MARIN COUNTY GOVERNMENT BASIC FACTS ABOUT PENSIONS

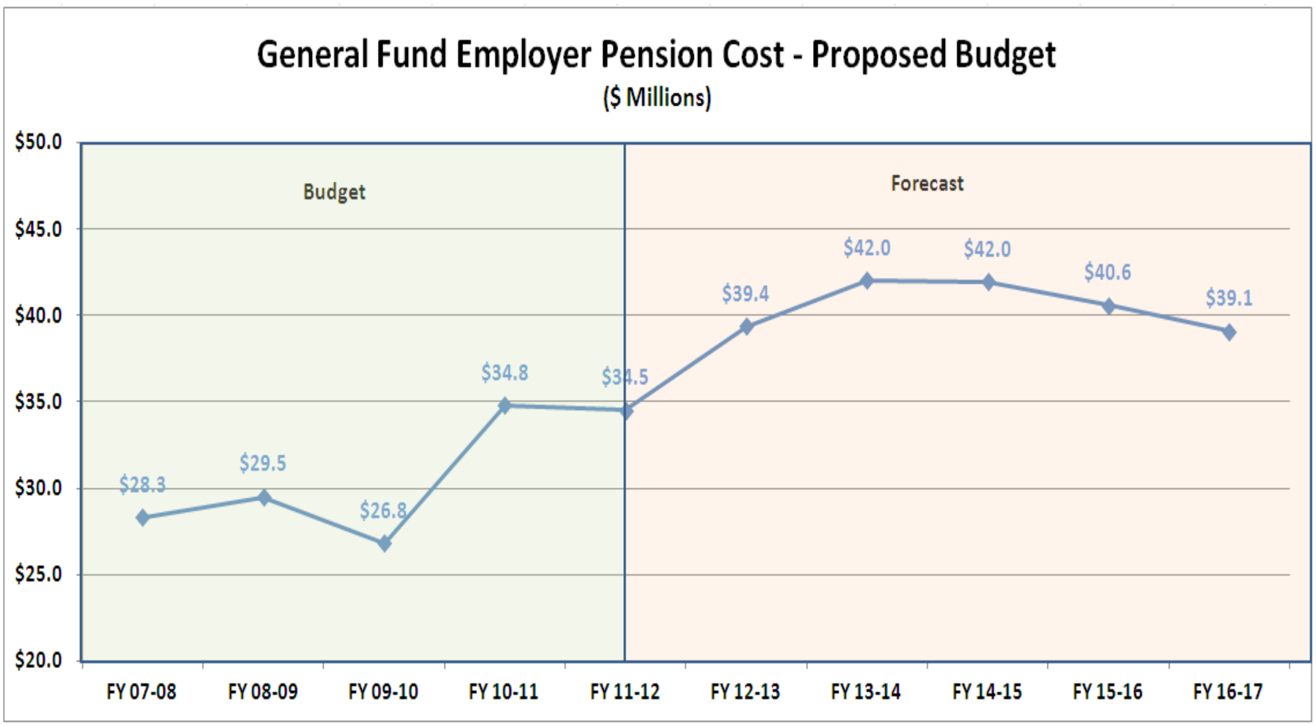
COUNTY OF MARIN

OVERVIEW: Why Are Public Employee Pensions in the News So Much?

Marin County's General Fund is expected to have budget shortfalls for the next several years. The main reasons are increased pension and health care costs plus a significant decline in property tax collections. The cost for public employee pensions is an issue at *all* levels of government. Across most local governments in California, increased pension expenditures relate to these factors:

- Significant investment losses by pension funds, especially in 2008 and 2009
- Higher retroactive benefits adopted when investment returns were higher
- Retirees living longer today than when pension plans were established

In Marin County, the cost to pay pensions is increasing at a time when difficult choices are being made about what services to keep or cut:



Changing the County's pension system is a complex issue based on a series of state laws and local negotiations. There are no "quick fixes." The County of Marin has already taken steps to reduce future pension costs. But the discussion needs to continue. County leaders are inviting all interested community members to learn about and weigh in on options for Marin to keep making progress toward a sustainable pension program.

WHAT IS A PENSION?

A pension is a type of employee compensation paid upon retirement. Usually, both the employee and employer contribute toward the pension every pay period. These funds are pooled and invested to ensure funds are available over the long term to pay promised benefits when they are due. The employee is eligible to collect the pension when they reach a specified retirement age and stop work.

Marin County Government, like most public agencies, offers a **"defined benefit"** that is a known amount upon retirement, along with a capped cost of living adjustment to help address inflation. This differs from a **"defined contribution"** retirement plan where the amount put in (usually by a combination of employee and employer) is known and the payout in retirement varies based on investment earnings.

HOW ARE MARIN COUNTY EMPLOYEE PENSIONS DETERMINED?

Pensions are defined by state laws and local labor agreements with employee unions. Marin County government operates in partnership with twelve different employee unions. The largest, Marin Association of Public Employees (MAPE), represents about 50% of the County's total. County employees are classified as either "Safety" or "Miscellaneous" depending on their function.

Each of these kinds of employees is assigned to a different "tier," usually based on their hire date. The tier sets a **"benefit formula"** using retirement age and a specific percentage of salary that gets applied to years of service to calculate what annual benefit is received in retirement. The formula also defines a maximum cost of living adjustment.

For Marin County, the average annual benefit for Miscellaneous retirees is about $30,000 and $50,000 for Safety retirees. The average annual health benefit paid to these retirees is $7,660. Marin County employees do not contribute to, nor will they benefit from, Social Security for any years worked as a County employee.

HOW DO THE BENEFIT FORMULAS WORK?

As an example, most county "Miscellaneous" employees have a formula shown as 2%@55. This means at a retirement age of 55, these employees are eligible to receive 2% times their final salary for every year of service. The salary used for the calculation is an average of the last three years of service. If that average was $80,000, after 20 years of service, the "defined benefit" would be (2% x 20) x $80,000 = $32,000, plus up to 2% in annual cost of living adjustment (COLA).

Most Marin County safety employees have a formula of 3%@50. Last year the County negotiated a lower tier for new safety employees of 3%@55 and a tier of 2%@61 ¼ of for new Miscellaneous employees. These return to levels in place in the 1980's and 1990's, before more generous benefit formulas were adopted in 2002 for Miscellaneous employees and 2005 for Safety employees.

WHO ADMINISTERS MARIN COUNTY GOVERNMENT PENSIONS?

Marin County Employees' Retirement Association (MCERA) is the agency that operates the pension system for Marin County and some other local jurisdictions in Marin (like the City of San Rafael and the Novato Fire Protection District). As of July 1, 2011, MCERA had 1,813 active employees and 1,397 retirees from Marin County government.

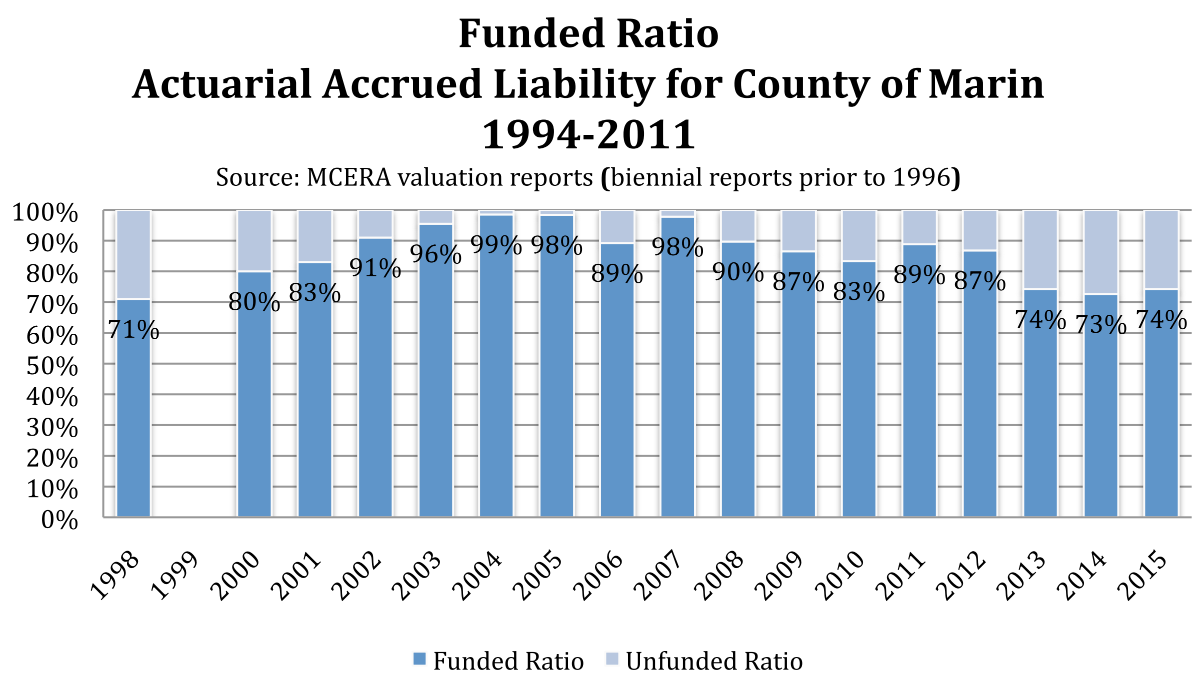
Twenty of California's 58 counties, including Marin, operate their own pension systems governed by the County Employees' Retirement Law of 1937 (often referred to as CERL, or the '37 Act), which authorizes MCERA. MCERA is overseen by a nine-member board that includes appointees of the Board of Supervisors, the County's Director of Finance (Ex Officio), and active and retired employees who are plan members. Almost all other California counties participate in CalPERS, the state's pension administrator.

HOW DO EMPLOYEE PENSIONS GET FUNDED?

Public pensions programs like Marin County's have three main funding sources:

- Employee contributions – fixed by negotiation
- Investments – variable, based on market conditions
- Employer (taxpayer) contributions – fluctuate to make up any difference

When investments decline significantly, as in 2008, the County must increase its payments to meet the retirement obligations. The gap between costs to pay the liability for current and future retirees and the income to do so is called an **"unfunded liability."** Marin County's ability to fund retirement obligations has declined in recent years due to the significant market declines of 2008/09:



HOW DOES MCERA DETERMINE TOTAL UNFUNDED LIABILITY?

Marin County Employees' Retirement Association (MCERA) is responsible for making the actuarial predictions that determine what Marin County's accrued liability will be for pension obligations. These projections use assumptions for factors such as when employees will retire, how long they will live, what kinds of investment returns will be achieved, and what inflation rates will be in the future.

MCERA recently adopted an assumption of a "nominal" 7.5% return for investments. With a 3.25% inflation assumption, the assumed "real" rate of return is 4.25% over the long term. This is the same nominal assumption that CalPERS just adopted. Unlike CalPERS, MCERA uses a shorter 17-year amortization period. That means that MCERA is assuming the unfunded portion of current and future retiree costs must be paid in 17 years instead of 30 years.

Per MCERA's June 30, 2010 actuarial valuation, the County's funded ratio is 72.6% and the current unfunded liability is $384.3 million. There are different views as to whether and how quickly the unfunded liability should be eliminated and about what assumptions should be made regarding investment returns.

Marin County government, like other agencies, also has an unfunded liability to pay health insurance costs for retirees. This is separate and in addition to the County's unfunded liability for pension. The unfunded liability for retiree health care is $382.7 million. Local references to a $700 million unfunded liability is a *combination* of pension and retiree health unfunded liabilities. Main County has been setting aside funds to pay its retiree health liability. Next year, it plans to establish a trust fund for these payments, which creates savings, while fully funding retiree health liabilities going forward.

WHAT KINDS OF CHANGES TO PENSION PLANS CAN BE MADE?

There are three basic ways to reduce the County's pension costs:

- Increase what the employee contributes
- Share the investment risk, e.g. by introducing "hybrid" plans
- Reduce total benefits by adjustments in variables such as retirement age

Some pension adjustments can be accomplished via labor agreements. But more significant pension changes require state legislation.

WHAT HAS BEEN DONE SO FAR TO REDUCE PENSION COSTS?

Both past and recent agreements to reduce pension costs have made Marin County a leader among most of its peers in this area. Over the years, these decisions have been put in place:

- Capped pension COLAs to 2% annually
- Require employees to pay 50% of the cost for any COLA's, and 50% of the cost for enhanced formulas
- Use average of the highest three years' earnings for pension calculations
- Negotiated new, lower cost 2% @ 61 ¼ tiers for new Miscellaneous employees
- Negotiating new, lower cost 3% @ 55 tiers for new Safety employees
- Embraced Governor's pension reform plan

WHAT IS GUIDING FUTURE ACTION?

In December 2011, the Marin County Board of Supervisors adopted pension reform policy guidelines, with the overall goals of fairness to employees and fiscal responsibility to residents. In addition to supporting the Governor's 12-point plan, the Board issued this statement: "Although we would prefer statewide solutions, we are also willing and expect the need to pursue Marin-specific solutions. Our support of pension reform includes but is not limited to:

- Creating lower cost hybrid defined benefit/defined contribution pension options
- Prohibiting unfunded retroactive increases
- Providing new options to exclude certain types of pay from being pension-eligible to prevent pension spiking
- Prohibiting retirement systems from granting ad hoc COLAs to retirees without support of the Board of Supervisors or the employer's governing board
- Exploring limits on so-called double-dipping between other government agencies
- Capping pension benefits to certain percentage of pay or dollar amount."

Any of these Marin-specific solutions would require agreement with employee labor unions and special legislation. The April 3, 2102 Community Forum is an opportunity to develop broader understanding of different perspectives about these and other options for further reducing pension costs.

FOR MORE INFORMATION

Marin County information about pensions: www.co.marin.ca.us/cao/pension/
Marin County Employees' Retirement Association (MCERA): www.mcera.org.
Institute for Local Government Pension Glossary www.ca-ilg.org/PensionGlossary