Renne Sloan Holtzman Sakai
Public Law Group™
350 Sansome Street, Suite 300
San Francisco, CA 94104
t: 415.678.3800
f: 415.678.3838

Jonathan V. Holtzman
415-678-3807
jholtzman@publiclawgroup.com

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Via Email

David Weinberg
35 Miller Avenue, Suite 117
Mill Valley, CA 94941
dwmedarb@gmail.com

Kristy Sermersheim
Service Employees International Union, Local 521
517B Mission Street
Santa Cruz, CA 95060
Kristy.sermersheim@seiu521.org

Dania Torres Wong
Renne Sloan Holtzman Sakai LLP
1220 Seventh Street, Suite 300
Berkeley, CA 94710

Re: County of San Benito/Service Employees International Union, Local 521
PERB Case No. SF-IM-131-M

Closing Brief of the County of San Benito

Dear Fact-Finding Panel Members:

I. INTRODUCTION

The County of San Benito (the "County") has a severe structural deficit. Based on undisputed information from the County's 2012 Comprehensive Annual Financial Report (the "CAFR"), the County's General Fund balance has been declining by about $3 million a year, and is less than half of what it was in FY2008-09. Although much of the discussion during the hearing focused on the County's "financial ability," AB 646 also requires the fact-finder to look at other express and "traditional" criteria. These also strongly support the County's last, best and final offer (the "LBFO"). Most critically, the state legislature has expressly found that "[e]qual sharing of normal costs between a contracting agency or school employer and their employees shall be the standard. *It shall be the standard* that employees pay at least 50 percent of normal costs and that employers not pay any of the required employee contribution." Cal. Gov't Code, § 20516.5 (emphasis added). Arguably, this fact alone compels the conclusion that the panel should recommend the County's LBFO on pension contributions. But that is not all: the County's LBFO on pension contributions is appropriate because the undisputed reality is that pension costs have risen steeply since the era when employers first picked up the employee contributions – and are likely to continue rising by as much as 50% over the next six years. Under these circumstances, it is entirely reasonable to expect, at a minimum, that employees pay their own statutory share of the pension costs. Finally, the County's pension proposal is equitable; new employees in the same unit receive a lesser pension, but currently contribute 6.25% of salary towards pension costs. Employees in all safety units pay the full 9.0% statutory share of pension, and all other groups have been paying 4.0% of salary *for the last two years*. Those groups are now being asked to pay the full 7.0%.

The County's proposal to flat-rate health benefit contributions for both active and retired employees is also supported by the County's fiscal condition, especially in light of the 62% increase in healthcare costs to the County since FY2008-09. The County's proposal helps to effectuate the policy underlying AB 646, which mandates that all benefits must be considered in the bargaining context. Flat rating the medical contribution means that, as each successor contract is negotiated, the benefit costs will be considered. Finally and perhaps most important, flat rating the health benefit will reduce the County's other post-employment benefit ("OPEB") costs. The County's OPEB liability is very high, and, unlike many other counties, San Benito is funding the full amount of its Annual Required Contribution ("ARC"). The County's healthcare proposal will free up money for employee compensation, and to restore services to the public, while continuing above market retiree health benefits.

Like many public agencies, the County's services have been decimated in the wake of the Great Recession. The only hope to begin restoring services, in the face of known future increases in benefits costs, is to address the structural problem the County faces. The County's LBFO does so in a manner that is supported by sound public policy.

II. BACKGROUND

A. Negotiations and Tentative Agreement

The County engaged in good faith negotiations with SEIU from July through early October 2013. Curiously, SEIU itself demanded that the County issue its LBFO on October 2, 2013, threatening that it would file an unfair labor practice charge against the County if it did not. Per SEIU's request, the County issued its LBFO on October 4, 2013, which SEIU promptly rejected. Ultimately, the parties agreed to parallel tracks of mediation and fact-finding.

Following mediation, on November 6, 2013, the parties executed a tentative agreement, which included what the County believed were reasonable compromises on the most critical issues, specifically employee pension contributions and conversion of the County's healthcare contribution to a flat rate. However, the members of the SEIU bargaining unit voted to reject the mediated tentative agreement. Critically, it appears that the bargaining team itself failed to support the tentative agreement in its presentation to the membership.

B. The County's Proposal

In light of SEIU's rejection of the mediated agreement, the County proposes that the fact-finding panel recommend the terms of the County's LBFO. The critical terms of the County's LBFO are:

- <u>Employee Pension Contribution</u>: SEIU bargaining unit members increase their pension contribution from 0.0% to 7.0%, or an equivalent salary reduction.
- <u>Health Benefits:</u>
  - <u>Healthcare Contribution</u>: For both active and retired employees, County will contribute a flat rate, comprised of PEMHCA minimum plus an additional contribution towards a cafeteria plan.
    - Total contributions:
      - Employee Only: $464.71
      - Employee plus 1: $949.22
      - Employee plus family: $1213.83
  - <u>Eliminate dual coverage</u>: Employees whose "alternative insurance" is received through a spouse or domestic partner who is also a County employee shall be ineligible for the $150 per month payment in lieu of insurance
- <u>Cost Containment Measures</u>:
  - <u>Reduce Sick Leave Cash Out for New Hires from 50% to 25%</u>: The County must manage this unfunded liability on a going-forward basis. Accordingly, it proposes to reduce sick leave cash out upon retirement from 50% to 25% for new hires only. Importantly, the parties agreed to this proposal as part of the tentative agreement.
  - <u>Eliminate Step G for New Hires</u>: This proposal, to which the parties agreed as part of the tentative agreement, will allow the County to manage future salary costs without impacting current employees.
  - <u>One-time 1.5% Wage Reduction</u>: Given the delay in reaching agreement with SEIU, the County proposes a one-time 1.5% wage reduction to allow the County to recoup the savings lost because of this delay.
  - <u>Reopener Regarding Elimination of CalPERS § 22893 Vesting Schedule</u>: The parties agreed to this term as part of the tentative agreement. The County believes it is important to continue discussions on this issue as the vesting schedule serves as an automatic

escalator of the County's contributions to retiree health and the County has no control over the rates set by CalPERS under this program.

III. DISCUSSION

A. County's Financial Condition

By sharing pension and healthcare costs with its employees, the County will be able to manage its structural budget deficit by reducing its on-going expenditures. As seen in SEIU's own Exhibit 1, the County's CAFR for the fiscal year ended June 30, 2012, the County's expenditures have exceeded its revenues each year since FY2007-08. (Union Ex. 1, at 104). As a consequence, the County's General Fund reserve has decreased by approximately 59% since FY2008-09, from approximately $25.84 million to approximately $10.74 million in FY2011-12. (Union Ex. 1, at 103). This method of balancing its budget is unsustainable; the County has used an average of $3 million in reserves to cover its General Fund deficit and at this rate will fully deplete its reserves in the next two to three fiscal years. Through its cost-sharing proposals, the County is taking the fiscally responsible step of addressing an on-going deficit by reducing on-going expenditures.

SEIU asserts that the County has been too conservative in its budgeting; but the sad truth is, whether or not the *budgets* were conservative, the County's actual financial results have been poor. SEIU also argues that the County's actual reserves are above the minimum acceptable amount; whether or not this is true – there was conflicting evidence on this point -- it is clear that, absent significant changes in its cost structure, they will not be for long.

Importantly, the decline in the County's financial condition has occurred despite huge service reductions. Some key facts:

- The number of General Fund employees has been reduced by over 100 positions since FY2008-09;
- The number of deputy sheriffs in the County has been cut in half since FY2011-12;
- Public office hours for a number of County departments have been slashed since 2009;
- Staffing in the Assessor's Office, which is a revenue generating function for the County, has been cut by 30%; and
- The Auditor's Office, which is responsible for, among other things, the County's CAFR, does not employ a single accountant.

SEIU asserts that the County is or may be inadvertently "hiding money." Yet SEIU has completely failed to identify such funds, and the CAFR reflects – no doubt due to the small overall size of the budget – there are relatively few "internal service funds" or designated reserves. The one specific example SEIU pursued during the hearing was the assertion that, because the amount transferred out of the General Fund to the "risk management" fund did not match the exact number received by the fund, there must have been a second transfer of equal size into the fund. Of course, the conclusion that the County paid twice does not flow ineluctably from the assertion that the numbers in the budget documents do not match perfectly. A more reasonable conclusion is that other expenses resulted in the transfer being slightly smaller than anticipated. In fact, at SEIU's request, the County continued to review this issue after the hearing and has found that risk management expenditures were under-budgeted in the FY2013-14 Adopted Budget estimates for premiums. To cover the full actual costs of risk management, the County will need to request a budget augmentation out of the General Fund Contingency from the Board of Supervisors. To be clear, there is *no* evidence a second transfer of $1.7 million ever occurred.

Importantly, the County's Board of Supervisors felt it necessary to cut services to the bone, and yet, the County continues to have a structural deficit. Cutting services has also meant cutting jobs – painful medicine to say the least. Given these painful sacrifices, SEIU's suggestion that the problem is overblown defies common sense.

B. Terms of the County's LBFO

1. Shared Pension Costs

The County's LBFO regarding employee pension costs is supported by the majority of criteria set forth under AB 646.

a. State Law

The County's pension proposal is supported by PEPRA, which provides that "the standard" shall be that employees pay at least half of the normal cost of their pension. Cal. Gov't Code, § 20516.5. Based on CalPERS most recent valuation of the County's miscellaneous pension plan, the total normal cost is approximately 14.7% for FY2014-15. Under the County's proposal, SEIU members' pension contribution would be approximately half of this amount, 7.0%.

b. Financial Ability

Cost sharing of pension costs is a critical step towards resolving the County's structural deficit. Based on its most recent CalPERS valuation, the County's pension expenses are expected to increase by **44%** of payroll by FY2019-20. It must be noted that this increase does not account for the County's pickup of employee contributions, which amplifies the County's cost concerns. Based on this same valuation, the County's miscellaneous pension plan is only 68.7% funded, on a market value basis, meaning that the County has insufficient funds saved to pay for current retirees and survivors and has no money set aside to cover the pensions of current employees. Increasing the pension contribution of SEIU's employees is an important step towards managing the increased rates attributable to this unfunded liability.

During the hearing, SEIU seemed to suggest that the contribution rates provided to the County by CalPERS are pessimistic and, in reality, the County's actual contribution rates will be significantly lower than currently projected. This assertion is baseless. Due to CalPERS' extraordinary asset smoothing, even fairly large market gains will have little effect on projected rates going forward. Worse, CalPERS has publicly stated that it is planning to adopt modified mortality tables, which will assume improved life expectancy for future retirees. This change is expressly excluded from CalPERS' pension rate projections. In addition, it is anticipated by industry experts that CalPERS is going to reduce its discount rate from 7.50% to 7.25% -- though hopefully not for a couple of years. Even a change of this small magnitude would likely increase contribution rates significantly. In light of these facts, it is more likely that CalPERS current projections for employer contributions are *too low*, not too high.

c. Internal Equity

SEIU is the sole outlier among the County's miscellaneous employee groups with respect to pension contributions. The County's other miscellaneous bargaining units, and many of its safety units, have been paying between 4.0% and 9.0% of their pension costs since as early as 2011. The County is seeking to have all of its employees pay the entire employee share of the pension contribution starting this year. Importantly, PEPRA requires that SEIU members who are "new" as defined under PEPRA contribute 6.25% to their pension costs. SEIU's "classic" members, on the other hand, make *no* contribution to their pension costs. The County's proposal reflects the concessions necessary to bring SEIU in line with other bargaining units while ensuring that the County will not need to further reduce services to its residents.

2. Shared Healthcare Contribution

The criteria set forth in AB 646 also support the County's LBFO with respect to the sharing of healthcare costs.

a. State Law

Under the terms of AB 646, which guide the fact-finding panel's analysis, the panel must consider, among other factors "the overall compensation presently received by the employees, including direct wage compensation, vacations, holidays, and other excused time, insurance and pensions, medical and hospitalization benefits, the continuity and stability of employment, and all other benefits received." Cal. Gov't Code, §3505.4(d)(7). Under this criterion, it follows that non-wage aspects of compensation should be subject to bargaining, not automatic escalation. The County's proposal embodies this principle; it proposes a flat rate that will be subject to bargaining in subsequent negotiations. The County has also proposed terms similar to those before SEIU in its current negotiations with other bargaining units.

b. Financial Ability

The County's proposal on healthcare benefits will result in short term savings of approximately $270,000 in second half of FY2013-14. More importantly, however, the County's proposal to flat rate its contribution to retiree health costs will reduce the County's unfunded OPEB liability and will likely reduce the County's ARC. This is especially important as the County has made the fiscally responsible commitment to pay its full ARC each year.[1]

3. Cost Containment Proposals

In addition to its proposals with respect to employee pension contribution and healthcare cost sharing, the County's LBFO also includes a number of proposals that support the County's goal of cost containment, which will in turn help the County address its budget deficit. These proposals include (i) elimination of dual healthcare coverage, (ii) reduction of sick leave cash outs for new hires, (iii) elimination of Step G for new hires, (iv) elimination of the CalPERS § 22893 vesting schedule and (iv) one-time reduction of wages by 1.5% . These proposals will result in both short and long-term savings, helping to address the County's structural deficit.

IV. CONCLUSION

SEIU has characterized the County's argument as "the sky is falling" with respect to the County's financial condition. To be clear: The sky is not falling solely and exclusively because County officials have taken prudent steps. On the strength of less than a week of study, SEIU's expert suggests the County could raise more revenue (it is already planning to do so), is hiding money (no evidence), is moving too quickly to seek concessions (SEIU trails other groups by a full two years), pension costs will not rise as quickly as CalPERS anticipates (the evidence suggests the opposite), the economy is improving (true, but there is little evidence that County

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[1] In addition to being fiscally responsible, by paying its full ARC, the County benefits from a higher discount rate, which in turn reduces its OPEB liability. SEIU's own expert agreed that the County realizes a measurable benefit from payment of the full amount of its ARC.

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revenues are rising significantly), and the County should take on debt to fund employees' compensation (bad idea).

The County reached the tentative agreement with SEIU in good faith, and moved significantly on a number of issues to reach that agreement. In light of SEIU's failure to ratify (or even really attempt to ratify), it seems clear that the labor peace the Board of Supervisors had hoped to attain will remain elusive. For that reason, and recognizing that fact-finders accord very great deference to tentative agreements reach cooperatively by the parties at the table, the County requests the fact finding panel recommend the County's last best offer as it fully conforms to the criteria set forth in AB 646.

Sincerely,

Jonathan Holtzman
Renne Sloan Holtzman Sakai LLP
Attorneys for the County of San Benito