



PROFESSIONAL & TECHNICAL ENGINEERS, LOCAL 21, AFL-CIO  
*An Organization of Professional, Technical, and Administrative Employees*

Date: January 27, 2014  
To: Libby Schaaf, Chair, Finance Committee and all members  
From: Rachel Richman, Policy and Political Director, Local 21

**Re: Finance and Management Committee meeting 1/28: Item 5, 'Unfunded liabilities': on fixing problems that are being addressed, mixing apples and oranges, throwing in the kitchen sink while omitting bonds and other debt, and distorting the real numbers**

We read the report on long-term financial needs of the city with great concern. While claiming to be a report on unfunded liabilities, the report is actually a mish-mash of short-term budget issues, long-term capital investment needs, retirement obligations, and miscellaneous items all called 'unfunded liabilities'. Used in this sense, "unfunded liabilities" is a pejorative term we believe is designed to create a panic about city finances. It is completely unwarranted and may have the unintended effect of discouraging economic development if businesses think the city is in dire straits. Moreover, the report is highly selective about which obligations to focus on – many of the costs identified in the report are associated with employee compensation and benefits, yet obligations to bond holders and other City creditors are conspicuously absent from consideration.

True unfunded liabilities are contractual obligations for future (often long-term) payments for which there are currently insufficient funds to pay. For example, someone buying a house for \$500,000 with 20% down doesn't have an 'unfunded liability' of \$400,000. They have an income and plan to pay the long term cost over 30 years in monthly installments.

Of note, there is no mention of the City's total bonded indebtedness or other loans that have to be repaid. Those are liabilities too, and they are as much unfunded as post-employment benefits - there's no pot of money set aside to pay them, just a pledge of future revenue. *Why do obligations to banks and investors (including \$11.5 million per year for the Raiders/Coliseum deal) get overlooked while obligations to employees are scapegoated?*

We are not completely surprised by the tone of this report as the Administrator has consistently taken a 'San Jose approach' which we find is inappropriate for Oakland. Please keep in mind that this same approach and attitude in San Jose has led to an exodus of hundreds of police officers and skilled city staff, discouraged business development and created a hiring problem so grave that the city has resorted to paying bonuses to the remaining city employees for recruiting new workers.

*We caution you that City librarians, business recruiters, recreation center program leaders and senior services staff should not bear the brunt for decisions made by elected City leaders and we will vigorously oppose efforts to use them as political scapegoats in an election year.*

Let's break the report into its parts:

#### Operations

This section is a mish-mash of operational costs like shortfalls in Head Start and OPD overtime – which should be dealt with as part of the mid-year budget. They are budget decisions like any other, not 'unfunded liabilities'. This section also includes \$9-12 million for fleet replacement and new police radios which are actually capital projects and should be listed and financed as such. It is unclear why the cost of police attrition is included in the report as this is first and foremost a personnel and policy issue that the Council should be addressing to retain officers. And

the presumption that Measure Y will not be renewed is speculative and premature. We believe the city should plan in case the measure isn't renewed but should also not sit passively by as the renewal date approaches.

**Capital needs** \$2.3M in Capital expenses, \$222.3M in Deferred Capital Expenses

The city estimates that funding is needed over the next five years for capital improvement, some of which are mistakenly listed as operating costs (i.e.: fleet upgrades, radios).

Most large cities have Capital Plans and propose bond measures at regular intervals to make those upgrades. For example, San Francisco has a 10 year plan and will put forward a June 2014 bond measure to upgrade public safety emergency needs and the crime lab and a November 2014 bond for street, pedestrian and transit upgrades.

We have previously suggested that Oakland develop a long term Capital Plan including a bond program to address capital needs as most big cities do. Using bonds for capital improvements is analogous to refinancing one's house to put on a new roof or add a bedroom.

**Long term costs for which the city has a plan in place or has proposed one**

**Negative fund balances \$105.7M**

The City has had a plan in place for many years to begin to pay this down. These are essentially internal debts – certain funds have expended more than they had, requiring borrowing from the City's General Fund. We support the City's plan, recognizing that in the same way it took many years to reach the negative fund balances, it will take many years to complete paying them down. As the report itself notes, the City has made substantial progress paying these obligations down, even during the recession.

**CalPERS** \$424M CalPERS civilians over the next 30 years, \$317M sworn employees over the next 30 years  
CalPERS is currently funded at just less than 80%, well above the 70% level Fitch considers to be adequate. The retirement system has recovered all of its losses from the recession and posted a 16.9% gain in earnings in 2013. It is important to note that CalPERS' "unfunded liability" is just a snapshot in time, and fluctuates depending on investment returns and other factors. In the early 1980's, CalPERS funding ratio was only 55%, yet by 2000 it was over-funded at 130 percent (<http://www.letstalkpensions.com/newsroom/memos/182-public-pension-unfunded-liability-fact-versus-fiction>).

Pension funding gaps do not need to be paid off all at once since they represent long term obligations. Instead, they are amortized over a long period of time through employer contributions. In fact, during the recession, when the funding gap opened up due to the market crash, the cost to the City of Oakland remained flat because employees agreed to increase their contributions by 5% of salary, offsetting the increases in employer rates. The actual dollar cost was also reduced as the City shed nearly 1,000 positions. Future costs for amortizing the funding gap will also be offset to some degree by reduced retirement benefits for new employees that will reduce the City's contribution rate.

We note that increases in the employer's costs have been shared equally with employees, who increased their contribution. The employee contribution was made during a recession in the midst of additional salary cuts from furloughs. During the recession, nearly 90% of the cost increases were picked up by employees (temporarily reducing the City's cost since employees started paying extra before the rates went up), and it's only now, in a situation of improving revenues, that the City has been bearing a fair share of those cost increases.

**OMERS \$0** This is a small, overfunded retirement fund for civilians hired before Oakland joined CalPERS.

**Other Post-Employment Benefits (OPEB)** \$512 Million over 30 years

This represents the cost of health insurance for sworn retirees and a small, flat-rate (\$425/month) reimbursable stipend given to offset health insurance for civilian retirees. The civilian reimbursement rate has not increased in 13 years and we do not anticipate it will go up anytime soon. Civilians originally negotiated a benefit equal to the cost of Kaiser for two people in 1999. Since there hasn't been an increase in the dollar amount since 2001, the value to the employee has fallen to 60% of the cost of 1 person. That's a 70% reduction in the real value of this benefit, with all of the increases borne by employees and none by the employer.

Like most cities, the cost of OPEB, about \$18M a year is budgeted on a pay-as-you go basis. That said, the City is proposing setting aside \$10M a year starting in 2015 to create a trust fund that will begin to stabilize costs to the city. This is a long-term issue that should be addressed over time. It's not a liability that has to be funded 100% in the immediate future – the “unfunded liability” is the future cost of benefits earned by current employees who will not actually qualify for these benefits for many years. We agree that the City should begin setting aside money in the next budget.

### Avoidable long term costs

#### General liability - Pending lawsuits

Much of this liability is due to police misconduct lawsuits and the violation of the City Charter with regard to labor law at the Oakland Museum. While we understand that every city experiences a certain amount of litigation due to accidents, police issues and slip and falls, Oakland's numbers continue to far outstrip other cities. In the last 12 years, Oakland has paid out about \$50 million in police misconduct settlements, more than what SF and San Jose paid out combined. For several years we have recommended that the City reduce its risk of these lawsuits through stronger training at OPD and accountability for the command staff. Now that OPD is in de facto receivership, we hope this cost will come under control. The \$10 million proposed for the 2015-16 and 16-17 budgets is more in line with what a city of Oakland's size should have. As for the liability associated with the privatization of the Oakland Museum, this cost was entirely avoidable had the City Council heeded the warnings of the unions and others who pointed out that this action was in violation of the City Charter, as has now been confirmed by two separate arbitration decisions.

### Long term costs that should have a plan

#### Accumulated leave

The "liability" is the amount it would cost to cash out everyone's leave right away. *However City policies and contract provisions limit the ability of this to happen - there are restrictions on sell-back of leave and the City isn't about to let everyone take all of their leave at once.* The City already took substantial steps a decade ago to reduce this liability by negotiating limits on the amount of vacation that could be accrued, which led to an orderly reduction in leave balances.

The City should clarify how it's calculating the liability for accrued sick leave because it's cashed out at a 1:3 ratio when people separate from the City - and only if they have 10 years' service – *employees who have less time with the City don't get any cash out.* If the City is valuing the accrued sick leave at 100%, it's inflating what it will really cost.

This amount of money is expected to drop significantly as employees who are back to work full time are able to afford to take vacations. The Legislative Analyst found that accumulated leave increased significantly during the recession as many employees took unpaid leave (partly because they were taking unpaid time off, and partly because the reduction in income and the increase in workloads made extended vacations more difficult to take). These balances will be worked down over time now that furloughs have ended.

#### Police and Fire Retirement System – PFRS \$203.7M

The City financing of this debt ends in 2017 and the City may have to pay \$21-24M annually to cover costs not paid by a special override tax approved many years ago. This is a closed end retirement fund that actuaries estimate will have obligations for 12 more years.

We suggest two steps to address this:

- Recalculate actual costs due to a favorable court decision on retiree benefits that will lower costs. Review the actuarial assumptions underlying all of the projections. The actuarial report assumes a lifespan for these retirees that is far in excess of what is realistic.
- Approach the legislature for legislation to re-open the 'window' that will allow the City to adjust the tax to cover the actual cost. The City sponsored, along with about a dozen other cities similarly affected, legislation to do this in the 90's and 00's and it bears revisiting.

## Debt to Banks and Investors

Conspicuously absent from this report is any mention of the City's other liabilities – debt obligations to bond holders and investors, loan guarantees, etc. Since no pot of money exists currently to pay off these debts, they are also unfunded liabilities. Yet somehow obligations to banks and wealthy investors are ignored while obligations to employees are scapegoated as an imminent fiscal catastrophe. Debt obligations are being paid off over time – it would be useful to see when different debt obligations expire, freeing up millions of dollars that could then be used for other long-term obligations. Similarly, as the obligations of the former Redevelopment Agency are paid off, a portion of those funds will be returned to the City.

## Conclusion

It is a distortion of facts to say the City has \$1.6 Billion in 'unfunded liabilities'. In fact, the City has put in place fiscally sound plans or has proposed such plans to pay most of these long term costs through orderly long-term payment plans. As a matter of long-term financial planning, the City needs to look at unfunded liabilities and long-term spending/ investment needs, but they are two different issues and lumping them together in one big number is pandering to fear and inciting the public against public employees and against local government in general.

The report needs to better distinguish between long term costs that ARE being paid down over time - retirement, negative fund balances - from those that still need a plan. And it needs to distinguish between actual contractual liabilities versus things that it needs/wants to do but isn't actually required to do by law or contract.

Finally, the City's ability to pay down its long-term obligations is tied to growth in City revenues. The City needs to look seriously at a real economic development strategy – one that focuses not on chasing big box retail with low paying jobs, but on creating good paying jobs with the goal of reducing unemployment and raising incomes in the City, which in turn will bring greater City revenues.

In closing, we urge the City Administrator and elected officials to refrain from using dishonest numbers, fabricating a crisis and using hard working City workers - disaster preparedness staff, 911 dispatchers and crime prevention specialists for political fodder and to promote a political agenda during an election year.

Cc: Council President Kernighan  
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