

STATE OF CALIFORNIA
PUBLIC EMPLOYEE
POST-EMPLOYMENT BENEFITS COMMISSION



PUBLIC MEETING



Tuesday, November 13, 2007
10:00 a.m.

CalPERS Headquarters
Lincoln Plaza West, Community Room 1600
400 Q Street
Sacramento, California



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A P P E A R A N C E S

PUBLIC EMPLOYEE POST-EMPLOYMENT BENEFITS COMMISSION

Commissioners Present

GERRY PARSKY, Commission Chair
Aurora Capital Group

MATTHEW BARGER
Hellman & Friedman LLC

PAUL CAPPITELLI
San Bernardino County Sheriff's Department

TERESA GHILARDUCCI, Ph.D.
Trustee
General Motors Retiree Health Pensions

JIM HARD
President
Service Employees International Union Local 1000

LEONARD LEE LIPPS
California Teachers' Association

CURT PRINGLE
Mayor, City of Anaheim

ROBERT WALTON
Retired (CalPERS)

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A P P E A R A N C E S

PUBLIC EMPLOYEE POST-RETIREMENT BENEFITS COMMISSION

PEBC Staff Present

ANNE SHEEHAN
Executive Director

JAN BOEL
Staff Director

TOM BRANAN
Policy Director

STEPHANIE DOUGHERTY
Research Director

MARGIE RAMIREZ WALKER
Office Manager

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Public Testimony

(No public testimony was offered.)

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Subject Matter Experts

JOHN BARTEL
Actuary

TOM DITHRIDGE
Department of Finance

BOB PALMER

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1 BE IT REMEMBERED that on Tuesday, November 13,
2 2007, commencing at the hour of 10:13 a.m., at CalPERS
3 Headquarters, 400 Q Street, Community Room 1600,
4 Sacramento, California, before me, DANIEL P. FELDHAUS,
5 CSR 6949, RDR, CRR, in the state of California, the
6 following proceedings were held:

7 --oOo--

8 *(The following proceedings commenced with*
9 *Mr. Pringle absent from the hearing room.)*

10 CHAIR PARKSY: Ladies and gentlemen, if we
11 could just have everyone's attention.

12 I apologize for being a little bit delayed, but
13 I want to welcome everyone to the tenth commission
14 meeting.

15 We've embarked on a process of trying to
16 conduct our hearings throughout the state.

17 I want to thank CalPERS for making this
18 facility available to us this morning.

19 And I think the agenda for today's meeting is
20 available to everyone, at the back of the room.

21 And as I think everyone that has followed us
22 knows, we're in the phase of our commission hearings that
23 is oriented around trying to develop our recommendations
24 that we will be providing in January to the Governor and
25 the legislative leadership. And so this is a

1 continuation of that. We'll be discussing a specific set
2 of recommendations which have been posted. They're in
3 draft form as developed by the staff.

4 I just want to make sure that everyone
5 understands that -- I say this at every hearing -- that
6 on the establishment of the Commission, the terms of
7 reference established by the Governor and the legislative
8 leadership made it clear that from the policymakers'
9 standpoint, promises that have been made to public
10 employees with respect to pensions and health care were
11 promises that were to be met.

12 The purpose of this Commission is not to
13 challenge those promises in any way, but to first
14 identify with some specificity the magnitude of these
15 obligations that exist today and that will accrue; to
16 evaluate various approaches that have been taken, to try
17 to make sure that these promises will be met; and then to
18 come forward with a plan that would address what I think
19 the public is now beginning to become aware of, which is
20 the mounting level of the obligations, especially in the
21 health-care area, that would be characterized as
22 "unfunded obligations"; and what approach this Commission
23 can recommend to the policymakers to try to ensure, in a
24 fiscally responsible way, that these promises will be
25 met. And so that's what we have embarked on.

1 And we broke down the areas of recommendations
2 into three categories, and in Fresno and Oakland and here
3 we're discussing each of those three categories with
4 recommendations. And so it's meant to be an interchange
5 between the Commission members and the staff.

6 We have preserved time for public comment at
7 every hearing.

8 From what the staff tells me, we don't have
9 anyone that has signed up for public comment this
10 morning. If anyone changes their mind, please sign up.
11 But with that being the case, unless any of the
12 Commission members have anything else they'd like to say
13 or -- Anne?

14 MS. SHEEHAN: No, I don't.

15 CHAIR PARKSY: We can move right ahead into our
16 discussion of the various recommendations.

17 So Tom and Stephanie, our two leading staff
18 members. They have been guiding this Commission through
19 the thicket of various subjects. And we'll see how they
20 handle it today. We'll reserve our grade until the end
21 of the day.

22 Tom, why don't you start us off?

23 And I think we've distributed, and the public
24 should have a copy of the draft of these.

25 And, once again, the general concept, I think,

1 is up on the screen. I'd just remind everyone, the
2 general concept under which these recommendations will be
3 made is defined up there.

4 And so, Tom, why don't you start with that, and
5 then kind of go into each of the categories? We'll try
6 to get through, according to the agenda, before lunch
7 what's on the list.

8 MR. BRANAN: Thank you, Mr. Chair.

9 Is this on?

10 CHAIR PARKSY: Yes, you're on.

11 MR. BRANAN: Mr. Chairman, Commissioners.

12 Actually, if you knew my sense of direction, you probably
13 wouldn't want me leading you through this thicket or any
14 other; but we're into it now.

15 CHAIR PARKSY: Well, that's why Stephanie is
16 here.

17 MR. BRANAN: Actually, there's more truth to
18 that than you know.

19 We have started this first page with the third
20 principle that you've seen. And we've done something
21 different this time which we hope will simplify things,
22 and that is to group the topics that we're going to be
23 hearing under parts of the overall third principle that
24 you see there.

25 So it says, "In order to build awareness,"

1 you'll see two things under "Awareness." There's one,
2 "Creating an Open and Defensible Process for Adoption and
3 Payment of Benefits," and then "Building Taxpayer Support
4 and Trust." All of those come from the lead principle at
5 the top of the page.

6 So we'll turn to those.

7 The first is: "Timeliness of Reporting Data"
8 and the background information.

9 "For pensions, all public retirement systems
10 are required to annually report their financial actuarial
11 and benefit status to the State Controller's Office or be
12 fined \$5,000."

13 The second point: "Government Code section
14 7504(d) requires the State Controller to publish an
15 annual report on the financial condition of all public
16 retirement systems."

17 The third point: "The State Controller's
18 Office has often delayed the publication of this
19 information."

20 And I should point out, this is in no way
21 singling out the current occupant of that office. This
22 has been an ongoing, years-long problem for people
23 working in the retirement arena.

24 Under "OPEB": "There is no standardized
25 process for collecting and making public OPEB information

1 from public agencies."

2 Now, this time, we've added some additional
3 information before each of the recommendations to see if
4 we can make them more clear.

5 In this case, "It is in the public's interest
6 for public retirement systems and employers providing
7 OPEB to report on the status and adequacy of funding for
8 these benefits. Current reporting mechanisms do not
9 provide for the timely and accurate disclosure of pension
10 and OPEB liabilities."

11 The first recommendation growing from that is:
12 "Legislation should be introduced directing the State
13 Controller's Office to develop a simple and inexpensive
14 procedure to regularly collect and report OPEB data from
15 California public agencies. The State Controller's
16 Office should publish the report of OPEB data at least
17 once every two years, within nine months of the close of
18 the fiscal year."

19 Now, just as additional information, there is a
20 group that addressed you at Fresno, and it's a coalition
21 of local agencies. They've been helping us a great deal
22 gain access to public agencies, both with our survey and
23 our case studies. That group has signed off on this
24 concept. They want there to be a central location where
25 they can submit their OPEB data. And so that includes

1 the League of Cities, the CSAC with the counties, a
2 collection of school representatives, and also the
3 independent special districts.

4 And the reason we said "every two years" is due
5 to the GASB requirement that smaller agencies report this
6 data every three years, and larger ones every two years.
7 So it really doesn't make sense to have an annual report.

8 CHAIR PARKSY: Okay, why don't we take them one
9 recommendation at a time, or you can make comments on
10 both? Why don't we kind of go through the list?

11 Lee, do you want to start us off here?

12 MR. LIPPS: First of all -- is this on?

13 CHAIR PARKSY: Yes.

14 MR. LIPPS: First of all, Tom, that's not the
15 way that I read at least the preamble to these
16 recommendations.

17 I see that the recommendation would have the
18 Controller publish it every two years; but for the
19 Controller's office to collect this information
20 regularly, which theoretically could be more than once
21 every two years, particularly if it's simple and
22 inexpensive, why wouldn't we want to do it yearly, if we
23 wanted to have a reporting requirement, is part of the
24 question.

25 And the other part of the question is, at what

1 point would doing this extra work as required result in a
2 mandated cost to the State?

3 MR. BRANAN: Well, the first point, in terms of
4 why not annual, they can collect it -- certainly this
5 recommendation would not prevent them from collecting
6 anything that was available on an annual basis. We're
7 talking about publishing the data every two years. And
8 the reason, again, is, there's no GASB requirement that
9 they report annually. There is a requirement that they
10 report two years or three years, depending on their size.

11 CHAIR PARKSY: Your recommendation then really
12 relates to the accessibility of the data?

13 MR. BRANAN: Well, right now, for OPEB data,
14 there is no source. This Commission, in its survey, is
15 the first group that has gathered such information. And
16 it was difficult to get it.

17 For one thing, people didn't even really
18 understand what we were asking for. I think local
19 agencies, as well as staff, have learned a lot from
20 figuring out what needed to be reported, how to ask for
21 it. And the feeling among those groups is, let's keep
22 doing that now that it's set up.

23 CHAIR PARKSY: Well, I think there were two
24 parts to Lee's question, though.

25 One had to do with, it would suggest that they

1 were going to collect data; and maybe inherent in that --
2 they were going to collect data more frequently than the
3 two-year publication requirement. The first sentence, I
4 think, might suggest that.

5 And I think your response was that the data
6 might not be required to be available except on a
7 two-year basis?

8 MR. BRANAN: This is on Recommendation 1?

9 CHAIR PARKSY: Yes.

10 MR. BRANAN: Yes, all we said was that they
11 regularly collect it, and it's up to them to decide how
12 to do that.

13 CHAIR PARKSY: I see.

14 MR. BRANAN: So it isn't available -- new data
15 is not available annually for an agency that is reporting
16 based on its GASB requirements.

17 Now, some of them might have it annually, but
18 we thought it would just be wasted effort to tell the
19 Controller that you have to publish this annually, when
20 there may well not be new data.

21 CHAIR PARKSY: Maybe you want to reverse the
22 sentences, and the legislation should require a report
23 every two years, and then they can collect the data as
24 they deem fit in order to prepare such a report.

25 MR. BRANAN: We can certainly do that.

1 The reason that it's written as it is was from
2 the request of CSAC and the League. They think that by
3 requiring the Controller to come up with a simple,
4 inexpensive procedure, that that is a way that we can
5 address mandated costs.

6 CHAIR PARKSY: I see.

7 MR. BRANAN: So that's why we put that first.

8 MR. LIPPS: But it would still be a mandated
9 cost, regardless of how inexpensive?

10 MR. BRANAN: I really don't know.

11 I think we certainly can assume that it would
12 be. But it's something -- it's data that they have to
13 collect, anyway. This would simply be -- the way they do
14 now with the Controller's pension report is, the
15 Controller's staff have developed an electronic form that
16 retirement systems fill out. I would imagine that
17 something like that could be done for OPEB at relatively
18 low cost.

19 MR. LIPPS: And, really, that was going to be
20 sort of the next part of my question. It seems we
21 already have a similar provision to this on the pension
22 side. This would just apply it to the OPEB side.

23 The problem hasn't been with collecting the
24 data regardless of the frequency, in terms of pensions.
25 Apparently the problem has been with the Controller

1 publishing it in a timely fashion.

2 MR. BRANAN: That's absolutely right.

3 MR. LIPPS: Regardless of how simplified
4 they've made it in terms of the Web site.

5 Is there any chance of fining the controller
6 \$5,000?

7 MR. BRANAN: I didn't hear that.

8 MR. LIPPS: Is there any chance of fining the
9 Controller \$5,000?

10 MR. BRANAN: Well, we actually --

11 MR. LIPPS: I know we'd be fining ourselves. I
12 understand how that works.

13 MR. BRANAN: We have spoken to some people from
14 local retirement systems who have had to pay the \$5,000
15 for not reporting on a timely basis, and then see a year
16 or two go by before it's published. I think they might
17 support your idea.

18 CHAIR PARKSY: I think the only thing the
19 Commission ought to, I think, step back and understand is
20 that one of the terms of reference for the Commission was
21 to identify the magnitude of these obligations.

22 So coming out of the Commission, a set of
23 recommendations relating to this being done on an annual
24 basis is very much part of what our charge was, it seems
25 to me. How we word it is clearly open.

1 Matt, any thoughts on this subject?

2 MR. BARGER: I guess I have two.

3 The first one would be, I'm unclear, you really
4 didn't go into any detail why it's late. Is there
5 something cumbersome about the process or is the data
6 inconsistent? Or what was the issue with the existing
7 system?

8 MR. BRANAN: I don't know currently.

9 Years ago, when I worked for the Legislature,
10 I dealt with -- there were two people in the Controller's
11 office that were responsible for this report. Their
12 complaint at the time was, they just -- they were very
13 low priority within the internal hierarchy, as far as
14 staff and computer time. That's been 20 years ago. I
15 don't know what the cause is but the problem is still
16 there.

17 MR. BARGER: It just seems like it's one of
18 those classic things somebody can put it into a computer
19 on one end and then just go onto a spreadsheet and
20 "boom."

21 MR. BRANAN: I think that's probably true.

22 When I was concerned with it, it was all manual
23 input from paper submissions by the retirement systems.
24 So it would seem that it would be simplified now.

25 MR. BARGER: Right. I mean it's one thing for

1 us to sort of dictate that it should be timely if there's
2 some underlying cause that's the problem.

3 MR. BRANAN: I've never heard an explanation
4 from the Controller's office.

5 MR. BRANAN: A priority?

6 CHAIR PARKSY: Well, just to follow. And there
7 may be something that could be included in the
8 legislation -- I don't know whether it's cost or whether
9 it's time or whatever it is, but I think it's a valid
10 point. If there's something that's needed from the
11 Controller's office in order to make sure that this could
12 be honored, we ought to find out about that before the
13 final recommendations are put forward.

14 MR. BRANAN: That's true.

15 What we had in mind was, since this is going to
16 be put through the Legislature, that as part of
17 publishing what the legislation would look like, those
18 items would be discussed.

19 MR. BARGER: They'd be discussed?

20 The other point I would have is just a
21 consistency point. In other words, how do you address
22 sort of the garbage-in, garbage-out, if people have
23 different standards about what, say, health-care
24 inflation is or mortality assumptions? How do you
25 actually get this information to be consistent and useful

1 with this recommendation?

2 MR. BRANAN: For which reporting requirement?

3 MR. BARGER: The OPEB liability.

4 MR. BRANAN: That's a good point.

5 And as I said, right now there is very little
6 in the way of those kinds of assurances, but it's never
7 been really reported on a systematic basis before.

8 CSAC took a stab at this a couple years ago,
9 the League of Cities did. But I think the work of this
10 Commission has been much more far-flung and systematic.

11 I could only suggest that people would build
12 off of what Commission staff has done, and to come up
13 with something that would be satisfactory in those terms.

14 MR. BARGER: I mean, it strikes me when one of
15 the things we're supposed to do is come up with a
16 magnitude and have a transparent process, et cetera. All
17 you do is have 50 different assumptions. It's sort of a
18 hodgepodge of stuff.

19 MR. BRANAN: Well, what we've collected is
20 really not assumption-driven but hard data in terms of
21 how many people they have, what benefits have they
22 promised, are they prefunding, those kinds of things.

23 MR. BARGER: Yes. But aren't you actually
24 trying to take all that and come up with a number?

25 MR. BRANAN: Yes.

1 MR. BARGER: And that is dependent on mortality
2 assumptions, health-care inflation?

3 MR. BRANAN: That is, yes.

4 MR. BARGER: To a big extent; right?

5 MR. BRANAN: Yes.

6 CHAIR PARKSY: Well, is your point, though,
7 Matt, that there ought to be some --

8 MR. BARGER: Without a consistency standard
9 about the consistency of, you know, what the inputs
10 are -- you know, you're just at risk to me, anyway, of
11 ending up with a bunch of stuff that's not really
12 comparable.

13 MR. BRANAN: The collection of data, that's
14 hard data, that's what we've gotten.

15 The Controller certainly has an accomplished
16 actuarial staff. They could work on that, and the
17 legislation could also set out some guidelines.

18 MR. BARGER: Well, to me, that seems like an
19 important thing to do. There ought to be guidelines to
20 provide the consistency of input or, you know, something
21 along those lines.

22 MR. BRANAN: Well, there is something of a
23 model there with the legislation that required annual
24 pension-system reporting. There is a checklist there of
25 things that, at a minimum, should be included. And some

1 of those are actuarial assumptions.

2 MR. BARGER: So the equivalent would be, you
3 know, what are your health-care assumptions, what are
4 your health-care inflation assumptions, what are your
5 mortality assumptions -- you know, what are the drivers
6 in terms of your assumptions. So even if you didn't
7 happen to use the same ones, at least you would have
8 information on what people are using?

9 MR. BRANAN: Yes. And that was done with the
10 pension legislation some years ago.

11 MR. BARGER: To me, that's something that would
12 be important for us to suggest that they have in this.

13 CHAIR PARKSY: Yes, I think at the heart of
14 these recommendations was the issue of data and
15 timeliness. But I think Matt's point is that, well, the
16 collection of the data needs to then include a
17 methodology that is consistent across the board so that
18 the end result will be utilizing the same methodology so
19 if you annually publish something, it would be
20 consistent.

21 So I think maybe we ought to add -- maybe it's
22 a section that deals with methodology as opposed to just
23 the timeliness of it, what the report should be based on
24 or what input should there be.

25 MR. BRANAN: If you have your background

1 document, that's the bottom one. On page 3, you'll see
2 reference, and under that code section 7502. And there
3 is a set of considerations and assumptions that should be
4 considered. So we certainly could include similar
5 language.

6 MR. BARGER: Yes.

7 CHAIR PARKSY: Yes, that would be very good.
8 Okay, yes? Let's continue.

9 MR. CAPPITELLI: Yes. Overall, I support this
10 concept. I think this is good.

11 My only question is, in reading through this
12 here, 7504 requires that -- it only requires that the
13 Controller compile and publish this report on an annual
14 basis.

15 And if we're suggesting that there is other
16 data that comes out every two years, I wonder why we
17 couldn't just say, in the annual report include the data
18 that includes the OPEB liability. I mean, that's easier
19 said than done. But it seems to me if you have an annual
20 report and you're going to the agencies to get them to
21 submit the information for the report, to me, it would be
22 just as easy to include that report on an annual basis
23 rather than every two years.

24 MR. BRANAN: Well, Commissioner, we could do
25 that. And the reason we didn't in this case was, we

1 wanted to clearly set out the fact that we wanted to
2 create a new report for OPEB, and we wanted to improve
3 the timeliness for an existing report.

4 So they certainly could be combined somewhere
5 down the line, but we thought it would be clearer when we
6 were discussing them to have a recommendation based on a
7 needed report and one based on an existing report that
8 just has a particular problem.

9 MR. CAPPITELLI: And in the end, I think either
10 will work.

11 My only -- my main reason for bringing this
12 up is if this is something -- if our goal here is to
13 try to make this more transparent, from the public's
14 perspective, I would rather it be one-stop shopping. I
15 would rather be able to go to a particular place to get
16 a report and be able to see at a glance everything that
17 was happening in OPEB and also in pensions. But, you
18 know, however it's presented I guess would be something
19 that could be vetted out through the process; but that
20 was the only suggestion.

21 MR. BRANAN: That would certainly make sense.
22 And since the existing report is to be produced annually,
23 anyway, the OPEB could be included as a chapter.

24 MR. CAPPITELLI: Okay.

25 CHAIR PARKSY: Bob?

1 MR. WALTON: Thank you.

2 Yes, I certainly support the concept of what
3 staff has recommended. I would kind of follow what Paul
4 has indicated, that one report would be better.

5 The difficulty, in my experience, with the
6 current report on pensions, is that it is not very
7 timely. And it's a matter of priority and staffing at
8 the State Controller.

9 And this is not in any way to discredit them;
10 they're reacting to it for the need for the demand of
11 this report, which is little, if any, in the current
12 situation. I think what this Commission has an
13 opportunity to do is emphasize how important this
14 information is.

15 As I recall that report, to address some of
16 Matt's concerns, is there's tables that indicate for
17 pensions what methodology did you use: Entry-age normal,
18 unit credit. What assumptions do you use as far as
19 interest return, that sort of thing, amortization of
20 unfunded liability, so all that information is there. It
21 can be different, but there's a source to tell you what
22 the ultimate liability is based on.

23 And you could do the same thing for OPEB. It
24 certainly probably will be different than pension for a
25 number of reasons, but there is no reason why they

1 couldn't be combined if it's operationally possible.

2 I think the context of what staff is
3 recommending is, currently there is a central repository
4 of information for pensions. That is not timely, but
5 it's there. And we want something similar for OPEB. And
6 then to put more emphasis on getting this information out
7 there.

8 I would suggest that instead of this Commission
9 trying to design what the parameters ought to be, that
10 like there was established under the pension legislation,
11 that we recommend an advisory committee be established
12 that includes actuaries, people that are expert on the
13 health side of the aisle, to set those parameters for the
14 Controller to make this reporting a part of the normal
15 process.

16 Also, I think part of the problem the
17 Controller faces now is it's been a paper product. It's
18 not an online document, as far as I know. It never has
19 been. And they're only as timely as their latest report.
20 And if this could be put more -- and updated periodically
21 based on whatever information is available, you wouldn't
22 have to wait for the last person; you could do it on an
23 ongoing basis. As information comes in and it's reviewed
24 and determined to be accurate, it's updated to file. So
25 anybody could access it at any point in time to get the

1 most current information available.

2 CHAIR PARKSY: I think you could add that, Tom,
3 that concept.

4 Jim?

5 MR. HARD: I think you folks have covered
6 everything that I would.

7 Teresa?

8 DR. GHILARDUCCI: Perhaps this language would
9 work. Just right after "within nine months of the close
10 of the fiscal year," so that it is: "The State
11 Controller's Office should publish a report of OPEB data
12 at least once every two years within nine months of the
13 close of the fiscal year following best-practice
14 guidelines issued by the Controller's office."

15 And then the implication would be that the best
16 practices would be reviewed by the actuarial review board
17 that we're going to talk about later.

18 But it makes -- I really like the way this
19 discussion went because one of the charges of this
20 Commission was to bring in pensions and OPEB on sort of
21 the same treatment, the same importance. And so probably
22 when we look at that actuarial review board, that they
23 would also be charged with looking at the OPEB
24 assumptions and review those as well.

25 You probably had that in mind, but I didn't

1 read it when I first saw it.

2 So I guess what we're doing now is -- is this
3 right, that we're saying that we want the Controller's
4 office to issue guidelines to the entities about how to
5 report the data? Is that the issue here?

6 CHAIR PARKSY: Well, collect it -- certainly
7 collect the data; and then through a system that is
8 uniform, convert the data into information that can be
9 made public on the magnitude of the obligations.

10 DR. GHILARDUCCI: Yes, I was being a little
11 more proscriptive. That the Controller's office actually
12 tell the agencies what assumptions to use or random
13 assumptions. So I was actually being a little
14 heavy-handed.

15 MR. HARD: Yes, that I don't think -- I don't
16 know how that would work, you know, to -- I don't think
17 that's actually -- that would definitely require
18 legislative change.

19 DR. GHILARDUCCI: Right. Well, that's what
20 they're doing.

21 MR. HARD: Yeah, but I don't know that that one
22 would fly, for us to tell them how to do their actuarial
23 assumptions, although it might be more uniform. But I
24 would doubt its ability to get passed.

25 MR. BRANAN: I think those details would come

1 out of the collaborative process --

2 DR. GHILARDUCCI: The legislative, yes.

3 MR. BRANAN: -- in the Legislature.

4 Before they would write something like this,
5 they would talk to -- in essence, they would create an
6 ad hoc group, like Bob is talking about.

7 DR. GHILARDUCCI: But we have to decide how
8 proscriptive we'd like to be as a commission.

9 CHAIR PARKSY: That's true.

10 Well, I guess maybe you can use what happened
11 on the pension side as illustrative.

12 DR. GHILARDUCCI: Yes.

13 CHAIR PARKSY: And maybe we'll build into the
14 recommendation that -- the suggestion that there be an
15 advisory group and that the advisory group -- I mean, the
16 process should result in the public having an awareness
17 of the magnitude of these obligations and that the
18 methodology be made clear so that it could be done.

19 So maybe we want to include what the advisory
20 panel would be asked to advise on, along those lines.

21 MR. BRANAN: I think we can build this
22 recommendation based on the comments here, as well as
23 these code sections that establish what is actually a
24 very successful data-gathering process for pensions.

25 CHAIR PARKSY: Exactly. Use that as an

1 example.

2 DR. GHILARDUCCI: Yes.

3 MR. CAPPITELLI: I have one final question on
4 this.

5 CHAIR PARKSY: Sure.

6 MR. CAPPITELLI: This would be compulsory for
7 the Controller's office.

8 Does it automatically imply that it would be
9 compulsory for the agencies or entities to submit the
10 information?

11 MR. BRANAN: I believe it is compulsory for
12 retirement systems; isn't it?

13 DR. GHILARDUCCI: Yes, that's one of the codes
14 you gave us.

15 MR. BRANAN: So I would think that it would be
16 compulsory although this idea came from local agencies.

17 MR. CAPPITELLI: I would only suggest that we
18 just ensure that there is some emphasis placed on that,
19 because I'd hate to see a report that had -- similarly
20 to when you did your surveys, if, you know, you had a
21 100 percent response from everybody all the time. But
22 if it was not compulsory, then it might leave the door
23 open for people to make it a low priority.

24 CHAIR PARKSY: Well, and, again, if you're
25 modeling it after what was adopted on the pension side,

1 and if the legislation put that compulsory aspect in it,
2 there's no reason that it couldn't do it on the OPEB
3 side.

4 MR. BRANAN: That's correct.

5 CHAIR PARKSY: Yes, Lee?

6 MR. LIPPS: In general, I'm very much in favor
7 of combining everything into one report as well, for the
8 same reason that Paul mentioned. One-stop-shopping,
9 particularly if it's simplified and all the rest of that.

10 The problem that I see at the local agency
11 level is that there are a number of local agencies that
12 do not report -- they don't carry their own pensions.
13 Most school districts, for example. What they would
14 have, many of them would have retiree benefits. So that
15 would be a problem that would have to be ironed out.

16 For those that do carry their own pension
17 systems, incorporating the OPEB piece shouldn't be -- I
18 don't see that as a big deal. It's just when they're not
19 normally reporting pension figures, then reporting the
20 OPEB piece.

21 CHAIR PARKSY: Okay, any other comments?

22 You have appropriate guidance there?

23 MR. BRANAN: Yes, sir.

24 The second topic is "Increasing Public
25 Transparency" and the background material.

1 For pensions, "For both state and local
2 agencies, existing law requires that if an agreement
3 provides for an increase in retirement benefits, the cost
4 of the benefit enhancement must be made public at least
5 two weeks prior to the adoption."

6 The next point: "Required cost information
7 must be prepared by an actuary and contain information on
8 the 'future annual cost' of the retirement benefit.
9 There is no requirement for the cost information to be
10 presented in an easy-to-understand format."

11 For OPEB: "No comparable cost-disclosure
12 statute exists."

13 Draft recommendations, "Although existing law
14 requires public disclosure of proposed pension benefit
15 changes prior to adoption, some local agencies place the
16 proposal on the consent calendar where it passes without
17 discussion. Existing 'sunshine' provisions for pensions
18 do not apply to changes in retiree or active health-care
19 benefits."

20 The third recommendation is, "Existing state
21 law, Government Code section 7507 which requires specific
22 public notice concerning the cost of proposed pension
23 benefits, should be amended to also apply to the granting
24 or changing of OPEB benefits. This statutory change
25 would require that the future costs of the proposed OPEB

1 benefit change be determined by an actuary and made
2 public at least two weeks prior to adoption."

3 And would you like me to read the next one as
4 well?

5 CHAIR PARKSY: We'll only stay with this first
6 and then we'll go on.

7 MR. BRANAN: Okay.

8 CHAIR PARKSY: Comments on this recommendation?
9 Lee?

10 We'll start from the right and move to the left
11 for a few, and then we'll move from left to right.

12 MR. LIPPS: Gerry, I've never been on the
13 right.

14 CHAIR PARKSY: Well, you're on my left.

15 MR. BARGER: Far left.

16 MR. LIPPS: And especially the far right.

17 CHAIR PARKSY: At the end of the Commission
18 process, tell me how you feel.

19 MR. LIPPS: From a practical matter, Tom, this
20 completely does not work for a variety of reasons for
21 public education agencies.

22 The first would be the immense cost. If, for
23 example, during the course of local negotiations, and
24 OPEB benefits were all locally negotiated by the seven,
25 nine hundred -- almost a thousand school districts, if

1 you were going to do a benefit increase, and
2 presumably -- I'm just looking at the language again --
3 and even presumably a decrease, because it just refers to
4 a benefits change, if the requirement were to have it be
5 projected out by an actuary, that's a very expensive
6 process, first of all, for a local school district to
7 have to engage in, even though the change might be
8 relatively minor.

9 The second part of that is that then to require
10 it two weeks prior to its adoption by the parties,
11 negotiations just don't work that way. You have
12 negotiations, at some point you have an agreement. The
13 school districts are required to do their own kind of
14 sunshining period under AB 1200, and then the school
15 board adopts and the teachers or the classified
16 association adopts. And how long you would have to wait
17 before an actuary could put together projections, that
18 would be very, very unmanageable.

19 MR. BRANAN: Just on that one point, if I could
20 clarify. That's not talking about -- the adoption
21 referred to there is the adoption by the agency of the
22 new benefit. So the bargaining process is over.

23 MR. LIPPS: But the agency that bargained the
24 benefit, at least in the case of education agencies, are
25 going to be local school districts. And a lot of those

1 benefits go into effect immediately upon adoption, both
2 by the ratification by the school board and by the
3 employee union, whether it's the classified side or the
4 teachers' side. So where that might work, perhaps --
5 when we're talking about an agency like CalPERS and
6 their OPEB benefit structure, it might work at the state
7 level. I don't see it working at the local level, at
8 least for a lot of the very small agencies like school
9 districts and perhaps some of the others.

10 CHAIR PARKSY: And is that because of the time
11 of adoption?

12 MR. LIPPS: Both time and money. You know, the
13 money to actually go out and get an actuarial valuation
14 of the cost of this prospective new benefit, and then you
15 have to put it out there for public comment. It
16 doesn't -- the time period would be almost prohibitive.

17 CHAIR PARKSY: Well, I'm not quite sure public
18 comment is inherent in the recommendations. I think
19 inherent in the recommendation is the desire to make
20 the public aware, in a clear way, of changes on the
21 health-care side comparable to the pension side.

22 And so I guess the first question is, if the
23 actuarial analysis is expensive, what is done as part of
24 the bargaining process to know what the magnitude of what
25 is being adopted?

1 MR. LIPPS: If what is done is under AB 1200,
2 when an agreement is reached that has cost implications,
3 the school district is required to project what it's
4 going to cost it this year and each of the next two
5 years.

6 And as part of that disclosure, they have to
7 project out their budgets for each of the next two years,
8 estimating beginning balance, ending balance, with all of
9 these additional costs projected. But it's a three-year
10 projection; it's not a 30-year projection.

11 CHAIR PARKSY: I see.

12 MR. LIPPS: But if something -- you know how
13 many retirees -- or if it's even not the retirees, if
14 it's just an increase in benefits for active employees,
15 you know how many employees you're going to have. You've
16 got ABA projections, you know how many employees you're
17 going to have, either up or down, and you can project
18 these costs reasonably accurately over the course of
19 three years.

20 MR. BARGER: Do they calculate normal cost or a
21 pay-go cost?

22 DR. GHILARDUCCI: Pay-go.

23 MR. LIPPS: Pay-go. It's a pay-go projection
24 for the current year into the next two.

25 CHAIR PARKSY: Well, I guess. But if we're

1 trying to suggest to local authorities that the magnitude
2 of these obligations need to be identified, and with a
3 methodology that is consistent, let the public know what
4 it is that is being accrued, how do we deal with that in
5 the context of the local educational entities?

6 I mean, what is it that --

7 MR. LIPPS: First of all, I think that you let
8 the public know what is the cost -- which is current
9 now -- what is the cost of increasing this benefit or
10 decreasing this benefit this year, what impact does it
11 have on this year's budget.

12 CHAIR PARSKY: Okay.

13 MR. LIPPS: And also part of the requirement
14 is, what budget adjustments are we going to make this
15 year in order to afford that? That is part of the
16 AB 1200 process.

17 CHAIR PARKSY: Okay.

18 MR. LIPPS: Then the projections for each of
19 the next two years, as Matt pointed out or questioned,
20 are on a pay-go basis. And, again, you have to show that
21 you're going to have reserves and so on.

22 I think you leave it up to the local entity --
23 school business officials, the superintendent,
24 management, teachers' association -- as they project
25 costs out in future years, again, on a pay-go basis, they

1 make budget adjustments as necessary so that they can
2 fund the current year's obligations.

3 And each year, remember, they still have to
4 project another two years out into the future. So they
5 also have to project out what changes are they going to
6 make if the reserves begin dwindling, either drastically,
7 or certainly below the 3 percent, or whatever percent
8 reserve they're required to have, 1, 2, 3, 4, 5 percent.

9 So there is an adjustment mechanism that's put
10 into place every year because you always have to project
11 out an additional two years, but it is done on a pay-go
12 basis.

13 But then also you do let the public know in the
14 first year what the cost of this benefit is for the
15 current year and each of the next two years.

16 CHAIR PARKSY: Well, the data that we are
17 collecting, how does it differ from what we just said
18 in terms of any actuarial analysis?

19 MS. DOUGHERTY: Are you talking about the
20 current OPEB survey?

21 DR. GHILARDUCCI: Well, pensions, too.

22 CHAIR PARKSY: Yes, either. But we are now
23 collecting data from the same entities on a voluntary
24 basis.

25 Are they providing us only the data just

1 described, or are they providing us data that would
2 suggest that they did an actuarial analysis going
3 forward?

4 MS. DOUGHERTY: What we've asked them for are
5 their annual OPEB costs, and then what their
6 pay-as-you-go cost is; and, if they are prefunding, what
7 are they currently setting aside for prefunding.

8 DR. GHILARDUCCI: That's not quite the
9 question. It's now they're required to report the
10 pension costs. Do they report the actuarial liability
11 over 30 years, or is it just the pay-as-you-go -- the
12 normal cost of the pay-as-you-go cost?

13 MS. DOUGHERTY: Under the AB 1200?

14 DR. GHILARDUCCI: Yes.

15 MS. DOUGHERTY: (*Nodding head.*)

16 MR. BRANAN: I don't know. I'm not familiar
17 with 1200.

18 MR. LIPPS: Actually, I do. For public
19 education agencies that offer post-employment benefits --

20 DR. GHILARDUCCI: Yes, okay.

21 MR. LIPPS: -- past age 65 -- only past age 65,
22 not up to age 65 --

23 DR. GHILARDUCCI: Right.

24 MR. LIPPS: -- and they are required to have
25 an actuarial valuation every three years. And what they

1 have to disclose in their adopted budget in the criteria
2 and standards pages is, what is the projected cost of
3 their -- what is their OPEB valuation and what was the
4 date of the last OPEB valuation. So that's current law.

5 DR. GHILARDUCCI: So why is this a problem?

6 CHAIR PARKSY: Yes, that's my next question.

7 MR. LIPPS: Why? Because this is done every
8 three years, not every time a benefit is approved.

9 DR. GHILARDUCCI: Okay.

10 MR. LIPPS: This would apply -- could apply to
11 any negotiation in any given year if a benefit is
12 approved or, theoretically, if a benefit was decreased.

13 And, again, for those districts where the
14 additional cost comes in for most districts is, most
15 school districts do not offer retiree benefits past
16 age 65.

17 CHAIR PARKSY: Well, what if -- and I don't
18 know whether this would be responsive -- but what if the
19 recommendation with respect to local school districts had
20 a requirement that as they publish every three years
21 their actuarial analysis, they include a separate section
22 that deals with the increased benefits that have been
23 created since the last publication?

24 MR. LIPPS: Well, I think that's almost
25 implicit in what GASB 45 is now currently requiring;

1 because any school district that offers retiree benefits
2 has to do this actuarial valuation at least every two
3 years.

4 DR. GHILARDUCCI: Every two years?

5 MR. LIPPS: Which will not be without -- or
6 three years, if you're below a certain size --

7 DR. GHILARDUCCI: Okay.

8 MR. LIPPS: -- which would not be without its
9 costs. But they are going to be required to publish the
10 actuarial valuation of what those OPEB liabilities are.
11 So I think that's what GASB 45 is currently requiring.

12 What may not be apparent, which may have been
13 implicit, Gerry, in your question, is if somebody looks
14 at an actuarial valuation of let's say \$40 million three
15 years ago, and this year it's \$60 million, you may not
16 know if that is a result of increased benefits or if that
17 is a result of changed actuarial assumptions.

18 CHAIR PARKSY: Right.

19 MR. LIPPS: You may have changed -- an
20 actuarial firm that may have changed the assumptions.
21 There could be any number of reasons why the number was
22 different. And in a parallel way, if the number went
23 down as well.

24 So it doesn't get exactly to what you were
25 asking; but I believe school districts at this point,

1 anybody that offers any school district -- any school
2 district that offers a retiree benefit is going to have
3 to have these actuarial valuations.

4 CHAIR PARKSY: And at the time of adoption of
5 new benefits, that analysis isn't done?

6 DR. GHILARDUCCI: Is not done.

7 MR. LIPPS: No.

8 DR. GHILARDUCCI: Is not done.

9 CHAIR PARKSY: Well, what about -- Lee, we'll
10 come back to the local school districts.

11 What about every other entity that we are
12 looking at?

13 MR. BRANAN: For other public entities -- and
14 you'll see this on page 8, it gives the text of
15 Government Code 7507. *"The Legislature and local*
16 *legislative bodies shall..."* So it applies to all local
17 agencies, I would say with a -- I'm not sure if that
18 would exclude school boards or not; but certainly city
19 councils, boards of supervisors, the boards of special
20 districts do have to comply with 7507. That's the basis
21 of the recommendation.

22 CHAIR PARKSY: And, Lee, do you know whether or
23 not the local school districts are covered by 7507?

24 MR. LIPPS: Let me take a look at 7507 again
25 before I answer that question.

1 CHAIR PARKSY: Okay.

2 But inherent in the recommendation is to create
3 a parallel requirement to this?

4 MR. BRANAN: That's correct. In fact, in
5 several of the recommendations today, you'll see that the
6 idea behind them is to take a third party, a neutral
7 party, and inject them into the decisions being made for
8 benefit changes.

9 DR. GHILARDUCCI: Right.

10 CHAIR PARKSY: Which, in and of itself, a
11 process has been done on the pension side?

12 MR. BRANAN: That's correct.

13 MR. LIPPS: Gerry, this wouldn't apply to local
14 school-district agencies because it only refers to
15 pension benefits. And those pension benefits are out of
16 the hands of local school districts. That's all done at
17 the CalSTRS agency.

18 CHAIR PARKSY: Well, I do think a broad
19 approach by this Commission to send a signal that
20 consistency of reporting data and information with
21 respect to health-care benefits paralleling what I think
22 is in place on the pension side sounds like a sensible
23 thing to do if we're really trying to identify the
24 magnitude of these costs and make the public aware of
25 them.

1 Now, I think we need to be sensitive to what is
2 practical. But isn't that inherent in what you're
3 suggesting, Tom, to basically move in that direction?

4 MR. BRANAN: Yes, that's our goal as staff, is
5 to open these up, these processes and decisions to the
6 public, and to have a third party involved to come up
7 with the costs.

8 CHAIR PARKSY: Well, and with certain
9 exceptions. If it's been accepted on the pension side,
10 I'm not quite sure why it wouldn't be accepted on the
11 health-care side.

12 MR. LIPPS: Again, Gerry, in theory, there's
13 not a problem with that, except that on the pension side,
14 most pensions are covered by large state agencies. The
15 local public agency doesn't have to do any reporting.
16 That's all compiled at the state level if we're talking
17 about CalSTRS, CalPERS, and some of the larger
18 independent systems.

19 The local school districts -- and I'm sure that
20 there are other public agencies as well -- don't have
21 this pension-reporting requirement on an annual or
22 biannual basis because they belong to part of the larger
23 system.

24 CHAIR PARKSY: Well, I think maybe in
25 recrafting this recommendation, maybe we want to

1 differentiate in terms of what the state agencies can do
2 and what the local agencies may do. I don't know how
3 we're going to acknowledge, or make the recommendation
4 with respect to legislation, acknowledge those
5 differences.

6 MR. BRANAN: We'll certainly look into
7 necessary changes for the school districts. But I really
8 don't think there's any argument against including other
9 local agencies in this recommendation.

10 CHAIR PARKSY: Right.

11 MR. BRANAN: Even if a city contracts with PERS
12 for health care, that city is still choosing a certain
13 health-care package. And it does have a cost; and I
14 would think they could get -- I know they can get costs
15 from PERS or they could hire their own actuary.

16 CHAIR PARKSY: Let's see if we can only
17 acknowledge the issues relating to local school districts
18 then.

19 MR. BRANAN: Okay.

20 CHAIR PARKSY: Any other comments on that
21 recommendation?

22 Sorry, Bob?

23 MR. WALTON: Yes, thank you.

24 I think the theme of increased transparency is
25 very important, not only from the view of the employer,

1 the plan sponsor, but also the member; but even more
2 importantly I think from the general public, as far as
3 credibility and what public agencies and public members
4 are agreeing to in their benefit package, both in the
5 retirement and pensions and health.

6 Several things I think I would characterize as
7 somewhat minor. I'm not sure that the actuary, an
8 enrolled actuary would be the best person to present an
9 item before a local governing board. No disrespect to
10 actuaries; but to have them present it in a layperson's
11 understanding may be an oxymoron, I'm not sure. But
12 nevertheless, I think at a minimum, actuaries ought to
13 be present to explain the financials. There ought to be
14 a requirement, whether it's a CalPERS actuary or someone
15 that the local government wants to bring in is fine.

16 CHAIR PARKSY: We gave the actuarial community
17 one of these commission sessions, and all of them could
18 come forward in that one session. They succeeded in
19 confusing the entire Commission during that one session,
20 but that's perfectly okay.

21 MR. WALTON: I wasn't too confused, so I
22 questioned my credibility in this area.

23 Disclosure of cost. The current law requires
24 for pensions the future annual cost. I think that ought
25 to be expanded. Part of the problems that we saw in the

1 late nineties -- when most systems were flush with
2 overfunding - is, often, the future annual cost would be
3 shown as zero because there were sufficient surpluses to
4 pay for the ongoing cost. That misled people to say that
5 the benefits don't cost anything, which, of course, is
6 foolish; they do cost something.

7 So I think we need to expand both what the
8 current law requires for pensions, as well as OPEB
9 benefits, to be more inclusive of the true total cost,
10 not just the future annual cost. What's the normal cost
11 ongoing, what's the unfunded liability being created, and
12 how is that unfunded liability going to be paid, whether
13 there's sufficient surpluses or whether it's going to be
14 amortized over a set period of time.

15 It's not unlike when you go in and sign the
16 closing papers for a mortgage. You have to sign a
17 document that says, "I acknowledge this is my cost, this
18 is my annual payment, this is my total payment over
19 time." It's something like that.

20 And to that extent, I would have a requirement,
21 the head of the local governing body that is approving
22 benefits has to sign a document acknowledging these
23 costs.

24 Currently, they have to be in a public setting;
25 but, as you say, often it's consent and it's passed among

1 many other things and isn't really noticed. And I think
2 it ought to be carved out and highlighted.

3 The other -- and, Tom, I don't know if you plan
4 to have it somewhere else -- but something I've brought
5 up before is, I think in approving benefit changes, both
6 in pension and health by the governing board ought not to
7 be made contingent upon action by the plan
8 administrator -- a retirement board, or whoever is over
9 the OPEB trust, as we've seen in the past. So it's not
10 only at times the retirement system, quote, unquote,
11 manipulating the actuarial to make it more attractive,
12 it's also the employer's side, the plan sponsor, the
13 governing board, putting criteria contingencies: "We
14 approve these benefits only if the retirement board does
15 X, Y, or Z." I think that ought to be eliminated and not
16 allowed.

17 MR. BRANAN: We do have a recommendation on
18 that later today.

19 MR. WALTON: Okay, and I think that's it.
20 Thanks.

21 CHAIR PARKSY: Okay, go ahead -- sorry, Jim?

22 MR. HARD: Well, I do think that this is
23 overall a good recommendation.

24 I'm not sure -- I'd like to hear more from Bob
25 maybe sometime about the last couple things that were

1 brought up about a document signed by the local agency
2 head, and also the projection on how things are going to
3 be funded. It seems like the cost is one thing, but the
4 funding of it is a political question that an agency has
5 to deal with. And if they are an agency that has a
6 taxing authority, then it's a question of either raising
7 revenue or cutting other expenses and balancing out. So
8 I guess I got a little lost on the last two pieces, and
9 so I'm not sure about those two.

10 MR. BRANAN: Commissioner Hard, I think that
11 the part about finding a funding source came from
12 Commissioner Lipps' description of the process at the
13 local school level. But for this recommendation, there's
14 no such requirement.

15 MR. HARD: Right. I understood that. But I
16 was just listening to Bob. I always listen to him.

17 DR. GHILARDUCCI: Yes, I wanted to clarify
18 that.

19 Bob, you're getting fun.

20 You ought to bring Sarbanes-Oxley to
21 California.

22 CHAIR PARKSY: Not every acknowledgment goes
23 directly into Sarbanes-Oxley.

24 DR. GHILARDUCCI: Well, I heard a little
25 passion there.

1 It seems like what you want to do is actually
2 expand 7507?

3 MR. WALTON: Correct.

4 DR. GHILARDUCCI: Got it. Okay.

5 And then you want 7507 to -- the language would
6 be "an actuarial impact on future annual costs before
7 authorizing the increases."

8 You say that's not responsible enough?

9 MR. WALTON: Well, I think it can be
10 misleading. As I said, in the late nineties, you may
11 have a system that -- a plan that is 130 percent funded.

12 DR. GHILARDUCCI: Sure.

13 MR. WALTON: And so there's no increase
14 annually in cost.

15 DR. GHILARDUCCI: I understand it. Oh, so you
16 would like it -- I just want to know what you would like
17 it to be -- the actuarial impact -- I see. You would
18 want --

19 MR. WALTON: The increase in normal costs.

20 DR. GHILARDUCCI: -- a statement of future
21 liabilities.

22 MR. WALTON: What's the increase in normal
23 cost. There's always an increase in normal cost if
24 there's a benefit.

25 DR. GHILARDUCCI: The liabilities?

1 MR. WALTON: Correct.

2 DR. GHILARDUCCI: You want liabilities to be
3 restated?

4 MR. WALTON: And what's the increase in
5 unfunded liabilities if this is a retroactive benefit
6 applying to past service.

7 DR. GHILARDUCCI: Sure. So you really just
8 want one word change?

9 MR. WALTON: I'm not sure if one is right. The
10 actuaries could tell me better what --

11 DR. GHILARDUCCI: But you want liabilities
12 reported, not costs?

13 MR. WALTON: Yes.

14 DR. GHILARDUCCI: Got it.

15 MR. WALTON: Both.

16 CHAIR PARKSY: He wants normal costs.

17 MR. WALTON: I want normal cost, I want
18 unfunded liability. I want all of that disclosed.
19 Again, it's not unlike what you do when you acknowledge
20 your mortgage statement.

21 DR. GHILARDUCCI: I understand.

22 MR. WALTON: When you sign your closing papers,
23 you acknowledge the monthly payment, the total cost,
24 what's going to be paid over time, that sort of thing;
25 and not where those funds are going to be coming from.

1 DR. GHILARDUCCI: And you wanted who to sign
2 the document?

3 MR. WALTON: I want the head of the governing
4 board. Because often -- and CalPERS can tell you their
5 experience -- in later years, when somebody challenges
6 why this is done, they claim, "We didn't know there was a
7 cost to it" --

8 DR. GHILARDUCCI: Got it, okay.

9 MR. WALTON: -- when, in fact, they did.

10 CHAIR PARKSY: John?

11 That, in part, keys into Recommendation 4 as
12 well as 3?

13 MR. WALTON: Yes.

14 MR. BRANAN: Yes.

15 DR. GHILARDUCCI: It does.

16 CHAIR PARKSY: Do you think you have that
17 concept?

18 MR. BRANAN: Yes.

19 CHAIR PARKSY: That was a hesitant "yes."

20 MR. BRANAN: The only hesitation in not
21 understanding, do you still want to take up 4 or do you
22 think it's covered?

23 CHAIR PARKSY: Well, there may be some other --
24 any other comments on 4; but I think Bob's comments fit
25 in with 4.

1 MR. WALTON: Yes, that was my intent.

2 CHAIR PARKSY: Yes.

3 Any other comments on -- do you want to -- any
4 other thing you want to say about 4 before we move off of
5 it?

6 It's pretty straightforward, but go ahead.

7 MR. BRANAN: No. Actually I was just going to
8 read it. But if everybody understands it, I might muddy
9 the water.

10 CHAIR PARKSY: If you want to have mud, it's
11 okay. You can throw in a little mud.

12 Any questions on Number 4?

13 DR. GHILARDUCCI: No, we did it.

14 MR. HARD: It seems like it was covered.

15 CHAIR PARKSY: Okay, go ahead.

16 MR. BRANAN: The next topic is the "Actuarial
17 Review Panel" and "Actuarial Assumptions."

18 For pensions: "Current law requires each
19 public retirement system to conduct an actuarial
20 valuation at least once every three years; and to have
21 annual financial audits and submit annual financial
22 reports to the Controller."

23 "CalPERS and CalSTRS employ full-time actuaries
24 and also contract with outside actuarial consulting firms
25 to perform annual parallel valuations."

1 I should say also that several of the '37 Act
2 requirement systems, that's two of them also.

3 For OPEB, "There is no similar statutory
4 requirements for OPEB."

5 The next point is, "Actuaries are responsible
6 for making method and assumption recommendations to
7 retirement system boards. Ultimately, retirement system
8 boards have the constitutional authority to select
9 methods and assumptions."

10 "Some retirement system boards have at times
11 used this selection process to encourage benefit
12 improvements."

13 And two examples that we put here, you've heard
14 before, sitting as the Commission, in the late nineteen
15 nineties the PERS board offered to increase the value of
16 assets of any agency that would provide enhanced benefits
17 to its employees.

18 And you heard in the City of San Diego, this
19 wasn't an actuarial failing, it was more of a political
20 failing, but the City Council made recommendations that
21 were based on things other than the actuarial
22 assumptions: Primarily, political considerations and
23 funding changes.

24 The next point: "General opinion is that the
25 above examples did not violate actuarial standards of

1 practice. However, they did not encourage best
2 practice."

3 "In addition, several California public
4 pensions have also experienced significant problems
5 regarding the quality and/or accuracy of their actuarial
6 studies

7 Recommendations: "The actuarial standards of
8 practice from the American Academy of Actuaries only
9 addresses actuaries who practice outside the acceptable
10 range of practice and do not help actuaries and boards
11 select best-practice methods and assumptions."

12 Recommendation 5: "In order to encourage
13 greater transparency and understanding of actuarial
14 methodology and assumptions, there should be a California
15 actuarial advisory panel created at the state level.
16 This panel should be within the office of the State
17 Auditor. Permanent staff should be assigned to support
18 the activities of the advisory panel."

19 CHAIR PARKSY: Comments? Both about the panel
20 or where it's located or any other comments?

21 Bob?

22 MR. WALTON: I think this recommendation has a
23 lot of merit. I'm not sure I wouldn't take it a little
24 further than what's being proposed here.

25 Currently, benefits for state employees,

1 classified school members, teachers, are done at the
2 statewide level through legislation. They can't be
3 bargained at the local level. And the respective
4 retirement systems perform actuarial analysis on benefit
5 improvements for those groups. Those are generally
6 discussed through both the legislative policy committee,
7 as well as appropriation before they're passed.

8 I think it would be helpful if there was a
9 function at a statewide level, perhaps within the
10 Legislative Analyst's office, that could add their
11 expertise in this area.

12 Currently, I don't believe the Leg. Analyst has
13 a staff actuary available. I think it would be helpful
14 if they did. It might be a better place to locate this
15 rather than the State Auditor; but I'm flexible on that.

16 The bottom line is, I know some other states
17 actually have a state actuary that, before legislation
18 can be considered to improve or change benefits, the
19 State Actuary has to prepare a report and testify on the
20 cost of those benefits.

21 I'm not sure we have to go that far; but that
22 capability, at least, ought to be within California. And
23 I think that would provide credibility to the numbers
24 that's being discussed.

25 MR. BRANAN: In terms of where this advisory

1 panel would be housed, we also first thought of the Leg.
2 Analyst. But we settled on the State Auditor because
3 that office already has audit authority, and we thought
4 that it would be -- an audit often needs an actuarial
5 component, and we thought that this could be a helpful
6 combination of the audit authority and the expertise of
7 the advisory panel.

8 MR. WALTON: To me, the location, as long as
9 the expertise are there -- and the audit is usually
10 thought of in the concept of post-facto, after the fact.
11 And I would want that work done as legislation is being
12 considered and not just after the fact.

13 The State Auditor normally doesn't testify
14 before policy and appropriation committees. And that's
15 what I was looking for.

16 CHAIR PARKSY: Other comments?

17 Yes, Paul?

18 MR. CAPPITELLI: Is this something that we are
19 suggesting be done prospectively, or is this something
20 that would be done retroactively, or to look at the
21 existing benefits?

22 MR. BRANAN: What we had in mind, primarily,
23 was prospectively. That this would be, in essence, a
24 clearinghouse that retirement systems, boards of
25 trustees, various groups that are interested in this

1 could run, say, a local actuarial practice by this group
2 and get a reaction from them on how it fits in with best
3 practices.

4 MR. CAPPITELLI: Okay, but the question that
5 comes to my mind as the reason we are here is because
6 somewhere along the line it is our sense that some of
7 this may have gone off-track. So does this -- by putting
8 this in place then, then all of a sudden, everybody, you
9 know, stands still, the deer in the headlights, and say,
10 "Oh, we'd better straighten up and fly by this," or do we
11 have a means by which we should go back or should
12 encourage analysis of things that are already in place?

13 MR. BRANAN: I would say primarily the former.

14 But I would like for John Bartel to -- he is
15 the actuary -- one of our two actuaries on staff.

16 MR. BARTEL: Inherent in best practice is to
17 look at benefit improvements, quantifying future benefit
18 improvements, but it's also looking at current funding,
19 current contribution rates. So I think inherent in what
20 you're asking about is the nature of best practice.

21 MR. WALTON: I would say this also goes to the
22 previous discussion about transparency, about the
23 advisory panel would recommend, "Here's what we think
24 ought to be disclosed when government is considering
25 benefit improvements."

1 It goes back to the last meeting, where,
2 "Here's the best practices as it relates to the
3 amortization of unfunded liability, or the smoothing of
4 assets or those things." That's what the advisory panel
5 would do, is a whole arena of actual policies and
6 practices.

7 MR. BRANAN: That's correct.

8 And if you'll look on page 10 of the background
9 document, we listed arguments for establishing such a
10 review panel, as well as possible responsibilities.

11 MR. WALTON: Okay.

12 CHAIR PARKSY: And I think what will be
13 important, as each of these recommendations are developed
14 for the report, that they're placed in the right context,
15 so that this background material would be provided either
16 around or before we actually get to the recommendation.

17 Isn't that what you had in mind, Tom?

18 MR. BRANAN: Yes, that's correct.

19 CHAIR PARKSY: Lee?

20 MR. LIPPS: In general, I'm not opposed to the
21 concept, but I can't help but being struck by the idea
22 that this recommendation is almost analogous to a panel
23 that would be very similar to GASB, and that would make
24 recommendations of best practices, it would be advisory,
25 no binding of law.

1 If you don't follow their recommendations or
2 what they think are best practices, is there a penalty,
3 you know, besides some sort of notation?

4 But I think we have to be a little careful of
5 overregulation, and particularly setting up a panel here,
6 what if this panel were to come up with different things
7 that conflicts with some of the things that GASB says
8 should go into generally accepted accounting principles?
9 It's not beyond the possibility that there could arise
10 conflicts in the future. I just think we have to be
11 careful of a little bit of the overregulation.

12 MR. BRANAN: Well, we did have --

13 CHAIR PARKSY: And that's why he is on the
14 right.

15 MR. BRANAN: That's true.

16 We did have a lively discussion at the staff
17 level over would this be an advisory panel or would it
18 have some regulatory teeth. And we settled on advisory.
19 I think it's more acceptable, and it's in keeping with
20 what the general tenor of these recommendations have
21 been, and that is to get impartial information out in the
22 field of pensions and OPEB.

23 And, really, there is no single clearinghouse
24 in the state to take up these types of questions of where
25 does a given actuarial assumption fall.

1 MR. LIPPS: Don't get me wrong. I see a lot of
2 merit in the recommendation.

3 I just think we need to be careful about what
4 the scope of its responsibility is to the extent that we
5 get to that.

6 CHAIR PARKSY: Again, I think if you refer to
7 page 10 of the background piece, the responsibilities
8 could include what's listed there. And I do think that
9 inherent in making the recommendation would be to include
10 some recitation of the responsibilities.

11 MR. WALTON: Well, I think to address Lee's
12 concern, too, I think we also ought to include -- maybe
13 it's understood -- that it's within current -- you know,
14 whatever the GASB or accepted actuarial practices -- it's
15 within that confines that this body would work. They
16 couldn't work outside of what's accepted practice within
17 the industry today. And I'm sure John wouldn't have a
18 problem with that.

19 That's understood, but it wouldn't hurt to say
20 it.

21 MR. BRANAN: Well, there goes your idea of a
22 kingdom.

23 CHAIR PARKSY: Well, you know, you can't have
24 everything in the kingdom.

25 Jim?

1 MR. HARD: I just did wonder if GASB doesn't do
2 pretty much the same thing? It doesn't, apparently.

3 MR. BARTEL: Yes, a big difference in that
4 GASB -- all GASB really is doing is requiring each agency
5 to report information in their financial statement. What
6 we're really talking about here is a different sort of an
7 animal.

8 DR. GHILARDUCCI: Yes.

9 MR. HARD: Yes, they don't do best practices in
10 these areas.

11 MR. BARTEL: Right.

12 CHAIR PARKSY: Teresa?

13 DR. GHILARDUCCI: Yes, just two comments.

14 One: This seems to suggest that the Commission
15 state that we want the actuary's voice to be elevated;
16 that the actuary can actually speak first and say, "These
17 are best practices," rather than the current practice,
18 where the actuary is asked, "Hey, is this really wrong?,"
19 and then the actuary is there saying, "This is way out of
20 bounds" or not. That seemed, to me, the difference
21 between best practices and just acceptable practices.

22 And the second question I had is, does any
23 other state have a functioning actuarial review board
24 like this?

25 MR. BARTEL: There are a couple that have

1 similar sorts of things.

2 And I might ask Paul to confirm whether or not
3 I have these things right.

4 DR. GHILARDUCCI: Is it New Jersey?

5 MR. BARTEL: Yes, New Jersey. There's
6 Florida, Texas has something --

7 DR. GHILARDUCCI: It does, yes.

8 MR. BARTEL: Yes, but on the pension side.

9 And in a couple of those, they actually -- you
10 need to get the board's authority to go ahead --

11 DR. GHILARDUCCI: Exactly, exactly.

12 MR. BARTEL: -- and make changes.

13 In other words to do something outside of
14 bounds, the board will not let you do that.

15 DR. GHILARDUCCI: Right.

16 So this is the first -- this is really -- this
17 would be unique among all states, that the actuarial
18 panel would have its own voice, and would be expected to
19 actually issue some of the best practices, as if it were
20 the American Academy of Actuaries in California issuing
21 reports and making judgments?

22 MR. BARTEL: I might even kind of describe it a
23 little bit differently. The American Academy of
24 Actuaries does a great job of talking about ethics and
25 where your out-of-bounds markers are.

1 DR. GHILARDUCCI: Acceptable practices.

2 MR. BARTEL: Acceptable.

3 But I kind of think of best practice as maybe
4 inside the hash marks of a football field, and that's the
5 difference.

6 DR. GHILARDUCCI: Got it.

7 *(Mr. Pringle entered the hearing room.)*

8 CHAIR PARKSY: Any other comments on Number 5?

9 *(No response)*

10 CHAIR PARSKY: Okay, Tom?

11 DR. GHILARDUCCI: He's for it *(indicating*
12 *Mr. Pringle)*.

13 CHAIR PARKSY: Do you mean the man on my left?
14 The far left, yes.

15 But you see when the audience is looking, it
16 can be the opposite, too. So it's whatever you're
17 comfortable with.

18 Tom, go ahead.

19 MR. BRANAN: "In-depth and independent review
20 of actuarial assumptions and their forecasts are critical
21 to all interested parties. A secondary review of
22 financial and actuarial activities is in the best
23 interest of the pension or OPEB fund, the plan sponsors,
24 the taxpayers, and the active and retired employees of
25 the plan sponsor."

1 Recommendation 6: "In addition to annual
2 financial audits conducted by an outside independent
3 financial auditor selected by plan trustees, the State
4 Auditor should perform a complete financial audit on
5 statewide retirement systems every three years. If a
6 statewide retirement system administers an OPEB fund,
7 that fund should also be included in the audit."

8 CHAIR PARKSY: Okay.

9 MR. LIPPS: Outside of the OPEB piece, how does
10 that differ from the current practice? I understood
11 that -- doesn't the State Auditor currently do an audit
12 of the statewide retirement systems?

13 CHAIR PARKSY: Bob?

14 MR. WALTON: PERS currently has an annual
15 independent auditor that they hire. They also have a
16 separate independent actuary that reviews the actuarial
17 process and assumptions.

18 The State Auditor has the authority to audit
19 that at any point in time. They don't do it every year,
20 but they do it occasionally.

21 I know, just before I retired, they were doing
22 an audit. But it isn't done on a periodic basis, it's
23 based on whenever requested or they feel it's needed.

24 So they have the authority today to audit at
25 any point in time; they just don't do it every year or

1 every two years. It's periodic.

2 MR. BRANAN: I think the last one, before the
3 one Bob mentioned, was in 1994. So there can be a long
4 stretch there.

5 MR. LIPPS: You're talking about frequency,
6 every three years it's recommended?

7 MR. BRANAN: We are. And the reason is, again,
8 to bring in a disinterested party rather than somebody
9 who has been hired by the system that's being audited.

10 CHAIR PARKSY: Matt?

11 MR. BARGER: I apologize, I'm going to go
12 backwards now slightly.

13 CHAIR PARKSY: That's okay.

14 MR. BARGER: The GASB comment sort of threw me
15 for a little while, and I was thinking about the advisory
16 board only being within the realm of GASB.

17 I actually think that there are some things
18 that are sort of best practice that might not be within
19 the realm of GASB. I'll give an example that GASB is
20 just silent on. Things like sensitizing the critical
21 assumptions. It might well be best practice to say
22 rather than just pick a point in health-care inflation
23 assumptions, we'd like to now -- what are the
24 implications if you look at a range of health-care
25 inflation assumptions that might well be a best practice

1 that this group would want to recommend GASB would -- you
2 know, there's no place within GASB, I don't think, for
3 that kind of concept.

4 So I don't -- just stepping backwards, I do
5 want to say that only within GASB would I feel
6 comfortable with something that's trying to say what our
7 best practice is, what should people be thinking about.

8 MR. LIPPS: Yes, just to respond to that. When
9 I introduced a comment, what I said was that I saw this
10 as analogous to a GASB type advisory body. Not that it
11 would just remain within the confines of GASB, but it
12 would be an advisory body that would say, "Here is how
13 you want to do things if you want to conform with" --

14 MR. BARGER: Here are suggestions for best
15 practices?

16 MR. LIPPS: Right.

17 CHAIR PARKSY: Okay. Any comments on
18 Recommendation 6?

19 MR. HARD: Well, does CalSTRS also get audited
20 independently?

21 MR. BRANAN: They have similar arrangements
22 where they bring in auditors annually. But this would
23 also apply to them.

24 CHAIR PARKSY: Any concerns, Bob, about --

25 MR. WALTON: No. I think the difference is the

1 perceived independence.

2 CHAIR PARKSY: Right.

3 MR. WALTON: Now, the audit today is done
4 independently by an outside auditor, but it's paid for by
5 the system.

6 This is adding another outside auditor that's
7 paid for by the state or someone else. And so from the
8 public's perception, it's perceived to be even more
9 independent because it isn't paid for by the system
10 that's being audited.

11 MR. BRANAN: That's exactly what's behind the
12 recommendation.

13 CHAIR PARKSY: That's right.

14 MR. BRANAN: It's another non-partisan check
15 and balance.

16 CHAIR PARKSY: I don't see any --

17 MR. WALTON: I don't have a problem since they
18 have the authority to do this today. It's merely
19 suggesting to the state that you ought to do this more
20 often than what you're doing it today.

21 CHAIR PARKSY: Exactly.

22 Okay, let's keep moving.

23 MR. BRANAN: "Funding benefit changes. In the
24 '37 Act counties, employers have the choice of applying
25 new retirement benefits on a prospective-only basis or on

1 the total-service basis," meaning, prospectively and
2 retroactively.

3 "Local bargaining decides which application is
4 chosen."

5 "Local CalPERS employers must apply new
6 retirement benefits on a total-service basis," meaning
7 both prospectively and retroactively.

8 Recommendation 7: "All public agencies which
9 have the authority to determine their own pension
10 benefits should have the flexibility to adopt pension
11 benefit increases on a prospective basis only," and I
12 should say, or on a total-service basis.

13 "How the benefit is adopted should be decided
14 through the local bargaining process."

15 CHAIR PARKSY: Okay, Lee, you can start.

16 MR. LIPPS: Explain to me, Tom -- I understand
17 the CalPERS requirement that it has to be offered both
18 retroactively and prospectively. But this is going to
19 apply to all public agencies: How is limiting an option
20 giving them more flexibility?

21 MR. BRANAN: How is what?

22 MR. LIPPS: How is limiting an option that
23 currently public agencies have -- right now they have the
24 option of doing it prospectively or retroactively. This
25 proposal which would apply to all public agencies would

1 limit them only to a prospective change.

2 MR. BRANAN: No, that's not correct.

3 This recommendation would give them the choice
4 of either prospective only or prospective and
5 retroactive.

6 MR. LIPPS: That's where I'm missing this then.

7 The recommendation says, "All public agencies
8 which have the authority to determine their own pension
9 benefits should have the flexibility to adopt pension
10 benefits increase on a prospective basis only."

11 MR. BRANAN: Yes.

12 MR. LIPPS: I don't see the retroactive.

13 CHAIR PARKSY: I think that will be additive to
14 what exists today.

15 MR. BRANAN: That was the intention. But
16 you're correct, it's not clear.

17 MR. LIPPS: Okay.

18 MR. BRANAN: And the intention is to give them
19 the choice of either/or.

20 MR. LIPPS: Okay, that's not clear from this
21 reading.

22 CHAIR PARKSY: You're right.

23 The lead-in was not meant to be replaced, but
24 this was meant to add to it. But I think we can make
25 that clear.

1 Anyone else?

2 Yes, Bob?

3 MR. WALTON: Just a comment.

4 From my experience at CalPERS, the reason, I
5 think, of the current policy to apply both retroactively
6 and prospectively is more based on being able to explain
7 the benefit to the members and administering that
8 benefit.

9 Public agencies make numerous benefit changes
10 over the years. And if you only made it prospectively,
11 you would have a whole bunch of pieces.

12 Well, this five years applies to this benefit
13 formula, this two years applies to this final comp, this
14 three years. So it becomes really difficult to
15 administer because you have to take into account each one
16 of these pieces to get a total benefit.

17 Also, there are certain benefit increases. We
18 normally think of benefit increases as formula changes.
19 Well, CalPERS has about 50 options, like using unused
20 sick leave, various death-benefit options, which are a
21 fixed sum.

22 Well, how do you apply changing from a \$500
23 death benefit to a \$2,000 death benefit, based on
24 service?

25 It's not based on service, it's a fixed amount.

1 So I think if we're going -- and I'm not
2 suggesting we do -- but I think if we go down this road,
3 it has to be a little narrower to only certain types of
4 benefits because some just aren't appropriate.

5 DR. GHILARDUCCI: Yes, that's a great
6 clarification.

7 Tom, I just wanted to make sure I understand.
8 You seem to be referring here more to benefit formulas.

9 MR. BRANAN: That's correct.

10 DR. GHILARDUCCI: So that's the flexibility
11 you're going to give?

12 MR. BRANAN: Yes.

13 DR. GHILARDUCCI: Okay.

14 MR. HARD: Yes, I was misunderstanding this, I
15 guess, because it did not seem like it was directed at
16 expanding flexibility at all. So I'm happy to hear that.
17 But I guess I'd like to see this another time.

18 DR. GHILARDUCCI: Yes.

19 CHAIR PARKSY: Oh, you mean --

20 MR. HARD: Edited a little bit.

21 CHAIR PARKSY: You will definitely have a
22 chance to see it at another time, that's for sure.

23 Again, the process that we're going to go
24 through is, this was meant to be an open discussion so
25 staff could take away and then revise the

1 recommendations.

2 MR. HARD: Right.

3 CHAIR PARKSY: Then you'll see them in draft
4 form once or twice more.

5 MR. HARD: That would be good.

6 CHAIR PARKSY: Any other?

7 Okay.

8 MR. PRINGLE: Mr. Chairman, therefore, on this,
9 the clarification, both sides of the equation: One, in
10 the preamble or something, state that there is the
11 ability to have retroactive benefits or prospective
12 benefits, and this would allow the agency to negotiate
13 prospective benefits only.

14 In I think what was suggested, is to try to
15 define then what those areas would be.

16 CHAIR PARKSY: Yes, right.

17 MR. PRINGLE: Is that what I had heard, Bob?

18 MR. WALTON: I think -- and someone from
19 CalPERS can correct me -- I think today you can adopt
20 prospective benefits but only for new hires. In other
21 words, if it applies to current hires, it has to apply
22 to all their service, both in the future and past
23 service.

24 Again, it's from an administrative standpoint,
25 how do you keep carving out pieces of benefits for each

1 person. It's very difficult to administer that, it's
2 very difficult to explain the benefit if you have
3 different pieces that you have to add up. It's an
4 administrative issue that can be quite burdensome.

5 So I think staff may want to -- Commission
6 staff may want to talk to CalPERS, as well as STRS, to
7 see how this can be worked so it makes it more
8 manageable, I guess would be the word.

9 MR. LIPPS: In truth, as I'm thinking about
10 this, doesn't this recommendation only apply to CalPERS?
11 The '37 Act counties can already do it prospectively and
12 retroactively. Local agencies can do it prospectively
13 and retroactively.

14 DR. GHILARDUCCI: Yes, I think it's just
15 CalPERS.

16 MR. LIPPS: Tom, retroactively and
17 prospectively.

18 DR. GHILARDUCCI: That's right.

19 MR. LIPPS: So who does this apply to but
20 CalPERS?

21 DR. GHILARDUCCI: CalSTRS.

22 MR. BRANAN: It's primarily CalPERS.

23 MR. WALTON: It applies to CalPERS and applies
24 specifically to local government within CalPERS, because
25 classified school and state has to be passed by statute.

1 And in the statute, the legislature/governor can specify
2 whether to retroactive or prospective only.

3 MR. BRANAN: And in STRS, it's also a
4 statewide --

5 MR. WALTON: Statewide.

6 DR. GHILARDUCCI: So it's just local
7 government.

8 MR. WALTON: So it's local government within
9 CalPERS.

10 CHAIR PARKSY: Right.

11 MR. PRINGLE: Mr. Chairman, it's interesting.
12 If, in fact, it is something that's acceptable on '37 Act
13 counties and even some locally managed health-care plans,
14 it's somehow being -- it's operational there. So I would
15 assume with the great expertise of CalPERS, you'd be able
16 to figure out how that could be operational on the state
17 board level.

18 MR. WALTON: I'm sure they can. In the past,
19 their old data system was preventative in this area.

20 Keep in mind that CalPERS -- and it's really
21 true for local government -- when a person works for a
22 city or county, it's quite common for them to work for
23 many cities and counties all under the CalPERS umbrella.
24 And when you jump from a city that may have had two or
25 three benefit changes to another city that has two or

1 three, we've got now six benefit components. And if you
2 have it broken between prospective and retroactive, it
3 just is very difficult.

4 MR. BRANAN: And I should say that within the
5 '37 Act, it is the larger benefits that this is available
6 for.

7 MR. WALTON: Sure. And that's where the large
8 cost is.

9 MR. BRANAN: That's right.

10 CHAIR PARKSY: Okay, Tom?

11 MR. BRANAN: Number 8, "To avoid
12 intergenerational cost shifting, the total cost of
13 retroactive benefit increases should be funded over a
14 period no longer than the average future working lifetime
15 of the active members."

16 And our actuaries have told us that that period
17 is usually 15 to 20 years.

18 MR. WALTON: I believe CalPERS uses 20 years
19 now for their benefit.

20 DR. GHILARDUCCI: 20?

21 MR. WALTON: I think this is a subject that
22 really, where we're recommending an advisory panel, this
23 is the type of thing that the advisory panel ought to be
24 looking at.

25 DR. GHILARDUCCI: Yes, but I think --

1 MR. WALTON: And it would be better left to
2 them rather than this Commission making a recommendation
3 on this issue.

4 CHAIR PARKSY: Well, maybe what we ought to do
5 is to include this in the responsibilities of the
6 advisory panel. That would maybe address it.

7 DR. GHILARDUCCI: Or decide we wanted to say
8 it. That's what I thought we had.

9 I can't speak for John, but I bet he would say
10 he wanted it.

11 CHAIR PARKSY: So you agree with Tom?

12 DR. GHILARDUCCI: Yes.

13 CHAIR PARKSY: So you'd like to --

14 DR. GHILARDUCCI: Yes, I thought that's what we
15 had talked about when CalPERS talked about the importance
16 of making sure that a symmetric outlook was done. You
17 know, that if you need to treat surpluses symmetrically
18 with liabilities. So I thought that's what we talked
19 about in Oakland.

20 And then when CalPERS first told us why they
21 changed policies, I think --

22 MR. WALTON: I'm not speaking for CalPERS,
23 certainly; but I think that -- I don't think there's an
24 issue there as long as you can look at it from an
25 aggregate basis.

1 CalPERS has 1,100 to 1,200 plans -- well,
2 employers. They have over 2,000 plans. You have some
3 plans that have a membership of one. You have several
4 that are two, three, four, five. So the current policy
5 is kind of an average.

6 DR. GHILARDUCCI: Yes, I understand.

7 MR. WALTON: They don't want to do it plan by
8 plan. And have them look at: Well, this one only has
9 one member, and how old is he or she, and...

10 DR. GHILARDUCCI: Yes.

11 CHAIR PARKSY: I think you made a good point,
12 Teresa. Because in one sense, this recommendation
13 relates to you how to deal with retroactive benefit
14 increases as a best practice --

15 DR. GHILARDUCCI: Yes.

16 CHAIR PARKSY: -- as opposed to a
17 responsibility of the review panel.

18 DR. GHILARDUCCI: Right, right.

19 CHAIR PARKSY: So is that why you separated it
20 out?

21 MR. BRANAN: That's correct.

22 CHAIR PARKSY: Well, Bob, how do you feel about
23 that?

24 MR. WALTON: Well, still, it's an actuarial
25 assumption that the methodology, practice, procedure,

1 whatever you want to characterize it as, that's being
2 considered; and it may differ system by system.

3 DR. GHILARDUCCI: Under ERISA, under the
4 private-sector law, it does specify that past service be
5 amortized over, you know, 30 years.

6 MR. WALTON: Up to 30 years.

7 DR. GHILARDUCCI: Up to 30 years. There's that
8 recognition there, too.

9 MR. WALTON: Right.

10 CHAIR PARKSY: Well, I guess the question is,
11 what would the advisory panel be considering as an
12 alternative?

13 MR. WALTON: What is the best practice as it
14 relates to funding retroactive benefit increases and
15 paying for those benefit increases.

16 MR. BRANAN: We purposely did not add a
17 specific number of years here, because we thought it was
18 more a policy that should come before the Commission.

19 DR. GHILARDUCCI: CalPERS is 20 or 30? Is
20 it --

21 MR. WALTON: 20.

22 DR. GHILARDUCCI: It's 20?

23 MR. WALTON: For that component.

24 DR. GHILARDUCCI: For the back service?

25 MR. HARD: Retroactive benefits?

1 MR. WALTON: That's correct.

2 DR. GHILARDUCCI: And surpluses over 30 years?

3 MR. WALTON: It can be up to. It can be.

4 MR. HARD: Well, my concern is that we were
5 putting in an actuarial specificity here of the average
6 future working life of active members. I mean, does
7 CalPERS calculate that on an actuarial basis when they
8 come up with it? Or do they just use 20 years?

9 DR. GHILARDUCCI: That's a good question.

10 MR. HARD: What do they do?

11 MR. BRANAN: I think all retirement systems
12 calculate that, but I don't think that there is a set
13 number of years.

14 MR. WALTON: My understanding is that 20 years
15 the CalPERS established was based on an average. Some
16 employers are more than that, some are less than that.
17 It's an average. And that's why they chose it. They
18 wanted a single component, so they chose an average of
19 all the employers.

20 MR. BRANAN: So it could vary from retirement
21 system to retirement system somewhat.

22 MR. HARD: Yes, I thought that was kind of in
23 line with our direction on different agencies having
24 flexibility.

25 So it seems like different workforces might

1 be -- you know, in particularly the lifetime of -- the
2 future working lifetime of active members, that might
3 differ from agency to agency.

4 MR. BRANAN: That's absolutely correct. And
5 because of that, we just said that it should not be
6 longer than the average future working lifetime.

7 And it's up then to each retirement system and
8 their actuaries to determine that number. But we
9 wouldn't be mandating a number.

10 CHAIR PARKSY: Lee?

11 MR. LIPPS: So Tom, just to clarify, is this
12 intended only to apply to pension systems, not to other
13 post-employment benefits?

14 MR. BRANAN: This is pension systems.

15 MR. LIPPS: Pension systems?

16 And so in the case of STRS, where the STRS
17 board doesn't have the right to set its -- if we're not
18 going to require this kind of funding, wouldn't that also
19 require giving the STRS board the right to set what the
20 contribution rates are going to be for employers and
21 employees in a given year if there is a benefit increase?
22 Or would it require the Legislature to adopt the
23 actuary's recommended funding rates?

24 Both of those, I think, are problematic.

25 MR. BRANAN: Yes.

1 MR. LIPPS: But I'm just wondering which one
2 you're contemplating here.

3 MR. BRANAN: Under current arrangements, that's
4 not a decision that would be made by the STRS board but
5 by the Legislature. Now, the STRS actuary could tell the
6 Legislature what that number should be, but the
7 Legislature moves in mysterious ways.

8 MR. LIPPS: But if this is a recommendation,
9 are we also then recommending a change in how STRS rates
10 are set? I guess that's what I'm --

11 MR. BRANAN: No, that's not part of this
12 recommendation.

13 CHAIR PARKSY: And I think what you're saying
14 also is, by establishing the period, with the words "no
15 longer than," you're still giving plenty of flexibility
16 to adjustments, what the numbers should be; right?

17 MR. BRANAN: That's correct.

18 CHAIR PARKSY: Well, I think, for now, why
19 don't we maybe leave it as a recommendation; but we may
20 want to adjust it to be part of the panel issue. I think
21 it is different under the heading of how you're going to
22 fund and make the public aware of the funding of benefit
23 changes.

24 Okay, go ahead.

25 MR. BRANAN: "Funding benefit changes. The

1 cost of pension or OPEB benefit changes ultimately
2 depends on the level of benefits which will be paid to
3 members over time."

4 "Plan funding policies determine the immediate
5 impact on contributions and how any change in
6 contributions will be spread over future years."

7 "On occasion, some retirement boards have
8 conditioned changes to their funding policy on plan
9 design actions by either the Governor, the Legislature,
10 or employer agencies."

11 A case of this was when the governor,
12 Deukmejian, signed the one-year final compensation bill
13 for state workers in exchange for the PERS board giving
14 them more flexibility on the state PERS contribution.
15 We talked about the PERS board and benefit enhancements
16 in the nineteen-nineties and the City of San Diego. In
17 all of those, there was some level of quid pro quo.

18 The draft recommendations: "There have been
19 times when some public retirement systems" -- and I think
20 as Commissioner Walton has said, not just the systems,
21 but the employers as well -- "have manipulated aspects of
22 their funding policy to encourage employers to grant
23 benefit increase."

24 Number 9 draft recommendation, "Benefit
25 improvements by the employer should not be contingent

1 upon the actions of the retirement board."

2 CHAIR PARKSY: Comments here?

3 Bob?

4 MR. WALTON: The only comment I have -- and I
5 do support this, I've brought it up before -- but in your
6 background information, I think you may have given the
7 carrot and the stick to the wrong people. I think it's
8 the actions by the employer that cause the retirement
9 board, in some cases, to take action, and sometimes it's
10 the reverse.

11 In the case of the one-year final comp, it was
12 the employer, the state, the State Legislature, that
13 said, "You'll get one-year final comp only if the CalPERS
14 board does certain things," as opposed to the converse.

15 So both sides are guilty of acts in that
16 regard. It's not one-sided.

17 MR. BRANAN: Well, would that require a change
18 in the wording?

19 MR. WALTON: Only in the background.

20 CHAIR PARKSY: Just the background.

21 MR. WALTON: Just the background.

22 CHAIR PARKSY: The recommendation seems pretty
23 clear.

24 MR. PRINGLE: It does. But I don't understand
25 how it's enforceable, applicable, effective in any way.

1 And this verbiage, as a stand-alone sentence of
2 the recommendation, it sounds kind of goofy to me. You
3 know, if the Legislature says you can do this and passes
4 legislation and the PERS board takes action, how does --
5 I mean, I don't -- I would like to have it clearer in
6 terms of what we're trying to get at.

7 This sentence makes it sound to me as if, you
8 know, maybe it happens more in a '37 Act County -- or
9 maybe I'm improperly referencing that at all -- but where
10 you do have a lot of local influence where a retirement
11 board serves a singular purpose, therefore, they're able
12 to deem -- there are more resources available over a
13 period of time. And with that understanding, "Okay, now
14 we can afford that benefit."

15 I see where, from my interest, that is what I
16 would like to make sure this sentence means, if we can;
17 but I have a hard time adding up all of those background
18 comments to get to this sentence from legislative action
19 that changed -- to move to the one-year highest pay as a
20 retirement benefit than PERS taking the action to
21 San Diego and the others.

22 I don't necessarily see this as answering
23 those.

24 I mean, I understand what this sentence is
25 about; I don't necessarily see how it applies to the

1 background information as such, nor do I really see it
2 getting to the point that -- well, maybe I don't even see
3 the points that we're trying to get to.

4 I see this one sentence as kind of a simplistic
5 response to maybe '37 Act counties that may have undue
6 influence of the decision-makers over their retirement
7 boards, but not necessarily how it might apply to
8 CalPERS.

9 CHAIR PARKSY: Well, in one sense, the lead-in
10 here, Tom, would suggest that retirement systems have
11 acted in a way that is meant to, in your words,
12 manipulate the funding policy in order to encourage
13 benefit changes from the employer.

14 And what you're -- but the recommendation isn't
15 clearly linked to that introduction. You then start from
16 the opposite, that the employer shouldn't make any
17 benefit increases contingent on the board acting.

18 So in one introduction, you kind of come at it
19 from one side, and then in the recommendation from
20 another.

21 Is that intended?

22 MR. BRANAN: That's not intended.

23 Originally, we had two mirror sentences here.
24 That the employer -- actions of the employer should not
25 be contingent on actions of the retirement board; and

1 then the same thing, that the actions of the retirement
2 board should not be contingent on those of the employer.

3 But we thought that those two taken together
4 sounded kind of goofy.

5 CHAIR PARKSY: Well, you've succeeded in
6 convincing the mayor that the entire page sounds goofy.

7 So is it your intent to suggest that both sides
8 of this equation should be addressed here in this?

9 MR. BRANAN: Absolutely. This is something
10 that both parties enter into. No matter which one
11 initiates it, the other party has to play the game.

12 And while it certainly has happened in the
13 '37 Act, I would say the most egregious examples are more
14 at the state level.

15 MR. WALTON: One other comment --

16 MR. HARD: I do, too.

17 CHAIR PARKSY: Would you put that into the
18 category of hurting credibility, or this is a practice
19 that -- what you're trying to do is to have each of these
20 two bodies be able to, quote, act independently of the
21 other, for whatever they have authority to do?

22 MR. BRANAN: Well, certainly they should act
23 largely independent of each other, if not entirely.

24 And as far as credibility, I think that's been
25 a real casualty in this kind of collusion, that costs and

1 costing periods can be manipulated. The level of assets
2 supposedly on account can be manipulated all in order to
3 get, say, a new benefit offered to the members of the
4 system.

5 CHAIR PARKSY: But I guess the question
6 inherent in that is, are these kinds of statements really
7 to get at that, as opposed to policies that would address
8 the manipulation of the kind of information you're
9 talking about.

10 I think in one sense, Curt is really right. I
11 mean, inherent in saying "each of the bodies should act
12 on their own" doesn't really address -- what you're
13 saying is, underneath all this, there is some element of
14 collusion.

15 I mean, if one part doesn't want to take
16 certain action, the other part may kind of move the data
17 around to get that action to happen. That's really what
18 you're addressing here?

19 MR. BRANAN: That's correct. Would the second
20 sentence that I described close this loop?

21 DR. GHILARDUCCI: No. I think it's the
22 structure.

23 MR. HARD: I think that Curt made me wonder --
24 I don't think the manipulation of the actuarial
25 assumptions is a healthy thing, probably, for the fund

1 or transparency or public confidence. But what Curt
2 made me think as well that the fund, actually -- the
3 circumstances of the fund actually change, these
4 statements -- do these statements take into consideration
5 actual, legitimate changes in which the fund changes so
6 that the employer might want to negotiate something
7 different? Because I don't see the way the
8 recommendation is written making any distinction between
9 actual, legitimate recognition of fund changes versus
10 manipulation.

11 Do you think it does?

12 MR. BRANAN: Yes, I think it does. It may not
13 be worded correctly. But it sounds like what you're
14 talking about is a retirement system becomes better
15 funded over time.

16 MR. HARD: Perhaps. It could be worse, too.

17 MR. BRANAN: Yes. But let's say it gets
18 better.

19 MR. HARD: Right.

20 DR. GHILARDUCCI: They make good decisions.

21 MR. BRANAN: And then the employer having more
22 money on account may feel that they can grant a new
23 benefit. That's entirely different than the retirement
24 board saying, "If you grant a new benefit, we are going
25 to artificially inflate your assets on account by 5 or

1 10 percent."

2 MR. HARD: Absolutely. And I understand that.

3 And I don't think that's a very good policy. But I'm
4 just wondering if our recommendation is clear on that
5 distinction? Because "The benefit improvements by the
6 employer should not be contingent upon actions of the
7 retirement board." Well, that doesn't mean that the
8 action of the retirement board was a manipulation rather
9 than a legitimate action of the board.

10 MR. BRANAN: Well, if they -- and this is --

11 MR. HARD: I have no disagreement with where
12 you're trying to go or --

13 MR. BRANAN: It just seems to me that if a
14 retirement system, through its investments, becomes
15 better-funded, the employer's action is not contingent
16 on --

17 DR. GHILARDUCCI: It is.

18 MR. BRANAN: That's not an inappropriate
19 behavior by the retirement board.

20 MR. HARD: Right.

21 MR. BRANAN: But that's also not what we've
22 been talking about.

23 MR. HARD: No, I know it's not what we've been
24 talking about. But I'm just wondering if the
25 recommendation makes the distinction. And just for me,

1 it doesn't.

2 MR. BRANAN: Okay.

3 MR. HARD: But I know what you're talking
4 about. I agree with where you're going.

5 CHAIR PARKSY: Well, maybe what you need to do
6 is to think about somewhere in this report, there should
7 be a way to address manipulation of aspects of funding
8 policy. That's one thing. And then separate from that
9 idea is the notion that there should be a somewhat
10 requirement for an independent review on the part of the
11 employer of any information that's being provided, that
12 would result in a benefit increase.

13 I just -- I think what you're hearing is, these
14 two sentences don't seem to say what you want and,
15 therefore, in the words of our august mayor, look goofy.

16 MR. BRANAN: Well, we can't have that.

17 CHAIR PARKSY: Bob?

18 MR. WALTON: A couple observations, thinking
19 about this a little further.

20 This recommendation deals with benefit
21 improvements. And I assume you're talking about
22 retirement benefit improvements.

23 MR. BRANAN: Yes.

24 MR. WALTON: As I recall, I believe it was
25 about 1981, it was the first year that the state had

1 adopted -- were asked to adopt negotiated MOUs with state
2 bargaining units. And I think it was 1981. The
3 Legislature, in their wisdom, had to fund those MOUs.
4 And in doing so, they added language in law that said,
5 "We'll only fund these MOUs" -- and they didn't have
6 anything to do with retirement benefits. They had salary
7 increases and other things. But the Legislature said,
8 "We'll only fund these if the CalPERS board reduces the
9 state contribution to the retirement system by the cost
10 of these other things."

11 Well, that had nothing to do with the
12 retirement benefits, but that was a clear quid pro quo.

13 CHAIR PARKSY: Correct.

14 MR. WALTON: So it's beyond just retirement
15 benefit improvements.

16 On the other time, in 1991, when the one-year
17 final comp, which was used as an example here, the State
18 wanted to go from a monthly to a quarterly payment. And
19 in exchange for that, they offered a one-year final comp.
20 Now, there was other moving parts to that, but, in
21 essence, those were the two primary issues, as I recall.
22 And that was adopted.

23 Then later, the State Legislature/Governor
24 unilaterally extended the payment schedule from quarterly
25 to semi-annually, and eventually to annually, one-year

1 paying in arrears. Now, that was litigated. And in the
2 court finding, the question was, where should they move
3 back to? Should they go all the way back to monthly?
4 And as I recall the court ruling, their words were, in
5 effect, "No, they only have to go back to quarterly."
6 Because in going from monthly to quarterly, that was
7 arguably a take-away from the members. That arguably the
8 system wasn't as well-funded on an ongoing basis as it
9 was when they made monthly payments. But they got a
10 benefit improvement for that, so it balanced it.

11 Under law, you can't take away a retirement
12 benefit unless you give something of equal or greater
13 value in return. And the court said it was of equal or
14 greater value.

15 So here, you had to have a case where you had
16 to have the quid pro quo, or both sides wouldn't have
17 gotten what their ultimate objective was. So I don't
18 know how you address that in a statement like this.

19 I think we all know what we'd like to see, it's
20 just going to be very difficult to define in the words,
21 I think.

22 CHAIR PARKSY: Matt?

23 MR. BARGER: In reading these examples, they're
24 all based around actuarial assumptions that were changed.
25 Here, you're being asked to change the actuarial value of

1 the assets or, you know, they all revolve around that, to
2 just say --

3 MR. BRANAN: I think the payment schedule in
4 the City of San Diego was involved in that one. Changing
5 the payment schedule for a benefit increase.

6 MR. BARGER: Because I would draw a distinction
7 between the two, honestly. One is, you know, you're
8 changing -- and it gets to the credibility and the
9 transparency -- you're just changing what is supposed to
10 be sort of to be assumed to determine the calculations
11 for political reasons. But that bothers me a lot more
12 than, honestly, the state determining that, you know, it
13 doesn't have enough money this year and it's going to
14 change the law and the city or whatever, that that's what
15 it's going to do. I don't think that's so great, either;
16 but I don't think it's as corrupt as the first one.

17 CHAIR PARKSY: So you'll take a shot at
18 changing that around?

19 MR. BRANAN: Yes.

20 CHAIR PARKSY: Okay, before we break here, I
21 just wanted to come back -- Matt raised a couple of
22 issues in previous discussions; and I just want to see,
23 Tom, how we can -- where we might consider addressing
24 those.

25 Are you familiar with what Matt had raised

1 about the disclosure of liabilities using financial as
2 well as actuarial discount rates?

3 MR. BRANAN: Yes, I am.

4 CHAIR PARKSY: Where would you recommend that
5 issue be addressed?

6 MR. BARGER: Discussed.

7 CHAIR PARKSY: Or discussed.

8 MR. BRANAN: I think we should do that at the
9 next hearing. That way, we'll have time -- rather, that
10 will still give us time to get a reaction and see if the
11 Commission wants to come up with something in writing.

12 MR. BARGER: And just to be clear on what it is
13 that I'm suggesting, I'm not suggesting that financial
14 valuations replace actuarial valuations. It's similar to
15 my comment about analysis of sensitizing health-care
16 inflation.

17 I think looking at these things more than one
18 way, to my way of thinking, is appropriate and, you know,
19 whether or not it falls within the purview of an advisory
20 committee on actuarial standards or what, but just some
21 sort of best practice that there's probably more than one
22 way to evaluate these things.

23 MR. BRANAN: That's something like the New York
24 model?

25 MR. BARGER: Yes, like the New York City model.

1 CHAIR PARKSY: And, Matt, I had interpreted
2 that question or comment to be just that, that it would
3 be additive.

4 MR. BRANAN: Yes.

5 CHAIR PARKSY: It's not replacing anything.

6 In the New York City model, it is additive; is
7 that --

8 MR. BRANAN: That's correct.

9 CHAIR PARKSY: Well, I don't see -- I mean, I
10 think we should discuss it and maybe put something
11 forward that would be in the form of a recommendation.
12 But it seems to me that it's something that we ought to
13 really think about including.

14 MR. BRANAN: We'll have that ready for the next
15 hearing.

16 CHAIR PARKSY: Okay.

17 Matt, is there anything else that you had on --
18 I know that we're going to talk a little bit about
19 composition of retirement boards.

20 MR. BARGER: The qualifications, yes.

21 CHAIR PARKSY: That will come up this
22 afternoon.

23 MR. BARGER: Actually, I don't have my e-mail
24 in front of me. But did we cover the other one? I can't
25 remember what the other one was.

1 MR. BRANAN: You and I spoke about it this
2 morning.

3 MR. BARGER: Yes.

4 CHAIR PARKSY: All right, if that -- I think
5 that we can take a 30-minute break now for lunch and then
6 come back and address the items that are listed
7 afterwards.

8 Thank you.

9 *(Midday recess taken from 12:12 p.m.*
10 *to 1:00 p.m.)*

11 CHAIR PARKSY: We can begin our afternoon
12 session.

13 Tom, are you ready for us, or are we ready for
14 you?

15 MR. BRANAN: That remains to be seen,
16 Mr. Chair.

17 CHAIR PARKSY: Well, you were definitely a
18 challenge this morning. We'll see what happens this
19 afternoon.

20 MR. BRANAN: The sun is out.

21 DR. GHILARDUCCI: Spiking is easy.

22 CHAIR PARKSY: And hopefully we can get through
23 these recommendations.

24 I do want to come back and make sure the
25 Commissioners -- we clarify a little bit of the

1 statistical information relating to the prefunding issue,
2 which was a little bit confusing in the last meeting, and
3 so I'd ask the staff to be ready to clarify that.

4 DR. GHILARDUCCI: That's right.

5 MR. BARGER: Gerry, didn't we skip over also
6 the question about medical?

7 CHAIR PARKSY: Yes. There is one area that we
8 need to come back on. And I didn't have it in mind here;
9 but if we have time, we can come back to that. Or I know
10 you had it on either the next meeting or the last
11 meeting.

12 I think I'd like to save the last meeting some
13 extra time. So we'll get it in next time, if we don't
14 have it here. That's the one item we didn't cover in the
15 last agenda.

16 MR. BRANAN: Oh, cost containment? Yes, that's
17 on at the next hearing.

18 CHAIR PARKSY: At the next hearing? Okay.

19 Let's move ahead with the next item.

20 MR. BRANAN: The next item is pension spiking.

21 CHAIR PARKSY: Well, it's an overall heading;
22 right? I mean, we were going to have actions which hurt
23 the retirement system credibility; is that --

24 MR. BRANAN: That's correct.

25 CHAIR PARKSY: It under that category?

1 MR. BRANAN: And under that category was
2 spiking and disability abuse or fraud.

3 CHAIR PARKSY: Okay.

4 MR. BRANAN: For spiking, spiking is generally
5 seen as the intentional inflation of final compensation
6 so as to increase the retirement benefit. And I might
7 add, that's almost always done without proper funding.

8 "It is easier and more effective to spike final
9 compensation when the final compensation period used to
10 calculate a pension is shorter rather than longer."

11 "Responses from the Los Angeles County
12 Employees' Retirement Association or system, CalSTRS" --
13 we have two CalSTRS - "and CalPERS, to the 'Thirty Ways
14 to Spike Your Pension' document provide examples of
15 symptomatic procedures adopted by the major retirement
16 systems to control spiking."

17 And I should say that that document, "Thirty
18 Ways to Spike Your Pension," was handed out at a previous
19 hearing by Ted Costa, who was representing a group known
20 as People's Advocate.

21 Finally, "Spiking, while not eliminated
22 completely, is now a less serious problem than it was
23 earlier.

24 Spiking recommendations: "Since spiking most
25 often takes place shortly before retirement, the inflated

1 benefit which spiking produces is usually unfunded.
2 Historically, it's been primarily a management abuse."

3 Number 10, "Retirement systems and public
4 agencies should be open and transparent concerning what
5 elements are included in final compensation for
6 management."

7 CHAIR PARKSY: Okay, comments?

8 You like it?

9 MR. LIPPS: Yes, I do.

10 CHAIR PARKSY: That's good.

11 And do you think it's properly -- there was a
12 comment about how we position this issue, not just out
13 there, but within this overall category of what hurts
14 credibility, which is, I think, important that the
15 Commission, to the extent that we're aware of things,
16 highlight.

17 So no objections? Comments?

18 Yes, Mr. Mayor?

19 MR. PRINGLE: Well, I guess I'm having a hard
20 time understanding what we're recommending. We're
21 recommending that the retirement systems and public
22 agencies hold open and transparent benefit formulas or
23 retirement structures?

24 I mean, under the definition of the word
25 "recommendation," I would say we're asking -- we're

1 suggesting something should be done; and I guess I don't
2 see what we're asking should be done.

3 CHAIR PARKSY: Well, again, I think you have to
4 start with at least what is being suggested as --
5 although there's no hard and fast definition of
6 "spiking" -- that the underlying concept here is final
7 compensation is at the heart of where, quote, "spiking"
8 comes into play.

9 And I think Tom or the staff was suggesting
10 that the way to address this, quote, "abuse," is to make
11 sure that there is a clear recitation of all the elements
12 that are in compensation.

13 Is that where you're coming from?

14 MR. BRANAN: That's correct. And I think you
15 have to appreciate the history of this problem.

16 Spiking used to be a very serious problem. And
17 the way it was usually done was by hiding elements that,
18 at the last minute, went into final compensation.

19 So we kind of have a recommendation that does
20 come after the fact where the retirement systems have
21 dealt with spiking and have -- it will never go away.
22 Humans are very creative.

23 But it has been greatly reduced. And the
24 retirement systems have systematic procedures in place to
25 catch it.

1 And so what we are really --

2 MR. PRINGLE: Are we -- some of those are
3 articulated, I guess, in the fuller draft; right?

4 MR. BRANAN: That's correct.

5 MR. PRINGLE: I just would like to offer a
6 suggestion, that some of those that have been adopted --
7 I mean, why would we not suggest those are best practices
8 for openness and transparency for retirement systems to
9 guard against abuses or something, so that at least there
10 is something here?

11 I just view at some point in time people will
12 pull all our recommendations out and say, "Okay, what are
13 the recommendations of this Commission."

14 And this one, on an issue that is contentious
15 and public and out there, without demonstrating any meat
16 behind the bone, I think it might just look hollow. And
17 I think what you're suggesting is, there's a lot of
18 things that have already taken place. Maybe we mention
19 in one sentence what some of those have been as examples
20 of openness and transparency that have eliminated that by
21 many, the potential for improper spiking of a pension.

22 MR. BRANAN: We could do that easily. There
23 are several good examples.

24 MR. PRINGLE: Okay.

25 CHAIR PARKSY: Bob?

1 MR. WALTON: I think, Tom, correct me if I'm
2 wrong, but -- we're just talking about Recommendation
3 Number 10 now?

4 CHAIR PARKSY: Right.

5 MR. WALTON: A recent example took place here
6 in the City of Sacramento, well-publicized. And the
7 City, they gave a pay increase to their chief of police.
8 And they reported that because the chief was only going
9 to be on employment for a short length of time, while it
10 was a big increase on an annual pay level, it was only
11 going to, quote, cost the City like \$8,000 because he was
12 only going to be here for this period of time; where, in
13 fact, because that increased his final compensation for
14 retirement purposes, the cost to the City is going to be
15 substantially more than that. And reporting that
16 substantial cost to the City is being more transparent.
17 That's the sort of thing that you're talking about here.

18 MR. BRANAN: That's correct. And had this
19 happened, say, before 1994, it may well have gone
20 unnoticed. But in this case, that person is a member of
21 PERS. And PERS has both a computer system and a human
22 manual check, both of which would catch this.

23 MR. PRINGLE: Excuse me, if I may,
24 Mr. Chairman.

25 It catches that unusual increase in final

1 compensation, and it stops it?

2 MR. BRANAN: I think it's worth noting, I
3 specifically asked PERS, STRS, and LACERA, when you do
4 catch this, are you authorized to deny them? And all
5 three have the statutory authority, and report that they
6 regularly do deny things that don't fall within their
7 acceptable practices.

8 MR. PRINGLE: Therefore, under this,
9 Mr. Chairman, I would like that to be a recommendation,
10 that that is a best practice, that is something that
11 needs to be in place for all retirement systems. And if
12 it is particularly on those large three, shouldn't
13 others -- we don't know if it is on others. And it may
14 be of value to specifically point that out, particularly
15 for the public who is going to be looking at this, and
16 looking at this section to see if those issues have been
17 addressed.

18 CHAIR PARKSY: Is that -- Paul?

19 MR. CAPPITELLI: Just a question. And it's
20 addressed here in your supporting documentation, but just
21 for clarity: There were a number of items that were
22 identified on the list that was presented to us that are,
23 in fact, considered as part of case law or other
24 decisions, they are considered in somebody's final
25 compensation. And it's not an abusive practice, it's

1 something by which they are entitled to, either through
2 collective bargaining or through the court process or
3 otherwise; correct?

4 MR. BRANAN: That's correct.

5 MR. CAPPITELLI: So will that be embedded in
6 our final report, too, or do we need to call attention to
7 that somehow?

8 MR. BRANAN: Both in this background material
9 and then in an appendix that will be in the final report,
10 that point is made.

11 As I noted in here, more than PERS or STRS or
12 any of the independent systems, the '37 Act system's
13 guidelines for what is acceptable for reporting as final
14 comp has been set out by the courts.

15 For PERS and STRS there have been court cases,
16 but primarily, it's been set out by the Legislature.

17 But they all -- now, those two processes have
18 come up, in some cases, with different items, some that
19 are acceptable in one system and not in another. But it
20 is systematic within the systems.

21 MR. CAPPITELLI: Thank you.

22 CHAIR PARKSY: Do you think you have enough
23 guidance here now?

24 I do think the way the recommendation reads
25 now, people wouldn't naturally link it to what you're

1 driving at here.

2 MR. BRANAN: We have some very good examples
3 that I'll include there.

4 CHAIR PARKSY: Okay, all right, keep going.

5 MR. BRANAN: "During current bargaining between
6 the State and its employees, almost all bargaining units
7 which have settled, have approved a return to a
8 three-year final compensation from a one-year final
9 compensation period."

10 Recommendation 11: "The three-year final
11 compensation period recently bargained at the state level
12 seems to be a best practice for discouraging pension
13 spiking. When local agencies with a one-year final
14 compensation period are engaged in the collective
15 bargaining process, the Commission recommends that they
16 bargain a return to a three-year final compensation
17 period.

18 CHAIR PARKSY: Okay, yes, Jim?

19 MR. HARD: Well, you were starting on the
20 right. We can start right here?

21 CHAIR PARKSY: I can start wherever you like.

22 MR. HARD: I'd like you to start right here.

23 CHAIR PARKSY: That's okay.

24 MR. HARD: My experience over the last 32 years
25 in public service doesn't give me any insight into the

1 vast majority of public employees having any spiking of
2 their -- in the rank and file out of management of their
3 pensions whatsoever. I don't know anybody that it's ever
4 happened to, and I certainly don't -- this last thing, of
5 moving from one year to three years was negotiated, and
6 it was negotiated in a complex negotiation with a lot of
7 other factors involved.

8 And, frankly, I read your background material,
9 and somebody from state management told somebody at
10 CalPERS that that was about spiking, and that it was
11 about a public perception. But my recollection -- and I
12 was involved in some of that -- is spiking was never,
13 ever an issue in what I heard at the bargaining table.
14 It was not an issue at all, ever. It was a matter of
15 saving the state money.

16 Pay raises for a hundred thousand employees has
17 nothing to do with their final compensation. They may be
18 in their second year of employment, they may be in their
19 32nd year of employment.

20 You know, I don't -- I know in your background
21 also it says something about this has occurred in
22 bargaining units; and I don't challenge that at all. I'm
23 curious to hear about it because I'm unaware of it. It
24 may well have happened, I don't know. Not in my
25 experience, though.

1 So I'm completely opposed to this. This is --
2 it isn't necessarily any kind of best practice,
3 particularly when I don't see any evidence that it
4 happens with rank-and-file workers.

5 If it happens with management people -- which
6 I've read in the newspapers enough to know it happens --
7 that's one thing. But I don't understand how the
8 negotiation of the calculation of the final compensation
9 for purposes of retirement could be considered spiking
10 when you have a hundred thousand people. You are
11 negotiating for six months of -- one month of employment
12 to who-knows-how-many years. So I don't think this is a
13 very appropriate recommendation from this Commission to
14 direct people how to do their collective bargaining
15 across the state.

16 CHAIR PARKSY: Well, I guess the real question
17 is, does the Commission want to address this one-year
18 versus three-year; not necessarily indicating that there
19 is, quote, "*spiking*" going on anywhere. But is it a
20 practice that, among other things, would certainly be a
21 buffer, if you will, toward any spiking at any level that
22 may occur?

23 MR. HARD: Well, I guess it might, except for
24 I just heard an example of a one-month spike in
25 Sacramento that appeared to be, like, \$8,000, and has

1 much bigger ramifications. And that's less than a year.

2 So I don't know where this would go in the end,
3 but it doesn't sound like a place that I think we should
4 go.

5 CHAIR PARKSY: Yes?

6 MR. CAPPITELLI: I think Commissioner Walton
7 really summed it up. Maybe this issue is not
8 best-addressed here. It speaks to the broader issue,
9 which has to do with the future liability that could be
10 considered unfunded, as opposed to it being a spiking
11 issue. I'm talking one-year versus three-year.

12 And if perhaps that would make it more
13 palatable, we could address it there. But I think maybe
14 that's the bigger issue here as opposed to where it
15 belongs to.

16 CHAIR PARKSY: Do you mean, keep the
17 recommendation --

18 MR. CAPPITELLI: Yes.

19 CHAIR PARKSY: -- but not have it suggested as
20 part of a spiking abuse issue?

21 MR. CAPPITELLI: Yes, because, you know,
22 spiking -- if you go -- if you look at what it is we're
23 trying to get to the root of here, when you're talking
24 about spiking, we're talking about something that has to
25 do with something that appears to be a gift or something

1 that's granted at the eleventh hour, for which there's no
2 future funding to back it up or to support it, which
3 means that somebody has to pay for it out of the system
4 somewhere. So maybe it's more palatable if the
5 recommendation lies somewhere else within the report, but
6 not here.

7 CHAIR PARKSY: Lee? I know you were poised.
8 So go ahead.

9 MR. LIPPS: For the record, I'm -- forgetting
10 the issue of spiking, I don't think it should be linked
11 to spiking whatsoever. Even to imply that somehow
12 final-year compensation provisions encourage spiking in
13 some fashion, I find problematic. But for the record,
14 I'm opposed to moving away from what the current
15 final-year compensation provisions are in various
16 agencies.

17 It seems to me entirely appropriate --
18 particularly when we're talking about the employee ranks,
19 particularly where many of them in this state are subject
20 to collective bargaining agreements, you're not going to
21 get a significantly large increase in any particular year
22 that is going to jump up somebody's pension more than 2,
23 3, 4 percent. Just mathematically, it just doesn't work.

24 I don't see any need for this whatsoever.

25 CHAIR PARKSY: Well, again, taken outside the

1 context of spiking --

2 MR. LIPPS: I am.

3 CHAIR PARSKY: -- then the question is, is it
4 sound policy or not?

5 MR. LIPPS: No, I don't believe it is.

6 CHAIR PARSKY: Bob?

7 MR. WALTON: Yes, I was probably troubled by
8 this recommendation more than any other. I think it
9 would be symbolic, at best, it's no different than this
10 Commission recommending changes in retirement formulas or
11 anything else.

12 I think fundamentally the consensus has been,
13 at least that I've heard, that your retirement benefits
14 are part of your total compensation, and it's up to the
15 local government and their respective employee
16 organization to decide how best to compensate. If their
17 decision is to base retirement on one-year final comp,
18 that ought to be their option.

19 I think if you want to address spiking -- which
20 I think is a problem -- this isn't the way to do it.
21 There's better ways to address spiking. For instance --
22 and I'm not suggesting this, but just as an option -- you
23 simply limit how much your compensation goes up during
24 your final-comp period to a set percentage.

25 There's other states that have done that. It

1 eliminates spiking all together, whether it's one-year --
2 you can have spiking with three-year final comp. It just
3 lessens the effect of it, but you can have it.

4 So it really doesn't address it, only from a
5 public-perception perspective only. So if we want to
6 address spiking, which I think we should, I think this is
7 not the right way to do it.

8 CHAIR PARKSY: Teresa?

9 DR. GHILARDUCCI: The reason why ERISA and
10 most personnel best practices discouraged one-year
11 compensation, is actually to prevent employers from
12 artificially lowering the wage of an older worker right
13 before they retired. It was mainly to prevent the abuses
14 on the employer's side to demote or lower the hours, so
15 that you had an artificially low salary before you
16 retired.

17 And it also seems that the consensus is that
18 it's distortionary to have your benefit only rely on your
19 last year's salary, when the pension is supposed to
20 reflect your buying power and your standard of living
21 throughout your life.

22 So I think it's a bad idea to have one-year
23 comp. I can't think of a situation -- that doesn't mean
24 there isn't, but I can't think of a situation where it's
25 ever a good policy to have it on one-year comp because it

1 encourages all sorts of distortionary behavior, both on
2 the employer and employee's side.

3 However, whether or not we should go so far as
4 to say what the benefit formula should look like seems to
5 be beyond what we would do here.

6 CHAIR PARKSY: Well, but consistent with what
7 you were just saying, though, you would make a
8 recommendation that highlighted the inappropriateness of
9 one-year?

10 DR. GHILARDUCCI: Yes, for all sorts of
11 unforeseen consequences, that it could be distortionary.
12 And one of them could be spiking, but it could also
13 encourage bad behavior on the employer's side.

14 CHAIR PARKSY: Bob?

15 MR. WALTON: Just a point of reference, that in
16 California -- I know CalPERS as well as '37 Act, while
17 it's commonly called "*final compensation*," your benefit
18 is based on your highest consecutive 12 or 36 months. It
19 can be any, 12 or 36 months. Whether it's your final one
20 or not is irrelevant. It usually is, but it doesn't have
21 to be.

22 CHAIR PARKSY: Usually it's the highest?

23 MR. WALTON: It's the highest consecutive 12-
24 or 36-month period, depending on whether you're under
25 one-year or three-year.

1 MR. HARD: Which eliminates the management.

2 MR. WALTON: It can be any period, as long as
3 it's consecutive.

4 DR. GHILARDUCCI: But it doesn't have any bite.

5 MR. WALTON: See, I think a policy from this
6 Commission that went to more -- a broader concept of to
7 discourage practices that inflate pensions, whatever that
8 may be, without mentioning one-year, but there's many
9 others that can do it.

10 DR. GHILARDUCCI: And one of them would be
11 this CalPERS review which discourages it. It's a
12 case-by-case --

13 MR. WALTON: Well, that's to uncover it. But
14 to do something in a nature that unjustly rewards through
15 retirement a person's compensation or something as --
16 it's very difficult to find the wording for it, but I'm
17 sure staff could take the task if we want to go that
18 direction.

19 CHAIR PARKSY: It seems that there are kind of
20 two concepts. One concept is to shine a light on, or
21 disclosure of what compensation by definition is.

22 MR. WALTON: Correct.

23 CHAIR PARKSY: And that is inherent in some of
24 the changes you'll make in Recommendation 10.

25 Then the only question is, do we want to go

1 farther than that and indicate something more specific
2 with respect to these calculations.

3 And I gather that this Commission is not
4 inclined in that direction other than people wouldn't
5 want to indicate that the one-year is something that
6 ought to be reconsidered or -- make a statement about
7 one-year?

8 MR. WALTON: I'm opposed to the one-year. But
9 I think a statement about compensation practices that
10 unduly reward those that are ready to retire -- for
11 instance, I didn't want to get into this detail, but I
12 know one public agency under CalPERS has 120 different
13 forms of special compensation. I know an agency in
14 CalPERS that has a special comp called "bell-ringing
15 pay." And that every hour they ring the bell and they
16 get a special comp for that purpose, that's reportable
17 under the law in CalPERS; and they assign that duty to
18 the senior-most person in order to increase their
19 retirement.

20 Now, that has nothing to do with --

21 MR. PRINGLE: Is it a physical bell?

22 MR. WALTON: What's that?

23 MR. PRINGLE: Is it a physical bell?

24 MR. WALTON: It's a physical bell.

25 DR. GHILARDUCCI: What?

1 MR. WALTON: It's a physical clock that they
2 wind that they get clock-winding pay. Those are the
3 types of things that you ought to be concerned about.

4 MR. PRINGLE: I think someone could add 32 ways
5 to --

6 DR. GHILARDUCCI: Yes, 32.

7 CHAIR PARKSY: Tom, do you have a comment?

8 MR. BRANAN: Well, it sounds like what the
9 Commission would be more comfortable with is expanding
10 Number 10 --

11 CHAIR PARKSY: Right.

12 MR. BRANAN: -- to talk about, in some
13 partially, more general concepts of spiking; and then
14 also specific points that can be made showing how
15 retirement systems have taken it upon themselves to
16 identify the items that should not be reported and to
17 deny them. Because, really, that's the point that we
18 wanted to make. Spiking was a very significant problem
19 leading up to the early nineteen nineties.

20 It will always go on, but the magnitude of it
21 has really dropped due to these kinds of actions by this
22 retirement system.

23 CHAIR PARSKY: The actions taken.

24 MR. HARD: Can I ask a question?

25 MR. BRANAN: Yes.

1 MR. HARD: Bob was reminding me that it's
2 really not your last 12 months; it's the 12 months of
3 highest compensation. It could have been five years ago.

4 Is that the case in the local agencies, cities,
5 counties? Is that the same?

6 MR. BRANAN: For --

7 MR. HARD: Is that the same rule of --

8 MR. BRANAN: Yes, I believe it is.

9 MR. HARD: -- either 12 or 36 months?

10 MR. BRANAN: Yes.

11 MR. HARD: So it's not really the last
12 12 months, anyway?

13 MR. BRANAN: It's not -- it's just a term
14 that's used, "final comp."

15 MR. HARD: Right.

16 MR. BRANAN: But it doesn't have to be -- it
17 often is your final compensation because you're at the
18 end of your career, but it doesn't have to be.

19 MR. HARD: Right. And normally, it probably
20 would be.

21 I don't want to go too far down this road; but,
22 I mean, the fact of the matter is, if you're going to
23 talk about the number of years and all that, you could
24 also talk about the negotiated general salary increase
25 that employees, through their bargaining process, might

1 achieve. I mean, that will change their retirement if
2 they stick around and that happens to be their highest
3 year. So I just think it's not the right road to go
4 down.

5 MR. BRANAN: I think that I get that is the
6 sense of the Commission; and we will not pursue
7 Recommendation 11.

8 CHAIR PARKSY: Okay.

9 Yes, Matt?

10 MR. BARGER: Actually, I didn't have a chance
11 to look at these before, but I'm sure in paging through
12 the responses of LACERA and PERS in terms of specific
13 actions they've taken to address the things -- that they
14 can address. Some of this is court actions and saying,
15 "I'm sorry, you do have to count that." I wonder, rather
16 than just that bald statement about is ten -- whether or
17 not more exhaustive commentary about actions that are
18 taken and examples of best practice or something to make
19 that a little beefier. Because I don't think it really
20 matters whether or not there's more or less going on than
21 ten years ago. I think all you really need are a couple
22 of headlines like this and some stories like Bob's to
23 just cast doubt about the credibility of the system. I
24 think, you know, coming out firmly and strongly with a
25 fair amount of detail about, "We're against this, here

1 are things that are being done that we recommend as best
2 practices," et cetera.

3 MR. BRANAN: I think that's the direction we've
4 gotten.

5 CHAIR PARKSY: I think that's where you should
6 go here.

7 MR. BRANAN: And I would point out one
8 difference. In the case that Mr. Walton brought up, had
9 this come out 20 years ago, there would have been no
10 remedy for it because there were no real guidelines.
11 Whereas now, even though it does get the press, also in
12 some of these reports, it's been brought up that just
13 because he got that doesn't mean it's going to show up in
14 his pension; that that's a decision PERS makes. So
15 things have changed.

16 MR. BARGER: Although that's only true for
17 PERS; correct?

18 MR. BRANAN: No, that's true for STRS, the
19 teacher's retirement, and the '37 Act as well.

20 MR. PRINGLE: Mr. Chairman?

21 CHAIR PARKSY: Yes?

22 MR. PRINGLE: One point. I guess I thankfully
23 am not in Sacramento enough anymore to regularly read
24 The Sacramento Bee. But, in fact --

25 CHAIR PARKSY: Except when you are in

1 Sacramento?

2 MR. PRINGLE: Of course, I would read it when
3 I'm up here.

4 But just a question. I guess I don't
5 understand the whole -- even the police chief's example.
6 That would be his 12 months' highest compensation under a
7 CalPERS model. Therefore, how would one month worth of
8 that have, as you all had suggested, a dramatic effect on
9 his overall retirement benefit?

10 I'm just trying to see if there's --

11 MR. WALTON: It increases his, quote, unquote,
12 "final comp," depending on how long he's paid that
13 amount.

14 Keep in mind, there's other moving parts.
15 Let's assume the person in question has six months' worth
16 of vacation pay. Well, that higher salary now is applied
17 to vacation pay. And while they may physically end
18 today, they don't retire for six more months. And that
19 pay at the higher range is reported for that six months.

20 So there's other moving parts here that affect
21 the person's, quote, unquote, retirement.

22 MR. PRINGLE: But in this case, was there any
23 three-year averaging retirement on --

24 MR. WALTON: I think there's one year for the
25 City of Sacramento, if I'm not mistaken. Somebody can

1 correct me if I'm wrong.

2 There's other ways to do it. This is just one
3 example.

4 Public agencies, especially at the management
5 level, have the ability to reward sick-leave credit to
6 their managers. While under the retirement law, an
7 agency can contract to give retirement benefits for
8 unused sick leave. Well, you simply give a person more
9 sick-leave credit before they retire, and all of a sudden
10 that's converted to a retirement benefit.

11 MR. PRINGLE: In all of this level of
12 discussion, it is interesting, but much of these are
13 management-level employees that would have -- I mean, the
14 difference between our bargained employees and management
15 employees, there is probably a different way in which
16 some of that could be applied.

17 I could understand maybe someone working in a
18 public-safety position where you did have great access to
19 overtime and other things like that; but that's
20 self-inspired additional work to boost your --

21 MR. WALTON: Well, overtime isn't included in
22 those.

23 MR. PRINGLE: Oh, is that right?

24 MR. WALTON: It's not.

25 MR. PRINGLE: So in terms of many of these

1 examples, what would you say the percentage would be in
2 terms of management employees versus non-management
3 employees?

4 MR. WALTON: My experience is the vast majority
5 are management employees outside the bargaining process.

6 MR. PRINGLE: Well, see, I think, Mr. Chairman,
7 there is a way to get something like this, and maybe even
8 something stronger without stepping on the toes of
9 bargaining units that feel that they have a right to have
10 these discussions. Because I think we should separate
11 the two issues and say, you know, many of these issues
12 are bargainable issues if you're a bargaining employee.

13 But in the cases of management employees, where
14 spiking has been historically defined as a greater
15 problem, these types of things -- local agencies, state
16 agencies, should not allow these types of things to take
17 place, and there should be a greater averaging over a
18 longer period of time of the definition of "final
19 compensation."

20 I think we should say something like that
21 without, again, making it look like we're trying to
22 interrupt the collective bargaining process. Because I,
23 too, often think it's awfully hard for a collectively
24 bargained employment position to overstep too many of
25 these bounds, yet we see how easy some of that could

1 occur in a separate management spot where two or three
2 people can set your salary -- or one person -- a city
3 manager could set the salary of every department head.
4 And if there are two or three of those department heads
5 choosing to retire that year, they could be overly
6 augmented through that salary system and create that
7 spiking level.

8 I do think there may be value in separating
9 this.

10 CHAIR PARKSY: Well, maybe, again, you can
11 include in this recommendation -- or recommendations --
12 the acknowledgment of distinction between management and
13 others, and in addressing the ways in which abuses have
14 been dealt with include the notion of a longer period for
15 measuring final compensation.

16 If it has been adopted, it would show up on
17 your list of things that have been adopted.

18 MR. BRANAN: Yes, that would be good.

19 MR. CAPPITELLI: Should we define the term
20 "*spiking*"?

21 MR. BRANAN: Well, that's -- I think the
22 working definition that LACERA, STRS, and PERS have is --
23 and it's not precise -- but it is an increase in final
24 compensation for the primary reason of increasing the
25 pension, okay.

1 Now, and what they look at, is this thing part
2 of a systematic program? Like, bonuses are acceptable,
3 but they have to be part of a well-defined,
4 described-on-paper bonus system. And it can't be that,
5 in reality, the only people that get the bonuses are the
6 management people just ready to retire. So there are
7 definitions, but usually it's a general definition and
8 then with lots of specifics under it to catch the
9 specifics.

10 MR. CAPPITELLI: Because I think what I would
11 like to see is -- I know in a prior hearing we had a
12 conversation about whether or not it should be called
13 "spiking" or something else.

14 MR. BRANAN: Right.

15 MR. CAPPITELLI: But I think if we're going to
16 call it "spiking," we need to define what it is we're
17 talking about. And I think that's a good starting point.

18 But the broader definition is that it's not
19 only that, but it's anything that could have an adverse
20 impact on this system, and then include the public
21 perception, the credibility element to that, too. But I
22 think that's what we're talking about here, is all of
23 those things.

24 And then if you make that all-encompassing, I
25 think all these recommendations that we're discussing

1 here would fall right into that, and people would be able
2 to read it and see exactly where it fits.

3 MR. BRANAN: I'll go back to the three
4 retirement systems that helped us with this and see if we
5 can come out with a generally acceptable definition.

6 MR. CAPPITELLI: Okay, thank you.

7 CHAIR PARKSY: Okay, move on, Tom.

8 MR. BRANAN: The next topic under this general
9 issue is "Disability Retirement Reform."

10 "Within the '37 Act, each county retirement
11 board rules on disabilities within its own system. The
12 CalSTRS board decides on disability applications in that
13 retirement system."

14 "Prior to 1975, CalPERS made disability
15 determinations for all state, school, and public agency
16 members, as well as the decision of whether disabilities
17 were the result of a job-related injury or illness for
18 state and local safety members."

19 "After 1975, responsibility for disability
20 determinations for local safety members was statutorily
21 changed to local public agencies."

22 "Consequently, there can be significant
23 differences between employers as to what constitutes a
24 '*disability*.'"

25 And probably a better way to say that is, there

1 are significant differences in the interpretation by
2 employers as to what constitutes a disability.

3 These are out of order, actually. I'd rather
4 take 13 first.

5 "Legislation should be introduced to return to
6 decision-making authority for CalPERS local safety member
7 disability determination to the CalPERS board."

8 CHAIR PARKSY: Okay, Lee?

9 MR. LIPPS: I think my comments are sort of
10 overarching in terms of the whole question of why are we
11 taking up disability reform in the first place.

12 As I understand it -- and perhaps I can be
13 corrected if I don't understand correctly -- anything
14 that we have here, there's no difference in terms of the
15 impact on the retirement system whether somebody goes out
16 on a regular retirement or a disability retirement. As
17 I understand it, the difference is that if you're on a
18 disability retirement, if you're a public safety officer,
19 for example, then half of your retirement is tax-free and
20 the other half is taxable.

21 In other public employee categories, it may not
22 be half, it may be some 40 percent or 30 percent is
23 tax-free. But the impact in terms of the disability
24 reform or the impact of the disability retirement is
25 really on the state in its losing some tax revenue, which

1 is very, very different than I think that we've been
2 charged with.

3 I don't really -- as much as we'd all like to
4 curb abuses and fraud and things like that, where we see
5 them, I don't see this whole package of items as
6 something that falls under our charge.

7 CHAIR PARKSY: Well, the theory was -- and we
8 certainly can be responsive to that -- but the theory was
9 that things that hurt the credibility of the system, are
10 things that we should be reporting on, we should be
11 commenting on, we should be identifying practices that
12 try to address this. That was the underlying theory.

13 And I think, to some extent, disability fraud
14 or disability abuse is within that.

15 Is that your --

16 MR. BRANAN: Well, that's part of it,
17 Mr. Chair. But, actually, what you're saying is only
18 true if the person has served long enough to have a
19 comparable service retirement as to what they get for
20 disability. A safety member who is disabled on their
21 first day on the job qualifies for a disability pension.

22 Now, I agree, we're not talking about what --
23 it's not the place of the Commission to come up with a
24 checklist of what's a reasonable disability. But the
25 reason we're making this recommendation is, first -- and

1 it gets back to finances -- staff looks at pensions,
2 health care, all of it coming out of essentially the same
3 pot of money. So if there were savings on disabilities,
4 that would be money available for other benefits.

5 The reason we think this should go back to the
6 PERS board, as it once was, is the PERS board is the
7 fiduciary body of the system. When they look at a
8 disability application, they look at it, in my opinion,
9 on those items that should be looked at, and that is the
10 medical information.

11 What has happened at the local level, in some
12 cases, is those people making the decision are not
13 fiduciaries to the system. And a lot of personnel issues
14 and disciplinary issues get mixed up in the decision of
15 who should get a disability.

16 The system works very well at STRS. They have
17 an excellent disability program. They also have a very
18 tough program to get through and to show that you deserve
19 it. But it works very well.

20 And in the '37 Act, each '37 Act board makes
21 the decision for all disabilities of its members. And
22 that was the case in PERS. They still make all those
23 decisions except for local safety.

24 So we think it would be a much more rational,
25 defensible system if the PERS board had that

1 responsibility.

2 CHAIR PARKSY: Bob?

3 MR. WALTON: Tom, I'm not arguing for or
4 against what your recommendation is to agree somewhat --
5 or to agree entirely with what Lee said, looking at the
6 public perception, and the fact that a number, if not a
7 majority, in some cases, like Highway Patrol, are
8 disabilities for a person already eligible for a service
9 retirement. The public perception is that if there was
10 less disabilities, it would, quote, "save money," where,
11 in fact, it wouldn't. The cost to the system is the
12 same.

13 I think that needs to be made -- the public
14 needs to be made more aware of the situation and what's
15 actually transpiring.

16 The difficulty at least from a process
17 standpoint -- I know it's come up in the past -- on PERS
18 doing these determinations. Even under the current
19 system, we've had cases where public agencies -- and I'll
20 look for someone for PERS to correct me if I misstate any
21 of this -- have found a person disabled.

22 A person doesn't want to be disabled. They
23 want to work. And they've appealed to the PERS board,
24 and the PERS board has found them not to be disabled.

25 The bottom line is, though, the public agency

1 refuses to hire them back to work. So the member is put
2 in a no-man's or no-woman's or no-person's zone: Well,
3 they're not disabled but they have no job.

4 MR. BRANAN: Well, that's what I was talking
5 about.

6 MR. WALTON: Because that's part of the
7 problem. But you have to look at this in a larger
8 context of exactly what the problem is and what the best
9 approach is.

10 MR. PRINGLE: I think we should have a
11 recommendation to ensure that there's no no-person zones
12 created.

13 CHAIR PARKSY: Any other -- yes, Paul?

14 MR. CAPPITELLI: Yes. Okay, I think what the
15 issue here is that we're trying to address deals with
16 disability fraud or fraudulent-type actions; correct? I
17 mean, that's the overarching goal?

18 MR. BRANAN: Yes.

19 MR. CAPPITELLI: I'm not so sure that -- and
20 clearly, when you read through the abstract of the text
21 of some of these legislative proposals here, it does
22 address that. But I kind of struggle as to how Number 13
23 addresses that issue, how it really speaks to remedy
24 that. The others are clearer to me than 13 is.

25 MR. BRANAN: Well, our thinking on Number 13 is

1 that you take it out of an environment where many more
2 things than the question of disability get mixed in.

3 As Bob was saying, there are cases where
4 somebody is considered a difficult employee. And rather
5 than fire them, they find out they're disabled. I don't
6 think that happens at the PERS board level. They have a
7 much different perspective of why they're there, and a
8 much narrower range of what should go into the mix.

9 MR. CAPPITELLI: Okay. And I understand that.
10 I guess I just don't accept that notion. And as a
11 career public-safety management person, I would suggest
12 that those situations are far and few between.

13 In the broader sense, I think that the vast
14 majority of the decisions that are made at the level by
15 which they're currently made are probably made taking all
16 the same factors into consideration. But I think we need
17 to be careful over introducing recommendations that
18 somehow speak to a very small, limited amount of possible
19 things that could occur and forget about the broader
20 picture here. I just don't want to be on the record just
21 to say that I don't see how that recommendation speaks to
22 the issue of fraud. It's not as clear to me as the
23 others.

24 MR. HARD: Can I follow up, Tom, with that?

25 MR. BRANAN: Yes.

1 MR. HARD: He asked, well, how prevalent is
2 this.

3 I guess, do we have statistics? I mean, we
4 must have statistics on, like, convictions for disability
5 fraud. But how big is this problem? Even though I agree
6 that we should try to address perception of the public.
7 But do you have any statistics on this actual problem?

8 MR. BRANAN: Well, first -- and on both these
9 points -- 13, we're really not putting that forward as a
10 remedy for fraud, but, rather, it's an opportunity to
11 make that system more rational and more defensible.

12 As far as statistics, I don't think -- Bob
13 would know more than I -- I don't think I've seen --
14 I know I haven't seen those statistics. I don't know
15 if they exist. But that's something more that we were
16 going to discuss under 12.

17 MR. HARD: So can I reasonably conclude that
18 this is really about headlines in individual cases we've
19 seen and bad publicity about bad individuals in the State
20 of California?

21 MR. BRANAN: On 13?

22 MR. HARD: Disability fraud and trying to
23 address it, yes.

24 Well, 13 you said wouldn't address fraud.

25 MR. BRANAN: That's right, yes.

1 MR. HARD: And that's good, because I was
2 beginning to feel uncomfortable for the local boards and
3 agencies about their determinations on disability.

4 Yes, so that's what I mean. But there's no
5 statistics, but this is a problem because it's been in
6 the headlines for an individual or two or three or...

7 MR. BRANAN: Well, certainly those kinds of
8 things are in the headlines. And they're not rare as
9 such.

10 MR. HARD: Well, if you don't have statistics,
11 how do you know they're not rare? I really hope they are
12 rare, but I don't know.

13 MR. BRANAN: I don't know. I just mean they're
14 not rare in the media.

15 MR. HARD: They're not rare in the media?
16 Okay, got it. I agree.

17 MR. BRANAN: There's a steady flow of those.
18 That's not to say they are representational. But, no,
19 they do provide bad publicity.

20 MR. HARD: Absolutely.

21 DR. GHILARDUCCI: Gerry?

22 CHAIR PARKSY: Yes, Teresa?

23 DR. GHILARDUCCI: I feel uncomfortable with
24 some of the same reasons we all -- well, that's been
25 expressed here, making some determinations on disability

1 without any hearings on it or experts testifying here.
2 And I know it's a huge issue all around the world, you
3 know, where people are trying to deal with training,
4 return-to-work issues, unemployment insurance bleeding
5 into disability insurance. This is a huge issue. And so
6 I'm going to turn to you, Gerry, and ask if you can
7 defend or make a case for us, as Commission members,
8 whether or not we should include this within our purview?
9 Because if we do, we'll need more testimony and
10 experts -- at least I would.

11 So can you make the best case for this?

12 CHAIR PARKSY: Well, I think the best case can
13 be made around evaluating best practices.

14 DR. GHILARDUCCI: Yes, okay.

15 CHAIR PARKSY: Part of our charge is
16 identifying the magnitude of the obligations, presenting
17 best practices or approaches that have been taken that we
18 would endorse without necessarily applying it across
19 everything.

20 DR. GHILARDUCCI: And this is a post-employment
21 benefit?

22 CHAIR PARKSY: Right, exactly. That's where we
23 might want to include it. I think what everyone is
24 struggling with is how does it fit within this.

25 DR. GHILARDUCCI: I'm also struggling with I

1 don't know anything about it, about the disability
2 situation in the state. That's mainly what I'm
3 struggling with. We've had lots of testimony about all
4 sorts of other things, but this is really unfamiliar.

5 CHAIR PARKSY: Well, maybe what we ought to do
6 is to step back and think a little bit on the disability
7 if we really think that it's important to include, and
8 maybe we want to hear something more about it before we
9 finish. And if we don't, then I think we at least ought
10 to reference the fact that we didn't include it, even
11 though it's an area -- one of the two, it seems to me.

12 MR. BARGER: Gerry?

13 CHAIR PARKSY: Yes, Matt?

14 MR. BARGER: I wouldn't want to step away from
15 this one because I think it's sort of fascicled to
16 pretend like the money doesn't come out of the same pot
17 in the state.

18 And if you fund a bunch of pension -- and I
19 don't know if there's a bunch or not a bunch -- pension
20 promises and expect to get taxable income off of it and
21 you don't, it's going to affect the finances of the
22 pension system. I mean, it seems to me to be obvious.

23 Two, and just sort of anecdotally, things that
24 bug people and sort of call into question the repute or
25 the credibility of the system, the integrity of it, which

1 people have to believe in to continue to fund. This is
2 one of those things that keeps coming up. And to sort of
3 pretend like, oh, it's not an issue just because it's in
4 the headlines, that doesn't seem like a reasonable thing
5 to do, either. I mean, as long as there's even a handful
6 of examples of it that continue to cause a problem, not
7 addressing it just seems to be wrong.

8 How you exactly do it -- I understand Paul's
9 point of, you just picked on public safety officers as
10 the problem, and here's a recommendation to do it.

11 That isn't where I'm recommending going. I'm
12 much more, I think, we ought to acknowledge, disability
13 fraud is wrong, period. Two, to the extent there's some
14 best practices that can go to address it, we ought to
15 endorse those. To me, that would be the direction I
16 would want to head, not more --

17 CHAIR PARKSY: Not just key into safety?

18 MR. BARGER: -- narrow something to one group
19 or another personally.

20 CHAIR PARKSY: Bob?

21 MR. WALTON: Along those lines, in looking at
22 Recommendation 13 -- and it's hard to remove yourself
23 from 12, affecting that -- but an alternative to
24 Recommendation 13 is for us to consider that a process
25 for determining disability ought to include some best

1 practices, no matter where it's made, that do not take
2 into account personnel issues, discipline issues, saying
3 that and using the right words, as opposed to just
4 saying, "We'll move it from the local to PERS," but
5 saying "The process for determining disability retirement
6 needs to include these best-practice factors," whatever
7 those may be.

8 The difficulty going with what Jim indicated,
9 the "what is fraud" part of the recommendation you'll see
10 in 12 is, as I understood it at the time these were
11 drafted -- and I helped draft some of them -- in applying
12 for disability retirement, it's not fraud until you get
13 the money. So you can lie, cheat, and steal on your
14 application. If you're caught, it's no harm, no foul.
15 "Oh, I'm sorry, I lied." You haven't committed a fraud
16 yet. That's part of the definition -- which is
17 ludicrous, but that's how it works.

18 And so that needs to be changed to somehow
19 discourage that type of activity. But, again, that can
20 be part of the process, I guess.

21 MR. HARD: I would endorse, too, what Matt
22 said. I don't think we should ignore it. I just think
23 that moving it to CalPERS, one, without more context kind
24 of implies that the local boards kind of are suspect, and
25 then just moving it up to CalPERS; and then it really

1 doesn't address fraud unless CalPERS is better at
2 ferreting out fraud than other agencies. And I don't
3 know if that's factual, either.

4 But I think we should take the position out of
5 disability fraud, that we're against it.

6 MR. BARGER: Yes.

7 CHAIR PARKSY: I don't think we can take a
8 position that it is bad without elaborating on what's
9 been done to try to address it, that we would state
10 people ought to consider.

11 MR. CAPPITELLI: Do we have a consensus on
12 Number 13? Because I think the way Bob stated it, I'm
13 more comfortable with it that way where we talk about the
14 broader concern and the broader issue. But an actual
15 recommendation that suggests that we want to make this
16 significant policy shift away from the way it's being
17 done to something else that impacts all these people.
18 I'm not so sure that addresses the issue.

19 CHAIR PARKSY: I think we can come back around
20 without doing that and still endorse the notion of
21 addressing abuses in this area without necessarily saying
22 the recommendation that you've got laid out here.

23 MR. BRANAN: I think so.

24 CHAIR PARKSY: Okay, keep going.

25 What was 12 is now 13.

1 MR. BRANAN: Yes. Just by way of background
2 for Number 12, in the last legislative session, there
3 were three bills that were sponsored by PERS dealing
4 with -- last gasp.

5 MR. WALTON: It got you all choked up, huh?

6 MR. BRANAN: Yes, it's very emotional.

7 CHAIR PARSKY: When you start listings AB's,
8 that chokes you up, I know.

9 MR. BRANAN: Yes. All three of these bills
10 were sponsored by PERS. All of them dealt with
11 disability fraud. This is not to be confused with
12 disability abuse -- verbal abuse here.

13 So what happened was in the background material
14 on page 21, we just briefly summarized these bills.

15 After some of you got your background material,
16 you called me and said, in essence, "How are we supposed
17 to make a decision like this based on no information on
18 the bills?"

19 So this morning I handed out this document.
20 It's my analysis of the three bills, and it gives also
21 their legislative history.

22 And I think one thing that's worth pointing out
23 is that two of these bills went through both houses of
24 the Legislature with no "no" votes. One of them went
25 through both houses with one "no" vote.

1 Now, for partisan reasons, these bills were
2 kept in the Legislature and died eventually; but it had
3 nothing to do with the content of the bills not being
4 acceptable to both parties in the Legislature.

5 This year, those three bills have all been
6 reintroduced. And in my discussions with some labor
7 representatives, they are putting together a
8 disability-abuse package for January 2008. And they
9 think that these three bills may very well be included in
10 that package.

11 So for that reason, we have this
12 recommendation: The Commission endorses the reform
13 policy language found in the current legislative sessions
14 AB 36, AB 219, and AB 545, and urges that the Legislature
15 enact that language in 2008.

16 And what I tried to get across here but based
17 on earlier discussions today, I may not have done that.
18 This is not saying that you should endorse these three
19 bills now, but the concepts found in the bills. Because
20 if they are included in an omnibus bill next year, they
21 won't have these authors or these bill numbers. And
22 that's why it made sense that you use a description of
23 what's actually in the bills.

24 CHAIR PARKSY: Yes, Curt?

25 MR. PRINGLE: Yes, on this, looking at the

1 quick synopsis on page 21, the one-sentence version of
2 what you're talking that the bill is trying to
3 accomplish, I feel comfortable with it, and I'm sure most
4 everyone else does.

5 On this one, though, it gives me maybe an
6 opportunity to suggest, I would really like to think,
7 Mr. Chairman, when each of these recommendations are
8 presented, how they can be presented in a consistent
9 format. And in that regard, where we're directing
10 certain state action, we should say things like what was
11 referenced in Recommendation 13: "Legislation should be
12 introduced to" or "Legislation should be introduced to
13 enact," and then articulate what we want to have enacted.
14 When we want to direct CalPERS to take an action:
15 "CalPERS, CalSTRS, and other retirement agencies should
16 do this," "Local governments, in developing a
17 compensation plan, should do this," so that we are
18 really, specifically, clearly saying: This is what
19 should be enacted.

20 In this regard, I like all of these and this is
21 fine. I just think we should say again, "Legislation
22 should be introduced and enacted that does..."

23 CHAIR PARKSY: And, in effect, extract the
24 policy language?

25 MR. PRINGLE: Right.

1 CHAIR PARKSY: Or the form policy language from
2 each?

3 MR. PRINGLE: I really -- and I know what Tom's
4 trying to do. I always have hesitancy of ever
5 referencing a bill number at a moment in time knowing
6 exactly what's there or what's not, there's a technical
7 flaw in it, there's some issue. We just have to say what
8 the policies are that we want to enact so, again, when
9 the reader looks at this report, they know what we're
10 seeking and why we're seeking it. So that would be my
11 recommendation.

12 CHAIR PARKSY: And you could still introduce it
13 with a reference to whatever bills you want to refer to
14 that attempted to do this; but going forward then, take
15 the -- as far as the recommendation, take the bill
16 references out and put the policy language in that we
17 want to have included; is that --

18 MR. BRANAN: That would be fine.

19 CHAIR PARKSY: Is that okay with everyone?

20 All right, let's keep going.

21 MR. BRANAN: The next broad category is
22 "Operational and Administrative Governance."

23 "Pension fund governance has received greater
24 attention in recent years as pension funds have become
25 larger and investment options more complex."

1 "Concerns have also been raised about
2 retirement system mismanagement, misuse of funds, and
3 conflicts of interest."

4 "Retirement systems have adopted reforms to
5 address these governance issues."

6 "The rules to eliminate 'pay to play' have been
7 adopted by the CalSTRS board."

8 AB 246 was recently signed by the Governor. It
9 prohibits county retirement board members from selling or
10 providing investment products to any '37 Act retirement
11 systems.

12 And SACRS, which is the umbrella organization
13 for the twenty '37 Act retirement systems, SACRS has
14 created the Uniform Trustee Appointment Policy, which
15 recommends appointment procedures and qualifications for
16 appointed retirement board members.

17 "According to best-practice literature,
18 effective fund management requires that the appointed
19 members of retirement system boards should have expertise
20 which balances representation of members and the public
21 and minimizes political influence and economic conflicts
22 of interest."

23 Number 14 is: "Trustees of public retirement
24 systems should receive continuous training related to
25 the understanding and fulfillment of their fiduciary

1 responsibilities, as well as ongoing training for the
2 investment of fund assets."

3 CHAIR PARKSY: Okay, no objection.

4 Bob?

5 MR. WALTON: Just one editorial comment. The
6 investment of assets is a fiduciary responsibility. So
7 I would just change that "including the investment of
8 assets" as -- it sounds like now it's in addition to.

9 MR. BRANAN: That's true. And that wasn't the
10 meaning we were looking for.

11 MR. WALTON: No, I understand.

12 MR. BRANAN: But we wanted to emphasize
13 fiduciary duty. In most cases, people want educational
14 programs for investments, and then throw in something
15 about fiduciary duties.

16 MR. WALTON: I understand.

17 DR. GHILARDUCCI: This is something I've
18 thought about many decades. And I'm just wondering if
19 your language isn't too weak.

20 There's lots of programs that are called
21 "training programs," and they're just one long golf game.
22 And it's a big waste of money.

23 No offense to the golfers.

24 MR. WALTON: You said that like it was a bad
25 thing.

1 DR. GHILARDUCCI: And the men are talking to
2 each other on the golf course, right, and very little
3 training goes on at all.

4 CHAIR PARKSY: Let's not just make reference to
5 the men on the golf course, or make reference to the
6 boys, or nothing like that.

7 DR. GHILARDUCCI: Show me a gaggle of women
8 trustees on the golf course and I'll eat my words.

9 But that actually speaks to even bigger issues
10 about how exclusive and cliquish, you know, these
11 so-called training programs are. It's something that
12 I care a lot about, and there's been lots of evaluations
13 about how effective this training is.

14 So if we can put any language about quality
15 training or recognized training or credentialed training,
16 I'd be happy.

17 MR. BRANAN: Actually, we wrestled with that,
18 to the point of naming some places.

19 DR. GHILARDUCCI: Yes.

20 MR. BRANAN: But I think we could use some help
21 with that.

22 DR. GHILARDUCCI: I can help. Maybe I could
23 help you with that. I will help you with that.

24 Also, I think adding the clause that "as well
25 as ongoing training for investments" defeats your

1 purpose, because much of that training, when it happens
2 between, you know, tee-offs, is only about investments.
3 And people can walk away with lots of sophisticated
4 knowledge about style differences in mutual funds and
5 equities, but really have not a clue what an unfunded
6 liability is. And that, I think you were trying to write
7 that in balance. So I would say "as well as ongoing
8 training for actuarial assumptions or actuarial methods,"
9 and you really emphasize it that that training has to be
10 balanced.

11 CHAIR PARKSY: Matt?

12 DR. GHILARDUCCI: And there should be exams at
13 the end of each quarter.

14 MR. CAPPITELLI: We thank you, Professor.

15 DR. GHILARDUCCI: And indoors, right.

16 CHAIR PARKSY: No exams on the golf course.

17 MR. PRINGLE: In Anchorage.

18 DR. GHILARDUCCI: Right.

19 In Indiana.

20 MR. BARGER: I actually have the same reaction,
21 which was this is fine, but it's incredibly weak. And
22 not only in regards to training but sort of
23 qualifications for who should be able to serve. You
24 know, this is an increasingly a complex area, both on the
25 investment side and --

1 DR. GHILARDUCCI: Right. Yes, and the
2 corporate side.

3 MR. BARGER: We've been sitting here for a long
4 while. I don't think we would score 100, with the
5 exception for Bob, on our actuarial test on pension
6 plans.

7 This is not an easy area. And having some sort
8 of standards that say, you know, preference for actuarial
9 backgrounds, finance backgrounds, academic -- I mean,
10 just in some ways, establishing that there are best
11 practices for who should be on these and how they're
12 picked, and what you're agreeing to, your political
13 background. I mean, having some process that's trying to
14 get the best and the brightest with representative
15 backgrounds strikes me as that ought to be the best
16 practice for that as well.

17 CHAIR PARKSY: Well, and I guess inherent in
18 that is the overall -- I guess at one point we had a
19 reference to board composition in the heading, and it
20 wasn't -- we didn't quite include that here.

21 MR. BRANAN: Well, that's true. Board
22 composition is something that's now covered by
23 Proposition 162. To change the composition of a board
24 requires a vote, a majority approval of the electorate
25 within that area that the board covers. So, say, for

1 PERS or STRS, you'd have to have a statewide election.
2 We didn't include it largely for that reason.

3 But I think Bob Palmer here can give some
4 detail on what we mentioned in the background as the
5 SACRS policy for who should be appointed. And we're
6 talking about appointed members.

7 MR. PALMER: Yes, thank you. Within the
8 Government Code that sets up the 1937 Act, it defines the
9 type of members that could be serving on the board of
10 retirement. Some are appointed and some are elected. So
11 the SACRS organization developed a proposal that they
12 present to all 20 county supervisors on what they should
13 be looking at for criteria for future appointments to
14 their board of retirement.

15 There is no mandate and there is no requirement
16 that they do that; but it was done trying to focus on the
17 need for the expertise that we think this business needs.

18 I was just told that the City and County of
19 San Francisco also has a criteria in place that they use
20 for that. That causes a problem. If you're going to
21 look at the appointees, what do you do about the elected?
22 How do you handle the elected?

23 And so the language that you see up there goes
24 to, if you will, both sides, but in particular, about the
25 elected ones, the officials, participating that they will

1 have continuous, ongoing training.

2 As has been pointed out, there is a lot of
3 training for investments but not a lot of serious,
4 accredited, strong training for the other side of our
5 business -- the liability side of our business. And so
6 that's why we wrote this thing, if you will, backwards.
7 We're trying to highlight that fiduciary responsibilities
8 are critical in addition to investments. And so that's
9 why the language was presented to you in that fashion.

10 CHAIR PARKSY: Well, but I do think that maybe
11 inherent in Matt's point, although you may have a
12 difficult time because, by statute, where the
13 appointments come from, I do think that trying to make
14 sure that the composition of the boards carry with it
15 experience in areas, somehow we ought to be able to
16 emphasize that.

17 I mean, in either of these two areas that have
18 been mentioned, either in the investment area or in the
19 actuarial area, the notion that you will be able to train
20 an inexperienced person to become -- to carry with it
21 expertise, I think, is a stretch. That doesn't mean that
22 you should have training; and you certainly should have
23 training about your responsibilities; but I do think that
24 it's going to be -- certainly on the investment side, it
25 will be very difficult to kind of bring someone who is

1 not experienced to a knowledge base that would, quote,
2 reach qualified status.

3 MR. BRANAN: Well, two things: One, I think we
4 should keep in mind that investment boards or retirement
5 boards in the public sector aren't like retirement boards
6 in the -- what did I say, the private sector? Those in
7 the public sector are not like those in the private
8 sector, nor should they be.

9 CHAIR PARKSY: Right.

10 MR. BRANAN: In the public sector, there are,
11 and I think should be, representatives of the public and
12 of the members on the board. And although there is, it
13 seems, a growing literature out there that some of those
14 people should be replaced by investment experts, I think
15 that is a very narrow look at the public sector.

16 And the other half of that is, if you look at
17 the history of public pensions and the investments that
18 they've made, most of those decisions are made by chairs
19 who are the elected members of the board. Now,
20 obviously, the chair doesn't make all the decisions.

21 CHAIR PARKSY: Right.

22 MR. BRANAN: But just because they came in with
23 limited knowledge doesn't mean that with hiring the
24 correct professionals as advisors that they can't make
25 good investment decisions.

1 CHAIR PARKSY: No question about that.

2 It's just that the reference to training would
3 suggest that training can almost put someone in a
4 position of being able to take the place of the expertise
5 that they bring to bear, not necessarily change the
6 composition.

7 Curt?

8 MR. PRINGLE: And I just want to -- Prop. 162
9 pretty much delineates categories of where individuals
10 come from as opposed to further delineation, saying that
11 a collective pool should have certain talents and
12 components.

13 And I don't think when you talk about board
14 composition we're really going against, you know,
15 mandating something on a '37 Act county, necessarily, or
16 mandating that we overturn Prop. 162 or go for a vote, if
17 we say, "...and the collection of appointees should include
18 someone with experience in actuarial, or with actuarial
19 knowledge, someone with experience in liabilities or plan
20 management, someone with experience in this."

21 I mean, most boards and commissions in the
22 state do, in fact, have those underlying conditions, not
23 necessarily just saying, "The Legislature gets one
24 appointment," but, in fact, say that among this pool of
25 appointees -- among the Governor's five appointees on

1 CalSTRS, one should have an actuarial knowledge and one
2 should -- or whatever. I mean, those are the levels,
3 I think, of encouragement we could make so you not only
4 have -- we don't need to disturb the appointment pool
5 process.

6 I would assume, in many instances, there are
7 folks that come from the represented communities that
8 have experience in a lot of those things. And, you know,
9 if, in fact, one of the bargaining units that are
10 represented on that have someone they wish to offer with
11 that knowledge, I think that just adds to it.

12 And setting a guideline as to what are some of
13 those things that we think are important to have
14 reflected in your membership, your board composition, I
15 think would go a long way to suggest. We just don't want
16 bodies to fill the seats that are appointed from certain
17 places but, in fact, bring certain talents to those seats
18 as a collective.

19 MR. BRANAN: That's a good point. And we will
20 send out this week the SACRS policy document that Bob was
21 just talking about, because that's exactly what it does.
22 It says, "Of the appointed members, we recommend that you
23 look for the following qualities."

24 DR. GHILARDUCCI: Yes, I want to clear up what
25 I said, too, when I said we should have exams. And it

1 wouldn't have been -- my perfect exam, based on the
2 research about what makes an effective trustee and what
3 makes an effective board, in terms of actually yielding
4 good rates of return and stable contributions and
5 benefits, are qualifications that refer to whether or not
6 a trustee can recognize a conflict of interest, whether
7 or not they understand the role of staff and the experts,
8 and put their recommendations in proper perspective.

9 This is the catch-all fiduciary, but it's an
10 important part of the skill base that they need.

11 Whether or not a trustee has to have a time
12 perspective that exceeds the quarter or a year, they in
13 some ways have to think about the whole list of needs of
14 the employer, the taxpayer, and the beneficiary, at the
15 same time making the beneficiary and the participant the
16 primary beneficiary. That all takes judgment. That
17 would be on my ideal test and would be a part of my
18 training.

19 So there are lots of reasons to have
20 representatives from different constituent groups, and
21 lots of reasons to have training. But it does have to be
22 of a particular kind or else it's worse than nothing.
23 You know, that it's a waste of time, but it also could
24 cause the wrong decisions.

25 MR. BRANAN: Well, we'll get in touch with you

1 this week.

2 DR. GHILARDUCCI: Okay, I have some citations.

3 CHAIR PARKSY: Bob?

4 MR. WALTON: I like the idea that Teresa and
5 others have talked about, of having a best practices as
6 to training, and especially I would agree with Bob. It's
7 really the liability side that's underrepresented, it's
8 not the asset side.

9 DR. GHILARDUCCI: Right.

10 MR. WALTON: But, really, the responsibility of
11 a fiduciary is not to become an expert, it is to hire
12 experts.

13 DR. GHILARDUCCI: Right.

14 MR. WALTON: To recognize where they don't have
15 the expertise and have the ability to hire, and depend on
16 those experts where they need them. And so training in
17 that regard is always helpful.

18 I think as part of that, we've talked about an
19 advisory actuarial panel or board of some sort. That
20 would be a wonderful group to recommend courses to learn
21 about actuarial science for a pension fund and for an
22 OPEB trust as an example. So that's really what has to
23 take place.

24 My specific knowledge about PERS, with one
25 exception, the appointed members come from a particular

1 point of view, like one of the Governor's appointees
2 represents local government. They have to be a local
3 elected official.

4 MR. BRANAN: And that's set out in the law.

5 MR. WALTON: That's right, it's set out in the
6 law.

7 The one that represents the public, that
8 doesn't have an expertise other than representing the
9 public, is a legislative appointee, if I recall.

10 But all have some segment that they're
11 supposedly representing.

12 One of the things, I think, in my experience,
13 though, is once you become a fiduciary, you don't
14 represent just that perspective; you have to represent
15 the entire membership.

16 DR. GHILARDUCCI: Right.

17 MR. WALTON: You can't sit there and say -- or
18 even the elected side -- "I was elected by the retired
19 members, and here's what they think."

20 Well, that's part of the education. When you
21 become a fiduciary, you have to represent the total
22 system.

23 So I think the process of delineating best
24 practices for education and training in this area, and
25 especially highlighting the liability side, however you

1 want to characterize that, is really important.

2 CHAIR PARKSY: Matt?

3 MR. BARGER: I want to point out, you're
4 touching on the established pension plans, you're
5 presumably at some point going to suggest setting up some
6 form of trust or parallel universe for OPEB, where this
7 is all fair game.

8 MR. BRANAN: Yes.

9 MR. BARGER: And so saying, "Oh, this is needed
10 for a pension plan system," doesn't mean they have to
11 copy exactly the same thing for this, and presumably
12 they've got a whole slate of new people to choose, so it
13 would be nice if they started out with some best-practice
14 recommendations of what would be a good composition to do
15 that.

16 MR. WALTON: That's a good point.

17 CHAIR PARKSY: That's a very good point.

18 Lee?

19 MR. LIPPS: As a trustee on a private-sector
20 trust, it's my understanding that I am required each year
21 to undergo at least 15 hours of continued education
22 training each year. I mean, that's an actual
23 requirement. It's not just --

24 DR. GHILARDUCCI: Your board would have set
25 down that requirement. It's nowhere required in the law.

1 So each pension board would have its own requirements of
2 its trustees.

3 MR. LIPPS: Okay, it's my understanding -- and
4 it wasn't the board -- is that this was something that
5 certification was required for, that I attended the
6 training, which is why the International Foundation is
7 such a popular place.

8 DR. GHILARDUCCI: Yes, that's good. Yes.

9 CHAIR PARKSY: Okay, Tom, do you think you have
10 the sense here?

11 MR. BRANAN: Yes.

12 CHAIR PARKSY: Okay, Teresa will help you.

13 DR. GHILARDUCCI: Yes.

14 CHAIR PARKSY: Okay.

15 MR. BRANAN: "Adoption of sound governance
16 policies helps to ensure better organizational
17 performance and fewer conflicts of interest and provide
18 less opportunity for misuse of fund assets. Such
19 policies also lend credibility to the governance
20 requirements which trustees place on companies where plan
21 assets are invested."

22 Number 15, "Boards which oversee pension and
23 OPEB trust funds should meet or exceed the transparency
24 governance requirements they place on companies or other
25 investment vehicles where plan assets are invested."

1 CHAIR PARKSY: Here's where Sarbanes-Oxley
2 comes in.

3 DR. GHILARDUCCI: Yes.

4 CHAIR PARKSY: Okay, let's just pause on that
5 one.

6 I'm not quite sure how people would interpret
7 what it means, but how do people think about that general
8 reference.

9 DR. GHILARDUCCI: That's great.

10 MR. HARD: It sounds good to me, but I don't
11 know how it would be implemented or whatever.

12 CHAIR PARKSY: Well, I think a question is, in
13 your mind, Tom, it's clear as to the requirements that
14 individual boards place on companies?

15 MR. BRANAN: Yes, and we --

16 DR. GHILARDUCCI: It's Sarbanes-Oxley.

17 MR. BRANAN: -- we especially added
18 transparency here, so that it doesn't apply to all
19 governance requirements. And if you would like, when we
20 bring this back for final approval, we can add a few
21 examples.

22 CHAIR PARKSY: I don't see how -- I don't see
23 how people can object to this, it's just a question of --
24 it certainly wouldn't be uniform. Different boards will
25 take a different approach.

1 DR. GHILARDUCCI: That's okay.

2 CHAIR PARKSY: That's okay.

3 DR. GHILARDUCCI: As long as they have the
4 internal audit.

5 CHAIR PARKSY: Okay, keep going.

6 MR. BRANAN: Number 16.

7 CHAIR PARKSY: Keep going.

8 This will be the Teresa-Sarbanes-Oxley
9 recommendations. Okay.

10 MR. BRANAN: "Public retirement systems boards
11 and trustees should publish an independent audit
12 committee made up of trustees to oversee and participate
13 in the opening, processing, and closing of the annual
14 audit report to the full board. This recommendation is
15 made to make trustees more active participants in the
16 audit process."

17 CHAIR PARKSY: The last sentence I'm not sure
18 quite fits with all the other recommendations to explain
19 why.

20 DR. GHILARDUCCI: Right.

21 CHAIR PARKSY: You can introduce that.

22 DR. GHILARDUCCI: It should be a background.

23 CHAIR PARKSY: Yes, it's not quite consistent,
24 but I think we understand why.

25 Any objections to this best practice or this

1 recommendation?

2 MR. CAPPITELLI: No objection.

3 MR. LIPPS: I guess my question would be going
4 back to something you said earlier, Gerry. Even with a
5 great deal of training, could we bring trustees who are
6 either elected or appointed by virtue of their office,
7 could we bring them up to a level to understand fully
8 enough about the audit process to oversee it?

9 CHAIR PARKSY: Well, I think inherent --
10 correct me, Tom -- but I think inherent in this
11 recommendation is a separation of board responsibility
12 with respect to audit and executive/staff responsibility
13 with respect to audit.

14 Isn't that the distinction you're trying to
15 draw?

16 MR. BRANAN: This comes not from the statewide
17 retirement systems, as much as what some of us have
18 observed in local retirement systems, where the auditor
19 comes in, sits down with senior staff, has the audit, and
20 the trustees are essentially inert and they receive the
21 audit report.

22 What we're trying to do is to get a group of
23 them that will have, by virtue of being on the audit
24 committee, a responsibility to get into it and to
25 understand what's going on.

1 CHAIR PARKSY: Well, and the audit report -- or
2 independent auditor would be reporting to the board as
3 opposed to the ongoing management.

4 MR. BRANAN: Well, and they do report to the
5 board currently. But if the board hasn't played any role
6 in it, it's not as valuable an experience as it ought to
7 be.

8 CHAIR PARKSY: That's true.

9 Okay, next?

10 MR. BRANAN: 17, "Boards which govern pension
11 and OPEB trusts should have very strong conflict of
12 interest policies. All trustees should annually attest
13 in writing that they understand and are in compliance
14 with the conflict-of-interest policy."

15 So we are not saying what that
16 conflict-of-interest policy should be; but going back
17 to what Mr. Walton said earlier, there is often a lapse
18 of any memory about what you were told at a given time.
19 And that's why trustees should annually say in writing
20 that they understand the policy and that they adhere to
21 it.

22 CHAIR PARKSY: Are there any comments there?

23 MR. CAPPITELLI: No, no objection. It's a
24 great recommendation.

25 I think we ought to kind of expand or focus in

1 more on what those policies should be and how they should
2 be written. Maybe something that's more standardized,
3 the best practice, or something of that nature. Because
4 I think if you just put that recommendation out there,
5 you really leave it up to the individual boards and
6 groups.

7 I'd like to see something that's more of an
8 organized or collaborative effort to come up with
9 something that it doesn't necessarily need to be part of
10 this recommendation, but it could be an ad hoc group that
11 could be established to come up with a best practice and
12 best recommendation, and then they be disseminated to all
13 these different boards.

14 MR. BRANAN: We could develop that before the
15 next meeting. And if you are in agreement with it, it
16 could become part of the index or the appendix on the
17 final report.

18 MR. CAPPITELLI: I think that would be even
19 better.

20 DR. GHILARDUCCI: That would be wonderful.

21 MR. CAPPITELLI: Even stronger, yes.

22 CHAIR PARKSY: Okay.

23 DR. GHILARDUCCI: We just missed Thanksgiving.

24 CHAIR PARKSY: Tom, any others?

25 MR. BRANAN: No, that's it.

1 CHAIR PARKSY: Before we conclude, I just
2 wanted to come back on a subject that I think was a
3 little bit confusing, I mentioned it to Tom, and that has
4 to do with our discussion of prefunding. There were some
5 questions raised about what the magnitude of the dollars
6 needed to be in order to fully prefund beginning now, in
7 the upcoming budget cycle.

8 And I thought it would be helpful just to make
9 sure we clarified that, and not necessarily changing any
10 of the recommendations that are being redrafted. But
11 let's separate out the amount of money necessary to fund
12 the pay-as-you-go amount. That, as I understood it, was
13 \$1.3 billion?

14 MR. BRANAN: That's correct.

15 CHAIR PARKSY: And that, it was assumed, as it
16 has in the past, would be in the current -- in the
17 upcoming budget. That's just being assumed that that
18 would be the case.

19 What we were talking about is how much
20 incremental money would be necessary to prefund the,
21 quote, "unfunded liabilities" that are accruing over and
22 above the \$1.3 billion.

23 MR. BARGER: Of those two, isn't there the
24 normal cost and the amortization?

25 CHAIR PARKSY: Yes. And I thought it was

1 confused. So we start with the current cost, that's the
2 \$1.3 billion.

3 MR. BARGER: Yes.

4 CHAIR PARKSY: Now, that is somewhat irrelevant
5 to the question of prefunding. So we can put that aside
6 for the moment. It's dollars in the current budget, so
7 it's not a question of whether the money is needed.

8 But in just trying to address the notion of do
9 we want to recommend prefunding begin at the state level,
10 and if so, to what extent -- partial, full, whatever --
11 and do we want to use a specific number, just to give
12 everyone the notion of what it would take to be fully
13 prefunded, what would that number be.

14 MR. BRANAN: As I recall, Mr. Chair, the total
15 number would be about \$2.59 billion.

16 CHAIR PARKSY: The total number of what,
17 though? That was what was --

18 MR. BRANAN: You pay as you go, and then added
19 on to it approximately \$1.3 billion.

20 CHAIR PARKSY: Yes, so that was the confusing
21 thing. It's approximately \$1.3 billion on top of what
22 would be the pay-as-you-go, \$1.3 billion.

23 MR. BARGER: Let's just say, the normal cost is
24 2.6.

25 MR. BRANAN: That is your full prefunding cost.

1 MR. LIPPS: No, that would only just be the
2 pay-as-you-go; and the normal cost, which is the cost
3 from today going forward, doesn't include the ARC, which
4 is the accrued unfunded liability. That's what we're
5 trying to get.

6 CHAIR PARKSY: That's what I think needs to be
7 clarified -- well, two things need to be clarified: One
8 element of statistic, which is what does it take to
9 actually honor the pay-as-you-go number. That's
10 \$1.3 billion. I think everyone has agreed with that.

11 Now, the question is, what more do you need to
12 do -- I think if John Cogan were here, he would emphasize
13 the importance of not just looking at the current
14 obligations going forward, but at the obligations that
15 have accrued in addition. So that's what I think would
16 be helpful to clarify.

17 MR. LIPPS: And if we could have them broken
18 out between each of those three groups, both the normal
19 cost and then the unfunded liability.

20 DR. GHILARDUCCI: Right. Liability over
21 30 years.

22 CHAIR PARKSY: And who are you bringing to the
23 table?

24 MR. BRANAN: I'd like to introduce Mr. Tom
25 Dithridge. He's from the Department of Finance, and is

1 prepared to talk about this.

2 CHAIR PARKSY: Do you work with our executive
3 director when there's another hat on, is that --

4 MR. DITHRIDGE: I do occasionally, yes.

5 The report that was prepared by the actuaries
6 indicate that if we were to fund -- fully fund the ARC,
7 we would need to spend about \$2.6 billion. About
8 \$1.3 billion of that is what we're currently providing in
9 the budget. And that includes the \$1 billion to
10 \$1.1 billion that we spend for state employees for the
11 current benefits -- for the retirees, for the current
12 benefits; and it includes the implicit subsidy that has
13 to do with the way the rates are structured. And we have
14 a single rate for all employees.

15 The remainder would then fund the unfunded
16 liability for retirees and for existing employees.

17 DR. GHILARDUCCI: Would be how much?

18 MR. DITHRIDGE: What?

19 DR. GHILARDUCCI: Is how much?

20 MR. DITHRIDGE: That would be the 1.3.

21 CHAIR PARKSY: So the total of the two,
22 including prefunding what's referred to as the ARC, was
23 2.6?

24 MR. DITHRIDGE: Right.

25 CHAIR PARKSY: And, again, you would just take

1 away the two 1.3's to get there, but you take away the
2 1.3, which is the obligations currently due in the
3 current year --

4 MR. DITHRIDGE: The pay-as-you-go.

5 CHAIR PARKSY: The pay-as-you-go, and you still
6 have another 1.3?

7 MR. DITHRIDGE: Yes.

8 CHAIR PARKSY: And that would take care of both
9 the retirees and the existing employees?

10 MR. DITHRIDGE: Correct.

11 CHAIR PARKSY: On the prefunded basis; is that
12 right?

13 MR. DITHRIDGE: On the benefits as they're
14 accruing, yes, the so-called normal cost.

15 DR. GHILARDUCCI: So paid over how long?
16 Thirty years?

17 MR. DITHRIDGE: Thirty years.

18 CHAIR PARKSY: Let's ask the questions we need
19 to ask.

20 MR. DITHRIDGE: By the way, it also includes
21 the unfunded liability for the existing -- yes, that's
22 right. I'm sorry, yes.

23 CHAIR PARKSY: We've covered that.

24 Matt?

25 MR. BARGER: Teresa and I had the same

1 question.

2 MR. LIPPS: Do you have a sense -- let's forget
3 the pay-go part, the first 1.3. The second 1.3, do you
4 have a sense of the breakout between normal and the ARC?
5 Because the numbers that you're saying are different than
6 the numbers that I recall hearing in a much earlier
7 presentation.

8 MR. DITHRIDGE: Let's clarify --

9 MR. LIPPS: That's what I'm trying to --

10 CHAIR PARKSY: This is an important point that
11 we need to make is to make sure that everyone understands
12 the numbers we're talking about.

13 MR. DITHRIDGE: Let's clarify. The ARC is the
14 actuarially required contribution. That is a term that
15 has been developed by GASB. And that is the
16 \$2.6 billion.

17 If you fully fund -- if you're going to fully
18 fund over 30 years, it's \$2.6 billion.

19 MR. BARGER: And fully funding meaning
20 including taking care of the existing \$46 billion --

21 MR. DITHRIDGE: No, the \$46 billion is a
22 different number. That is the obligation, if we do it on
23 a pay-as-you-go basis. And what it does -- and this is
24 the way the accounting board set it up -- it takes the
25 unfunded liability and then looks at what it would take

1 to amortize that over 30 years at about 4½ percent, I
2 think is what they used in there, which is what the State
3 gets on its short-term investments. It's sort of a
4 contrived number for accounting purposes.

5 MR. BARGER: Okay, so you're saying it's not
6 the 46, it's the second number, it was the 30 or
7 something?

8 MR. DITHRIDGE: The 30 -- if we want to -- if
9 we decide to fully fund the --

10 MR. BARGER: It would take 30 years --

11 MR. DITHRIDGE: -- the normal and the -- yes,
12 over 30 years, the normal cost and the unfunded
13 liability, the report says that we need to spend
14 \$2.6 billion a year.

15 DR. GHILARDUCCI: Every year?

16 MR. BARGER: Just for clarity, that includes
17 the 1.3 million pay-as-you-go?

18 MR. DITHRIDGE: Yes.

19 DR. GHILARDUCCI: Every year, an annual
20 contribution. That's not a level --

21 MR. DITHRIDGE: Right, that would be a
22 30-year --

23 DR. GHILARDUCCI: Annual payment?

24 MR. DITHRIDGE: Yes.

25 CHAIR PARKSY: And doing it that way, taking

1 all the calculations, at the end of the 30 years, you
2 would be fully funded for the obligations?

3 MR. DITHRIDGE: And now there's another caveat
4 in here. This is on a closed group because it's not
5 figuring in the growth of employees.

6 DR. GHILARDUCCI: Right.

7 CHAIR PARKSY: Okay.

8 MR. DITHRIDGE: So it's going to change every
9 time they do the valuation.

10 CHAIR PARKSY: Okay, but if, in the -- if the
11 infinite wisdom of the Department of Finance, if the
12 infinite wisdom of the Department of Finance -- you're
13 included -- and the State Legislature decided that you
14 wanted to fully prefund as defined, then you would
15 include 2.6 billion in the forthcoming budget?

16 MR. DITHRIDGE: That gets a little bit -- we
17 would be including 2.6 billion. But remember that part
18 of that is actually included in what we're paying for
19 active employees for their health benefit, because we
20 have the implicit subsidies. And that's paid on behalf
21 of active employees.

22 And just as a little background, the theory is
23 that older employees, which retired employees are going
24 to be predominantly, are going to have higher health
25 costs on average than younger employees. So if you have

1 the same rate for everybody, there is a subsidy that the
2 younger employees are paying on behalf of the older
3 employees because they're not taking advantage of the
4 level of services that the older employees are taking
5 advantage of.

6 CHAIR PARKSY: That clarifies a lot, I'm sure.

7 But let me just state -- and this gets back to
8 what I think Lee was asking -- which was we heard from
9 another member of the Department of Finance in testimony,
10 and I am sure that it was perfectly consistent with you,
11 because you're all part of the same department. And that
12 was how much money would need to be found, if you will,
13 in the current budget cycle in order to honor a policy
14 that said, "I want to begin fully funding -- fully
15 prefunding," if you will.

16 MR. DITHRIDGE: Right.

17 CHAIR PARKSY: And I guess one answer, if I've
18 got this right, one answer is, "Well, it's a given that
19 \$1.3 billion will be in, in the current budget."

20 MR. DITHRIDGE: Okay.

21 CHAIR PARKSY: But you still have somewhere
22 between a seven or eight billion, maybe higher, deficit
23 potential.

24 So on top of being able to find that money, if
25 we were going to fully prefund, you would -- and that

1 includes an assumption that the \$1.3 billion will be in
2 it -- you'd need to find another \$1.3 billion, thus
3 increasing whatever that deficit is, you have to find
4 another \$1.3 billion.

5 MR. DITHRIDGE: That's correct. But I think
6 that the \$7 billion shortfall number you're talking about
7 is a general-fund number. Not all of the 1.3 billion --

8 CHAIR PARKSY: Sorry.

9 MR. DITHRIDGE: -- additional is general fund.
10 So that's going to be --

11 CHAIR PARKSY: Forget about the shortfalls.

12 Inherent in a recommendation to your department
13 to fully prefund, would be the need to find another
14 \$1.3 billion?

15 MR. DITHRIDGE: It would certainly exacerbate
16 the situation, and we would have to find additional
17 funds.

18 CHAIR PARKSY: We have great confidence in you,
19 so that's perfectly okay.

20 I think, at least from my standpoint, but I
21 think I understand those numbers. And I was confused
22 there. I really thank you very much.

23 Any other thoughts?

24 If not, we're adjourned.

25 *(Proceedings concluded at 2:41 p.m.)*

REPORTER'S CERTIFICATE

I hereby certify that the foregoing proceedings were duly reported by me at the time and place herein specified;

That the testimony of said witnesses was reported by me, a duly certified shorthand reporter and a disinterested person, and was thereafter transcribed into typewriting.

I further certify that I am not of counsel or attorney for either or any of the parties to said deposition, nor in any way interested in the outcome of the cause named in said caption.

IN WITNESS WHEREOF, I have hereunto set my hand on the 20th day of November 2007.

DANIEL P. FELDHAUS
California CSR #6949
Registered Diplomate Reporter
Certified Realtime Reporter