PREPARED STATEMENT OF ROBERT PALMER

For

THE CONFERENCE COMMITTEE on PUBLIC EMPLOYEE PENSIONS

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Introduction:

Thank you for the opportunity to appear before the Committee and to share my thoughts regarding the health and sustainability of public pension plans in California, and the public pension plans operating under the County Employees' Retirement Law of 1937 (the 'CERL' or '1937 Act') in particular.

I have been invited to appear before your Committee because of my position as the Executive Director of the State Association of County Retirement Systems. The State Association of County Retirement Systems, (SACRS) is a 58-year-old association consisting of the retirement systems in twenty California counties whose systems were created under the California County Employees Retirement Law (CERL). The SACRS member systems assets total approximately $90 billion and provide benefits to 400,000 county employees and retirees. These systems have been providing benefits to their members for over 75 years.

At the outset, I think it is important to articulate how the 1937 Act community generally views our responsibilities: Our job is to serve as the fiduciaries responsible for administering the pension benefit plan adopted by our participating employers and employees. If one views a pension as a "promise" made by the employer to its employees, we are the trustees to make sure that that promise is kept. We do not advocate for or against particular benefits or benefit levels. Instead, we strive to be a resource for our stakeholders, serving as the 'honest broker' of information, thereby helping the parties to make informed and well-founded decisions. We also try to assure that the decision-makers understand the fiscal and administrative ramifications of a given decision or course of action.

In the end, maintaining an independent, fair and balanced position with respect to the stakeholders in our systems is critical to preserving our credibility and assuring that the retirement system is being managed in a reasonable and prudent manner.

My written comments and remarks at this hearing are intended to reflect this perspective and goal of serving as the 'honest broker' of accurate information regarding our pension systems.

To that end, in the discussion that follows I will endeavor to provide information on the various topics that I believe are of interest to your Committee.

Overview of the 1937 Act Retirement Systems:

The twenty county retirement systems that operate under the parameters of the 1937 Act are similar to the large statewide retirement systems in a number of respects. Those counties are Alameda, Contra Costa, Fresno, Imperial, Kern, Los Angeles, Marin, Mendocino, Merced, Orange, Sacramento, San Bernardino, San Diego, San Joaquin, San Mateo, Santa Barbara, Sonoma, Stanislaus, Tulare and Ventura.

- The focus of the systems is to provide a defined benefit pension plan under the parameters established by the County Employees' Retirement Law of 1937.
    - Plans provide a guaranteed pension benefit based on a benefit formula, final average salary, number of years of service, and age at retirement.
    - Pension benefits are funded by contributions from the employer and employee and from investment earnings on those contributions. Historically, 70% of the benefits paid to retirees/beneficiaries are generated from investment earnings.
    - Retirement system is a trust fund separate from the county. The trust cannot be accessed by the county and the funds in the trust must be used exclusively to provide benefits to the members and to pay system expenses.

- There is a wide range of sizes (assets, active members, retirees) across the 20 systems, with the Los Angeles County Employees' Retirement Association at one end (approximately $34 billion in assets, 96,000 active members and 54,000 retirees/beneficiaries), and the Mendocino County Employees' Retirement Association at the other end (approximately $256 million in assets, 1300 active members and 1,000 retirees/beneficiaries).
    - The systems are geographically diverse, and are spread across California.

- Collectively, the systems provide pension benefits for more than 170 local government agencies.

- Collectively the systems manage more approximately $90 billion in assets.
    - Median size is about $1.7 billion.

- Collectively the systems cover more than 264,000 active employees.
    - Mandatory participation by full time employees.
    - Membership includes both General and Safety employees.

- Collectively pay monthly benefits to more than 152,000 retirees and beneficiaries.
    - Payments total more than $4.3 billion annually.

- All systems feature local control through a Retirement Board comprised of key stakeholders:
    - Four elected by employees (2 by General members, 1 by Safety members plus 1 Safety alternate).
    - One elected by retirees (plus 1 alternate).
    - Four appointed by the County Board of Supervisors.
    - County Treasurer (or equivalent position).
    - All serve 3-year terms.
    - Fiduciary duties owed to the retirement trust and participants in the system.

- State Constitution vests the Retirement Board with exclusive authority for management of the retirement system.

- Annual audits by independent, outside auditors.

- Annual actuarial valuations by independent outside actuaries.

- Subject to state open meeting/public record laws.

- Administrative costs limited to 0.21% of plan liabilities.

- Benefit formulas, established in the California Government Code, are set at the local level by the County Board of Supervisors (or governing body of the participating employer) based on the collective bargaining process.

    - Options regarding benefit formulas and cost sharing are established in 1937 Act.
    - Many counties (but not all) chose to enhance benefit formulas for both Safety and General members after the State enhanced the formulas for its members.
    - Some counties chose to enhance benefits prospectively but not retroactively.

- Systems generally do not administer health care benefits for active employees or retirees.

    - Some systems provide a subsidy toward retiree health care costs.

- Each system invests its assets through a professionally managed, diversified investment portfolio.

    - Investment programs are comparable to and have returns similar to those achieved by the statewide systems.

<u>Differences Between the 1937 Act Systems and the State Systems</u>:

There are some important differences in the structure of and the law governing the 1937 Act systems as compared to the statewide systems.

- Local control means that employers and employees are able to develop a benefit plan that speaks to the circumstances of the local workforce. Since there are fewer key parties than with statewide systems, local plans can be modified more quickly and easily to address changes in circumstances.

- Local control means local impact and local accountability. Plan members or stakeholders can express concerns to the local retirement system (as opposed to a larger, statewide entity) and/or to local officials or labor organizations.

- Local control means the systems are able to develop programs and policies that are consistent with the local perspective on issues and/or the local comfort level with risk or controversy.

- While the 1937 Act systems are independent legal entities, the county has a higher level of involvement than the lead employer in the statewide systems.

  - The county is the dominant participating employer, by a larger margin, with 90% or more of the members working for the county. In contrast, in statewide systems a single employer comprises less than 50% of members.
  - The county is the largest 'debtor' of the system and the county's financial situation and ability to pay is critical to the soundness of the plan.
  - Through its appointees and ex-officio representation on the retirement board the county has the ability to maintain de facto control.
  - Most systems continue to process expenditures (including the payment of monthly benefits) through the county.
  - The county continues to control the job classifications and compensation levels for most employees of the retirement systems.

- Given the high level of involvement of the lead employer, the 1937 Act systems do not have the same ability to dictate terms, impose requirements and/or have an adversarial relationship as the statewide systems have with their participating employers.

- The 1937 Act systems operate under a different set of rules governing what counts as compensation for the purposes of determining retirement benefits.

  - What qualifies as 'retirement compensation' is determined based on the rulings in two court decisions (generically, 'the Ventura' decisions). The court decisions changed the previous practice that limited permissible compensation elements. Now, almost all cash remuneration received by the member qualifies as retirement compensation.

    - For example, most regular, recurring pay differentials (e.g. uniform allowances, education incentives, bi-lingual pay, etc.) are considered for retirement benefit determination purposes. Overtime pay is excluded.
    - Up to certain limits, lump sum cash-outs of sick leave or vacation leave prior to termination of employment are considered for benefit determination purposes. Cash-outs at retirement (i.e., via termination pay) are excluded.

  - A further complicating factor is that several 1937 Act systems settled their Ventura litigation before the final court decisions and in some cases those settlements directed that certain types of compensation be counted for retirement purposes even though the subsequent court decisions ruled differently.

    - Those systems are trying to determine how best to 'unwind' such policies.

- Efforts to change the Ventura rules for existing employees presents substantial exposure to potential litigation on the theory that the compensation treatment set by Ventura (or a Ventura settlement) is a ‘vested right.’

Thank you for the opportunity to appear before your conference committee. The SACRS organization is more than willing to assist the committee in any fashion that would be useful to all parties involved.

Respectfully Submitted,

Robert Palmer

SACRS Executive Director