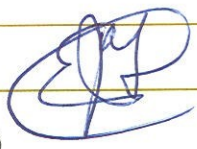



FROM	NAME & TITLE	Edward J. Gallagher, Director 	CITY of BALTIMORE MEMO	
	AGENCY NAME & ADDRESS	Department of Finance Room 448, City Hall (396-4940)		
	SUBJECT	City Council Bill 08-0220		

DATE: March 10, 2009

TO The Honorable President
And Members of City Council
Room 400 City Hall

Attention: Karen Randle

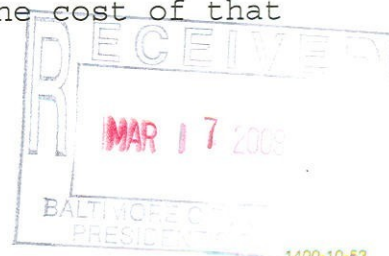
City Council Bill 08-0220 replaces the current variable benefit feature of the Fire & Police Employees' Retirement (F&P) System with a more sensible and rational application of the variable benefit, as well as moving the variable benefit assets into the general investment portfolio to improve earnings potential. This bill provides an initial step toward the necessary fiscal reform of the F&P System.

It is clear that the Fire & Police Employees' Retirement System is in serious financial difficulties and is in need of significant reform both because of the System's excessively enriched benefits and the impact of the recent significant losses experienced in its investment portfolio. The cost of the system to the employer, the taxpayers of the City of Baltimore, is totally out of control as can be seen in the attached exhibits. Exhibit A demonstrates the growth trend in the City contribution with the Fiscal 2010 being the largest growth in magnitude since Fiscal 1998. Exhibit B reflects what has been referred to by the Chairman of the F&P Board as a possible Fiscal 2011 City contribution requirement. The potential future required annual contributions by the City are going to be daunting by any ones estimate and quite frankly out of the reach for this municipality already struggling with its structural deficit just to provide basic city services, which is, after all, the purpose of City government.

Reform of an extremely popular employee benefit for a subset of City retirees is a difficult challenge for a legislative body, but the financial reality and thus the fiduciary responsibility imperative needs to supercede the understandable political challenge.

The current variable benefit must be restructured because future investment performance, less the amounts allocated to pay post-retirement benefit increases will not leave enough money in the F&P system assets to pay for the basic retirement benefits. F&P retirees receive an adjustment to their retirement benefit when the system investment performance is good but do not participate when the system investment performance is poor. The cost of that latter component has to be made up by the City.

F/A



Lacking legislative action on this restructuring proposal, the alternative would require the City to increase its contribution to the system by another \$61.5 million over the next several years just to stabilize the assets needed to pay basic benefits. To put that in perspective and using the Fiscal 2010 assessable base, that is equivalent to **19.3 cents** on the tax rate.

CC 08-0220 proposes to provide an annual guaranteed 1.5% increase in the retirees' benefit regardless of the system's investment performance. An additional adjustment can be provided if the system performance exceeds 8%, based on a running account balance. The retirees thus participate when there is good investment performance as well as when there is negative investment performance. Under the proposal the sum of the guaranteed 1.5% increase and the variable component cannot exceed the CPI on a June to June basis. The estimated cost of the guaranteed 1.5% adjustment is \$7.7 million. Even though the risk and burden falls on the City, the cost will be even greater if nothing is done as continuation of the current structure is reducing available assets necessary to pay the basic benefit.

It is noteworthy that the Employees' Retirement System (ERS) Board took the initiative on their own to request the City Council to amend their variable benefit provision for retirees in an effort to help stabilize their system. With quick, deliberate and non-controversial action of the City Council, the ERS retirees are now eligible for a guaranteed annual 1.5% adjustment and a variable on top of that depending on annual investment performance. Again, the total amount of an annual benefit increase would be limited to the CPI.

There is a provision in the ERS legislation that provides that if the F&P retirees were to receive an annual guarantee in excess of 1.5%, then the ERS retirees would benefit from that largess as well. If the City Council were to exceed the 1.5% guarantee, say, by moving to 2.0%, it would cost the City an additional \$17.7 million annually and the ERS system would require an additional \$7.8 million in City contribution for a total additional annual cost to the City of \$25.5 million.

To put into perspective what an additional \$25.5 million would cost the General Fund here are some equivalences in Fiscal 2010:

- Equivalent to the cost of 368 police officers
- Equivalent to the total cost of the Recreation & Parks budget
- Equivalent to 95% of the State's Attorney's budget
- In excess of the total Health Department budget (107%)
- In excess of the Library budget (111%)
- Equivalent to 8 cents on the property tax rate.

The Department of Finance would like to propose the attached amendment to CC 08-0220. The amendment provides a perspective for the need to restructure this variable benefit for the health of the F&P System as well as the fiscal imperative to do so.

The Department of Finance would recommend a favorable report from the Taxation, Finance & Economic Development Committee on City Council Bill 08-0220 with the proposed amendment.

Cc: Angela Gibson

EXHIBIT A

CITY CONTRIBUTION TO F&P RETIREMENT SYSTEM

(\$ - MILLIONS)

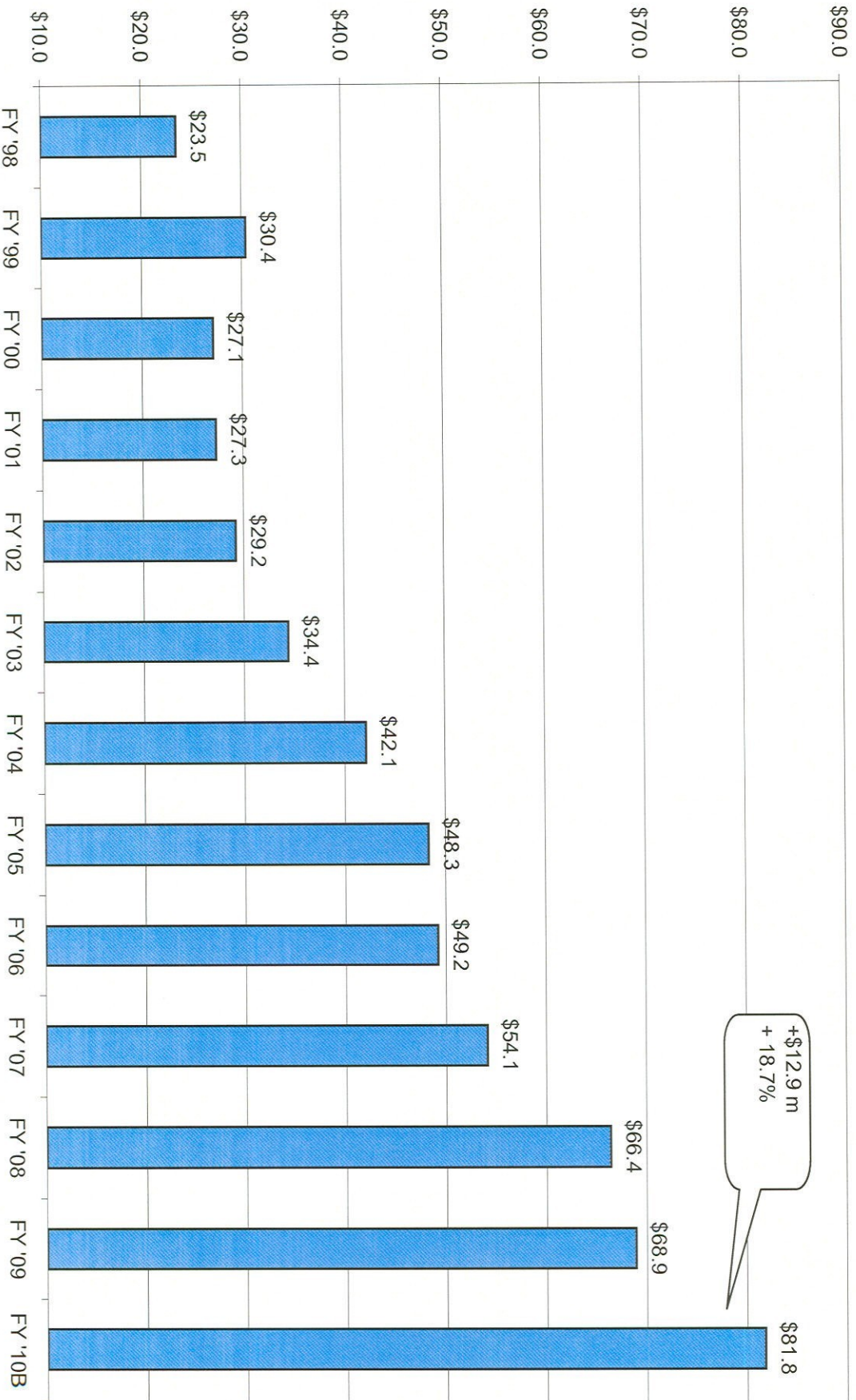
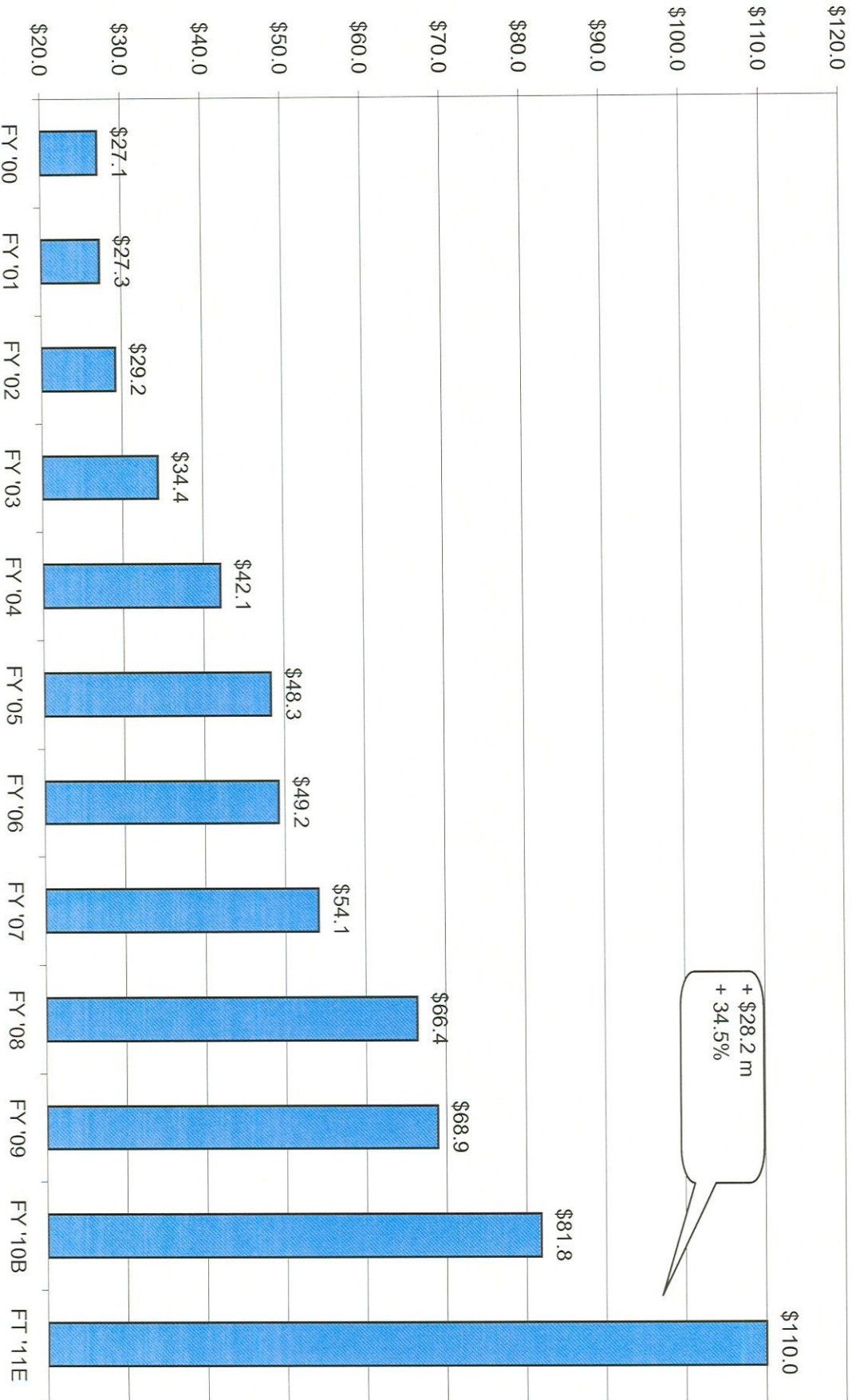


EXHIBIT B

CITY CONTRIBUTION TO F&P RETIREMENT SYSTEM

(\$ - MILLIONS)



AMENDMENTS TO CC 08-0220

On page 1, line 28, after "SECTION 1.", but before "BE IT ORDAINED BY THE MAYOR AND CITY COUNCIL OF BALTIMORE," begin a new paragraph on line 29 and insert:

Legislative Findings

WHEREAS, the members of the Fire and Police Employees' Retirement System (F&P) significantly benefit from the City's largesse by virtue of F&P's receiving annual contributions from the City's general fund, which have risen since FY1997 through FY2009 from approximately \$21 million to \$68.9 million, or 328%, relative to covered payroll, which has risen during the same period from approximately \$185.8 million to \$269.7 million, or 145%; and

WHEREAS, it is anticipated that the City's required annual contribution to F&P for FY 2010, before accounting for the cost of F&P's variable post-retirement benefit increases, will be \$81.9 million; and

WHEREAS, F&P law currently provides a variable formula for awarding post-retirement benefit increases to F&P retirees and beneficiaries in years in which the system achieves positive investment performance which does not take into consideration negative investment performance years; and

WHEREAS, the current formula results in an imbalanced asset structure under which the F&P cannot fully benefit from good investment performance since it must share a portion of investment earnings with retirees in good years but must bear the total brunt of investment losses in bad years; and

WHEREAS, it is now estimated that the annual F&P contribution needed to maintain the current variable post-retirement benefit increase is \$61 million in addition to the current annual contribution to the system, which would bring to \$142.9 the total annual contribution to F&P by the City for FY2010; and

WHEREAS, in its FY2010 budget, which takes into account only the estimated \$81.9 million contribution to F&P before accounting for the cost of F&P's variable post-retirement benefit increases, the City projects a \$65 million deficit which will likely be closed only after reducing basic services, closing facilities, laying off employees and abolishing budgeted positions and, given the current economic and employment environment, cannot practicably be reduced by increasing revenues through additional taxes; and

WHEREAS, it would be irresponsible for the City to contemplate adding to its FY2010 \$65 million budget deficit \$61 million more in F&P contributions to fund the cost of F&P's variable post-retirement benefit increases and thereby unduly encumber an already overstressed City budget struggling to provide basic City services or unfairly burden City taxpayers already facing myriad financial challenges resulting from the current economic situation; and

WHEREAS, the current F&P variable post-retirement benefit increase provides no minimum guaranteed annual increase and also fails to guarantee all increases previously awarded, allowing for the possibility that they may be eliminated in full; and

WHEREAS, under the current F&P variable post-retirement benefit structure, no increase was provided to F&P retirees and beneficiaries for four consecutive years from FY2000 through FY2003, nor in January, 2009 due to investment losses during FY2008, and, given the present general economic downturn, no increase is likely in FY2010 and, plausibly, may not be awarded over the next several years under the current law; and

WHEREAS, it is deemed desirable and prudent to preserve the actuarial soundness of the F&P and to advance the financial condition of the City by discontinuing the current, costly F&P variable post-retirement benefit structure and establishing a new post-retirement benefit increase structure for F&P retirees and beneficiaries which will provide a certain, minimum annual 1.5% benefit increase no longer dependent on market performance, plus, in addition to the guaranteed minimum, a new, modest variable component which accounts for negative investment performance years, with both components subject to a maximum limited by CPI, guaranteed by the full faith and credit of the City and on par with all other F&P benefits, and including a new guarantee by the City of all previously accrued benefit increases under the current law.

NOW, THEREFORE, BE IT ORDAINED BY THE MAYOR AND CITY COUNCIL OF BALTIMORE, That the Laws of Baltimore City read as follows: