Inside City Hall
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Police and Pension Reform

Burden of new contributions erased by pay hikes

By Craig Powell

After three long years of informal and formal bargaining, mediation, more formal bargaining and, finally, a binding determination by an arbitrator, the city has a new labor contract with the Sacramento Police Officers Association. City police will finally join all other major city bargaining unions and be required to contribute the full employee's share into the California Public Employees' Retirement System (9 percent of their salaries)—and then some. In addition, city cops will be required to pony up another 3 percent of their salary to pension contributions—replacing a portion of the city's existing contribution to cop pensions—for a total contribution by cops of 12 percent of their salary. In contrast, members of the next highest contributing city union, the firefighters, contribute 9.2 percent of their salaries to pensions.

To ease the pain of such a major reduction in take-home pay, the arbitrator awarded the police salary hikes, starting next year, of 3 percent in each of the next 3 years, totaling 9.3 percent once fully implemented. (Sergeants will get 7 percent raises.) The new contract's near-term impact on the city's general fund budget: a savings of $1.25 million in the current fiscal year and $2.24 million in 2014-2015, shifting to a net cost of $300,000 in 2016-2017 and $1.59 million in 2017-2018.

The arbitrator's decision caps off a three-year effort by city manager John Shirey to require all city employees to contribute 100 percent of the employee's share of their pensions. Until Shirey's initiative, most nonpublic-safety city employees paid between 3 and 4 percent of their salaries to their pensions, while police, firefighters and city managers paid zip toward pensions. Shirey kicked off his campaign to require full contributions by setting a good personal example: He insisted that his own employment agreement require him to make a full 7 percent pension contribution. (Of course, that's a little easier when you are making $258,000 per year.) Next, he required all nonrepresented city employees, including all city managers, to pony up. Then, as each city union contract expired, he insisted that each contract require workers to make full contributions.

This was easier with the nonpublic-safety unions, which were being asked to kick up their pension contributions from 3 or 4 percent to 7 percent. But it was a tougher ask of the police and fire unions, which had been paying nothing toward their pensions, with the city picking up the city's share as well as the workers' share of 9 percent for cops and 9.2 percent for firefighters.

His task was made a great deal tougher by a controversial city charter provision that requires labor disputes between the city and its public safety unions to be resolved through binding arbitration. In negotiating agreements with all other city unions, the city, if it reaches an impasse, can unilaterally impose its "last, best and final" offer on a union. But with binding arbitration, a third-party arbitrator sets the terms of a disputed contract, which commonly results in higher awards to unions than would otherwise be the case. So Shirey held the negotiating hammer over the city's nonpublic-safety unions and used it to force them to make their full pension contributions, but he had to take a different tack with police and fire unions. He struck a deal with the firefighters union that required firefighters to increase their pension contribution up to 9.2 percent in steps over two years in exchange for salary hikes.

At the same time Shirey was pressing employees to pony up their full share of pension contributions, he was also trying to eliminate the city's retiree health care benefit for new hires (which may do little to reduce the city's massive $470 million outstanding liability for such costs but keeps it from getting much worse). He successfully pressed every union into dropping the retiree health benefit for new hires—except for the firefighters, who resisted. (SPOA agreed last year to drop the benefit for new hires in exchange for the city's lifting a hiring freeze on new police officers.) Firefighters had more to lose: Firefighters get actual health insurance coverage in retirement, while all other city employees are given a much more modest $300 to $350 monthly retiree health care allowance.

So when the time came to press city firefighters to pay their full pension contribution, Shirey cut a deal with them that gave them offsetting salary hikes and also allowed new firefighters to continue to receive health care coverage in retirement.

But a deal with the SPOA proved elusive. Traditionally, the city has had an easier time coming to terms with city police than, say, with city firefighters. In 2009, when the Great Recession was slamming the city budget and the city was pressing unions to agree to salary concessions in the middle of multiyear labor contracts (a tough sell), the SPOA agreed to defer scheduled salary hikes in order to avoid police layoffs. That deal set the tone of labor negotiations with other city unions that year. All city unions agreed that year to open up their contracts and accept salary concessions with the exception of Local 39, the city's largest union, which elected to take layoffs of its members instead (which is why we lost so many park workers during the recession).

When the city's tax revenues failed to turn around and, instead, continued to fall, the city went back to the SPOA and asked for a further deferral of salary hikes and other concessions to avoid police layoffs. But the SPOA refused to accept further concessions and accepted, instead, major police layoffs from which the city is only now starting to recover.

Then, in 2012, Gov. Brown decided to dip his toe into pension reform and signed into law the Public Employees Pension Reform Act, which gives local governments the power to require current employees to start coughing up one-half of the "normal" costs of their pensions starting in Jan. 1, 2018. Based on actuarial numbers, the present annual normal cost of a Sacramento police pension comes in at 24.5 percent of police salaries. So the police have had something of a legal gun to their heads: Whether they agree to it or not, beginning in 2018, the city can invoke PEPRA to compel SPOA members to contribute 12 percent of their salaries to their pensions.

The SPOA has seen the handwriting on the wall for some time. SPOA president Dustin Smith reports that all the informal and formal contract offers the union has made to the city over the past three years have included offers to pay between 9 percent and 12 percent of police salaries to their pensions. The stumbling block has been SPOA's insistence that the city give its members salary hikes to wholly or substantially offset their big new pension contributions. The arbitrator settled that issue for the parties last month.

What's the fallout from the new SPOA contract? The contract gives the city some fiscal breathing room, particularly as it faces a serious "fiscal cliff" in 2018 when the Measure U one-half-cent sales tax expires, the city's contributions to CalPERS continue to ramp up and the full (and uncertain) effect of the new arena bonds kicks in.

The city will also face an uncertain echo effect from the 9.3 percent aggregate salary hike that it will be paying to city police under the new contract. The salary hikes will increase the "pensionable pay" of each police officer, which in turn will increase the annual pension payout that each retired police officer will receive. (An officer's payout is typically based on the average pensionable pay in the last three years of employment.) So if the average pay of a senior police officer in his last three years as a cop increases from $120,000 to $131,160 due to the 9.3 percent pay raises, and assuming he retires after 30 years of service at 52 with a standard police pension equal to 90 percent of his pensionable pay, his annual pension payout will increase from $108,000 to 118,044 for life. That $10,000 hike in annual pension payouts he will receive for, say, 35 years would add up to $350,000 in additional pension payouts. Based on a discount rate of 5 percent, that would add $163,742 to the city's current pension liabilities.

The normal annual pension cost attributable to an $11,160 increase in salary, at 24 percent, would amount to $2,678 per year, half of which, under the new contract and PEPRA, will likely be borne by the police officer and the other half borne by the city.

Smith believes that the echo effect of the new SPOA contract on the city's pension liabilities will be modest. It is unfortunate that the city has not publicly released its internal calculation of the anticipated increase in its pension liabilities and normal cost as a result of the 9.3 percent salary hike. I have asked pension specialist Marcia Fritz to calculate the likely hike in the city's pension liabilities from the new contract and will report on her findings in a future column.

The first I heard of the arbitrator's decision was from an Eye on Sacramento board member who had spoken with a neighbor who happened to be an SPOA member. The officer was in shock over the looming 12 percent reduction in her take-home pay and worried about its effect on her family. Smith said the impact will be particularly hard on single-parent households.

He's also worried about the impact of the new contract on police recruiting. "Sacramento has some of the highest hiring standards in the state, some of the highest education standards and the most stringent background standards. Well over 90 percent of applicants are rejected. It will be increasingly difficult for us to hire recruits who will continue to meet our high standards when we'll be offering net pay that is the lowest of all police forces in our region except one," Smith said.

When I asked him about the impact of the contract on morale within the police department, Smith said, "Many are feeling underappreciated by city government, but they know that the community still appreciates us." He added, "Morale will remain strong because police officers are not motivated by money but by a desire to serve the community."

Strong-Mayor Initiative

After six years of false starts, the strong-mayor measure will be decided by city voters this November. Unlike earlier iterations (this is Version 4.0), the latest version has not yet received the degree of media attention that prior versions received. In an effort to rectify the situation, Eye on Sacramento will prepare and publish a study of the measure. Look for a recap of the EOS study in these pages in October or sign up for updates at eyeonsacramento.org

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