79,189 (not including public

safety or probation officers salaries). If public safety and probation officers are included, the average annual salary was $82,464. [26]

11. In addition to pension benefits, all pensioners except retired safety members receive Social Security. The County pays the employer portion of Social Security, which adds 6% of payroll expense to the budget.

12. The County currently pays 61 cents on every dollar of salary (or 61% of salary) earned by current employees for fringe benefits including retirement benefits, per Table 5. These benefits are projected to gradually increase starting in July 2013, and for nine years thereafter, to 68 cents per dollar of payroll for County employees.

13. The number of active members of SamCERA (*i.e.*, active County employees) has been decreasing since 2009, per Table 6. In 2011, the County Manager told the Board of Supervisors that a $5.3 million reduction in retirement contributions could be achieved if 208 positions were eliminated. (The full reduction was not realized because some jobs were restored.)

14. A reduction in pension costs to the County has been achieved by obtaining union concessions, by reducing the employer pickup for management and other unrepresented groups, by continuing to introduce new less-costly plans for new employees (which will be realized in future years), and most significantly by reducing the number of County employees.

15. Many counties that have pension systems governed by the 1937 Act do not participate in Social Security.

16. Information on Social Security payments and employer pickups is not readily available from the County or on the County website, nor are recent meeting minutes available on the SamCERA website.

17. The State Legislature would likely have to amend state statutes in order to allow the County to make changes to current employee pension contracts going forward (without affecting pensions already earned).

Conclusions

The San Mateo Civil Grand Jury concludes that:

1. Increasing pension costs are adding to an already unsustainable budget deficit. Pension costs must be reduced and the Board of Supervisors must make some tough decisions to pay for increasing pension costs they approved in the past.

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[26] http://www.samcera.org/pdf/2011CAFR.pdf pp110

2. The County should continue to negotiate increases in employee pension contributions with its unions without increasing salaries and health benefit costs.

3. Given the restrictions of current State laws, the most effective way for the County to control retirement costs is to reduce the number of employees by introducing staffing efficiencies, reducing service levels and/or contracting out County functions.

4. The potential increase in County retirement benefit contributions must be factored into the cost of hiring new employees.

5. More information in easily understood terminology should be readily accessible on both the County and SamCERA web sites.

Recommendations

The San Mateo Civil Grand Jury recommends to the Board of Supervisors that it:

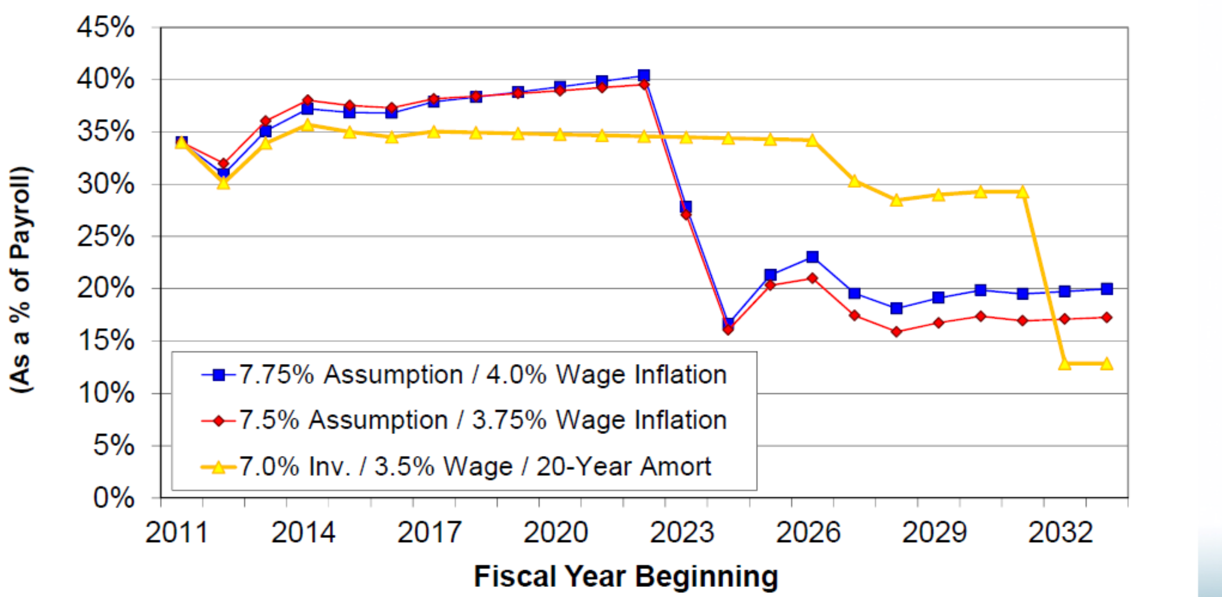
1. Develop and adhere to a specific budget strategy to lower County retirement contributions to SamCERA and restructure benefits by:
    a. significantly decreasing the number of County employees through outsourcing and/or reducing services, and by attrition;
    b. negotiating the elimination of the employer pickup and “right-sizing” future benefits with the unions without increasing salaries; and
    c. studying the possibility of withdrawing from Social Security.

2. Actively support State pension reform that would allow for changes to future retirement benefits for current employees (without effecting pensions already earned).

3. Make County and SamCERA information more easily accessible to the public, including the amount of employer pickups, the payments to Social Security, and the past and projected County (employer) and employee annual contributions to SamCERA.

Appendix A

On May 22, 2012, SamCERA adopted an assumed future rate of return on its assets of 7.5%. The graphic below charts the pension benefit as a percent of employee salary under three different assumed rates using different assumptions about wage increases. The dramatic turndown beginning in 2023 is founded on an assumption that current unfunded liability is reduced to near zero at that time. (From the SamCERA Valuation Preview, May 22, 2012, p. 12.)



County Manager's Office

COUNTY OF SAN MATEO

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October 3, 2012

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Hon. Gerald J. Buchwald
Judge of the Superior Court
Hall of Justice
400 County Center, 2nd Floor
Redwood City, CA 94063-1655

Re: Controlling the County's Escalating Retirement Costs

Dear Hon. Gerald J. Buchwald,

The responses to the Grand Jury Reports titled: Controlling the County's Escalating Retirement Costs, was approved by the San Mateo County Board of Supervisors at their regular meeting on October 2, 2012. Attached please find the Board Memo that includes the formal response.

Sincerely,

Shanna Collins

Shanna Collins
County Manager's Office

COUNTY OF SAN MATEO
Inter-Departmental Correspondence
County Manager

APPROVED BY
BOARD OF SUPERVISORS

OCT - 2 2012

CLERK OF BOARD
BY [signature] DEPUTY

Date: July 25, 2012
Board Meeting Date: October 2, 2012
Special Notice / Hearing: None
Vote Required: Majority

To: Honorable Board of Supervisors

From: John L. Maltbie, County Manager

Subject: 2011-12 Grand Jury Response- Controlling the County's Escalating Retirement Costs

RECOMMENDATION:
Approve the Board of Supervisor's response to the 2011-12 Grand Jury report titled: Controlling the County's Escalating Retirement Costs.

BACKGROUND:
On July 23, 2012, the Grand Jury filed a report titled: Controlling the County's Escalating Retirement Costs. The Board of Supervisors is required to submit comments on the findings and recommendations pertaining to the matters under control of the County of San Mateo within ninety days. The County's response to the report is due to the Hon. Gerald J. Buchwald no later than October 22, 2012.

Acceptance of this report contributes to the Shared Vision 2025 outcome of a Collaborative Community by ensuring that all Grand Jury findings and recommendations are thoroughly reviewed by the appropriate County departments and that, when appropriate, process improvements are made to improve the quality and efficiency of services provided to the public and other agencies.

DISCUSSION:
Controlling the County's Escalating Retirement Costs

Findings:

Grand Jury Finding Number 1. All permanent San Mateo County employees are members of the San Mateo County Employees' Retirement Association (SamCERA).

Response: Agree.

Grand Jury Finding Number 2. SamCERA was created in 1944 and is governed by the provisions of the County Employees' Retirement Law of 1937 as amended over the years.

Response: Agree.

Grand Jury Finding Number 3. SamCERA operates 10 different retirement plans. Within each plan there are multiple tiers based on a member's bargaining unit and date of hire. Each tier has different employee contribution and cost sharing requirements. These have been negotiated with the County's nine employee unions.

Response: Agree.

Grand Jury Finding Number 4. As of June 30, 2011, SamCERA had an unfunded liability of approximately $842 million. As of that same date, SamCERA was estimated to be 74.1% funded.

Response: Agree.

Grand Jury Finding Number 5. On May 22, 2012, SamCERA lowered the assumed annual rate of return for its invested assets from 7.75% to 7.5%, effective July 1, 2013.

Response: Agree.

Grand Jury Finding Number 6. County contributions to SamCERA have been increasing per Table 2. In fiscal year 2005-06, the County contributed a total of $78 million to SamCERA. In fiscal year 2006-07 there was a $22 million increase in the County contributions. In fiscal year 2010-11, County employer contributions jumped by $45 million to $150 million.

Response: Agree. Note that these figures include pick-ups.

Grand Jury Finding Number 7. For fiscal year 2013-14, the Grand Jury estimates that the required County contribution will increase again by approximately $13 million (assuming $435 million in salaries) unless salaries and/or number of employees are reduced, or other solutions are found.

Response: **Agree.**

Grand Jury Finding Number 8. Factors determining County contribution levels include past and future investment returns and losses on SamCERA's investment assets, salary levels, employer pickups, the total number of County employees, union agreements, and limits imposed by State statutes.

Response: Agree.

Grand Jury Finding Number 9. For 2010, per Table 3, the County paid 78% of the combined employer-employee share of contributions to SamCERA.

Response: Agree. Note that in subsequent years there will be a decrease in the percent share of contributions paid by the County as a result of negotiated increases in the share paid by employees.

Grand Jury Finding Number 10. Pensions are partly based on salaries. However, salary increases do not account for the near doubling in pension costs since 2006. In fiscal year 2010-11, the average annual salary for non-safety employees in San Mateo County was $79,189 (not including public safety or probation officers salaries). If public safety and probation officers are included, the average annual salary was $82,464.

Response: Agree. Recent increases in pension costs are attributable to a number of factors including investment performance, changes to the assumed rate of return, increased number of employees, and changes to actuarial methodology, to name a few.

Grand Jury Finding Number 11. In addition to pension benefits, all pensioners except retired safety members receive Social Security. The County pays the employer portion of Social Security, which adds 6% of payroll expense to the budget.

Response: Agree. Social Security is paid by both employer and employee. FICA rate is 6.2% for the employer and 4.2% for employees.

Grand Jury Finding Number 12. The County currently pays 61 cents on every dollar of salary (or 61% of salary) earned by current employees for fringe benefits including retirement benefits, per Table 5. These benefits are projected to gradually increase starting in July 2013, and for nine years thereafter, to 68 cents per dollar of payroll for County employees.

Response: Agree. A large portion of the increases are due to health insurance costs. As a result of recent negotiated changes, County employees are now paying a higher percentage of health insurance benefits which will significantly reduce the County's current and future benefit costs.

Grand Jury Finding Number 13. The number of active members of SamCERA (i.e., active County employees) has been decreasing since 2009, per Table 6. In 2011, the County Manager told the Board of Supervisors that a $5.3 million reduction in retirement contributions could be achieved if 208 positions were eliminated. (The full reduction was not realized because some jobs were restored.)

Response: Agree.

Grand Jury Finding Number 14. A reduction in pension costs to the County has been achieved by obtaining union concessions, by reducing the employer pickup for management and other unrepresented groups, by continuing to introduce new less-costly plans for new employees (which will be realized in future years), and most significantly by reducing the number of County employees.

Response: Agree.

Grand Jury Finding Number 15. Many counties that have pension systems governed by the 1937 Act do not participate in Social Security.

Response: Partially Agree. Based on initial survey results of the 20 '37 Act Counties, at least half do participate in Social Security including Alameda County, Contra Costa County, Stanislaus County, Tulare County, Ventura County, Santa Barbara County, Sacramento County, Mendocino County, and San Diego County.

Grand Jury Finding Number 16. Information on Social Security payments and employer pickups is not readily available from the County or on the County website, nor are recent meeting minutes available on the SamCERA website.

Response: Partially agree. Social security expenses are included in the County's Comprehensive Annual Financial Audit (CAFR), but rolled up with other government expenses. Employer pick-up formulas are included in the County's Memorandum of Understanding (MOU) with each bargaining unit and posted on the County's website (under Departments / Human Resources / Employee and Labor Relations). The specific amount of social security payments and retirement pick-ups are readily available upon request.

Disagree as to the Board of Retirement meeting minutes not being available on the SamCERA website. As part of the Board of Retirement agenda packet posted on its website for each monthly Board meeting, the draft minutes for the previous meeting are contained in the packet for the Board's approval.
(www.samcera.org/boardpackets.html). In addition, the approved Board of Retirement minutes are promptly placed on the website after approval. These minutes are available for meetings going back to 1999. (See www.samcera.org/minutes.html).

Grand Jury Finding Number 17. The State Legislature would likely have to amend state statutes in order to allow the County to make changes to current employee pension contracts going forward (without affecting pensions already earned).

Response: Agree. Note that such statutes affecting current employees may be subject to a constitutional challenge due to vested rights of current employees.

Recommendations:
The San Mateo Civil Grand Jury recommends to the Board of Supervisors that it:

1. **Develop and adhere to a specific budget strategy to lower County retirement contributions to SamCERA and restructure benefits by:**
    a. **significantly decreasing the number of County employees through outsourcing and/or reducing services, and by attrition;**
    b. **negotiating the elimination of the employer pickup and "right-sizing" future benefits with the unions without increasing salaries; and**
    c. **studying the possibility of withdrawing from Social Security.**

Response: The County has already gone a long way in reducing retirement costs and it continues to explore further cost reductions in this area within legal limitations. Recent changes to retirement benefits which resulted in significant cost savings include: 1) Reduced benefit formulas for new hires; higher age to receive maximum pension; 2) Reduced County pickup of employee share of retirement costs; and 3) Reduced County pickup of pension COLA cost. The County recently studied the possibility of opting out of the social security program. It was confirmed that the County cannot terminate its participation in social security.

2. **Actively support State pension reform that would allow for changes to future retirement benefits for current employees (without effecting pensions already earned).**

Response: Pension reform has already been approved by the state legislature. The main pension bill, AB340, awaits the Governor's signature which he is expected to approve. The County and SamCERA are currently analyzing this complex legislation and will provide more information as it becomes available and after the Governor has signed the bill.

3. **Make County and SamCERA information more easily accessible to the public, including the amount of employer pickups, the payments to Social Security, and the past and projected County (employer) and employee annual contributions to SamCERA.**

Response: SamCERA currently has information and reports reflecting the past and projected employer and employee annual contributions to SamCERA available on its website.

Social security expenses are included in the County's Comprehensive Annual Financial Audit (CAFR), but rolled up with other government expenses. Employer pick-up formulas are included in the County's Memorandum of Understanding (MOU) with each bargaining unit and posted on the County's website (under Departments / Human Resources / Employee and Labor Relations). The specific amount of social security payments and retirement pick-ups are readily available upon request.

FISCAL IMPACT:
There is no Net County Cost associated with accepting this report.