

ANTONIO R. VILLARAIGOSA
MAYOR

April 20, 2012

The Honorable Members of the City Council
c/o Office of the City Clerk
200 North Spring Street, Room 395
Los Angeles, CA 90012

Dear Honorable Members:

My Proposed Budget for Fiscal Year 2012-13 reflects an unwavering commitment to making Los Angeles a city of safe neighborhoods and strong communities, a city that protects core municipal services, and a city with its long-term financial health and economic vitality ensured. This \$7.2 billion budget closes an estimated \$238 million deficit through expenditure cuts, operational efficiencies and revenue maximization efforts. Two-thirds of these measures are on-going and will permanently reduce the General Fund structural deficit.

Two years ago the City Administrative Officer (CAO) estimated that the City's structural deficit would balloon to more than \$1 billion by fiscal year 2013-14. If you adopt my Proposed Budget, we will build upon the actions that we have already taken together as a city to weather the Great Recession; we will significantly reduce our structural deficit; and, we will ensure the continued delivery of the City's core services for all Angelenos. In addition to drastically reducing the City's projected gap between revenue and spending, we have prioritized strengthening of our cash reserves. My proposed budget establishes a \$211 million Reserve Fund. As a percentage of the General Fund, this is the largest reserve set aside since 2002.

While many difficult choices and necessary sacrifices have already been made, we must continue to directly address the city's major cost drivers. Regrettably, this will entail workforce reductions. Since 2008, the general fund civilian workforce has been cut by one-third, from nearly 14,000 positions to roughly 9,000 positions. This year, I am proposing the elimination of an additional 669 authorized positions. This represents one of the most difficult decisions in this year's budget, especially since 231 of these positions are currently filled and eliminating them will result in lay-offs.

Workforce reductions alone will not address our current fiscal challenges. Last year, we worked with our labor partners to reach a historic agreement. The vast majority of

active sworn and civilian employees agreed to increase their contribution toward their retirement benefits to 11% of pay. This saved the City hundreds of millions of dollars. However, the costs of pension and retiree healthcare benefits continue to represent a sizeable component of the City's structural budget deficit. By Fiscal Year 2014-15, the City could be contributing nearly 30 cents towards retirement benefits for every dollar it spends on salaries for civilian employees. Further reforms to employee health and pension benefits are needed to protect basic levels of City services.

Today I am proposing a pension reform plan for new civilian employees (attached) that increases the retirement age to 67, eliminates pension spiking and implements other reforms necessary to reduce long-term pension costs. At my instruction, the CAO is analyzing this proposal and will report to the full City Council in the next 30 days with recommendations to implement my plan. I strongly urge you to review and expeditiously adopt these reforms.

My budget plan will continue to maintain the size of the Los Angeles police force at its current strength. This has helped bring violent crime in the City down to levels not seen since the 1950's. My budget will also add funding to offset the loss of discretionary Federal monies to maintain the City's Office of Gang Reduction and Youth Development (GRYD). This program is responsible for the successful implementation of a comprehensive violence reduction strategy in communities most impacted by gang violence.

In order to further secure the safety of our neighborhoods and families, my budget restores Fire Department resources to improve emergency incident response times. These resources include funding for six additional ambulances, one Valley engine company, and the restoration of Emergency Medical Services (EMS) Captains. Funding will also be provided to begin the recruitment and hiring of new, well-qualified firefighters to lay the foundation of a multi-year strategy to strengthen the Fire Department, thereby ensuring the highest quality emergency services for all Angelenos.

In addition to these public safety related initiatives, the FY 2012-13 Proposed Budget includes the following key measures:

- Implements the first phase of a Performance-Based Budgeting system;
- Expands public library hours on Monday and Wednesday nights as well as Friday mornings at all 63 branch libraries citywide;
- Leverages Measure R local return dollars to preserve and resurface 800 miles of city streets (9% increase) and repair 350,000 potholes (17% increase);
- Initiates the first year of a five-year plan to re-write the City's 75 year old zoning code and continues funding for seven community plan updates;
- Centralizes Human Resource (HR) functions citywide and consolidates General Service police and security functions into the Los Angeles Police Department;

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- Provides seed money for the establishment of a new, city-wide economic development delivery model for the purpose of job creation, revenue generation and economic opportunity in under-served communities.

Over the last three years, we have confronted the most challenging budget situation in generations. We have faced this challenge squarely, and we have come together to make the hard, but necessary decisions. We have both addressed our annual budget shortfalls and made significant progress in reducing our City's long-term structural deficit. We have succeeded because a commitment to shared responsibility and shared sacrifice has guided our decisions. With your continued partnership and your continued strong sense of resolve, we will successfully meet this fiscal year's challenge, we will protect the vital services Angelenos rely on, and we will ensure that Los Angeles remains on a trajectory of long-term fiscal stability.

Very truly yours,



ANTONIO R. VILLARAIGOSA
Mayor

ARV:msr

Attachment



ANTONIO R. VILLARAIGOSA
MAYOR

Civilian Pension Reform Plan

April 20, 2012

The City of Los Angeles provides excellent post-employment benefits to its employees and their beneficiaries. Unfortunately, the rising cost of these pension and retiree healthcare benefits represent a key component of the City's structural budget deficit. By Fiscal Year 2014-15, it is projected that the City could be contributing nearly 30 cents towards retirement benefits for every dollar it spends on salaries for civilian employees. This percentage would be even larger had it not been for the cost reductions we have achieved as a result of the majority of active employees agreeing to contribute toward retiree healthcare.

While some progress has been made, it remains clear that further pension reform efforts are necessary and must be pursued. However, the options for reducing costs associated with active or retired employees are extremely limited as the benefits received by these employees are vested under the California State Constitution. One of the only measures left to reduce future retirement costs is the implementation of a new tier of retirement benefits for new civilian employees. I am therefore proposing the following measures to improve the City's long-term financial sustainability and ensure the efficient provision of reliable retirement benefits for future civilian employees.

1. Increase the Retirement Age to 67

Current City employees can retire as early as age 55 with full benefits. This is a very generous benefit at a time when the full unreduced retirement age for Social Security participants is age 67 and average life expectancy is 78 years. I propose increasing the normal retirement age to age 67, or indexing the retirement age to Social Security.

2. Cap the Maximum Retirement Allowance

Under the current plan, City employees can work enough years to obtain 100% of their salary in retirement. I propose capping the maximum retirement allowance to 75% of Final Compensation.

3. Reduce the Retirement Factor

The retirement factor is a percentage of Final Compensation that is earned for each year of City service. For example, a current 55 year old employee that had worked 30 years could retire with 64.8% of Final Compensation (2.16% per year of service). I propose reducing the Retirement Factor to a maximum of 2% at Age 67 with a reduced factor for earlier retirements. As a comparison, CalPERS offers an array of plans with retirement factors that range from 1.25% to 3%.



4. Restructure How “Final Compensation” is Calculated to Prevent “Pension Spiking”

The Retirement Factor (see #3, above) is currently applied to an average of the employee’s highest 12 months of base salary plus pensionable bonuses and premium pay. Although it is not a prevalent practice, the opportunity exists to “spike” the pension benefit, i.e., earn a higher pension benefit that has not been actuarially paid for by promoting the year before retirement. A more common sense approach would be to average Final Compensation over a longer period of time. I propose averaging Final Compensation over the last 5 years of highest salary and to end the practice of negotiating pensionable bonuses and premium pay.

5. Reduce Pension Cost of Living Adjustments (COLAs)

I propose reducing COLAs to a maximum of 2% per year based on CPI with no COLA banking from a maximum of 3% per year with COLA banking. (COLA banking allows unused COLAs in years where CPI is less than the COLA cap to be applied to future years in which the CPI exceeds the COLA cap).

6. Obtain Better Control Of Retiree Health Costs

We have already taken great steps to reduce our liability for retiree health costs. Decades ago, and far in advance of most jurisdictions throughout the nation, we changed from a Pay-As-You-Go system (one that pays only the current year liability) to one that pre-funds the cost of future liability. In addition, most employees agreed to contribute more to retiree health in exchange for vesting that benefit. Nevertheless, retiree health costs are expected to continue growing at near double-digit rates, and we must do more. I propose reducing the cap from \$1,190 per month per employee to \$596, eliminating the benefit for dependents, indexing cost increases to the single-party rate of the lowest cost standard plan (instead of the Kaiser two-party rate), and allowing employees to obtain 100% of the benefit only after 30 years of service.

7. Ensure the Cost Neutrality of the Government Service Buyback Program

As a recruitment tool, we have allowed employees with prior governmental service to “purchase” those service years by contributing more to the retirement system. However, the purchase cost appears to be less than the benefit derived, which creates an additional liability that must be paid by the City. I have instructed the CAO to study the program’s cost neutrality in order to preserve this important recruitment tool in a fiscally responsible manner.

8. Share the Risk of Future Retirement Cost Increases with Employees

Many jurisdictions are developing different models to share the future cost of retiree benefits with employees. The Governor has proposed phasing-in a “50/50” cost-sharing model and others have explored defined contribution models in which risk is transferred to the employee. While I am open to considering alternatives, I have instructed the CAO to study cost-sharing models that: 1) allow employees to “pre-fund” retiree health COLAs based on expected age and retirement, and 2) change the employee contribution from a fixed percent of salary to a percent of the Normal Cost of the retirement or health benefit.