

AGENDA REPORT

TO: Henry L. Gardner,
Interim City Administrator

FROM: Katano Kasaine, Plan Administrator
Oakland Municipal Employees'
Retirement System

SUBJECT: OMERS Charter Change for
November 4, 2014 General
Election

DATE: June 17, 2014

City Administrator
Approval



Date:

6/26/14

COUNCIL DISTRICT: City-Wide

RECOMMENDATION

Staff recommends the approval of this resolution to place a proposed charter amendment on the November 4, 2014 General Election. The purpose of this change is to authorize the City of Oakland ("City") the option to purchase a group annuity contract to guarantee pension payments to the remaining Oakland Municipal Employees Retirement System ("OMERS") retirees and beneficiaries.

EXECUTIVE SUMMARY

Article XX of the Oakland City Charter and Ordinance No. 713 C.M.S. established the Oakland Municipal Employees Retirement System ("OMERS") and vested in the OMERS Board exclusive control of the administration and investment of the OMERS Fund. The OMERS retirement plan was established in 1939 and was closed in 1970. The plan provides retirement benefits for non-uniformed employees hired prior to September 1970 who have not transferred to the California Public Employees' Retirement System ("CalPERS").

The OMERS System currently provides pension benefits for twenty-two retirees and beneficiaries with an average age of ninety-one years old. As of the most recent actuarial valuation of the retirement system, which was as of July 1, 2012, OMERS plan assets were actuarially valued at \$4,448,000 resulting in a funded ratio of 122.5%.

For several years, the OMERS Board and Staff have been discussing the increasingly disproportionate annual administrative costs required to maintain operations of the OMERS plan relative to the actual cost of annual pension benefits. After considerable research and analysis done by the staff, legal counsel, plan actuary and consultants, the OMERS Board decided at its January 30, 2014 Board meeting to pursue the option of converting the OMERS pension fund into a group annuity contract. Given the circumstances of the small size of the plan and the few

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number of participants remaining, shifting the OMERS plan to an annuity structure is the most practical and cost-efficient approach for winding down the retirement system.

Moving forward with an annuity structure eliminates the need for a Board of Administration and other administrative costs, as the annuity provider would assume these functions. The Board would therefore dismantle which requires amendments to Article XX of the City Charter that removes the Board's exclusive administration and investment of the System's funds. In addition, the Board's permissible investments under Ordinance No. 713 C.M.S. do not include annuities. Therefore, before the Board can invest in an annuity, the City Council must authorize investment in an annuity.

BACKGROUND/ LEGISLATIVE HISTORY

OMERS is a closed single-employer, defined benefit pension plan established pursuant to Article XX of the City of Oakland Charter ("the Charter"). The System covers the City's non-uniformed employees hired prior to September 1970 who have not elected to transfer to CalPERS. The OMERS plan is governed by a seven-member Board of Administration ("Board"). Article XX of the Charter and City Ordinance No. 713 C.M.S. together establish the rules and guidelines for the maintenance and operation of the OMERS fund.

The OMERS Board and the Staff to the OMERS Board ("Staff") have been discussing the administrative costs required to maintain operations of the OMERS plan for several years. Because the System has become so small and will continue to decrease over time, the Board's previous actuarial consultant, Bartel Associates, LLC expressed concern that the cost of administering the System would continue to rise relative to the benefits being disbursed to retirees. On April 25, 2013, after a Request for Information ("RFI") process, the Board hired Dietrich and Associates ("Dietrich") to assist in studying the possibility of purchasing annuities. If the Board decided to annuitize, Dietrich would assist in the process of selecting an annuity provider and transitioning the retirement plan to the carrier.

ANALYSIS

Why Annuitize the OMERS Plan?

The OMERS Board and Staff have been discussing the disproportionate administrative costs required to maintain operations of the OMERS plan for several years. The OMERS System currently has twenty-two retirees and beneficiaries with an average age of ninety-one years old. Annual administrative expenses for OMERS have steadily increased and are approaching the annual benefit payment amount. For instance, based on the most recent actuarial report, the System is projected to pay approximately \$327,000 in pension benefit payments in Fiscal Year 2013/2014, yet the administrative budget is \$341,494 for the same Fiscal Year.

The costs to operate the OMERS fund include staff payroll and benefit costs, actuary, auditor, custodian, investment managers and investment consultant expenses. The purchase of a group annuity contract to pay the retiree's benefits would lower costs by eliminating the level of staff payroll and all other operational costs associated with administering the plan. Upon successful

purchase of an annuity, administrative functions would transfer to the annuity provider thus eliminating current annual operating expenses.

Additionally, the plan is overfunded, the participants are living longer than expected, and the volatility of the investment markets further justify the decision to annuitize. By annuitizing, the OMERS Board eliminates risk and cost associated with this plan for approximately 68% of the current actuarial valuation. The insurance companies' preliminary bids for OMERS retiree liability average \$1.9 Million in premiums. The chart below compares the average annuity premium and the current actuarial valuation of the liability.

OMERS Pension Plan Liability	Estimated actuarial valuation as of 7/1/2014	Annuity Premium	Premium Cost as a Percentage of Pension Liability
Service Retirees	\$600,000	Included in cost	
Disability Retirees	112,000		
Beneficiaries	698,000		
Present Value of Future Expenses	1,362,000		
Total	\$2,772,000	\$1,897,000	68%
Estimated Market Value of Assets as of 7/1/2014			\$4,638,000

Note: Estimates may vary due to future changes in the interest rates underlying annuity quotes or changes in the investment markets.

As of July 1, 2014, the OMERS Fund is projected to have approximately \$4.64 million in trust assets. After each annuity has been created for each OMERS retiree and beneficiary, there will be excess funds remaining of approximately \$2.7 million. The excess funds will be put in a trust fund for any unanticipated expenditures and to protect against insurer insolvency.

How does an annuity work?

There are insurers in the market that specialize in annuitizing pension liabilities and underwrite non-participating single premium group annuity ("SPGA") contracts. A non-participating SPGA is an insurance contract that is typically used to irrevocably transfer pension liabilities from the balance sheet of the sponsoring organization (City of Oakland) onto the balance sheet of an insurance company. Non-participating means that the contract holder (OMERS) is not affected by investment or mortality gains/losses. SPGAs are customized to cover the specific pension lives, benefit forms, benefit amounts, and other protected benefits, rights, and features available under the pension plan documents. A single premium is paid upfront to the selected insurer, who then assumes the pension liabilities and takes over administering benefit payments to the retirees

and beneficiaries.

The transition to the annuity provider should be almost seamless for the members, as their benefits will not be impacted post-transition. The annuity provider would continue to provide the existing benefits of the current retirement system and duplicate OMERS' benefit provisions including 3% COLA, 50% pension continuance to surviving spouses and \$1,000 death benefit. In addition, cost savings will be realized in terms of administration as the annuity provider would continue providing services such as telephone assistance, withholding, deductions for health premiums from pension checks, and processing of qualified domestic relations orders.

Protection Against Insurer Insolvency

The primary protection against insurer insolvency would be through the selection of a reputable and stable insurer. The Board would have a fiduciary duty to select a highly rated insurance carrier that could reliably administer all remaining benefits.

Furthermore, the City would continue to be the ultimate guarantor of benefits payments in the unlikely event the selected insurer became insolvent. Under an SPGA contract, the System's liability would typically transfer to the annuity provider; however, this is not permissible under the City Charter. Pursuant to the Charter, the City is required to contribute such amount as may be necessary, when added to member contributions to provide the benefits payable under the retirement system. Since all members are retired and are no longer making contributions, the City is singularly responsible for funding the System. Therefore, if the insurance provider becomes insolvent, the City will have to assume the obligation of funding the System.

Consequently, post-annuitization the City has an ultimate obligation of fiduciary responsibility for the OMERS fund. If the insurer becomes insolvent, the City will still fulfill its duty of care to retirees and beneficiaries and assure prompt delivery of benefits and related services. As due diligence, all savings from annuitization will be placed into a trust fund for any unanticipated expenditures or shortfalls as long as there are any living retirees or beneficiaries.

Next Steps

If the City of Oakland voters approve the Charter amendment, the Board's staff, actuary and annuity consultant would work on the annuitization process as follows:

1. Development of Bid Specifications.
2. Establish the three critical annuity dates:
 - a. Final Bid Date/ Acceptance date: The day in which the Board or designated appointees will review final pricing and accept an offer.
 - b. Wire Transfer Date: The day the insurance company will receive the premium
 - c. Benefit Commencement Date: The date the insurance company will make the first payment to Retirees

3. Post Sale Transition: Upon successful acceptance of a bid, Dietrich and the Retirement staff will work closely together in the transition process which includes the following:
 - a. Completion of the purchase documentation
 - b. Data reconciliation and final pricing adjustment (if necessary)
 - c. Timely transfer of payment data requirements to the carrier
 - d. Plan sponsor notifications of selected carriers to participants
 - e. Draft contract and approval
 - f. Liquidation of fund assets
 - g. Release of participant certificates

Proposed Charter Change

Changes to the Charter require a vote by the citizens of Oakland in the November 4, 2014 general election, while updates and changes to Ordinance No. 713 C.M.S. require an amendment through the Oakland City Council. Staff proposes a charter change that transfers the administration of the retiree benefits to an annuity provider. Upon elimination of City staff costs, many management functions would no longer be required, and the need for the OMERS Board would be eliminated. Staff's proposed Charter Change would *not* remove the City of Oakland as the ultimate guarantor of the retiree benefit payments. **Staff proposes a charter change that would eliminate administration costs, while protecting the retirees from any possible insolvency of an insurance company.**

Cost for Charter Change

A ballot measure requires significant staff time and resources to prepare the measure with extensive collaboration with the City Attorney's Office. Staff reports must be approved by the City Council in order for the item to be placed on the November 2014 ballot.

Ballot measures consolidated with the general election are significantly cheaper than special elections. The City Clerk's Office has advised departments to budget approximately \$225,000 for a ballot measure. This cost includes legal publication, preparation (drafting, binding, printing, postage, and mailing) of the sample ballot book in five required languages with all required information, printing of the official ballot, and postage and return envelopes for permanent mail ballot voters. OMERS' portion of the ballot costs cannot be determined until the ballot participants have been finalized.

The City Clerk's Office is already conducting an election for the elected offices for November 2014, therefore OMERS will not need to budget costs associated with poll workers, the voting machines, the County's staff costs, Clerk staff processing, etc.

Charter Change Schedule

Staff has reviewed the probable timeline to meet the required deadlines to place a charter change onto the November 4, 2014 general election ballot. On May 22, 2014, the OMERS Board passed Resolution No. 4839 C.M.S. (**attached**) confirming support of an amendment of Article XX of the City Charter for the purpose of terminating the OMERS Board and authorizing the City to purchase a group annuity from a Board-approved insurance carrier for the payment of benefits. After City Council approval, the City Auditor's Office and City Attorney's Office will also have to provide analysis and/or opinion on the ballot measure. Below is a tentative schedule for the ballot measure:

Last Regular OMERS meeting deadline for City Council package submission; decision should be made by this date	Thursday, April 24, 2014
Last Date to submit OMERS Charter Change to Meet City Council deadlines and allow for deliberation (probably for June 6, 2014 Council Meeting)	Friday, May 23, 2014
Scheduled date of Finance & Management Committee for review and consideration before submission to the City Council	Tuesday, July 8, 2014
Ballot Measure approved by City Council; Last Scheduled 2014 City Council Meeting before 88 day deadline (possible second reading)	Tuesday, July 15, 2014
Last Date for Election Material Submission to Alameda County Registrar (88 days before E-Day)	Friday, August 08, 2014
Election Day	Tuesday, November 04, 2014

Excess Funding

The OMERS Legal Counsel has previously provided a legal opinion stating that the OMERS fund is required to provide each qualified OMERS retiree and beneficiary with a retirement benefit described in the City Charter. The current annuity plan being developed will continue to provide this uninterrupted service to each OMERS retiree and beneficiary. Based on a preliminary analysis, the costs of an annuity as of July 1, 2014 would be approximately \$1.9 million. The OMERS Fund currently has approximately \$4.64 million in trust assets. After each annuity has been created for each OMERS retiree and beneficiary, there will be excess funds remaining in the estimated amount of approximately \$2.7 million. The OMERS Board will need to ensure these excess funds are placed in a reserve account and the City will need to monitor that account going forward.

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PUBLIC OUTREACH/INTEREST

This item will require significant outreach to retirees, unions, councilmembers and stakeholders to explain the intention of the measure and to assure stakeholders that this measure will not result in a change to pension benefits.

COORDINATION

This report was prepared in coordination with the City Clerk's Office, Budget Office and Office of the City Attorney.

COST SUMMARY/IMPLICATIONS

There are no immediate implications to the General Fund budget.

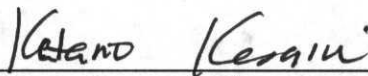
SUSTAINABLE OPPORTUNITIES

Economic: The City of Oakland seeks to continue the OMERS Retirement System in a cost efficient manner that will be beneficial to the City and to the System over the remaining life of the System without impacting the Retirees.

Environmental: There are no environmental opportunities associated with this report.

Social Equity: There is no social equity opportunities associated with this report.

Respectfully submitted,



Katano Kasaine, Plan Administrator
Oakland Municipal Employees' Retirement System

Prepared by: Téir Jenkins, Investment Officer
Retirement Division

Attachments:

- DRAFT CITY COUNCIL RESOLUTION NO. _____ C.M.S.
- OMERS Resolution No. 4839 – Confirmation of support of City Council amendment to Article XX of the Oakland City Charter

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OAKLAND MUNICIPAL EMPLOYEES' RETIREMENT BOARD
CITY OF OAKLAND, CALIFORNIA

RESOLUTION No. 4839

ON MOTION OF MEMBER RUBY SECONDED BY MEMBER KASAINÉ

RESOLUTION OF THE OAKLAND MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM ("OMERS") BOARD CONFIRMING SUPPORT OF AN AMENDMENT OF ARTICLE XX OF THE CITY CHARTER FOR THE PURPOSE OF TERMINATING THE BOARD AND AUTHORIZING THE CITY TO PURCHASE A GROUP ANNUITY FROM A BOARD-APPROVED INSURANCE CARRIER FOR THE PAYMENT OF BENEFITS

WHEREAS, as of May 14, 2014, there were only 10 retirees and 13 beneficiaries with an average age of 90 years remaining in the OMERS Retirement System ("System"); and

WHEREAS, the administrative budget for the 2013- 2014 fiscal year was \$341,494.00; and

WHEREAS, the Board's actuarial consultant, Bartel Associates, LLC, has informed the Board that the cost of administering the System will continue to rise over time relative to the benefits that are disbursed to retirees and beneficiaries; and

WHEREAS, the Board understands that a reduction of administrative expenses may require that the City Council eliminate the Board and replace the current System with a group annuity provided by an insurance carrier; and

WHEREAS, in accordance with Article XVI, section 17 of the California Constitution the Board has a fiduciary duty to select a highly rated insurance carrier that can best administer the remaining benefits under the System; and

WHEREAS, the Board is supportive of a Charter amendment that results in the payment of benefits by a group annuity from an insurance carrier that has been approved by the Board provided the retirees and beneficiaries of the System continue to receive the benefits to which they are entitled, including annual increases for cost-of-living adjustments (COLA); and

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OFFICE OF THE CITY ATTORNEY

OAKLAND CITY COUNCIL

RESOLUTION NO. _____ C.M.S.

INTRODUCED BY COUNCILMEMBER _____

RESOLUTION SUBMITTING ON THE COUNCIL'S OWN MOTION A PROPOSED CHARTER AMENDMENT TO BE VOTED UPON AT THE MUNICIPAL ELECTION TO BE HELD ON NOVEMBER 4, 2014 THAT WOULD (1) GRANT THE CITY THE OPTION TO PURCHASE A GROUP ANNUITY CONTRACT FROM A REPUTABLE AND STABLE ANNUITY PROVIDER TO GUARANTEE PAYMENT OF THE BENEFITS PROVIDED BY THE OAKLAND MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM (OMERS) TO THE APPROXIMATELY 22 REMAINING MEMBERS AND BENEFICIARIES AND (2) SAVE THE CITY THE COSTS OF ADMINISTERING OMERS, WHICH WAS CLOSED TO NEW MEMBERS IN SEPTEMBER, 1970; DIRECTING THE CITY CLERK TO FIX THE DATE FOR SUBMISSION OF ARGUMENTS AND TO PROVIDE NOTICE AND PUBLICATION IN ACCORDANCE WITH THE LAW AND AUTHORIZING CERTAIN OTHER ELECTION ACTIVITIES

WHEREAS, Oakland City Charter Article XX established the Oakland Municipal Employees' Retirement System ("OMERS") to provide retirement benefits for all City employees except sworn members of the Police and Fire Departments and created the Board of Administration to administer and manage the funds of the retirement system; and

WHEREAS, OMERS is a qualified pension plan under the requirements of the United States Internal Revenue Code and is subject to the provisions of the California Constitution pertaining to public retirement systems, which confers upon the retirement boards of public retirement systems plenary authority and fiduciary responsibility for the investment of moneys of those systems necessitating that the OMERS board conduct actuarial valuations, pay pensions, retain investment advisors and otherwise comply with the board's fiduciary duties; and

WHEREAS, OMERS was closed to new members in September, 1970 and thereafter all new miscellaneous (non-sworn) employees became eligible for membership in the California

Public Employees Retirement System ("CalPERS") and OMERS members were given the option to transfer their retirement benefits to CalPERS; and

WHEREAS, the annual administrative costs of maintaining OMERS now exceed the annual cost of benefit payments; and

WHEREAS, federal and state pension laws provide that a qualified retirement system can be terminated by purchasing an annuity contract with a qualified insurance provider whereby each member or beneficiary receives an individual annuity guaranteed and administered by the insurance provider; and

WHEREAS, termination of OMERS will allow the Board of Administration to be dissolved and the administrative costs to be eliminated; and

WHEREAS, OMERS holds funds sufficient to purchase an annuity contract which will guarantee the payment of all current accrued benefits; and

WHEREAS, the Internal Revenue Service provides a procedure for termination of OMERS that will confirm the tax-qualified status of the remaining benefits for members and beneficiaries; and

WHEREAS, under federal pension law assets remaining in OMERS after purchasing the annuity contract and satisfaction of all other outstanding liabilities, including payment of all retirement benefits provided by OMERS to all remaining members and beneficiaries, may revert to the City; and

WHEREAS, notwithstanding the annuity contract will guarantee payment of all benefits provided by OMERS to the remaining members and beneficiaries, the City shall retain any OMERS funds in a trust account until such time as all members and beneficiaries have expired; and

WHEREAS, the City Council desires to amend Oakland City Charter Article XX to authorize the City Council to terminate OMERS by subsequent ordinance and to require the performance of such functions as are necessary and proper for the termination of OMERS; and

WHEREAS, section 10400 et seq. of the Elections Code allows for the Oakland municipal election of November 4, 2014 to be consolidated with the statewide election to be held on the same date; now, therefore be it

RESOLVED: That the City Council hereby authorizes and directs the City Clerk, at least 88 days prior to November 4, 2014 to file with the Alameda County Board of Supervisors and the County Clerk certified copies of this resolution; and be it

FURTHER RESOLVED: That the City of Oakland does hereby submit to the voters at the November 4, 2014 general election, a proposed Amendment to Charter Article XX, which reads as follows (additions are indicated by underscoring and deletions are indicated by strike through type):

“Termination and Winding Up of Retirement System

Section 2017. Notwithstanding any contrary provision herein, the Council may by an ordinance adopted by four-fifths of the Council terminate the Retirement System and in connection therewith direct the Retirement Board to wind-up said Retirement System by performing the following actions:

- (a) Purchase life annuities for retired members, former members or other persons currently receiving Benefits under the Retirement System through a reputable and stable annuity provider provided that such annuities provide payments that are equal to the Benefits due under the Retirement System;
- (b) Provide for payment of any other outstanding liabilities; and
- (c) Any other actions which are necessary and prudent to terminate the Retirement System.

Notification of Termination and Winding Up

Section 2018. The City must give notice, or cause notice to be given, of its intention to terminate and wind up the Retirement System, in writing, to the following:

- (a) Each retired member and former member; or
- (b) If a retired member or former member has died, the surviving spouse, designated beneficiary or personal representative of the estate of the retired member or former member as ascertainable by the City.

The notice required under subsection (1) must give the effective date of termination and start of the winding up process, explain the manner in which Benefits will continue to be provided, and be given at least 60 days before the effective date of the ordinance terminating the Retirement System.

Reversion of Assets

Section 2019. Notwithstanding any contrary provision herein, in the event the Retirement System is terminated pursuant to Section 2017 herein, none of the assets of the Retirement System shall revert to the benefit of the City until provision has been made for the funding or purchase of Benefits accrued but unpaid under the Retirement System. Any remaining surplus shall revert to the City provided that such surplus shall be held in a reserve account with the necessary restrictions to ensure that the assets thereof shall not be used by the City, other than to satisfy any liabilities of the Retirement System which are not fulfilled by the selected annuity provider, until such time as the last retired member, former member or beneficiary thereof dies. For this purpose, the term “surplus” shall mean the assets of the Retirement System remaining after satisfaction of all liabilities.

Effect of Termination and Winding Up

Section 2020. If the Council adopts an ordinance to terminate and wind up the Retirement System, the Retirement System shall continue to be subject to the requirements of this Article XX and Ordinance 713, as amended, until all the assets of the Retirement System have been disbursed. Once the assets have been disbursed, the Retirement System shall terminate and the Retirement Board shall be dissolved."

;and be it

FURTHER RESOLVED: That in accordance with the Elections Code and Chapter 11 of the Oakland Municipal Code, the City Clerk shall fix and determine a date for submission of arguments for or against said proposed Charter amendment, and said date shall be posted in the Office of the City Clerk; and be it

FURTHER RESOLVED: That in accordance with the Elections Code and Chapter 11 of the Oakland Municipal Code, the City Clerk shall provide for notice and publication as to said proposed Charter amendment in the manner provided for by law; and be it

FURTHER RESOLVED: That the City Clerk and City Administrator are hereby authorized and directed to take any and all actions necessary under law to prepare for and conduct the November 4, 2014 election and appropriate all monies necessary for the City Administrator and City Clerk to prepare for and conduct the November 4, 2014 election, consistent with law.

IN COUNCIL, OAKLAND, CALIFORNIA,

PASSED BY THE FOLLOWING VOTE:

AYES - BROOKS, GALLO, GIBSON, MCELHANEY, KALB, KAPLAN, REID, SCHAAF
AND PRESIDENT KERNIGHAN

NOES -

ABSENT -

ABSTENTION -

ATTEST:

DRAFT

LATONDA SIMMONS
City Clerk and Clerk of the Council
of the City of Oakland, California