



SAN DIEGO COUNTY  
REGIONAL AIRPORT AUTHORITY  
**STAFF REPORT**

Item No.  
**15**

Meeting Date: FEBRUARY10, 2011

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**Subject:**

**Board Discussion and Possible Action Regarding Employee Purchases of Service Credits from the San Diego City Employees' Retirement System (SDCERS)**

**Recommendation:**

Provide direction to Staff on the San Diego County Regional Airport Authority's (Airport Authority) reply to the San Diego City Employees' Retirement System (SDCERS) Board of Administration's inquiry as to whether or not the Airport Authority wishes to exempt any or all of the affected employee Purchase of Service Credit (PSC) contracts from correction by continuing to fund the underpayment through the Airport Authority's Annual Required Contribution and, depending upon the Board's decision, also whether or not the Airport Authority would allow existing employees who entered into the Deferred Retirement Option Plan (DROP) to rescind their DROP contracts.

**Background/Justification:**

On January 21, 2011, the Airport Authority was provided with the requested detailed analysis of the individual and collective impact of the Purchase of Service Credit (PSC) "window period" pricing (see attached). According to the analysis, the net due to SDCERS will vary depending on the available option chosen by the respective individual. One of the options proposed (option 4) was to require employees to pay the difference between the true actuarial liability and the underfunding at purchase price. The impact of choosing to pay the entire net difference for individual employees due to SDCERS ranges from \$37,761 to \$271,107 with an average individual amount of \$90,155. The aggregate amount is \$3.5 million. This issue was heard by the Airport Authority Board on both September 2, 2010 and October 7, 2010. At the October 7, 2010 meeting, the Board inquired about the impact on individuals, which was not available as SDCERS was in the midst of conducting the analysis. At that time, the Board passed Resolution No. 2010-0112 requesting an extension of time to reply to SDCERS Board's request to notify them of the Airport Authority's interest in volunteering to pay for some, or all, of the purchase of service credit underfunding identified by an actuarial analysis. The SDCERS Board granted the requested extension with the stipulation that the Authority has 60 days from receiving the requested information to notify the SDCERS Board of its intentions.

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In the event that the Board determines that the Airport Authority will not exempt any or all of these contracts from being corrected, then the Board is asked to consider allowing individual employees who purchased PSCs and who entered into DROP to rescind their DROP contracts.

Thirty nine Airport Authority employees (36 current, 3 former) are affected by the outcome of the litigation between the City of San Diego and SDCERS. On June 7, 2010, the Fourth District Court of Appeals issued a ruling related to the pricing of PSCs. The decision relates to under-pricing of PSC contracts (which likely includes multiple types of PSC time) purchased by City of San Diego participants on or after August 16, 2003. The court's ruling focuses on PSC requests submitted or purchased between August 16 and November 1, 2003, (the "window period"), but more importantly, the decision applies to any City contracts calculated at the old rates and purchased on or after August 16, 2003. This court ruling appears to affect Airport Authority employees as the SDCERS Board of Administration raised Airport Authority PSC pricing at its April 16, 2004 meeting with an effective date of July 1, 2004, creating a "window period" which has subsequently been ruled as a violation of the plan provisions. Specifically, the court ruled that SDCERS had violated the provisions of the plan relating to purchase of service and could not recover the underfunding created by these underpriced PSCs from the City through the Unfunded Actuarial Liability (UAL). SDCERS' tax counsel has determined that the same is true relating to the delayed implementation of the rate change for Airport employees. This means that affected participants may need to pay additional money toward their purchase, or have their service credit reduced or request a full refund.

Absent the Airport Authority's Board indicating interest in continuing to absorb the cost of PSC under pricing through The Authority's UAL, 39 individuals will likely be asked by SDCERS to decide whether to pay the difference (plus interest), accept a reduced service credit, or receive a full refund. SDCERS Board has strived to fulfill its fiduciary duty to its participants on this issue. Because the Internal Revenue Service requires that SDCERS collect the underfunding from some source so that the trust fund is made whole, the only viable solution to this problem is to collect the underfunding from the affected participants.

The San Diego County Regional Airport Authority Board of Directors received an update on this item at its September 2, 2010 Board meeting from Authority General Counsel Bret Lobner, Jeff Lindeman, as well as from CEO of SDCERS, Mark Hovey. At that time, the SDCERS Board of Administration had not yet considered all available options for affected individual employees to correct the PSC "window period" contracts. After the discussion, Board member Finnilla moved that the Authority Board direct staff to not absorb the cost of PSC under pricing through the Authority's UAL. Board member Boland asked Ms. Finnilla to hold the motion in abeyance pending additional information such as SDCERS Board action, approved employee options, cost of underfunding, etc.

On Friday, October 1, 2010, the SDCERS Board approved, by a vote of 8-0, the options recommended to it by SDCERS staff. Those five options are included in the attached document entitled Purchase of Service Credit Corrective Action; Options Available to Correct PSC "Window Period" Contracts (Attachment A). In addition, the SDCERS Resolution (Attachment B), confirming the action is also included. SDCERS staff were on-site to present affected Airport Authority employees with the SDCERS Board approved options and answer general questions on Wednesday, October 6, 2010.

This situation may, depending upon the Airport Authority's Board decision, have an impact on the Airport Authority's Fiscal Year 2011 Actuarial Valuation report, with a likely small positive effect on the plan's UAL.

**Fiscal Impact:**

Pending no action by the Authority's Board of Directors to continue paying for underpriced PSCs, there will likely be a positive impact on the yet to be calculated FY 11 UAL as determined by the SDCERS Actuarial firm, Cheiron. Should the Board determine to pay for the underpriced PSC's, the actuarial cost of \$3.5 million will continue to be amortized in the Annual Required Contribution.

**Environmental Review:**

- A. This Board action is not a project that would have a significant effect on the environment as defined by the California Environmental Quality Act ("CEQA"), as amended. 14 Cal. Code Regs. §15378. This Board action is not a "project" subject to CEQA. Cal. Pub. Res. Code §21065.
- B. This Board action is not a "development" as defined by the California Coastal Act. Cal. Pub. Res. Code §30106.

**Equal Opportunity Program:**

Not Applicable

**Prepared by:**

JEFF LINDEMAN  
DIRECTOR, HUMAN RESOURCES



**Purchase of Service Credit Corrective Action  
Options Available To Correct PSC "Window Period" Contracts**

<b>Member Category</b>	<b>Option 1</b>	<b>Option 2</b>	<b>Option 3</b>	<b>Option 4</b>	<b>Option 5</b>
	<i>"Rescind and Refund 2003 Old Rate contract payments, plus interest"</i>	<i>"Rescind and Apply 2003 Old Rate contract payments, plus interest, to New Contract"</i>	<i>"Reduce Service Credit to equivalent of Amount Paid"</i>	<i>"Pay the difference between 2003 Old Rate and 2003 new rate"</i>	<i>"Rescind DROP Contract to the extent legally permissible"</i>
<b>Administrative Action Correction Priority:</b>					
<b>1. Active DROP</b>	Yes	Yes,  If DROP contract Rescinded (May require Plan Sponsor's consent)	Yes	Yes	Yes  If DROP contract Rescinded (May require Plan Sponsor's consent)
<b>2. Retired DROP (retired after 11/16/07)</b>					
a. DROP account annuity with SDCERS	Yes	No	Yes	Yes	Yes
b. DROP account zero balance at SDCERS	Yes	No	Yes	Yes	Yes
<b>3. Retired (retired after 11/16/07)</b>	Yes	No	Yes	Yes	No
<b>4. Active</b>					
a. Contracts paid in full	Yes	Yes	Yes	Yes	No
b. Installment contracts still in progress	Yes	Yes	Yes	Yes	No
<b>5. Deferred</b>	Yes	No	Yes	Yes	No
<b>6. Disability Retired</b>	Yes	No	Yes	Yes	No
<b>7. Continuances</b>					
a. Receiving a retirement allowance continuance	Yes	No	Yes	Yes	No
b. Receiving both a retirement allowance continuance and DROP annuity survivor benefit	Yes	No	Yes	Yes	No
c. Receiving a survivor's DROP annuity benefit (non-spouse beneficiary)	Yes	No	Yes	Yes	No

<b>Impacts of Options:</b>	
<b>Option 1</b>	a. Compute the amount of the contract refund, which is a return of member contributions, plus interest, from the member's contribution account; b. Return amounts to member's source plan (if available) for payments made by Plan-to-Plan transfers; c. Refund amounts to members for PSC payments made by Pre- or Post-tax installment contracts; d. Eliminate service credit for the rescinded contract; e. Compute benefits overpaid plus interest (if any, for retired or DROP active members) and recover from member.
<b>Option 2</b>	Calculate the net difference between a refund of the original contract (Option 1) and the cost of a new 2010 contract. A net refund would be returned to the member's source; a net additional cost would be paid by the member by any payment options currently available.
<b>Option 3</b>	a. No additional payment is owed by the member; b. Calculate reduced number of years of Service Credit equivalent to amount paid; c. Compute benefits overpaid plus interest (if any, for retired or DROP active members) and recover from member.
<b>Option 4</b>	Member pays additional contributions owed, in part or in full, plus interest. DROP Active and Retired members only may choose to retain only enough partial Service Credit to retain eligibility for service retirement and/or DROP, provided corresponding adjustments are made to any past and future retirement allowances, contributions, and interest.
<b>Option 5</b>	Applicable to Active DROP members only. Subject to collection of retirement contribution arrearages, unwinding the DROP benefit, and netting any amounts due to or from SDCERS and the member. May require Plan Sponsor's consent and to the extent legally permissible.
<b>Payment Options</b>	The available payment options include: lump-sum transfers from other qualified pension plans, including SPSP, 401(k), and 457 plans; transfers from a personal IRA; personal funds; payroll deductions from a post-tax installment plan; any other options that may be identified.



**BOARD OF ADMINISTRATION  
SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM  
RESOLUTION NO. 2010-02**

**RESOLUTION IMPLEMENTING FOURTH DISTRICT COURT OF APPEAL  
DECISION REGARDING SERVICE CREDIT PURCHASES UNDER SAN  
DIEGO MUNICIPAL CODE SECTION 24.1312 AND COMPARABLE PLAN  
DOCUMENT PROVISIONS**

WHEREAS, on June 7, 2010, the Fourth District Court of Appeal issued an opinion in *City of San Diego v. San Diego City Employees' Retirement System* 186 Cal. App. 4th 69 (2010) (the "PSC Decision"), in which it determined that SDCERS did not have the right to charge the City of San Diego ("City") for SDCERS' underfunding of service credits purchased under San Diego Municipal Code section 24.1312 (referred to in the PSC Decision as "air time") during a "window period" by continuing to use lower previously determined flat rates after the SDCERS Board of Administration ("Board") determined to increase those two flat rates to purchase service credit ("PSC") under that Municipal Code provision on August 15, 2003; and

WHEREAS, the court characterized its ruling in the PSC Decision as "very narrow," in that it applied only to the "window period" implemented by the Board after the Board had increased the two PSC purchase rates, and it applied only to the "air time" PSC provision in the San Diego Municipal Code that required employees to pay both the employee and employer cost of the PSC; and

WHEREAS, the court concluded in the PSC Decision that it was "not within SDCERS's authority to expand pension benefits beyond those afforded by the authorizing legislation." Specifically, the court determined that PSC contracts using the delayed "window period" flat rates were not authorized under Municipal Code section 24.1312, because SDCERS had no legal authority to continue to offer service credit at the old rates once the Board had determined that new higher flat rates were required to cover both the employee and employer cost of the service to be purchased.

WHEREAS, the court described various options potentially available to SDCERS to correct this situation, including "'voiding contracts,' 'collecting arrears payments,' 'offering rewritten contracts,' 'spreading out additional payments,' [and] 'reducing benefits levels,'" and stated that the "only thing [SDCERS] may not do is charge the City for the underfunding that was the subject of the [trial] court's order"; and

WHEREAS, as a result of the PSC Decision, SDCERS is prohibited from requiring the City to make up the underfunded amount by including it in the City's unfunded actuarial liability ("UAL"); and

WHEREAS, as a result of the PSC Decision, SDCERS also has no legal authority to continue to provide benefits based on the service purportedly purchased by the underpriced PSC contracts, absent a member/beneficiary's selection of one of the

correction options set forth below. *Medina v. Bd. of Retirement*, 112 Cal. App. 4th 864, 870-71 (2003); and

WHEREAS, based upon the PSC Decision and other applicable law, the Board makes the following findings:

1. If a PSC contract made under Municipal Code section 24.1312 was the result of a legally authorized offer made by SDCERS before the beginning of the August 15, 2003 window period (that is, before the Board determined that new flat rates should be charged), and the member signed and dated that contract before its 90-day expiration date, that contract was legally authorized and is not impacted by this Resolution. However, members who submitted PSC applications that requested a quote for PSC prior to the window period, but who were provided the "window" rate by SDCERS only after the Board had determined a new rate, are included within the scope of this Resolution as a result of the PSC Decision.
2. The PSC Decision was rendered based on the City's amended complaint against SDCERS, which specifically exempted any affected members who already had retired prior to the filing of that lawsuit on November 20, 2007. Consequently, the City has acquiesced to continuing to pay for the underfunding created by the PSC contracts of this group of retirees. This means that SDCERS members who retired from the City prior to November 20, 2007 are not impacted by this Resolution.
3. Although a very narrow ruling, the PSC Decision is to be applied to any "window period" purchase that SDCERS' Board previously unlawfully authorized with respect to a PSC contract subject to Plan Document provisions that required employees to pay both the employee and employer cost for the service credit ("Affected PSC Contract"). There may be other PSC contracts impacted by this Resolution that have not yet been identified. Any additional PSC contract types that may potentially be subject to this Resolution will be separately presented to the Board for action.
4. The "window periods" relating to "air time" purchases by employees of the San Diego Port District and San Diego Airport Authority commenced on April 16, 2004, and thus PSC contracts purchased during those window periods are also subject to this Resolution as "Affected PSC Contracts". Those employer plan sponsors have not yet formally advised SDCERS as to whether they will acquiesce to continuing to pay for any or all of the underfunding created by such PSC contracts, or if the employer plan sponsors will require that SDCERS follow the member correction procedures outlined in this Resolution.

5. The underfunding resulting from the underpricing of the Affected PSCs Contracts during the window period must be corrected before the full service credit originally intended to be granted by the Affected PSC Contracts may be provided to members.
6. Underfunding resulting from Affected PSC Contracts that are the subject of this Resolution can be corrected either by employers voluntarily making up the underpayment or, if not by the employers, then the members must voluntarily pay the difference or voluntarily rewrite their PSC contracts to have their service credit reduced to the amount for which they paid under the correct higher rate that was determined by the Board in order to retain any portion of the PSC intended to be purchased.
7. Alternatively, if members do not choose to reform their Affected PSC Contracts with SDCERS voluntarily in order to retain some or all of their PSC, then, after reasonable notice as set forth below, SDCERS will reduce their retirement service credit accounts accordingly, refund the member contributions made to purchase the underpriced PSC, together with interest credited to those contributions to date, and make any other necessary adjustments to member benefits in accordance with law.
8. All interest payments relating to the correction of Affected PSC Contracts calculated under this Resolution, both for payments to be made by SDCERS to members/beneficiaries and payments made to SDCERS by members/beneficiaries, will be set at the SDCERS actuarially assumed investment return rate in effect as of June 30 of each year, compounded annually. Interest payments for amounts owed to SDCERS by members/beneficiaries for repayment of overpaid retirement benefits required if a member declines or fails to exercise one of the corrective options to fully fund the service purchase will be set at the actuarially assumed investment return rate in effect as of June 30 of each year, compounded monthly, calculated through the date the member is sent a 90-day written Notice of Options by SDCERS.
9. To the extent that an active member with an Affected PSC Contract is currently in the Deferred Retirement Option Program ("DROP"), but declines to exercise one of the corrective options that would permit that member to retain sufficient service to remain eligible for DROP, SDCERS will deem the member's prior DROP election to be rescinded, subject to SDCERS collecting retirement contribution arrearages, unwinding the DROP benefit administered by SDCERS, and netting any amounts due to or from SDCERS and the member.
10. To the extent that an active member with an Affected PSC Contract is currently in DROP, but declines to exercise one of the corrective options that would permit that member to retain sufficient service to remain

eligible for DROP and the member affirms to SDCERS that, but for the lack of information regarding the impact of the affected PSC contract on the member's DROP election, the member would not have entered DROP, SDCERS will permit that member to reform his or her DROP contract to provide a different DROP beginning and end date, subject to SDCERS collecting retirement contribution arrearages, adjusting the DROP benefit administered by SDCERS. However, application of this paragraph 10 is conditioned on the member's employer's agreement to the reformation. (*Hittle v. Santa Barbara County Employees Retirement Assn.*, 39 Cal. 3d 374 (1985).)

11. To the extent that an active member with an Affected PSC Contract remains eligible for DROP, but affirms to SDCERS that, but for the Affected PSC Contract, the member would not have entered DROP, SDCERS will permit that member to rescind his or her DROP election, subject to SDCERS collecting retirement contribution arrearages, unwinding the DROP benefit administered by SDCERS, and netting any amounts due to or from the SDCERS and the member, However, application of this paragraph 11 is conditioned on the member's employer's agreement to the rescission. (*Hittle v. Santa Barbara County Employees Retirement Assn.*, 39 Cal. 3d 374 (1985).)
12. To the extent that a member with an Affected PSC Contract entered DROP, and thus fixed his or her retirement allowance amount before the City filed its lawsuit on November 20, 2007, and the member has since retired, SDCERS will specifically request that the City acquiesce to its continuing to pay for the underfunding created by the underpriced PSC contracts of this additional group of affected retirees.
13. SDCERS staff shall also meet with each of the affected employers to determine what (if any) assistance they might provide to members/beneficiaries impacted by Affected PSC Contracts.

WHEREAS, the above findings and correction methodology are implemented under the authority of Article 16, Section 17 of the California Constitution, which grants to SDCERS' governing Board "plenary authority and fiduciary responsibility" for administration of the fund; and

WHEREAS, the San Diego City Charter section 144 provides that SDCERS' governing Board "shall be the sole authority and judge under such general ordinances as may be adopted by the Council as to the conditions under which persons may be admitted to benefits of any sort under the retirement system..."; and

WHEREAS, San Diego Municipal Code section 24.0901 states: "The Board may make Rules it deems proper to administer the Retirement System consistent with its

fiduciary duties under Article 16, Section 17 of the California Constitution. The Board will identify the rules that are incorporated into this Article as part of the Plan document.”

NOW, THEREFORE, BE IT RESOLVED, that the Board hereby formally adopts the above findings and conclusions and instructs staff to present for adoption a Board Rule, to be designated as part of the Plan document, containing the following provisions:

***Board Rule No. \_\_\_\_\_ Regarding PSC Corrections***

1) **Employer Correction Option:** SDCERS will provide each of its employer plan sponsors with sixty (60) days following the adoption of this Rule to formally advise SDCERS whether or not they will voluntarily pay for some or all of the underfunding caused by the Affected PSC Contracts through the UAL amortization, or such shorter time period that the employer may elect.

2) **Member Correction Options:** To the extent that the employer of a member with an Affected PSC Contract does not pay for that underfunded amount, then SDCERS will provide the following correction options to members/beneficiaries with respect to all Affected PSC Contracts, subject to the timeline set forth in item 3 below and subject to any changes or adjustments required by the Internal Revenue Service in order to preserve the qualified status of the plans:

Option 1: Member/beneficiary may rescind the original Affected PSC Contract and receive a refund of his or her PSC contributions, plus interest. SDCERS will reduce associated service credit accordingly. In addition, if the member already has retired, SDCERS will adjust the member’s retirement benefit prospectively and if retirement benefits have been overpaid as a result of the inclusion of the underfunded service credit in the member’s retirement benefit calculations, then SDCERS will recover those overpaid amounts, plus interest, as set forth in this Rule.

Option 2: If the member is in active service and eligible to purchase PSC currently, the member may rescind the original Affected PSC Contract and apply the full refund plus any applicable interest to a new PSC contract based on the current rates and the member’s current salary.

Option 3: Member/beneficiary may request that SDCERS reduce his or her service credit to the lesser amount of service that would have been legally purchased by the member’s actual contributions under the Affected PSC contract if the higher post-window rate had been applied. Thus, no additional payment would be made by the member/beneficiary to SDCERS as a result of this correction; provided, however, that if the member has retired, is subject to this Resolution, and the member’s former employer has not agreed to correct the underfunding, then any benefits erroneously paid out as a result of the Affected PSC Contract are to be recomputed, and SDCERS is to recover overpayments plus interest from the member/beneficiary made to the member/beneficiary and adjust the member’s retirement benefit prospectively; or

**Option 4:** Member/beneficiary may pay, with interest, the difference between the amount paid at the “old” rate and the amount that should have been paid at the then Board determined rate to fund the full service credit originally anticipated in the Affected PSC Contract. In the alternative and if necessary for a member to remain eligible for service retirement and/or DROP, a member/beneficiary may make a “partial purchase” of PSC by paying, with interest, the difference between the amount paid at the “old” rate and the amount that should have been paid at the then Board determined rate to fund sufficient service credit in the Affected PSC contract to retain such eligibility; provided, however, that corresponding adjustments are made to any past and future retirement allowances, contributions, and interest. Payments due under this option may be made by lump sum or through a payment plan, including without limitation an after-tax payroll deduction, whose duration is not to exceed the amount of time to be purchased and will carry additional interest.

**Option 5 (DROP):** To the extent that a member with an Affected PSC Contract entered into DROP prior to the adoption of this Rule, SDCERS will permit the DROP election to be rescinded or reformed, to the extent legally permissible and, if applicable, subject to the member’s employer’s agreement. The member may then elect one of the above correction options.

**3) Timeline and Default Board Action:** If, within sixty (60) days of SDCERS providing written Notice of Options Re Purchase of Service Credit Corrections by certified mail of the above five options, any member/beneficiary does not voluntarily select one of the five options, then SDCERS will make a reasonable effort to contact that individual directly to determine whether the member has made a decision. If within ninety (90) days of SDCERS providing the original Notice SDCERS is unable to contact the individual or if the member does not voluntarily select an option, and if the Board, in its sole and exclusive authority, does not extend the time period for individual’s response based upon circumstances that may be presented to it by staff, then SDCERS will implement Option 1 above as to the member/beneficiary.

ADOPTED: \_\_\_\_\_, 2010

\_\_\_\_\_  
Raymond G. Ellis, Vice President  
Board of Administration, San Diego City  
Employees’ Retirement System

ATTEST:

\_\_\_\_\_  
Mark A. Hovey  
CEO



**Mark A. Hovey**  
*Chief Executive Officer*

January 21, 2011

Jeffrey Woodson  
Vice President/Administration  
San Diego County Regional  
Airport Authority  
3225 N. Harbor Drive  
San Diego, CA 92138

Jeff,

SDCERS has completed our analysis of the Purchased Service Credit contracts entered into by Airport Authority employees that are affected by the "window period" pricing. Attached are the details associated with our analysis. You'll see that the correction options are grouped according to the approach outlined in my previous communications to you and the Airport Authority Board. Your Board had requested the individual details in order to make an informed decision on whether or not they wish to exempt from correction any or all of the underpriced PSC contracts.

Of the 39 individuals with affected PSCs, 34 are active members, two are currently in DROP, and three are inactive members not currently employed by the Airport Authority. Their names have been withheld for confidentiality reasons. Summary conclusions:

- Option #1 (contract rescission and refund), would entail refunds to the members, including interest, of approximately \$2.7 million.
- Option #2 (contract rescission and repurchase using current rates) would be available only to the 34 active employees. They would be able to take their refunds from Option #1 and apply those refunds toward a purchase of a PSC contract under current pricing, with a net due to SDCERS of approximately \$1.7 million.
- Option #3 (reduce service credit) would apply to everyone. In addition, for the two Active DROP members, they would see their monthly retirement allowance decrease by a collective \$1,858, with an associated reduction in their current DROP accounts of \$35,945.
- Option #4 (pay the net difference between the old 2004 PSC rates and the new 2004 PSC rates) would require total contributions of approximately \$3.5 million. Comparing Option #4 to Option #2, it appears nearly all active employees will find it to their advantage to choose option #2.

Jeffrey Woodson  
January 21, 2011  
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You'll recall we also discussed an Option #5, which would apply only to the two Active DROP members. In both cases, the member already had sufficient age and service to have entered DROP without having purchased the affected PSC. However, the SDCERS Board approved a resolution recommending that the Airport Authority consider allowing the member to rescind their DROP election, forfeiting their accumulated DROP balances, and then pay additional employee contributions for the time while in DROP to what would have been paid were they an active member. Furthermore, as the member would now be restored to active member status, they would be eligible to repurchase their PSC at current rates. The cost to repurchase for employee #35 on the attached list would be \$254,268, and the cost to repurchase for employee #36 would be \$155,202. The additional employee contributions to reclassify their DROP time as active time would be approximately \$1,200 and \$450 for employees #35 and #36, respectively.

SDCERS Board Rule 4.90 regarding the PSC correction process was adopted at their November 5, 2010 meeting, and the relevant timeline language states:

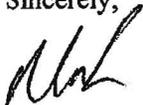
*"b.1) Employer Correction Option: SDCERS will provide each of its employer plan sponsors with sixty (60) days following the date that SDCERS provides written notice to the plan sponsor of the unfunded liability related to the Affected PSC contracts to formally advise SDCERS whether or not the plan sponsor will voluntarily pay for some or all of the underfunding caused by the Affected PSC Contracts through the UAL amortization, or such shorter time period that the employer may elect."*

With the detail attached, the Airport Authority has now been provided with the individual and total cost details regarding all affected members. Please advise whether or not the Airport Authority wishes to exempt any or all of these contracts from correction.

In line with the above Board Rule, SDCERS is requesting the Airport Authority's decision by March 23, 2011. If the Airport Authority's decision is for SDCERS to correct all of the employee's contracts, we will begin contacting employees with affected contracts and providing them with detailed information on each applicable correction option. Employees will have up to 90 days to decide which option best suits them. If the employee does not make an election, SDCERS will rescind the PSC contract and issue a full refund to the member, including interest.

Let me know if you have further questions.

Sincerely,



Mark A. Hovey  
CEO

Enclosure: SDCERS Board Rule 4.90 PSC Correction  
Detailed PSC Corrections Spreadsheet

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This Rule is incorporated into: (1) Chapter 2, Article 4 of the San Diego Municipal Code as part of the Plan document, (2) the Amended and Restated San Diego Unified Port District Retirement Plan and Trust, and (3) the Amended and Restated San Diego County Regional Airport Authority Retirement Plan and Trust.

Adopted March 5, 2010

**Rule 4.90 PSC Corrections**

This Board rule implements the Court's decision in *City of San Diego vs. SDCERS*, 186 Cal.App.4<sup>th</sup> 69 (2010) (the "PSC Decision") in which the court determined that SDCERS did not have the right to charge the City of San Diego ("City") for SDCERS' underfunding of service credits purchased under San Diego Municipal Code section 24.1312. This rule is enacted consistent with Board Resolution 2010-02 adopted by the Board at its October 2010 meeting. This Rule is incorporated into Chapter 2, Article 4 of the San Diego Municipal Code as part of the Plan document.

- a. "Affected PSC Contracts" means any "window period" purchase that the SDCERS Board previously unlawfully authorized with respect to a PSC contract subject to Plan Document provisions that:
  - 1) Required employees to pay both the employee and employer cost
  - 2) Were purchased on or after August 15, 2003 at the "old" 15% rate for City General Members and 26% rate for City Safety Members, unless the contract was the result of a legally authorized offer made by SDCERS before August 15, 2003 and the Member signed and dated that contract before its 90-day expiration date.
  - 3) Were purchased on or after April 16, 2004 at the "old" 15% rate for UPD and Airport General Members, 23% rate for UPD Safety Member and 15% rate for UPD and Airport Executive Members, unless the contract was the result of a legally authorized offer made by SDCERS before April 16, 2003 and the Member signed and dated that contract before its 90-day expiration date.
  - 4) Affected PSC Contracts do not include contracts purchased for City service credit by any City Member who retired from City service on or before November 19, 2007.
- b. Correction Options: Affected PSC Contracts will be corrected as provided in the following options:
  - 1) **Employer Correction Option:** SDCERS will provide each of its employer plan sponsors with sixty (60) days following the date that SDCERS provides written notice to the plan sponsor of the

unfunded liability related to the Affected PSC Contracts to formally advise SDCERS whether or not the plan sponsor will voluntarily pay for some or all of the underfunding caused by the Affected PSC Contracts through the UAL amortization, or such shorter time period that the employer may elect.

- 2) **Member Correction Options:** To the extent that the employer of a member with an Affected PSC Contract does not pay for that underfunded amount, then SDCERS will provide the following correction options to members/beneficiaries with respect to all Affected PSC Contracts, subject to the timeline set forth in item 3 below and subject to any changes or adjustments required by the Internal Revenue Service in order to preserve the qualified status of the plans:

**Option 1:** Member/beneficiary may rescind the original Affected PSC Contract and receive a refund of his or her PSC contributions, plus interest. SDCERS will reduce associated service credit accordingly. In addition, if the member already has retired, SDCERS will adjust the member's retirement benefit prospectively and if retirement benefits have been overpaid as a result of the inclusion of the underfunded service credit in the member's retirement benefit calculations, then SDCERS will recover those overpaid amounts, plus interest, as set forth in this Rule.

**Option 2:** If the member is in active service and eligible to purchase PSC currently, the member may rescind the original Affected PSC Contract and apply the full refund plus any applicable interest to a new PSC contract based on the current rates and the member's current salary.

**Option 3:** Member/beneficiary may request that SDCERS reduce his or her service credit to the lesser amount of service that would have been legally purchased by the member's actual contributions under the Affected PSC contract if the higher post-window rate had been applied. Thus, no additional payment would be made by the member/beneficiary to SDCERS as a result of this correction; provided, however, that if the member has retired, is subject to this Resolution, and the member's former employer has not agreed to correct the underfunding, then any benefits erroneously paid out as a result of the Affected PSC Contract are to be recomputed, and SDCERS is to recover overpayments plus interest from the member/beneficiary made to the member/beneficiary and adjust the member's retirement benefit prospectively; or

**Option 4:** Member/beneficiary may pay, with interest, the difference between the amount paid at the "old" rate and the amount that should have been paid at the then Board determined

rate to fund the full service credit originally anticipated in the Affected PSC Contract. In the alternative and if necessary for a member to remain eligible for service retirement and/or DROP, a member/beneficiary may make a "partial purchase" of PSC by paying, with interest, the difference between the amount paid at the "old" rate and the amount that should have been paid at the then Board determined rate to fund sufficient service credit in the Affected PSC contract to retain such eligibility; provided, however, that corresponding adjustments are made to any past and future retirement allowances, contributions, and interest. Payments due under this option may be made by lump sum or through a payment plan, including without limitation an after-tax payroll deduction, whose duration is not to exceed the amount of time to be purchased and will carry additional interest.

**Option 5 (DROP):** To the extent that a member with an Affected PSC Contract entered into DROP prior to the adoption of this Rule, SDCERS will permit the DROP election to be rescinded or reformed, to the extent legally permissible and, if applicable, subject to the member's employer's agreement. The member may then elect one of the above correction options.

- 3) **Timeline and Default Board Action:** If, within sixty (60) days of SDCERS providing written Notice of Options Re Purchase of Service Credit Corrections by certified mail of the above five options, any member/beneficiary does not voluntarily select one of the five options, then SDCERS will make a reasonable effort to contact that individual directly to determine whether the member has made a decision. If within ninety (90) days of SDCERS providing the original Notice SDCERS is unable to contact the individual or if the member does not voluntarily select an option, and if the Board, in its sole and exclusive authority, does not extend the time period for individual's response based upon circumstances that may be presented to it by staff, then SDCERS will implement Option 1 above as to the member/beneficiary.

Adopted November 5, 2010

## **ARTICLE III - BENEFITS**

### **Division 5 - Service Retirement**

#### **Rule 5.00 Time for Application**

- a. All applications for service retirement benefits must be filed before the date of retirement.

Airport Authority PSC Correction Calculations

#	Status	Option 1 - Rescind Service Credit				Option 2 - Rescind and Repurchase		Option 3 - Reduce Service Credit			Option 4 - Pay Difference
		Refund	Reduced Service Credit	Monthly Allowance Reduction	DROP Account Overpayment	PSC Purchase Cost	Net Due to SDCERS	Reduced Service Credit	Monthly Allowance Reduction	DROP Account Overpayment	Net Due To SDCERS
1	Active	\$24,548	5.0	\$0	\$0	\$49,235	\$24,688	1.1	\$0	\$0	\$41,496
2	Active	\$58,866	5.0	\$0	\$0	\$128,741	\$69,875	1.6	\$0	\$0	\$82,782
3	Active	\$54,514	5.0	\$0	\$0	\$103,342	\$48,828	1.2	\$0	\$0	\$84,415
4	Active	\$34,915	5.0	\$0	\$0	\$111,940	\$77,025	0.6	\$0	\$0	\$75,577
5	Active	\$51,151	5.0	\$0	\$0	\$110,417	\$59,266	1.5	\$0	\$0	\$73,669
6	Active	\$116,822	5.0	\$0	\$0	\$157,998	\$41,176	2.3	\$0	\$0	\$132,398
7	Active	\$46,726	5.0	\$0	\$0	\$61,869	\$15,142	2.3	\$0	\$0	\$52,956
8	Active	\$57,769	8.0	\$0	\$0	\$118,525	\$60,756	0.9	\$0	\$0	\$127,188
9	Active	\$53,566	5.0	\$0	\$0	\$109,703	\$56,138	1.5	\$0	\$0	\$77,844
10	Active	\$46,401	5.0	\$0	\$0	\$69,228	\$22,827	2.3	\$0	\$0	\$51,728
11	Active	\$56,808	5.0	\$0	\$0	\$110,873	\$54,065	1.6	\$0	\$0	\$77,280
12	Active	\$58,117	5.0	\$0	\$0	\$88,656	\$30,539	2.3	\$0	\$0	\$63,935
13	Active	\$56,637	5.0	\$0	\$0	\$97,795	\$41,158	2.3	\$0	\$0	\$64,188
14	Active	\$83,058	5.0	\$0	\$0	\$125,272	\$42,214	2.3	\$0	\$0	\$94,826
15	Active	\$214,032	5.0	\$0	\$0	\$327,929	\$113,897	2.2	\$0	\$0	\$271,107
16	Active	\$47,649	5.0	\$0	\$0	\$84,821	\$37,171	2.3	\$0	\$0	\$51,792
17	Active	\$23,436	3.6	\$0	\$0	\$60,886	\$37,450	0.9	\$0	\$0	\$37,761
18	Active	\$124,971	5.0	\$0	\$0	\$218,017	\$93,047	2.3	\$0	\$0	\$141,633
19	Active	\$95,275	5.0	\$0	\$0	\$160,820	\$65,545	2.3	\$0	\$0	\$110,440
20	Active	\$42,784	5.0	\$0	\$0	\$103,251	\$60,467	1.2	\$0	\$0	\$67,277
21	Active	\$153,067	5.0	\$0	\$0	\$188,883	\$35,816	2.3	\$0	\$0	\$172,927
22	Active	\$44,770	5.0	\$0	\$0	\$89,239	\$44,469	1.6	\$0	\$0	\$62,770
23	Active	\$53,969	5.0	\$0	\$0	\$59,717	\$5,748	2.3	\$0	\$0	\$60,122
24	Active	\$83,880	5.0	\$0	\$0	\$210,149	\$126,269	0.9	\$0	\$0	\$159,207
25	Active	\$33,768	5.0	\$0	\$0	\$68,218	\$34,449	1.5	\$0	\$0	\$50,435
26	Active	\$48,759	5.0	\$0	\$0	\$63,188	\$14,429	2.3	\$0	\$0	\$55,663
27	Active	\$46,249	5.0	\$0	\$0	\$81,265	\$35,016	2.3	\$0	\$0	\$52,956
28	Active	\$75,068	5.0	\$0	\$0	\$138,610	\$63,542	2.3	\$0	\$0	\$85,443
29	Active	\$32,764	5.0	\$0	\$0	\$68,535	\$35,771	1.1	\$0	\$0	\$57,793
30	Active	\$33,788	5.0	\$0	\$0	\$88,349	\$54,560	1.2	\$0	\$0	\$53,547
31	Active	\$107,921	5.0	\$0	\$0	\$203,749	\$95,829	1.8	\$0	\$0	\$145,632
32	Active	\$83,348	5.0	\$0	\$0	\$131,964	\$48,616	1.8	\$0	\$0	\$109,890
33	Active	\$28,706	5.0	\$0	\$0	\$66,483	\$37,777	1.1	\$0	\$0	\$49,034
34	Active	\$52,283	5.0	\$0	\$0	\$105,529	\$53,246	1.2	\$0	\$0	\$82,857
35	DROP	\$165,184	5.0	\$2,568	\$44,296	\$0	\$0	2.2	\$1,316	\$22,108	\$209,274
36	DROP	\$85,143	5.0	\$1,168	\$29,778	\$0	\$0	2.3	\$542	\$13,837	\$98,021
37	Inactive	\$58,337	2.3	\$0	\$0	\$0	\$0	1.1	\$0	\$0	\$63,525
38	Inactive	\$77,418	2.4	\$0	\$0	\$0	\$0	1.1	\$0	\$0	\$87,741
39	Inactive	\$70,488	5.0	\$0	\$0	\$0	\$0	2.3	\$0	\$0	\$78,928
		<b>\$2,682,954</b>	<b>191.2</b>	<b>\$3,735</b>	<b>\$74,074</b>	<b>\$3,963,196</b>	<b>\$1,736,812</b>	<b>68.8</b>	<b>\$1,858</b>	<b>\$35,945</b>	<b>\$3,516,062</b>

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**AIRPORT AUTHORITY BOARD CONSIDERATION OF  
SAN DIEGO CITY EMPLOYEES' RETIREMENT SYSTEM  
PURCHASE OF SERVICE CREDIT "WINDOW PERIOD"  
PRICING**

Jeff Lindeman; Director, Human Resources

**February 10, 2011**



# BACKGROUND

- ⊙ June 7, 2010, Fourth District Court of Appeals issues ruling on pricing of purchase of service credit (PSC) contracts entered into by City employees during a “window period”
- ⊙ Court ruling believed to apply to similar “window period” for Airport Authority employee PSC contracts executed on/after April 16, 2004 despite the fact that the SDCERS Board (at that time) allowed contracts to be purchased at lower price for contracts received through June 30, 2004



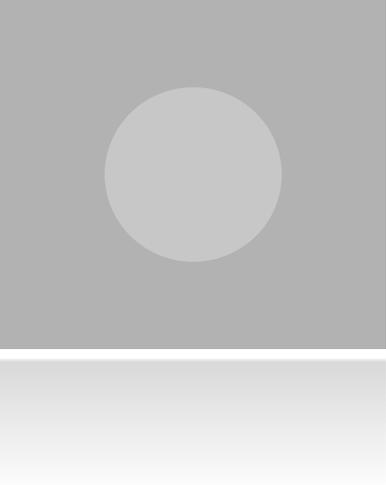
# BACKGROUND

- ⊙ Airport Authority Board received updates at September 2, 2010 meeting and October 7, 2010 meeting
- ⊙ SDCERS Board requested that Airport Authority Board provide notice as to whether Airport Authority would like to continue to absorb cost of underpriced PSC contracts (approx. \$3.5 million) through the Unfunded Actuarial Liability
- ⊙ At October 7, 2010 meeting, Airport Authority Board requested detailed analysis of impact on individuals prior to responding to SDCERS



# CURRENT CONSIDERATION

- ⊙ Airport Authority Board is being asked to decide whether or not to continue paying for underpriced PSC contracts through Annual Required Contribution
- ⊙ Assuming the decision is for Airport Authority to absorb individual cost through Unfunded Actuarial Liability, no additional Board action required
- ⊙ Assuming Board decides not to continue to absorb individual cost, Board is requested to permit the 2 employees in Deferred Retirement Option Program (DROP) the option to choose to rescind DROP contract



# Questions & Direction to Staff