

*Thomas P. Taneyhill*

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| FROM | NAME & TITLE          | Thomas P. Taneyhill, Executive Director   |
|      | AGENCY NAME & ADDRESS | Fire & Police Employees' Retirement System<br>7 E. Redwood Street, 19 <sup>th</sup> floor |
|      | SUBJECT               | City Council Bill 10-0482   |

CITY of  
BALTIMORE  
**MEMO**



TO

DATE:

May 21, 2010

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

Dear Mr. President and City Council Members:

City Council Bill 10-0482 amends benefit and administrative provisions of the Fire and Police Employees' Retirement System (F&P). This bill was introduced following a study and recommendations made by the Greater Baltimore Committee (GBC). The GBC was requested to review the funded status of the F&P and to make recommendations to maintain the viability of the F&P for current and future members. The GBC's report titled Task Force on Sustainable Funding of Baltimore City's Fire and Police Pension System is attached.

Position of the Board of Trustees of the Fire and Police Employees' Retirement System

At their meeting of May 18, 2010, the F&P Board of Trustees reviewed City Council Bill 10-0482 and the cost analysis report prepared by the System's actuary. The Board decided to take NO POSITION on this bill.

Fiscal Note

Attached please find the May 6, 2010, cost analysis prepared by the F&P's actuary regarding City Council Bill 10-0482. Exhibit 1 which follows page 8 of the analysis letter displays the total employer contribution requirements due to the F&P at July 1, 2010. The total contribution requirements include contributions due from both the City and the State of Maryland. The State contribution covers members who were grandfathered to the F&P by State law. The following displays just the City's contribution requirements due to the F&P at July 1, 2010.

|  |                 |
|--|-----------------|
| City contribution requirement based on current assumption rates and no changes made to the F&P benefit provisions:   | \$101.0 million |
| City contribution requirement based on lowering the post-retirement investment return assumption rate from 6.8% to 5.0% and no changes made to the F&P benefit provisions: | \$164.9 million |
| City contribution requirement if all provisions of CC 10-0482 are passed:<br>*estimated  | \$72.2 million* |

For the plan year beginning July 1, 2010 (Fiscal Year 2011), the F&P's actuary estimates that CC Bill 10-0482 will save the City \$92.7 million.

The \$92.7 million savings is comprised of the following:

|   |                |
|---|----------------|
| Savings due to replacing the “variable benefit” provisions: | \$63.9 million |
| Savings due to changes to other benefit provisions:         | \$28.8 million |

While savings are implicated if all benefit changes are approved before June 30, 2010, I believe the City Administration is still intent on making the previously published July 1, 2010, contribution requirement based on current assumption rates: \$101 million

Please note the sentence in the middle of page 2 in the 3<sup>rd</sup> paragraph of the actuary's May 6, 2010, cost analysis, in which the actuary states “However, regardless of whether the benefit changes described in this letter occur, in the absence of significant actuarial gains, we expect contributions will increase dramatically over the short term.”

Baseline projections prepared following the June 30, 2009, actuarial valuation report estimate that if no changes are made to the post-retirement investment return assumption or the plan provisions, contributions to the plan will increase from \$101 million a year to approximately \$165 million a year, in five years.

If the post-retirement investment assumption is lowered from 6.8% to 5.0% and no plan benefit changes are made, the baseline projections are that the contributions will increase from \$164.9 million a year to approximately \$220 million a year, in five years.

#### Summary of CC Bill 10-0482 proposals

City Council Bill 10-0482 proposes a number of changes to the F&P benefit and administrative provisions. The proposed changes are the following:

1. Establish new Normal service retirement benefit eligibility requirements for members who have not or will not attain the current service retirement eligibility requirements on or before June 30, 2010.

The CURRENT eligibility requirements for service retirement are:

- Members hired before 7/1/03, are eligible upon the **earlier** of age 50 or 20 years of service.
- Members hired on or after 7/1/03, are eligible upon the **earlier** of age 50 with at least 10 years as an F&P contributing member or 20 years of service of which at least 10 years must be as an F&P contributing member.

The PROPOSED eligibility requirements for Normal service retirement would be:

- Age 55 and at least 15 years of F&P membership.
2. Establish a new Early service retirement benefit and eligibility requirements for members who have not or will not attain the current service retirement eligibility requirements on or before June 30, 2010.

The CURRENT eligibility requirements for an Early service retirement are:

- None

The PROPOSED eligibility requirements for Early service retirement would be:

- Members hired before 7/1/03, and who do not meet the service retirement eligibility requirements on or before June 30, 2010, may still retire with a reduced Early service retirement benefit upon attaining the **earlier** of age 50 or 20 years of service.
  - Members hired on or after 7/1/03, may still retire with a reduced Early service retirement benefit upon the **earlier** of age 50 with at least 10 years as an F&P contributing member or 20 years of service of which at least 10 years must be as an F&P contributing member.
3. Change the average final compensation (AFC) calculation for members who have not or will not attain the current service retirement eligibility requirements on or before June 30, 2010.

The CURRENT Average Final Compensation calculation:

- Average of 18 consecutive months of a member's earnable compensation when the member's earnable compensation was the highest.

The PROPOSED Average Final Compensation calculation:

- Average of 36 consecutive months of a member's earnable compensation when the member's earnable compensation was the highest.
4. Discontinue DROP 2 for members who have not or will not attain the DROP 2 eligibility requirements on or before June 30, 2010.

The main CURRENT DROP 2 provisions, established January 1, 2010 are:

- A member must have 20 years of F&P service to be eligible to participate in DROP 2
- A member must participate in DROP 2 for at least 12 months
- The participation period is a maximum of 36 months
- A "DROP 2" account is established for the participant

- The DROP 2 account includes the maximum service retirement calculated at the member's DROP 2 start date plus member contributions made during the participation period
  - Interest on the DROP 2 account is credited at 5.5% compounded annually from the date the member starts DROP 2 participation until the member retires or terminates F&P covered employment
  - At retirement, the member can elect to receive the DROP 2 account in a lump sum, which can be taken in pocket or rolled over to an IRA, or can be annuitized to increase the member's annual retirement benefit
5. Establish DROP 3 for members who have not or will not attain the DROP 2 eligibility requirements on or before June 30, 2010.

The PROPOSED DROP 3 provides:

- A lump sum payment based on years of F&P covered employment at retirement
  - With at least 21 years, but, less than 23 years, the member can elect to receive 1 times the member's maximum service retirement benefit
  - With at least 23 years, but, less than 25 years, the member can elect to receive 1 or 1.5 times the member's maximum service retirement benefit
  - With at least 25 years the member can elect to receive 1, 1.5, or 2 times the member's maximum service retirement benefit
  - The amount of the lump sum benefit reduces the annual benefit paid to the member
6. Increase the member's contribution rate each pay.

CURRENT member contribution rate is 6.0% of regular compensation.

PROPOSED member contribution rates would increase as follows:

- July 1, 2010: from 6.0% to 7.0%
  - July 1, 2011: from 7.0% to 8.0%
  - July 1, 2012: from 8.0% to 9.0%
7. Reduce the interest rate credited on member contributions.

CURRENT rate credited on accumulated member contributions: 5.5%

PROPOSED rate to be credited on accumulated member contributions: 3.0%

Lowering the interest rate on member contributions will not change the retirement benefit that a member will receive.

Lowering the interest rate on member contributions will save when a member leaves City employment prior to retirement eligibility and is returned his/her member contributions and interest.

Certain lump-sum death benefits will be lower.

8. Discontinue the current post-retirement benefit increase provisions (“variable benefit”) and replace the variable benefit with an annual increase based on years retired and attained age as of the June 30 determination date.

The CURRENT variable benefit provisions:

- provide increases to eligible retirees and beneficiaries when F&P investment performance as determined at each June 30 exceeds 7.5%
- when F&P investment performance as determined at each June 30 does not exceed 7.5%, eligible retirees and beneficiaries do not receive an increase
- increases, if any, are paid as the same percentage to all eligible retirees and beneficiaries
- increases are paid beginning the January following the June 30 determination date
- retirees and beneficiaries must have received benefits for two or more years as of the June 30 determination date to be eligible for a variable benefit increase

The PROPOSED post retirement increase provisions:

- Retirees and beneficiaries must have received retirement benefits for two or more years as of the June 30 determination date
- Increases will be based on attained age as of the June 30 determination date
- Increases will be paid beginning the January following the June 30 determination date
- Increases paid will be the lower of the Social Security increase paid that same January, or the rate paid based on the retiree's or beneficiary's age
- Members and beneficiaries less than age 55 receive no increase
- Members and beneficiaries who have attained age 55, but, are less than age 65 receive a 1.0% increase
- Members and beneficiaries who have attained age 65 receive a 2.0% increase
- no increase will be paid in January 2011

9. Increase the number of members on the F&P's Board of Trustees.

CURRENT nine member Board of Trustees is comprised of:

- The City Comptroller, ex-officio
- The Police Commissioner, ex-officio
- The Fire Chief, ex-officio
- 2 Mayoral appointees who are City residents, one of which must have banking or similar experience
- 2 retired members of the F&P, 1 Fire Department and 1 Police Department, each elected by the retired members of their respective departments
- 2 active members of the F&P, 1 Fire Department and 1 Police Department, each elected by the active members of their respective departments

**PROPOSED additions to the Board of Trustees:**

- The Director of Finance or his representative
- 1 Mayoral appointee
- All Mayoral appointments must meet professional requirements

**10. Change the F&P's investment assumption rates.**

**CURRENT assumption rates:**

Pre-retirement assets: 8.25%

Post-retirement assets: 6.80%

**PROPOSED assumption rate: 8.0%**

This is the most commonly used assumption rate by public pension plans.

If the variable benefit provisions are changed as proposed, there will be no reason to have different rates for pre-retirement and post-retirement assets.

**Attached are:**

- a) a schedule that compares the current F&P provisions to the GBC recommendations and to the proposed changes;
- b) Questions and Answers concerning the proposals, and
- c) A schedule of past variable benefit increases.

I will be available to provide testimony at the hearing for City Council Bill 10-0482. Please call me at 443-984-2800/2803 if you would like to review or discuss the attached letter from the System's actuary or any of the other documents, or if you would like additional information.

TPT/dl

Attachments

Cc: Angela Gibson, Mayor's Legislative Liaison to the City Council  
Board of Trustees of the Fire and Police Employees' Retirement System