FROM

NAME & TITLE	Robert Q. Holley, Executive Director
AGENCY NAME & ADDRESS	Fire and Police Employees' Retirement System 7 E. Redwood Street, 18th Floor
SUBJECT	***City Council Bill 24-0532***

CITY of BALTIMORE

MEMO

TO

DATE: June 18, 2024

The Honorable President and Members
of the Baltimore City Council
Attn: Natawna Austin, Executive Secretary
Room 409, City Hall
100 N. Holliday Street
Baltimore, Maryland 21202

Re: City Council Bill 24-0532 **– Fire and Police Employees' Retirement System – Benefits Enhancements**

Dear Mr. President and City Council Members:

City Council Bill 24-0532 has been introduced by the Administration to amend the Fire and Police Employees' Retirement System ("F&P") law as follows:

Change definition of "average final compensation"

The Bill would change the definition of "average final compensation" to 24 months of highest paid service of a member - instead of the current definition of a member's 36 months of highest paid service - for calculating pension and death benefits. Inasmuch as F&P members generally enjoy their highest paid service at the conclusion of their careers, this change will result in higher average pension benefits paid to members. The estimated cost of this enhancement would add **$2.7 million** to the cost of the City's annual contribution to F&P. This amendment would be effective for calculations of retirements taking effect on or after July 1, 2025, death benefits for deaths occurring on or after July 1, 2025, and DROP 2 participation beginning on or after July 1, 2025.

Deferred vested benefit

The Bill would provide a new deferred vested benefit to members terminating employment after 10 years with no pension benefit. The deferred benefit would be calculated according to the normal service retirement rules (2.5% per year for the first 20 years and 2% per year thereafter) and would be payable for life after reaching age 60. This new benefit is estimated to add **$0** to the cost of the City's current annual contribution to F&P as no current active members are eligible for this benefit. This new deferred benefit would be available to F&P members entering the system on or after July 1, 2025. However, over time, as more members eligible for this additional deferred vested benefit are hired, **the normal cost for the future service of actives will nominally increase, estimated as 0.08% of total payroll.**

Elimination of 2-year waiting period for COLA eligibility

The Bill would eliminate the current 2-year waiting period for an F&P retiree to become eligible to begin receiving post-retirement benefit increases. The estimated cost of this enhancement would add **$2.5 million** to the cost of the City's annual contribution to F&P. This amendment would be effective for retired members or beneficiaries achieving post-retirement increase eligibility on or after June 30, 2025.

Increase in interest earned on DROP 2 accounts

The Bill would raise the interest rate earned by F&P members on their DROP 2 accounts from the current 3% to 5.5%. The estimated cost of this enhancement would add **$1.8 million** to the cost of the City's annual contribution to F&P. This amendment would be effective for calculation of interest on DROP 2 accounts beginning July 1, 2025.

Repeal of obsolete provisions

The Bill would repeal certain obsolete provisions relating to former variable post-retirement increase. The repeal of this language would result in no new cost savings to City; the variable benefit was repealed in 2010.

Actuarial Cost Impact

The Bill's provisions have been reviewed by Cheiron, F&P's actuary, whose cost report is attached. In total, Cheiron estimates that all the amendments proposed by the Bill would result in an additional **$7.0 million** to the cost of the City's annual contribution to F&P.

Cheiron's cost estimates for the Bill are dependent on the actuarial assumptions stated in the June 30, 2023 actuarial valuation report for F&P. That report (which may be accessed at: https://www.bcfpers.org/wp-content/uploads/2024/04/BALTPF0P_2023-AVR_20231024s.pdf) sets forth reliance language on Cheiron's sources of information for that valuation.

Cheiron wishes to emphasize that it is imperative to recognize that its Bill analysis is based on a model estimating such impact. The actual cost of any benefit change will be based on the actual benefits paid by F&P. As such, if any of the Bill's proposed benefit enhancements are adopted, the ultimate actual financial impact of the plan change will be based on the characteristics and behavior of members actually availing themselves of the adopted change. Thus, the greater the deviations between the actual experience and that assumed in this analysis, the more the costs actual incurred by F&P may differ. Please refer to Cheiron's attached analysis for additional information.

At their meeting of June 18, 2024, the F&P Board of Trustees resolved to issue a legislative report **neither supporting nor opposing** CC Bill 24-0532.

I will be available to provide testimony at the hearing scheduled for the Bill. Please call me at 410.497.7929 if you would like additional information.

Via Electronic Mail

June 14, 2024

Mr. Robert Holley
Executive Director
Fire and Police Employees' Retirement System
7 E. Redwood Street, 20th Floor
Baltimore, Maryland 21202

Re: ***Fire and Police Employees' Retirement System of the City of Baltimore***
Cost Impact of Benefit Enhancements

Dear Robert:

At the request on behalf of the City of Baltimore, we estimated the impact on the City's expected contributions for four separate modifications to Article 22 of the Baltimore City Code governing the Fire and Police Employees' Retirement System (BCFPERS or System) as outlined in City Council Bill 24-0532. To facilitate communication about this analysis, we have assigned a label, from Scenario A alphabetically through Scenario D, to each provision change we were asked to study in this analysis.

Bill Scenarios Detail

A. **Shortening the Average Final Compensation (AFC) for Non-Grandfathered DROP2 Active Members from the Highest 36 Months to the Highest 24 Months –** Changing the benefits for all actives currently identified as Non-Grandfathered (no changes for any other participants) as follows:

   I. Eligibility changes – None (same as current provisions).
   II. Benefit changes – Shorten the current number of months (Non-Grandfathered DROP2: 36) of consecutive period of service with the highest earnable compensation used to calculate the AFC to an AFC equaling the highest 24-month consecutive period of service with the highest earnable compensation effective from the date of implementation of Scenario A, here assumed to be July 1, 2025.

B. **Eliminating the two-year waiting period for Cost-of-Living-Adjustment (COLA) Eligibility for All System Members (With No Changes in COLA tiered 0%/1%/2% Benefit Provisions) –** Changing the benefits for all members as follows:

   I. Eligibility changes – Eliminate the required two-year deferral period of having received periodic benefit payments as of June 30 of a year to begin receiving a COLA to be eligible for the appropriate tiered COLA as of the following January 1 from the date of implementation of Scenario B, here assumed to be July 1, 2025.
   II. Benefit changes – None (same as current provisions).

C. **Increasing Interest Rate applicable to DROP2 Account Balances and Member Contributions during DROP2 for Non-Grandfathered DROP2 Active Members from 3.0% to 5.5% –** Changing the benefits for all currently Non-Grandfathered DROP2 actives (no changes for any other participants) as follows:

   I. Eligibility changes – None (same as current provisions).
   II. Benefit changes – Increase the interest credited to Non-Grandfathered DROP2 members for the balance of any DROP2 account balance and the member contributions paid by those impacted by this scenario during periods in which they are participating in DROP2 will be changed to 5.5% from 3.0% effective from the date of implementation of Scenario C, here assumed to be July 1, 2025.

D. **Adding an Additional Deferred Vested Benefit–** Changing the benefits for all future actives hired on or after July 1, 2025 (no changes for any current participants) as follows:

   I. Eligibility changes
      a. Introducing a new vested benefit for members currently as Non-Grandfathered who satisfy both of the following conditions:
         1. Completed a minimum of 10 years of service, and
         2. Had not yet met the normal retirement eligibility requirements.
   II. Benefit changes – For those who meet the eligibility conditions specified above, the new vested benefit is equal to the amount calculated in accordance with the current plan provisions for Non-Grandfathered retirement benefits, without any reduction, and is payable at age 60.

<u>Basis and Applicability of Scenario Impact Estimates</u>

We prepared these cost estimates based on the most recently completed actuarial valuation, which is as of June 30, 2023. As such, the following cost estimates represent the changes, or deltas, in key valuation results as a result of the identified eligibility and benefit changes for each of these scenarios. For the purposes of this analysis, we have assumed that the changes outlined in each scenario, if implemented, would be effective as of the currently most recent valuation date of June 30, 2023. While the actual effective date of these scenarios is assumed to be July 1, 2025, we believe that the cost impact information contained in this letter are reasonable proxies.

If actual implementation of a proposed enactment of these scenarios is later than that date, we would need to perform some additional analysis to determine if these cost estimates based on the valuation date of June 30, 2023 remain a reasonable proxy or if adjustments would need to be made to ensure these estimates provide a reasonable and appropriate estimate of the impact of the enacted scenarios.

In Scenarios A and C, the eligibility and benefit changes will apply only to Non-Grandfathered DROP2 active members. Scenario B will apply to all current participants eligible for a non-0% COLA. Scenario D will apply only to Non-Grandfathered DROP2 active members hired on or after July 1, 2025.

Scenario Impact Estimates Overview

The following table shows the key results of the June 30, 2023 actuarial valuation, which serves as the baseline for determining the impact of enacting the aggregated Scenarios A-D as detailed in the immediately preceding section of this letter.

June 30, 2023 Baseline Valuation Results		
Actuarial Liability (AL)	$	4,420,496,966
Total Normal Cost (NC)	$	72,052,777
Total Normal Cost (NC) Rate		22.61%
FY 2025 City Contribution	$	164,728,519
FY 2025 City Contribution Rate		51.68%

We provide an estimate of the impact of enacting the aggregated scenarios on the actuarial liability, which represents the portion of the change that is allocated to service that is completed as of the June 30, 2023 valuation date under the methods and assumptions adopted by the BCFPERS Board as of this date.

Additionally, we provide estimates of the impact of enacting the aggregated scenarios on the normal cost, which is the portion of the benefit allocated to assumed future service after the valuation date. The normal cost estimates are presented in two formats: the change expressed as a dollar amount as well as the impact of this change on the total normal cost rate, calculated by dividing this change in the dollars of normal cost by the earnable compensation for that same next year of service. Since employee contributions, currently 10%, remain unchanged in this analysis, the variations in the total normal cost rate mirror those shown in the employer normal cost rate.

Our final set of estimates for enacting the aggregated scenarios shows how the anticipated City contribution for fiscal year (FY) 2025 is affected by these changes. The FY 2025 information is shown because this is the contribution that is set by the baseline June 30, 2023 valuation. Accordingly, we present the change in FY 2025 City contribution both in dollar terms and as a rate, calculated by dividing this change in contributions by the earnable compensation for the subsequent year.

It is important to note that the City's contributions are based on the actual dollar amount calculated; thus, the contribution rate expressed as a rate of earnable compensation is provided solely for informational purposes. In the aggregated Scenarios A-D, the FY 2025 City Contribution Delta is positive, indicating that, if enacted, the FY 2025 City contribution would exceed the baseline figure of $164.73 million, as of the June 30, 2023 valuation.

Scenario Impact Estimates Detail

The following table shows the identified deltas for the aggregated Scenarios A-D relative to the June 30, 2023 actuarial valuation.

Change in June 30, 2023 Valuation Results (compared to baseline)		
		Aggregated Scenarios A-D
AL Delta	$	50,110,000
Total NC Delta	$	2,150,000
Total NC Rate Delta		0.67%
FY 2025 City Contribution Delta	$	7,020,000
FY 2025 City Contribution Rate Delta		2.20%

The enactment of the aggregated Scenarios A-D is estimated to result in an increase in the City's total FY 2025 contribution of $7.02 million to $171.75 million. This increase in the City's total contribution for FY 2025 is comprised of an increase in the normal cost applicable for FY 2025 of $2.15 million and an increase of $50.11 million necessary to amortize the additional $4.87 million in actuarial liability as a level dollar amount over a twenty-year period based on the System's funding policy beginning on the most recent valuation date, July 1, 2023.

Of the estimated $7.0 million increase in the City's total FY 2025 contribution, we have estimated the individual impact for each scenario to be an increase of: $2.7 million for Scenario A (AFC at 24 months), $2.5 million for Scenario B (No wait period for COLA), $1.8 million for Scenario C (DROP2 interest at 5.5%), and $0 for Scenario D (New vested benefit).

Note that for Scenario D, there is no increase in the City's current annual contribution because no current active members are eligible for this benefit. However, over time, as more members eligible for this additional deferred vested benefit are hired, the normal cost for the future service of actives will nominally increase, estimated as 0.08% of earnable compensation.

Certification and Reliance Statements

The cost estimates for the proposed Bill are dependent on the assumptions used. All assumptions used in the calculations presented in this letter were based on the actuarial assumptions stated in the June 30, 2023 actuarial valuation report for the System. Please refer to that June 30, 2023 actuarial valuation report for reliance language on our sources of information for that valuation that provided the baseline results for this analysis. If this Bill is adopted, the final financial impact of this plan change will be based on the data as of the effective date, which may change the results of the actual cost impact.

It is imperative to recognize that the analysis provided in this letter are based on a model estimating such impact. The actual cost of any benefit change will be based on the actual benefits paid by the System. As such, if the Bill is adopted, the ultimate actual financial impact of the plan change will be based on the characteristics and behavior of members that actual avail themselves of the adopted change. Thus, the greater the deviations between the actual behavior and that assumed in this analysis, the more the costs incurred by the System may differ.

Future actuarial measurements may differ significantly from the current measurements in this letter due to such factors as the following: Plan experience differing from that anticipated by the economic or demographic assumptions, changes in economic or demographic assumptions, and changes in plan provisions or applicable law.

This letter and its contents have been prepared in accordance with generally recognized and accepted actuarial principles and practices and our understanding of the Code of Professional Conduct and applicable Actuarial Standards of Practice set out by the Actuarial Standards Board as well as applicable laws and regulations. Furthermore, as credentialed actuaries, we meet the Qualification Standards of the American Academy of Actuaries to render the opinion contained in this letter. This letter does not address any contractual or legal issues. We are not attorneys, and our firm does not provide any legal services or advice.

This letter was prepared for Baltimore City Fire and Police Employees' Retirement System for the purposes described herein. Other users of this letter are not intended users as defined in the Actuarial Standards of Practice, and Cheiron assumes no duty or liability to such other users.

Sincerely,
Cheiron

Elizabeth Wiley, FSA, EA, MAAA, FCA
Consulting Actuary

Brett Warren, FSA, EA, MAAA, CERA
Consulting Actuary