Primal Scream--Double Header--A Reply to Burky Worel--8/22/08

Primal Scream

Double Header

A Reply to Burky Worel...Twice

8/22/08

See Mr. Worel's original Scream HERE

Kirk

Some thoughts regarding unfunded pension liability -- and how we got to this point. I also have questions regarding the "A word from Burky Worel" letter.

Starting in the early 90's, the city council put together a citizens group to study the financials of Vallejo. The report, complete with pie charts, graphs, converging & diverging revenue and expense lines, predicted the cities financial demise by 2010. The report, published in 1993, became known as the "Citizens Budget Advisory Committee Report". What happened between 1993 and 2000, is unclear to me. What happened in 2000, and beyond, is appalling.

Most notably was the 50% pension increase (2@50 increased to 3@50). Bad enough for a financially strapped city right. Wrong, the pension increase was made retroactive. Now an employee that worked 29 years under the 2% formula and one year at 3% , retires at 90%, instead of 61%. Under this scenario the PS employee, at the average salary in Vallejo, receives, essentially, an additional million dollars over his lifetime for doing no additional work. That’s a tax-dollar giveaway. That clearly, and significantly, contributed to the unfunded pension liability, along with escalating salaries, and struggling financial markets with lower ROI.

Joe

I noted Burky Worel's letter published on your web-site. Be advised that the information he provides is NOT correct. It could be that Mr. Worel is misinformed. It could be that he's trying to "spin" the information in a manner favorable to the public safety unions. It could be that he's just plain lying.

In his letter he claims that the improved retirement formulas were not the result of action by Vallejo public safety unions but rather by action of the state legislature. However, he either states or strongly implies that the change in the formula was REQUIRED because of the legislative action. That is absolutely FALSE. The legislature AUTHORIZED several new public safety retirement formulas but no public agency was REQUIRED to adopt them. Public agencies did so ELECTIVELY by action of their governing bodies and acceptance of the contractual requirements of the new formulas (i.e. the potential for higher cost to the public agency). In many cases, the adoption of the new formulas was via provisions of public safety contracts. Without action by the City Council to change the retirement benefit formulas to those made available by the legislature, the retirement benefit formulas would have remained exactly where they were.

In defense of past councils, this was probably agreed upon because city council tends to give the unions what they want, and it didn't require much additional funding. Pensions, in 2000, were over funded, and union officials used this fact to negotiate higher payouts. Other cities began doing the same thing and now 3@50 has become the standard in California. This over funding of pensions was primarily due to exceptional returns on investment during the 90’s as the stock market reached new highs. But now the new union negotiated perks have become a significant drain on pensions, and Under funded pensions are rapidly becoming a national problem.

Extravagant salary increases perpetuated the problem on both the front and backend of the contracts. In 2000, average PS salaries probably hovered around 85k (85k * .60% = 51K is a significantly smaller obligation than 131k * .90% = 118K). To put it another way -- the pension obligation has grown (from 2000 -2007) on average $67,000 per employee. That’s a 131 % increase in only seven years. The numbers would have been worse if the city had not declared bankruptcy and frozen salaries prior to the 2008 raise taking effect. That’s just the pension and doesn’t include retiree medical costs or salary increases. While the 2000 PS contract was a tax payer rip-off, the retroactive portion of the pension benefit should be illegal. The 2000 mayor, CM, and council should shoulder much of the blame for this mess. The 2000 PS contracts were terrible for Vallejo.

The PERS pension plan Vallejo uses is called a Defined Benefit Plan, as opposed to the alternative Defined Contribution plan which limit’s the cities liability (another topic worth exploring). What that means is that if the PERS pension fund underperforms (receives a net return of less than 7.75 percent annually), Vallejo (taxpayers) are stuck coming up with the money for the under funded portion of the pension. Alan Greenspan and Warren Buffet, have both written several articles about “defined benefit plans” and the assumptions the pensioners use (currently 7.75% return). In one article I read, Buffet suggests that the 7.75% number is not realistic and is/will lead to significant financial problems for municipalities. The next Tax Dollar Giveaway has to do with lifetime medical benefits.

Vallejo uses the “Pay As You Go” method to account for retiree medical expenses. That means Vallejo pays for medical benefits for all 30 years of employment, but doesn’t pay anything, nor set any money aside, for retiree health benefits until the employee retires. The benefit, per retiree, is currently about 13K per year. If that employee retires at 50, and lives to 80, he receives that benefit for 30 years (do the math: employee * average years retired * number of retired city workers) . Now, because no money has been set aside to pay for this rapidly escalating obligation, current tax payers are footing the bill for past obligations even if they never benefited from that employees service. The retired employee has been replaced by a new employee that is also receiving costly medical benefits.

In Dublin, Ca, rather than use the “pay as you go” system and account for retiree benefits as they are due, GASB 45 requires the agencies to account for the expenses as benefits accrue for the employees. The City engaged in an Actuarial Study Update with Bartel Associates, LLC and based on the 2007 actuarial result, the use of the CALPERS trust will reduce City contribution towards Retiree Medical in the future. On June 29, 2007 the City established an agreement with the California Public Employees’ Retirement System (CALPERS) to set aside funds, accumulate, and distribute assets for the exclusive benefit of retirees and their beneficiaries.

Here’s a side note regarding medical benefits. Several bay area cities offer certain union employees lifetime medical after 5 years of employment (maybe even Vallejo). For instance, as I understand it, if you worked from the age of 25 - 30, you would receive lifetime medical. This generous perk was used to help recruit candidates (teachers, street repair, facilities maintenance, etc…). Is that a Joke? Unfortunately it isn’t. That benefit is worth substantially more than the salary that employee earned. Think about it!

I also think its time to evaluate the hierarchy of the Fire Dept. During the 1980s, corporate America began the shift to flatten its structure. It appears that the FD has done the opposite. How many asst. chiefs, battalion chiefs, training chiefs does one FD need. There are no less than 30 FD employees that earned over 200,000 in salary (see the link below), and I‘m guessing many of them are not front line firefighters. How much management is needed when there is no: profit & loss responsibility, minimal budget responsibility (you go over budget you just go tell council you need more $), no setting of wages, no employee evaluations, and no hiring.

I have a friend that works as an admin for a bay area fire chief. I recently asked her how work was going and this is what she said, “Well, it’s kind of boring because there’s not a lot to do, but it’s a good job.” I don’t think it’s to big a stretch to assume that if someone’s executive admin. Isn’t busy the executive isn’t either.

Here’s the salary link:

http://www.sfgate.com/webdb/vallejo/?appSession=92522721172366

From IAFF local 21

Another disturbing trend happening across the IAFF and a result of the tanking economy are bankruptcies. I'm not talking about individuals, I mean municipalities going bankrupt. Vallejo, CA filed for bankruptcy allowing the city to nullify its collective bargaining agreement with Local 1186. This after the local offered up unprecedented concessions of over 10% in salaries to help keep the city solvent. The city decided that wasn't good enough and now the local is spending $750,000 to have the courts settle the issue. The cost burden has caused them to raise member dues to $231 per month. Think it can't happen to us. Think again!

This example illustrates the need for political action. When your union sounds the alarm we need you to answer the call because the person you help is ultimately your self. Our hard work over the last few years to build positive relationships with city leader is paying dividends right now. By the way did you see the mayor's proposed 2009 Fire budget? “

I have some comments an questions regarding the following :

A Word From Burky Worel

“The contract that was ratified by the council back in 2000 would not have gone to arbitration because it was proposed by the city manager when they were in the first year of an existing three year”

Why would a City Manager/administrator renegotiate a contract in its first year -- and give away so much? What was happening in Vallejo that compelled this action?

“When Martinez left everyone on the city council praised him, as did many community members, as being a great city manager following behind him blindly”

WHY?

“The old rate was done away and the two choices were 3%@50 or 3%@55. When it was agreed upon for the 3@50... “

Why give the choice when the answer is obvious. It’s like asking your 12 year old, do you want an allowance of 5 dollars a week, or 10 dollars a week?

“.. the cities' contribution went down but then went way up after the stock market tanked. In the 90's the city was only paying somewhere around 5% into PERS because PERS had so much money. Unfortunately the city didn't set the money they were saving aside to use when the rates went back up.”

O.K. The pension had money so Vallejo raised the pension obligation, and it cost less. I’ve read an article that talked about this. A study should have been conducted to determine the effect of the increased benefit, coupled with the rising salaries, to determine if it was sustainable. Now that it costs more, can PS reciprocate and help balance the fund? I believe I read where one city, in consideration of moving to 3@90, agreed to raise the employee contribution rate from 9% to 13% (from recollection - I need to verify that).

“As to the retirement changing in 2000 that was done by the state legislator not the VPOA.” I either need to be enlightened (quite possible), or this statement should be investigated. What does the state legislator have to do with contract negotiations between the unions and city? I’ve read the police contract, and anything to do with money (present or future) essentially says, we’ll accept what VFD gets. Can he be confusing the state legislator with the IAFF (and I’m only half kidding).

While it appears that the tone of the letter was both honest & sincere, there wasn’t any comment on the “retroactive retirement” portion of the contract.

Prior to the new public safety formulas made available by the legislature in about the year 1999-2000, there were 2 public safety formulas available for CALPers contracting agencies----2%@50 and 2%@55. Most public agencies, and likely Vallejo, contracted for the more generous of the 2 formulas---the 2%@50. This formula is FAR more generous than the vast majority of folks in the private sector will ever see.

As a result of the legislative action, AGGRESSIVELY lobbied for and promoted at the state legislative level by public safety organizations, THREE new public safety retirement benefit formulas were made available to PERS-contracting agencies like Vallejo----2.5%@55, 3%@55, and 3%@50. Most public agencies, including Vallejo, adopted the most generous of the new formulas, 3%@50, almost as soon as they were available. However, in virtually every case, this action resulted from intense pressure of public safety unions, either through contract language or, even, OUTSIDE of the normal contract renewal process. I don't know how it occurred in Vallejo.

A few other facts should be noted here. First, until the mid 90's, the public safety retirement formulas were limited to a maximum of 75% of the wage base that the retirement formula was calculated upon (usually, the highest 12 months salary prior to retirement but sometimes the average of the highest 36 months). In the mid to-late-90's, through intensive lobbying by public safety employee organizations, that maximum was increased several times to 90%. It may even be higher now; I'm not sure. The increases in the maximum were across-the-board and did not require action by governing bodies of PERS-contracting agencies. However, those increases in the maximum percentage allowed were not related, at all, to the making available of the new retirement benefit formulas. That action was separate and DID REQUIRE action and acceptance by PERS-contracting agency governing bodies (e.g. City Council).

Another little-known fact is that when the new formulas were adopted, they were RETROACTIVE. This means that, for example, a public safety employee with 29 years of service and at age 50 at the time of adoption of the new formula by the agency would have their retirement based upon the new formula (i.e. 29 years X 3% per year= 87%) rather than the old formula upon which they and the agency had been been paying for their entire working career. That formula would have given the same employee far less (i.e. 29 years X 2% per year= 58%). Ever wonder why so many retirements occurred and will continue to occur after the new formulas came into being? Wonder no more. This IS the reason. The cost of the increased benefits unsupported by working life contibutions is borne through MUCH HIGHER employer contributions to the CALPers system both now and in the future. It's as simple as that.

One other item that you didn't cover in your earlier expose of employee salaries is benefit costs. The combination of salary + benefit costs is known as TOTAL COMPENSATION. If you were to include benefit costs, you would find that TOTAL COMPENSATION of public safety employees is MUCH higher. A rough "guesstimate" for Vallejo would be an additional amount of about 70% of base salary (i.e. salary exclusive of overtime and other special pay).

Also, just to substantiate the information I provided regarding the current availability of the "old" 2%@50 and 2%@55 formulas for public safety, so the link below to the CalPers web site. You will note these formulas as still available under the "public safety" formulas section. These are the formulas which Bunky Worel states "went away" and, according to him, necessitated the adoption of one of the new (and more generous) formulas.

I also confirmed that 90% is still the maximum percentage for public safety.

http://www.calpers.ca.gov/index.jsp?bc=/member/retirement/service-retire/benefit-charts/localformulacharts.xml