TO: HONORABLE CITY COUNCIL
FROM: CITY MANAGER DEPARTMENT: ADMINISTRATIVE SERVICES
DATE: October 10, 2006
CMR: 388:06

SUBJECT: APPROVAL OF RESOLUTIONS AMENDING THE MERIT SYSTEM RULES AND REGULATIONS TO ADOPT A MEMORANDUM OF AGREEMENT WITH SERVICE EMPLOYEES’ INTERNATIONAL UNION (SEIU), LOCAL 715 AND ADOPTING A NEW COMPENSATION PLAN FOR SEIU CLASSIFIED PERSONNEL

RECOMMENDATION

Staff recommends the following to Council:

1. Approve the attached resolution amending Section 1401 of the Merit System Rules and Regulations to adopt a new Memorandum of Agreement between the City of Palo Alto and SEIU, Local 715 for an effective period of May 1, 2006 to June 30, 2009 (38 months).

2. Approve the attached resolution adopting a new Compensation Plan for SEIU Classified Personnel, effective with the pay period including May 1, 2006 through June 30, 2009.

BACKGROUND

The City’s agreement with SEIU Local 715 expired on April 30, 2006. The City commenced negotiations with SEIU on March 22, 2006 regarding the terms and conditions of employment for this represented unit. Following five months of negotiations consisting of 29 bargaining sessions, City staff and members of SEIU have reached an agreement within Council authorization, the details of which are contained in the attached Memorandum of Agreement.

Under State law, the City of Palo Alto is required to bargain in good faith and cannot unilaterally make contract decisions for represented employee groups. The City must also comply with collaborative bargaining laws and rules, and actions taken may be subject to review by the California Public Employee Relations Board (PERB).

The City of Palo Alto is part of a regional labor market and competes for talent with other public government and quasi-government agencies. For the purpose of negotiating labor agreements, the Bay Area Consumer Price Index (CPI) is generally used as a way to measure the impact of inflation on wages.
Based on recent negotiations involving SEIU and other organizations such as Stanford Hospital, County of Santa Clara and Santa Clara Valley Transportation Authority, City staff anticipated difficult negotiations with SEIU. The main issues of contract negotiations with these other organizations were salary increases and enhanced retirement benefits, with SEIU negotiating multi-year contracts with salary increases that have ranged between 9-12 percent as well as an enhanced retirement formula with the County of Santa Clara. Nine of the eleven labor market cities that were previously used as benchmarks for Palo Alto have improved or are in the process of improving their retirement formula beyond 2 percent @ 55 within the last several years. Attachment A provides a summary of Palo Alto’s 12 benchmark survey cities and identifies the cities which have enhanced retirement formulas.

One of City management’s key goals during this negotiation process was to contain escalating healthcare costs for existing employees and future retirees while retaining a competitive market position. According to a recent 2006 summary of findings by The Kaiser Family Foundation (KFF), employer health insurance premiums for family coverage have increased by 87.0 percent since the year 2000. For the City of Palo Alto, the increase has been substantially higher. Over the last five years, the average health premium costs paid by the City increased by 15.5 percent annually, for an overall total increase of approximately 93 percent. An article on the KFF website (kff.org) entitled, “Comparing Projected Growth in Health Care Expenditures and the Economy,” states that the Centers for Medicare and Medicaid Services projected national health care expenditure to increase from the current $2.16 trillion to $4.0 trillion by 2015, an increase of 85 percent. It also mentions that since 1970, health care spending has grown at an average annual rate of 9.9 percent or about 2.5 percentage points faster than the nation’s Gross Domestic Product (GDP). It adds that health care spending was at 7.2 percent of GDP in 1965 compared to over 16 percent today with a projection of 20 percent in 10 years.

During the past several years, the City has continued to work towards reductions in the high cost of health insurance benefits. One of the steps taken through prior negotiations was to cap the City contribution for healthcare premiums for the International Association of Firefighters bargaining unit and Management and Professional group. In addition, the majority of Palo Alto Police Officers Association employees agreed on a voluntary basis to be covered by less expensive health plans. In the prior SEIU agreement, the number of current employees allowed to enroll in PERS Care (the most expensive health plan) was limited to 62 of the 589 employees. The City also reached agreements with all the City’s bargaining groups to raise the vesting requirement for eligibility for retiree medical benefits from 5 years to 20 years for new hires. Finally, since fiscal year 2002-03, the City’s general fund (non-enterprise) workforce has been reduced by 10.0 percent (over 70 employees) through attrition and layoffs. These actions taken together have significantly reduced current healthcare costs.

**DISCUSSION**

Key items in the proposed agreement with SEIU include:
Healthcare Cost Containment

- The City will reduce maximum payment for medical premiums from the highest health plan (PERS Care) to the second highest (currently Blue Shield HMO) for all current employees and future retirees. This change represents approximately $450,000 annual savings in medical premium payments made by the City for current employees alone. To illustrate the impact in cost: monthly premium payments made by the City for an employee plus family in the PERS Care plan versus the PERS Choice plan are $2,001 compared to $1,183 for PERS Choice, a savings of $818 per month or $9,816 per year. The elimination of the PERS Care option will significantly cut healthcare premium costs of future retirees.

- The City will provide an annual stipend of $50,000 to cover the out-of-pocket costs for employees that move from PERS Care to PERS Choice. The maximum stipend will be $1,000 per employee or $2,000 for employees with family coverage for the term of the contract. The purpose of this stipend is to provide coverage for non-reimbursable costs incurred by employees with serious medical needs. It is not anticipated that all 57 employees will need reimbursement since some will retire, others will select plans other than PERS Choice, and many will not incur expenses requiring reimbursements.

CalPERS Retirement

- The agreement increases the pension formula from 2.0 percent per year of service to 2.7 percent @ 55 years of age effective January 6, 2007. Total cost for this change is 7.0 percent. Effective January 6, 2007, all employees will pay 1.0 percent share of the PERS pension expense, reducing the cost to the City to 6 percent. The net present value (NPV) of this enhanced benefit is approximately $25.0 million to be paid over the next 23 years, for an average annual cost of $1.08 million.

- Effective the pay period inclusive of July 1, 2007, all employees will pay an additional 1.0 percent share toward 2.7 percent @ 55 for a total of 2.0 percent, reducing the cost to the City to 5.0 percent.

Salary

- A 7.5 percent base salary increase over the 3-year contract. After taking into account the employee contribution of 2.0 percent towards the PERS expense, this provision results in a net salary increase of 5.5 percent over the term of the 3-year contract. The latest Bay Area CPI, reported in September, was 3.8 percent. This is the factor that is generally considered the benchmark for salary increases. The annual salary increases are as follows:

  a) A zero percent base wage increase from May 1, 2006 to January 1, 2007;
b) A 1.0 percent base wage increase to all classifications effective January 1, 2007 (impacts only half of the fiscal year);

c) A 3.5 percent base wage increase to all classifications effective July 1, 2007;

d) A 3.0 percent base wage increase to all classifications effective July, 1, 2008.

Strengthened Management Rights

- The City re-affirmed existing language in the contract which gives the City the ability to outsource workforce following timely notification.

- The City eliminated “in-lieu pay” for meals for Public Safety Dispatcher classifications. In-lieu meals were paid at time and one half base pay and will now be paid at the base salary rate only, eliminating 1/3 of the City’s previous costs in this area.

- The City has increased options for selecting qualified employees for promotional opportunities. Currently, if three qualified employees apply for a position in a department no other candidates may be considered. The City may now consider external candidates if three or more internal apply but do not successfully complete the selection process.

- Night shift premium will only be paid if an employee works a complete night shift.

Equity Adjustments and Other Modifications

- The City has added several provisions to address recruitment and retention issues for classifications where there are labor market shortages of qualified candidates. Lineperson/Cable Splicer job classifications have been modified to provide greater entry level recruitment opportunities. Water Treatment Plant Operators, Water Transmission Operators, and Utility Installer Repairers will receive 1 percent base pay premium for additional certifications.

- Work-out-of-classification pay has been capped at 5 percent for SEIU employees who receive authorized assignments other than lead or supervisory assignments. Lead and supervisor assignments will receive 7 percent. The reduction of qualifying days and the implementation of a pay code to address this issue will also significantly reduce administrative requirements.

- The agreement modifies various sections of the contract relating to reduction in work force, grievance and discipline procedures, union security, vacation accruals, worker’s compensation benefits, tool allowances, pay practices, certifications, bereavement leave, and use of sick leave.
• The impact of the above changes equals 0.75 percent of the base compensation and is effective September 30, 2006. A comprehensive summary of the changes made to the 2006-2009 SEIU Memorandum of Agreement can be found in Attachment B.

RESOURCE IMPACT

The proposed recommendations do not require a budget adjustment for fiscal year 2006-07 since the increases start at midyear or partially in the fiscal year and there are sufficient funds included in the adopted budget. The impacts for future years will be included in the proposed budgets submitted for fiscal years 2007-09. The total impact to the base compensation for SEIU totals $5.8 million or 11.65 percent for the 38 month agreement. Over a three-year period the agreement totals 11.0 percent: since staff wanted the SEIU agreement to coincide with the City’s fiscal year to facilitate budget preparations, two extra months were added to the agreement resulting in the additional 0.65 percent.

The City is balancing its risk between medical and pension costs by capping its medical premiums while enhancing the pension plan. Since CalPERS manages the pension fund (one of the largest funds in the world) and has a 9.2 percent rate of return over the last ten years, it is a more predictable expense versus extremely volatile health care expenses, which the City has little control over. The 7 percent annual costs of 2.7 percent @ 55 consist of 2 percent for the normal ongoing cost and 5 percent for the previous years of expense for current employees. The 5 percent figure will be paid over a 23 year period while the cost avoidance from capping medical expenses goes on into perpetuity.

As mentioned previously, the City currently has 57 SEIU employees enrolled in the highest cost medical plan, PERS Care, so the negotiated changes result in an additional $450,000 in healthcare expenses. Furthermore, of the 589 current SEIU members, over 40 percent are age 50 or over, and can currently select PERS Care as their medical plan upon retirement. Given the current expense for PERS Care it is likely that this amount would increase into the millions of dollars should future SEIU retirees select this option.

To illustrate the relative importance of capping retiree medical costs, if a current employee retires at age 55 with a life expectancy of 78 years of age, the City would pay the higher premium for approximately twenty-three years, a difference of approximately $333,600. Under this example, if all current 57 employees remained in the higher cost plan the cost difference over the projected 23 years would be approximately $20.7 million in current dollars, and cost avoidance would be approximately $8.8 million (NPV). Again, using this example, if the current 589 employees in the unit convert to the higher cost plan at the City’s current retirement plan selection rate, the difference in cost over the next twenty-three years would be approximately $78.7 million in current dollars and the projected cost avoidance would be $33.4 million (NPV). Using this analysis, the cost of enhanced retirement is offset by the significant reduction in future retiree medical cost. This change will significantly help control the over $148.7 million retiree medical liability recently documented in CMR 272:06 Results of Actuarial Study for Retiree Medical Benefits – Governmental Accounting Standards Board Statements Numbers 43 & 45 reported to Council June 20, 2006.
POLICY IMPLICATIONS

This recommendation is consistent with existing City policies.

ENVIRONMENTAL REVIEW

This action does not require an environmental review.

ATTACHMENTS

A. Summary of the City’s twelve benchmark survey cities, including Palo Alto.
B. Summary of the changes made to the 2006-2009 SEIU Memorandum of Agreement.
C. Total Cost of SEIU MOA
D. Resolution Amending Section 1401 of the Merit System Rules and Regulations.
E. Resolution Adopting a Compensation Plan for Classified Personnel (SEIU).

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