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BOARD OF SUPERVISORS RESPONSE TO

CONTRA COSTA COUNTY GRAND JURY REPORT 1603:

Pension Reform - If Not Now, When?

Findings:

F1. The County's largest outstanding debts relate to its pension liabilities. The unfunded pension liabilities of the County (including ConFire) as calculated by the CCCERA actuaries in September 2015 total $1.155 Billion. In addition to this UAAL figure, the County (again including ConFire) has outstanding $329 Million of long-term pension obligation bonds.

Response: The respondent agrees with the finding.

F2. The County's unfunded pension liability will increase in any year in which the rate of return on the CCCERA pension fund does not reach at least 7.25%.

Response: The respondent partially agrees with the finding. It should be noted that the rate of return has recently been changed to 7.00%. The rate of return on the CCCERA pension fund is one factor in determining the unfunded pension liability. It is possible for the pension fund to earn less than 7.25% and not experience an increase in unfunded liability due to changes in the other factors or policy changes; however, the statement is generally correct.

F3. According to the most recent CCCERA actuarial report, for every 1% drop below the CCCERA assumed rate of return of 7.25% the County's unfunded pension liability will increase by a figure equal to 9.9% of the County payroll of employees enrolled in the CCCERA pension plan. Based on its current payroll of over $572 Million that means the reported return of 1.9% achieved by the CCCERA pension fund in 2015 could result in an increased County UAAL of over $300 Million before actuarial five-year smoothing adjustments are made.

Response: The respondent neither agrees nor disagrees with the finding. The projection appears to be reasonable; however, Volatility Ratios are extremely complicated and therefore the respondent is unable to confidently respond to this finding.

F4. Unlike all other elements of compensation that it negotiates with the labor organizations, the County does not negotiate the rate of pension benefits employees will earn in future salary periods.

Response: The respondent partially agrees with the finding. Prior to the passage of the Public Employees' Pension Reform Act (PEPRA), the County was able to negotiate about which of the statutory pension benefit formulas available under the County Employees Retirement Law (CERL) would be available to new employees. PEPRA now specifies what the pension benefit will be for new hires, and the County cannot negotiate a different benefit. The County can and does continue to negotiate which of the statutory COLAs to the pension benefit will be applicable to new employees. In addition, the County is aware of the impact and cost of pension and negotiates wages and benefits accordingly.

F5. The reason the County does not negotiate such pension benefits is due to a long-standing legal precedent in California, known as the California Rule, which holds that public employees are covered by an implied contract on their first day of service guaranteeing that the level of pension benefits they earn each year may not be decreased in future years unless replaced by benefits comparable in value for the employee.

Response: The respondent partially agrees with the finding. The respondent understands the term "California Rule" to mean the body of case law regarding modification of pension benefits for current employees. The County must comply not only with these cases, but also with the statutory requirements of CERL and PEPRA.

F6. The California Rule is based on a case that was decided before public employees had the right to organize and engage in collective bargaining in California.

Response: The respondent partially agrees with the finding. The body of case law regarding the modification of pension benefits for current employees includes cases decided both before and after the enactment of the collective bargaining laws.

F7. The County has not taken steps to challenge or seek legal clarification of the California Rule in a California court.

Response: The respondent agrees with the finding.

F8. Negotiating the terms of future pension benefits to be earned could result in substantial cost savings for the County if permitted by a court ruling.

Response: The respondent partially agrees with the finding. The respondent notes that any changes would have to be negotiated with Labor Organizations and concessions that have a net savings would be very difficult to negotiate.

F9. There are legal avenues open to the County to seek judicial clarification or reform of the rule without subjecting the County to major financial risks if the challenge proves unsuccessful.

Response: The respondent partially agrees with the finding. While it is true that the County could seek judicial clarification, the cost of outside legal counsel to litigate this issue would be very expensive and would involve extensive amounts of attorney time.

Recommendations:

R1. The Board of Supervisors should seriously consider adopting a policy of seeking judicial clarification or reform of the California Rule.

Response: The recommendation will not be implemented at this time. The cost associated with any individual County pursuing judicial clarification or reform would be prohibitive. Any solution to this issue is best handled by the legislature.

R2. The Supervisors should consider empaneling a task force, a study group, or an internal committee to examine options for challenging the California Rule that would weigh the following considerations:

- Potential cost savings for the County;
- Potential resources to be freed up for other priorities such as service enhancements and other wage and benefit improvements;
- Opportunities to participate as an amicus curiae in existing legal cases;
- Opportunities for challenging the California Rule through legal proceedings such as a declaratory relief action that would not expose the County's financial position to undue risk in the event of an adverse result; and
- Whether the County should undertake the legal challenge alone or in cooperation with other jurisdictions or organizations with a common interest in the issue, such as the California State Association of Counties (CSAC).

Response: The recommendation will not be implemented at this time. There is no reason to examine options since the County is not willing to incur the extensive time and expense that would be required to challenge the California Rule.

R3. The Supervisors should consider issuing a formal statement on their policy toward seeking reform of the California Rule, with an explanation of how they propose to manage their unfunded pension liability in the event no steps are taken to reform or adjust the California Rule.

Response: The recommendation will not be implemented at this time. However, the County will continue to monitor its unfunded pension liability to determine whether or not appropriate action may be necessary in the future.

R4. The Supervisors should consider securing a legal opinion from outside counsel experienced in the field of pension and collective bargaining law on the merits of a legal challenge to the California Rule based on the argument that the Rule should now be modified based on California's collective bargaining system for public employees.

Response: The recommendation will not be implemented at this time. There is no reason to secure an outside legal opinion since the County is not willing to incur the extensive time and expense that would be required to challenge the California Rule.