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IN THE SUPERIOR COURT OF ARIZONA
IN AND FOR THE COUNTY OF MARICOPA

JENNIFER WRIGHT, *et. al.*, Plaintiffs, vs. GREGORY J. STANTON, in his official capacity as Mayor of the City of Phoenix; *et. al.*, Defendants.	Case No. CV2013-010915 **PLAINTIFFS' RESPONSE TO DEFENDANT PHOENIX POLICE PENSION BOARD'S MOTION TO DISMISS AND MOTION FOR STAY OF PROCEEDINGS** *Hon. John Rea* **(Oral Argument Requested)**

Plaintiffs Jennifer Wright, Eric Wnuck, and Jim Jochim, who are Phoenix taxpayers ("Taxpayers"), hereby respond to Defendant Phoenix Police Pension Board's ("Local Board") Motion to Dismiss or alternative Motion to Stay. The Local Board has an explicit statutory mandate to ensure that all pension payments it approves comply with state law. Despite its legal obligations, the Local Board has approved and continues to approve pension payments for Phoenix Police Department Sergeants and Lieutenants that violate state law at direct expense of Taxpayers. Moreover, the Local Board has had clear notice and ample opportunity to determine whether the components of compensation at issue in this case count as pensionable pay. The Local Board has shirked its statutory duty by answering that question in the affirmative by continuing to approve pension payments that are not pensionable under state law; hence, the Local Board's Motion to Stay these proceedings is unwarranted. Taxpayers have a right to challenge illegal expenditures that were made and continue to be made by the Local Board in this Court without referring this matter back to a body that has already failed in its obligations to lawfully administer pension payments for Phoenix Police Sergeants and Lieutenants.

For the reasons set forth below, Taxpayers respectfully request that Defendant's Motion to Dismiss and Motion to Stay be DENIED. This Response is supported by the following Memorandum of Points and Authorities and pleadings and matters of record filed with the Court, all of which are incorporated by reference.

MEMORANDUM OF POINTS AND AUTHORITIES

I. Preliminary Statement

On October 8, 2013, Taxpayers filed an Amended Complaint seeking declaratory and injunctive relief to prevent the Local Board from approving pension payments for Phoenix Police Department Sergeants and Lieutenants that clearly violate state law. (FAC).

As the Local Board observed in its Motion to Dismiss, the Local Board has broad powers to determine how retirement benefits are determined for and paid to Phoenix Police Department Sergeants and Lieutenants (Def.'s Mot. 2-3) within the Public Safety Personnel Retirement System ("PSPRS"). Specifically, the Local Board *shall* have the power "[t]o decide *all questions* of eligibility for membership, service credits and *benefits* and *determine the amount*, manner and time of payment of any benefits under the system." ARIZ. REV. STAT. § 38-847(D)(1) (emphasis added).

It is, of course, axiomatic that in exercising this broad authority the Local Board must comply with state law generally, and the statutory mandates of the PSPRS specifically, in classifying pension benefits and fixing the amount of benefits for Phoenix Police Department Sergeants and Lieutenants. State statute clarifies this requirement: "A local board shall have *no power to add to*, subtract from, modify or waive *any of the terms of the system*, change or *add to any benefits* provided by the system…." ARIZ. REV. STAT. § 38-847(E) (emphasis added). Specific components of pay that are defined as "compensation" under state law are benefits in PSPRS. *See* ARIZ. REV. STAT. § 38-842(12) (" 'Compensation' means, for purposes of computing *retirement* *benefits....*") (emphasis added).[1] Pursuant to A.R.S. § 38-842(12), "Compensation, does not include, for purposes of computing *retirement benefits*, payment for unused sick leave, payment in lieu of vacation, payment for unused compensatory time or payment for any fringe benefit." When the Local Board includes these components of compensation in "determin[ing] the amount of...payment of any benefits under the system," it is "modifying...the terms of the system" by "chang[ing] or add[ing] to...benefits provided by the system." *Id.* at § 38-847(E); 38-842(12) (emphasis added). Despite its broad powers, the Local Board cannot contravene the plain language of state statute by modifying the terms of the system by approving pension benefits specifically excluded by the system. ARIZ. REV. STAT. § 38-842(12). *See Cochise County v. Ariz. Health Care Cost Containment System*, 170 Ariz. 443, 445, 825 P.2d 968, 970 (App. 1991) ("The scope of an agency's power is measured by statute and may not be expanded by agency fiat.")

Indeed, the role of the Local Board in PSPRS is as "gatekeeper" and "arbiter" for Phoenix Police Sergeants and Lieutenants who participate in the system. (Def.'s Mot. 2). As the Local Board admits, the Local Board "is the agency entrusted with the initial call on the issues raised in the FAC, and is the agency with the expertise to make those calls with respect to Phoenix Police officers." (Def.'s Mot. 4). Of course, this admission does not reduce the responsibility of the other defendants in this case.[2] In this case, there is enough blame shifting to fill a convention hall at a political rally. But, as the Local Board readily admits (Def.'s Mot. 2, 4, 8-9) there is no question that the obligation to ensure pension payments for Phoenix Police Sergeants and Lieutenants comply with state law is squarely on the shoulders of the Local Board. As described below, despite clear and unequivocal notice of the issues present in this case, the Local Board has failed and continues to

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[1] The Local Board's Motion refers to the components of compensation at issue in this case as "benefits" over a dozen times. *See* (Def.'s Mot. 3-5, 8).

[2] The City of Phoenix was and is obligated to comply with state law when it entered into a contract with the Phoenix Police Sergeants and Lieutenants Association and when it reports pensionable pay to the Local Board (FAC ¶¶ 49, 53, 66, 67, 74, 75, 86, 87, 94, 95).[2] Likewise, PSPRS is obligated to protect the pension fund and ensure that payments are made in a manner that is "uniform, consistent, and equitable" for all members in the system. ARIZ. REV. STAT. §§ 38-841, 38-848(H)(7),(9); (FAC ¶¶ 22, 54, 97, 100, 102, 103). *See* (Def.'s Mot. 2) (Local Board "is generally subject to oversight of [PSPRS Board of Trustees]."); (Def.'s Mot. 3) (PSPRS is empowered "to object to local board determinations it determines to be improper.").

fail in that obligation, at ongoing expense to Taxpayers.

II. Legal Analysis

A. Taxpayers Have Clear Standing Because Taxpayers Directly Finance Pension Contributions Approved by the Local Board.

Taxpayers have plain and obvious standing in this case because Taxpayers directly finance pension contribution payments that have been artificially and unlawfully inflated and approved by the Local Board. Those contributions are made to a Phoenix-only account in PSPRS and pension payments are drawn exclusively from that account. (FAC ¶ 23-24, 26-30); (Hacking Decl. ¶¶ 7, 10-16); ARIZ. REV. STAT. § 38-843. Therefore, every time an employer contribution is made or a pension amount is approved that includes components of compensation prohibited by A.R.S. § 38-842(12), there is an unlawful expenditure of taxpayer funds that Taxpayers may rightfully challenge in this action.

In Arizona, standing "is not a constitutional mandate," but rather a "prudential or judicial restraint." *Armory Park Neighborhood Ass'n v. Episcopal Comm. Services in Ariz.*, 148 Ariz. 1, 6, 712 P.2d 914, 919 (1985). Moreover, as outlined in Taxpayers' previous responses, Arizona courts have consistently conferred broad taxpayer standing to challenge unlawful governmental expenditures. *Turken v. Gordon*, 220 Ariz. 456, 461, 207 P.3d 709, 714 (App. 2008), *rev'd on other grounds*, 223 Ariz. 342, 224 P.3d 158 (2010). Taxpayers will have standing to challenge unlawful government expenditures if taxpayers can show a direct expenditure of funds generated through taxation or an increased levy of tax. *See Dail v. Phoenix*, 128 Ariz. 199, 202, 624 P.2d 877, 880 (App. 1980).

The Court need look no further than the PSPRS statute mandating system contributions to establish there is clear standing in this case. ARIZ. REV. STAT. § 38-843. Each employer, including the Phoenix Police Department, contributes a specific percentage of each employee's salary to its separate account in PSPRS based on actuarial valuation ("employer contribution rate"). *Id.* at § 38-843(B); (FAC, ¶ 27); (Hacking Decl. ¶ 14).[3] The employer contribution rate for fiscal year 2013-

[3] Employee members of PSPRS, including Phoenix Police Sergeants and Lieutenants, also contribute a percentage of their pay to their department's separate account in PSPRS ("employee

2014 for the Phoenix Police Department is 34.50% of a member's compensation. Public Safety Personnel Retirement System, *Contribution Rates for Fiscal Year 2013/2014*, *available at* http://www.psprs.com/sys_psprs/employers/PS%20Employer%20Rates /PS%20FY2014%20ER%20Rates.pdf. Since the employer contributions rate is based on the percentage of the member's *compensation*, when a member's compensation amount is artificially increased through payment in lieu of vacation, payment for unused sick leave and compensatory time, and payment for fringe benefits, then the amount contributed to PSPRS by the City of Phoenix, and therefore Taxpayers, is *necessarily* higher. For example, if a member's monthly compensation is $5,000.00 and does not include payment for the components of compensation at issue in this case, then Taxpayers exclusively will contribute 34.50% of the member's pay, or $1,725.00, to PSPRS for that member. If another member's compensation (who may be the same rank and have the same years of service as the previous member) is $6,250 because that member's compensation includes payment for the components of compensation at issue in this case, then Taxpayers will contribute the same 34.50% of the member's pay, but the amount of Taxpayer funds expended will increase to $2,156.25. The difference between those employer contribution amounts is an unlawful and direct expenditure of funds generated through taxation on Taxpayers.

Moreover, "Each employer shall transfer to the board the employer and employee contributions...within ten working days after each payroll date." ARIZ. REV. STAT. § 38-843(D). Therefore, Taxpayers are making regular and recurring contributions. Each contribution taxpayers make based on unlawful compensation calculations is a direct Taxpayer expenditure. These unlawful expenditures are *currently ongoing*.

Additionally, pension payments to Phoenix Police Department Sergeants and Lieutenants in PRPRS are made from a Phoenix-only fund that is funded entirely and exclusively by Phoenix taxpayers and Phoenix Police Department employees. (FAC ¶ 23-24, 26-30); (Hacking Decl. ¶¶ 7, 10-16); ARIZ. REV. STAT. § 38-843. When the Local Board approves a pension payment that

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contribution rate"), but employee contribution rates are fixed by statute. ARIZ. REV. STAT. § 38-843(E). The employee contribution rate for members of PSPRS for fiscal year 2013-2014, including Phoenix Police Department Sergeants and Lieutenants, is 10.35%. *Id.*

includes the components of compensation at issue here, it creates a direct expenditure that Taxpayers are responsible for funding. The claim that there is no expenditure of taxpayer funds because "the contributions for benefits are commingled in an investment fund that generates income to pay a portion of the benefits" (Def.'s Mot. 6) is ludicrous. The entire financial world, including my personal checking account, operates by "commingling" funds for investment purposes. Is it also the Local Board's position that because deposits to my separate checking account accrue interest and are "comingled" with deposits of other bank customers that we cannot trace deposits and withdrawals to my account? In fact, we can trace directly the amount of taxpayer funds expended in the form of employer contributions to Phoenix's separate account in PSPRS as well as pension payments from Phoenix's separate account that include the components of compensation at issue.

Moreover, as described in note 3 *supra*, unlike employer contributions to the pension fund, employee contributions are fixed by statute. ARIZ. REV. STAT. § 38-843(E). Therefore, a rise in liabilities to the Phoenix Police Department's separate account in PSPRS will result in a rise of *employer*, or Taxpayer, contributions, rather than a rise in the fixed *employee* contribution rate. (FAC ¶¶ 27-29); (Hacking Decl. ¶¶ 15-16). Although not necessary to establish standing because there is an unlawful and direct expenditure of taxpayer funds through higher employer contributions, employer contribution *rates* also increase as a result of the additional liabilities placed on the system when the Local Board approves pension payments that include the components of compensation at issue. (FAC ¶¶ 28-29).

The direct harm to Taxpayers as a result of Defendants' unlawful actions in this case is clear and unequivocal. Taxpayers have established standing.

B. Taxpayers Have Stated a Justiciable Claim Against the Local Board for Unlawful Acts that Are Causing Taxpayers Regular and Recurring Harm.

Taxpayers have stated a justiciable claim because they are challenging the legality of public actions taken by the Local Board (and other defendants) in order to protect their interests as equitable owners of taxpayer funds they are obligated to replenish as a result of the Local Board's unlawful actions.

Taxpayers seek declaratory relief establishing that the Local Board does not have authority to approve pension payments that include the components of compensation at issue and seek to enjoin the Local Board from approving such payments. (FAC 15) "Declaratory judgment relief is an appropriate vehicle for resolving controversies as to the legality of acts of public officials." *Riley v. Cochise County*, 10 Ariz.App. 55, 59, 455 P.2d 1005, 1009 (App. 1969). In order to be entitled to relief, a plaintiff must have a protectable interest or right and a denial of that right by the other party. *Id.* at 60, 455 P.2d at 1010. Moreover, an "injunction is an appropriate remedy to determine whether rights have been or will be affected by arbitrary or unreasonable action of an administrative officer or agent." *Rivera v. City of Douglas*, 132 Ariz. 117, 119, 644 P.2d 271, 273 (App. 1982). Public officials "may be enjoined from acts which are beyond their power." *Williams v. Superior Court*, 108 Ariz. 154, 158, 494 P.2d 26, 30 (1972).

In this case, the Local Board is approving portions of pension payments for Phoenix Police Sergeants and Lieutenants that violate state law. Taxpayers have a clear right to bring this suit in equity based on Taxpayers' "equitable ownership of [public] funds and their liability to replenish the public treasury for the deficiency which would be caused by the misappropriation." *Ethington v. Wright*, 66 Ariz. 382, 386, 189 P.2d 209, 212 (1948). An injunction is appropriate to prevent the Local Board from engaging in actions that are beyond its authority.

Defendant Local Board argues that "[t]he Court should dismiss plaintiffs' claims against the Pension Board because it has not yet addressed the majority of issues raised by plaintiffs and therefore has not denied them any rights." (Def.'s Mot. 6). Taxpayers are unclear as to what the Local Board means by this assertion – because the Local Board "has not yet addressed the majority of issues raised" by Taxpayers is not a valid basis for Motion to Dismiss. Moreover, this statement is patently untrue. Each and every time the Local Board reviews and approves retirement benefits for Phoenix Police Department Sergeants and Lieutenants that include the components of compensation at issue, it has and continues to address "the majority of issues raised" by Taxpayers. Moreover, each and every time the Local Board approves pension payments that include payment in lieu of vacation, payment for unused sick leave and compensatory time, and payment for any fringe benefit, it has denied Taxpayers' right to have their tax dollars lawfully spent. The Local Board is and always was obligated to comply with state law in discharging its official duties. ARIZ. REV.

STAT. § 38-847(E); (Hacking Decl. ¶¶ 17, 31, 33). Because the Local Board has failed to do so at direct Taxpayer expense, Taxpayers have stated a justiciable claim in an action they have a clear right to bring.

C. This Court Can and Should Decide this Case Without Referring the Matter Back to an Agency that Has Already Failed in Its Statutory Duties.

The doctrine of primary jurisdiction is inapplicable to this case because the Local Board has already acted and continues to act in violation of state law and has had both notice and an ample opportunity to examine the pension payments at issue in this case.

The doctrine of primary jurisdiction is a discretionary rule created by the courts to determine whether the courts or an administrative agency should make the *initial* decision in a particular case. *See Campbell v. Mountain States Tel. & Tel. Co.,* 120 Ariz. 426, 429-30, 586 P.2d 987, 990-91 (App. 1978). "[T]he United States Supreme Court and other courts have explained that the doctrine of primary jurisdiction does not apply if the administrative agency has *already acted* or *otherwise been given an opportunity to determine matters* within its special expertise or explicit jurisdiction prior to judicial review." *Coconino County v. Antco, Inc.*, 214 Ariz. 82, 89, 148 P.3d 1155, 1162 (App. 2006) (emphasis added).

In this case, the Local Board has already acted – the Local Board has approved and continues to approve pension payments for Phoenix Police Sergeants and Lieutenants that violate state law. The Local Board is and always was obligated to comply with state statutes that define "compensation" for members of PSPRS and prohibit local boards from adding benefits to the PSPRS system. ARIZ. REV. STAT. §§ 38-842(12); 38-847(E). Every time the Local Board approves a pension payment that includes the components of compensation at issue here, it is adding benefits to the system that the Local Board has no power to add. (FAC ¶ 50). Moreover, as the Local Board observed, the Local Board has already specifically determined that one component of compensation challenged in the FAC, pay increases in lieu of a uniform allowance, is pensionable pay. (Def.'s Mot. 4, 9). Because the Local Board has already made the initial decision that the components of compensation at issue are pensionable by approving payments that include those components, the doctrine of primary jurisdiction is inapplicable.

Moreover, Taxpayers are not persuaded by the Local Board's assertion that "the specific issues alleged in the FAC by plaintiffs were never raised [with the Local Board]." (Def.'s Mot. 9); *See also* (Def.'s Mot. 2) ("[P]laintiffs' allegations respecting [the components of compensation at issue here] have never been presented to the Local Board.") As the Local Board Chairperson, Toni Maccarone, attested, "To the best of my knowledge, the Pension Board has never been called upon to examine, nor has it determined, the validity of the vacation, sick leave or compensatory time elements of compensation challenged in this action." (Maccarone Aff. ¶ 7). In fact, the Local Board generally, and Ms. Maccarone specifically, have had significant notice that the pension payments at issue in this case violate state law. As early as May 8, 2013, as part of an *Arizona Republic* story about whether state law bars the payments at issue in this action, Ms. Maccarone declared, "As part of their negotiated contracts, police officers and firefighters can receive monthly pay in lieu of sick leave or vacation leave accrual." Beth Duckett and Craig Harris, *Rising Arizona Public Safety Pensions Strain Budgets*, ARIZ. REPUBLIC, May 8, 2013, *available at* http://www.azcentral.com/news/politics/articles/20130502arizona-public-safety-pensions-strain-budgets.html. (**Exhibit A**). This statement, made over six months ago and three months before this action was filed, indicates that the Local Board Chairperson not only had notice of the questionable validity of the pension payments at issue, but affirmatively defended their legitimacy.[4]

Finally, the Local Board's reliance on *Far East Conference v. United States* to establish primary jurisdiction is misplaced. 342 U.S. 570 (1952). In *Far East* a federal administrative board set up to oversee international shipping was "passed over" when the U.S. Department of Justice sought to enjoin alleged violations of the Sherman Anti-Trust Act by an association of steamship

[4] Moreover, Taxpayers note the inherent conflict of interest some Local Board members have in making the pension determinations at issue in this case. Namely, the Local Board has two members "elected from the relevant department workforce." (Def.'s Mot. 3); ARIZ. REV. STAT. § 38-847(A)(1). Elected members that are Phoenix Police Department Sergeants or Lieutenants have a clear pecuniary interest in the outcome of any decision pertaining to these matters that may come before the Local Board. *See* ARIZ. REV. STAT. § 38-503(B) ("Any public officer or employee who has...a substantial interest in any decision of a public agency shall make known such interest in the official records of such public agency and shall refrain from participating in any manner as an officer or employee in such decision.")

companies in federal court. *Id.* at 572-74. Here, the Local Board was never "passed over." On the contrary, as described *supra*, the Local Board has had ample opportunity to determine whether the components of compensation at issue here count as pensionable pay; in fact, the Local Board has answered that inquiry in the affirmative by previously approving and continuing to approve pension payments for Sergeants and Lieutenants that include these components of compensation. *See Coconino County*, 214 Ariz. at 89, 148 P.3d at 1162 (holding that the doctrine of primary jurisdiction did not apply when the Arizona Department of Environmental Quality ("ADEQ") "was given ample opportunity to initially determine the underlying facts and circumstances of this case," but decided not to exert regulatory authority *after previously* inspecting a business's operations for regulatory violations.) Like the ADEQ in *Coconino County*, the Local Board was given ample opportunity to determine whether the components of compensation at issue in this case are pensionable. Because the Board has determined that these components of compensation are pensionable by approving pension payments that include them, they have already acted, and the doctrine of primary jurisdiction does not apply.

III. Conclusion

For the foregoing reasons, Taxpayers respectfully request that the Local Board's Motion to Dismiss and Motion to Stay be DENIED.

Respectfully submitted on this 27th Day of November, 2013.

/s/ Jonathan Riches
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CERTIFICATE OF SERVICE

ORIGINAL E-FILED this 27th day of November, 2013, with a copy delivered via the ECF system to:

The Honorable John Rea
Maricopa County Superior Court

Clerk of Court
Maricopa County Superior Court

COPY of the foregoing E-MAILED this 27th day of November, 2013 to:

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Exhibit A

Exhibit A

Rising Arizona public safety pensions strain budgets

By Craig Harris and Beth Duckett The Republic | azcentral.comWed May 8, 2013 10:20 AM

The cost of funding retirement for Arizona's first responders has risen 500 percent during the past decade, inflated by enhanced benefits and battered by investment losses, forcing some communities to curb their hiring of police officers and firefighters, *The Arizona Republic* has found.

Arizona taxpayers now spend more than $300 million a year to keep the Public Safety Personnel Retirement System solvent, while the typical retirement payout now exceeds Arizona's average wage and some former public employees receive more in retirement than they earned on the job.

Policy makers at the state and local levels contributed to this escalation in costs by enhancing public-safety pension benefits and allowing employees to inflate their salaries before retiring — which further increased pensions. The high costs of those policies became evident in the last few years.

Lawmakers have tried to rein in benefits and control costs, but lawsuits threaten those efforts. An *Arizona Republic* series in 2010 exposing abuses led Phoenix to curb some pricey practices, but the city's reforms exempted public-safety workers.

Phoenix's generous policies have made a handful of Police and Fire Department retirees millionaires in their first few years of retirement. They were allowed to cash in unused sick leave, vacation and deferred compensation benefits in the final years of service, boosting salaries which, in turn, significantly increased annual retirement payouts.

Former Phoenix Assistant Fire Chief Bobby Ruiz, for example, cashed in $110,877 in sick leave, $14,528 of vacation time and $43,152 in deferred compensation benefits shortly before entering a retirement-deferral program in December 2006. Those payments increased his final years' salary.

The 32-year city employee at that point enrolled in the Deferred Retirement Option Plan, or DROP, which permitted him to remain on the job for five more years at full salary, while the pension he would have earned was paid into an account with a guaranteed return of at least 8 percent.

When Ruiz left his job in December 2011, he took with him $795,983 that had accrued in the plan account. He also began receiving a pension now worth $130,046 ayear.

Months after leaving Phoenix, Ruiz became Peoria's fire chief, earning $145,000 a year. He receives an annual payment of $5,800 from Peoria toward another retirement plan.

Ruiz declined interview requests. He issued a written statement saying he worked hard for more than three decades, rarely called in sick, and followed city rules.

Phoenix City Councilman Sal DiCiccio, an outspoken critic of public pensions, said the city's rules need to change.

"When someone is walking away with $1 million, that represents 10 police officers you could have hired," DiCiccio said. "It's insane."

Average salaries of public-safety employees — a key factor in retirement pay — rose every year except one during the past decade, roughly parallel to overall wages in Arizona. Until last year, however, public-safety-system retirees were guaranteed annual cost-of-living increases.

The typical public-safety pension rose 47 percent — nearly twice the rate of inflation — to $49,480 between fiscal 2003 and 2012. By comparison, the average wage in Arizona rose by just 25 percent, to $43,950.

The Legislature over more than a decade had enacted cost-of-living increases for public-safety retirees and approved a deferred-retirement program, in part to recruit and retain workers. But as costs skyrocketed, lawmakers tried in 2011 to slow them by increasing employees' contributions to their retirement, and temporarily halting pensioners' cost-of-living raises.

Current and retired police officers sued, saying Arizona's Constitution and federal contract law prohibit changes to their benefits. The changes have gone into effect, but litigation is ongoing.

Phoenix also reined in some of its pension benefits last year, but did not touch public-safety pensions.

Police officers and firefighters are sympathetic to the cities' plight but say they didn't create the problem.

"We don't control the system. We are the players in the game," said Tim Hill, president of the 6,700-member Professional Fire Fighters of Arizona.

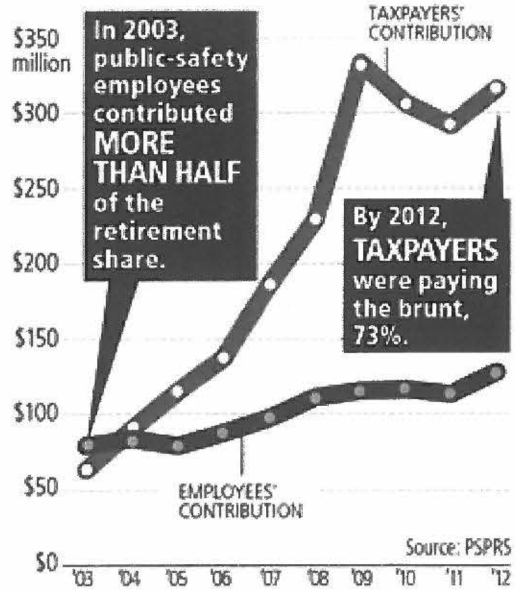
They say enhanced benefits did not create the problems and blame economic factors that tanked the system's investments, including Wall Street's failures during the 2008 banking crisis, and poor investments during the dot-com bust early last decade. The retirement trust lost more than $1 billion during the recession.

"We are caught firmly in the middle, and we understand the issues," said Jim Mann, a retired Maricopa County sheriff's deputy who represents the 6,500-member Arizona Fraternal Order of Police. "But why are we the ones taking the blame when there are not enough resources?"

Nearly everyone seems to agree on at least one thing: Rising pension costs, coupled with the effects of the recent recession, forced cities to scale back public-safety hiring. The number of first responders in the retirement system has fallen by 1,370 people since fiscal 2008, leaving some communities vulnerable.

"What do you do? Do you protect the public and eat the cost, or do you leave the public unprotected to save your budget? That's a tough call a lot of people are making these days," said Bisbee City Manager Stephen Pauken, whose city has been one of the hardest hit.

Taxpayers' tab rises



Two views of law

About 10,000 individuals, including surviving spouses and children of deceased officers, receive benefits from the public-safety retirement plan. Most do not contribute into the federal Social Security retirement system, and they do not receive those benefits in retirement.

Retirees have a defined benefit based on the number of years they worked and their compensation at the end of their career. Employees with a large ending salary and lengthy service will receive a higher pension that generally continues until they die, regardless of how much was contributed during their working years.

After 20 years on the job, a person in the plan can retire and receive half of his or her ending salary as the starting point for an annual pension. Typically, the maximum starting pension cannot exceed 80 percent of the average salary during the last three years of service.

State law bars public employees from using "unused sick leave, payment in lieu of vacation, payment for unused compensatory time or payment for any fringe benefit" to "spike" the final compensation on which retirement benefits are calculated.

Yet some cities like Phoenix interpret the law differently, allowing these buybacks over a longer period — essentially, their final few years of employment, which matches the three-year window typically used to calculate pension benefits.

"As part of their negotiated contracts, police officers and firefighters can receive monthly pay in lieu of sick or vacation leave accrual," Phoenix spokeswoman Toni Maccarone said.

Boosted by these additional payments, some retirees' pensions exceeded their base pay while they were employed. Nobody has challenged Phoenix's legal interpretation.

Plan officials say they don't track whether a city allows employees to spike their pay. It is not a concern to the statewide system, said Jim Hacking, the plan administrator, because each of the 237 jurisdictions in the system is responsible for funding the pensions of its current and retired employees.

"Ultimately, if the employer is allowing these kinds of practices, then the employer — and that employer only — is paying for the cost," Hacking said. "There is no free lunch."

Translation: Phoenix and Tucson taxpayers are on the hook.

The retirement system is also under strain from the Deferred Retirement Option Plan, the program allowing public-safety workers to stay on the job at full pay for up to five years after retirement.

It was designed to entice veteran police officers and firefighters to stay on the job for up to five additional years. The plan allowed a person to "retire" but keep working up to 60 months. During this time, the individual would receive a regular paycheck and have the pension placed into a pension-system savings account. The individual is then given a lump-sum check upon leaving employment and then his or her annual pension benefits begin.

But it has been costly. It carries a guaranteed return that in recent years was about 8 percent. This year, the rate was cut to 4.4 percent.

The Arizona Republic obtained more than 8,000 individual financial records from the plan under the state's Public Records Law. An examination of retiree benefits shows:

At least 79 retirees receive annual pensions greater than $100,000. The largest, at nearly $146,000, belongs to a former top Phoenix police executive.

The median Deferred Retirement Option Plan payment is $236,483. At least 1,367 retirees received more than that amount. At least 98 of them received a lump sum of more than $500,000.

Ten former Phoenix employees received plan payments in excess of $700,000 each.

More than 500 former employees of 12 suburban cities and towns received average plan payments of $222,000.

State Sen. Steve Yarbrough, who pushed through pension reform in 2011 and has two sons who are police officers, said *The Republic's* findings were "stunning to say the least."

"It's a relatively few people compared to the whole system, but when you hear those numbers you think: 'Oh my gosh, that is incredible,' " Yarbrough, a Chandler Republican, said. "Pension costs have risen significantly, and the number of personnel has gone down. That can only mean we are paying far more to sustain those pensions. ... It's because the program is so generous."

A few retirees like Ruiz hired onto new public jobs with additional pensions. Another was former Tucson Police Chief Richard Miranda, who received a $511,570 payment from the Deferred Retirement Option Plan in 2008 and now collects a $137,724 annual pension.

He immediately became Tucson's assistant city manager and has since become city manager. He is paid $200,000 annually and is provided a $23,000 annual payment into a second retirement account.

Miranda, who spent 30 years in law enforcement, did not respond to requests to discuss the matter. A Tucson spokesman said Miranda's compensation and retirement were negotiated with the City Council.

Exceptions to the rule

Law-enforcement and firefighting representatives say those kinds of deals are the exception.

"We're not going to walk away from this job after 20 years and have a very significant monthly pension check," said Jimmy Chavez, president of the Arizona Highway Patrol Association.

Chavez added that many active officers have not seen pay raises in more than six years, and most retiring public-safety officials are not getting rich off their pensions.

Hill, of the Professional Fire Fighters of Arizona, said a minority of top officers are well compensated in retirement, and, "Taken out of context, it looks really bad."

But Hill said many rank-and-file retirees get a $35,000 to $40,000 annual pension, and some pay as much as $18,000 a year for health insurance.

Among them is Fred Adler, who retired from the Lake Havasu City Fire Department in 2000 after 20 years. Adler, 61, receives just under $40,000 a year, according to plan records, and he says his medical costs have become so high that he dropped his family's dental insurance.

"By far, most retirees are like me at the lower end of the pension scale," Adler said. "For most of us, it's a struggle."

Adler said he has no problem with those who went into upper management and are now receiving large pensions.

"I know these guys went above and beyond to serve the community," Adler said. "I understand why some may not understand — or may just be jealous."

Adler adds that, unlike firefighters or police officers, most citizens don't risk their lives daily to protect the public.

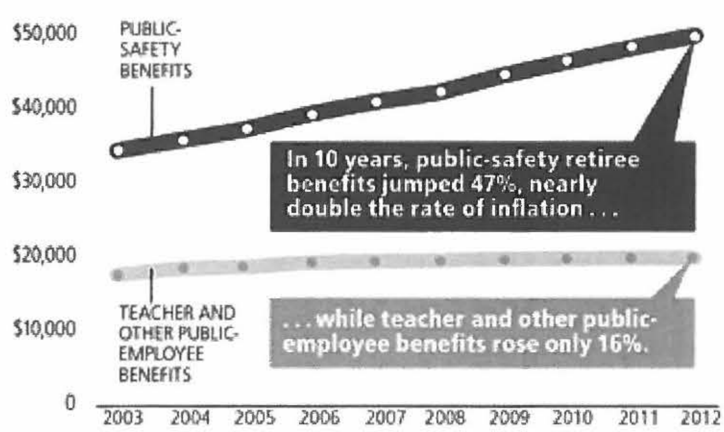
The Legislature long ago acknowledged that risk, and the service that public-safety workers provide, as key factors in how it crafted pension benefits. Lawmakers allow these workers to retire earlier and with better lifetime benefits than other public employees.

For example, the average age of a plan retiree is 51, after 23.6 years working. The average retiree gets back all of the retirement contributions he or she made within 22 months of retirement, according to retirement-system data.

A private-sector employee seeking the same average pension of $49,480 a year would have to save $1,088 a month for 23.6 years, and the savings would have to generate a return of at least 6 percent, according to Neal Van Zutphen, president of Mesa-based Intrinsic Wealth Counsel.

Van Zutphen, who did the calculation at *The Republic's* request, said the private-sector employee would have accumulated about $670,554, which would provide an annual pension of nearly $50,000 for 25 years.

Higher pensions for some, while others languish



Sources: PSPRS, ASRS

Trust in poor health

The system is not in danger of becoming insolvent, but it is in extremely poor financial health.

The trust, as of June 30, 2012, had $6.05 billion in assets and $10.32 billion in liabilities, meaning it has just 58.6 percent of the amount it needs to pay all current and future pension obligations for its active and retired members.

Ideally, a pension system is funded at 100 percent. Minimal contributions are needed when that occurs because investments, in the main, have kept the trust flush with money. A trust is considered healthy if it is at least 80 percent funded.

Investment losses, for the most part, cause a trust's funding ratio to decline. Then, more cash is needed to make it actuarially sound. Along with earnings, a trust typically is funded by payments from employers and employees. In Arizona, each is tapped for a contribution at a set rate applied to a worker's wages.

For years, the employee-contribution rate for police officers and firefighters was capped at 7.65 percent, but it gradually increased after 2011 legislative reforms to the current 9.55 percent. It will rise to 10.35 percent on July 1, when the new fiscal year begins. It can rise no higher than 11.65 percent by fiscal 2016.

Though that rate has slowly gone up, there are fewer active employees making those contributions. After four consecutive years of reductions in force, there were 18,542 employees paying into the retirement system in fiscal 2012 — down from 19,912 and the fewest since 2006.

The 237 cities, counties and state agencies whose employees make up the system contribute based on each jurisdiction's pension liabilities, with no caps. Some now contribute at rates equivalent to 50 percent of each employee's wage. Governments with high salaries and large numbers of retirees will have higher contribution costs, and costs can vary within a city for its Fire and Police departments.

Paradise Valley, an affluent town of 13,000 residents, has made budget cuts and stopped hiring police officers as a direct result of its higher pension costs, Town Manager Jim Bacon said.

"I don't see it getting significantly better for us because of the way the system is designed," Bacon said.

The Arizona Department of Public Safety and the Tucson Police Department also were smaller in 2012 than a decade ago. And Phoenix as of mid-February had 305 police vacancies and 90 Fire Department openings.

Mike Galloway, a retired Mesa police lieutenant who was the retirement system's chairman from 2008 to 2010, noted that shrinking workforces create a vicious cycle. By not hiring as many new public-safety employees, local governments still increase their pension costs indirectly because they have fewer workers to help shoulder the pension burden by contributing to the retirement system.

Twelve suburban Valley cities and towns saw their contributions to public-safety pensions soar by an average of 350 percent from fiscal 2003 to 2012. Collectively, the increases during those years totaled nearly $50 million.

Mesa had the highest increase during those years — about $13.4 million. The number of police employees has declined by 110 since 2003-04, to 707 employees in the last fiscal year. Mesa Mayor Scott Smith said the rising costs concern city officials, nearing the point where they could affect Mesa's ability to hire new police officers and firefighters.

Smith called the additional pension payments "a dead cost ... we're not getting benefits, but we're paying more. We don't mind investing more and paying more when we get more in return."

Tempe had the second-largest increase in the suburbs: roughly $7.8 million. Like other municipalities, it trimmed its budget and cut pay during the recession.

"It isn't until recently that the cost has grown to the point where it has become cumbersome and over-burdensome to our budget," said Ken Jones, Tempe finance and technology director. "We want to get back to reasonable retirement systems."

Scottsdale contributed nearly 450 percent more in fiscal 2012 than it did in fiscal 2003 to the retirements of its police officers. City officials predict annual increases for at least five more years.

David Draine, a senior researcher who specializes in public pensions for Pew Charitable Trusts, said there's no easy pill to fix the retirement system's problems.

"Part one of the solution, as painful as it will be, is to find resources to pay for the pension debt," Draine said. "The other piece going forward is that policy makers don't offer benefits they can't afford."

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