

City of Alexandria, Virginia

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MEMORANDUM

DATE: FEBRUARY 6, 2004

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: PHILIP SUNDERLAND, CITY MANAGER

SUBJECT: AN ORDINANCE TO AMEND TITLE 2, CHAPTER 5, ARTICLE D OF THE CITY CODE TO AUTHORIZE THE CONVERSION OF THE RETIREMENT INCOME PLAN FOR FIREFIGHTERS AND POLICE OFFICERS FROM A DEFINED CONTRIBUTION PLAN TO A DEFINED BENEFIT PLAN AND TO INCORPORATE THE DISABILITY INCOME PLAN INTO THE DEFINED BENEFIT PLAN

ISSUE: Consideration of an ordinance to authorize the conversion of the Retirement Income Plan for Firefighters and Police Officers from a defined contributions (DC) plan to a defined benefit (DB) plan and to incorporate the disability plan into the defined benefit plan.

RECOMMENDATION: That City Council pass on first reading and schedule for public hearing, second reading, and final passage on February 21, 2004, an ordinance (Attachment 1) authorizing the conversion of the Retirement Income Plan for Firefighters and Police Officers from a defined contribution plan to a defined benefit plan and to incorporate the existing disability plan for firefighters and police officers into the defined benefit plan.

The City Council Pension Committee, including Mayor Euille and Councilman Smedberg, has met and has recommended that City Council approve the conversion to a DB Plan.

KEY PLAN PROVISIONS: The following are the key provisions of the proposed defined benefit plan for firefighters and police officers:

Benefit Formula: Upon retirement a participant would receive a benefit equal to 2.5% of their Average Monthly Compensation multiplied by years of Credited Service up to and including 20 years; and 3.2% of the Average Monthly Compensation multiplied by years of Credited Service in excess of 20 years. The maximum benefit of 82% of Average Monthly Compensation is reached with 30 years of Credited Service.

Average Monthly Compensation: The Average Monthly Compensation is the highest average earnings received during any 60 consecutive months (5 years) while actively employed by the City and covered by the Plan. (The number of the months counted for monthly average

compensation may be reduced before February 21 depending on our analysis of the final financial information related to the plan, which was just received.)

Credited Service: Participants are credited for each month of active service, military leave, authorized leave and while disabled under the Plan. Credited Service will accrue from the date the new plan begins.

Past Service Election: Participants were given the opportunity to retain their old Defined Contribution account balance or to exchange their old Defined Contribution account balance for pre-2004 Credited Service under the proposed Defined Benefit plan.

Contributions: The City will pay the employer required contribution, which is expected to be 20% of payroll, the same contribution the City makes now for police officer and firefighter retirement. Employees will pay a contribution of up to 8% of pension earnings. **(The precise amount will be determined after we complete our analysis of the financial information on the plan, which was just received.)** All employee contributions will be in pre-tax dollars. Police officers and firefighters do not now make an employee contribution.

Deferred Retirement Option Program (DROP): A participant who has at least 30 years of Credited Service may voluntarily elect to retire for purposes of calculating his or her accrued pension benefit, continue working as a Covered Employee for a period of up to 3 years, and defer receipt of his or her accrued pension benefit until his or her DROP Retirement Date.

Normal Retirement: An employee in the plan will be first eligible for unreduced normal retirement when he/she reaches age 55 with five years of Credited Service, or with 25 or more years of Credited Service regardless of age.

Early Retirement: An employee in the plan will be first eligible for early retirement with reduced benefits when he/she reaches age 50 with at least 20 years of Credited Service

Current Plan: If Council approves these recommendations and thereby switches to the proposed Defined Benefit plan, the City will cease contributions to the current Defined Contribution plan. All then active sworn fire and police employees will be enrolled in the new plan. The employees will not be given the option to remain in the old defined contribution plan.

BACKGROUND: Since 1979, when it switched from a Defined Benefit program, the City offered sworn police officers and firefighters a Defined Contribution program. Under this DC pension plan, the City deposits a specific amount of money into an individual account (i.e., 20% of pay). The money in the account is then invested by the employee to provide income for retirement.

Approximately 18 months ago, police and fire employees asked the City to consider providing them with a DB plan. Unlike the DC plan, the City, not the employees, will assume, under the DB plan, the risk of positive or negative return on investments. We believe this is appropriate as it is the case with most other municipal employees' pensions plans.

Under a DB pension program (Attachment 2), an employee is entitled to a specific monthly income

starting at retirement. The amount is based on a formula, often a percentage of final average monthly salary multiplied by the employee's years of service.

We have worked with a committee of police and fire employee representatives to develop the provisions of the proposed plan. This committee has held many long open meetings in the last 18 months and all parties have worked cooperatively to find a better and fair pension system for police officers and firefighters. Last May, a non-binding survey of all firefighters and police officers was undertaken to determine actual employee interest in a proposed DB plan. The survey asked the sworn police and fire employees to indicate whether they would be willing to transfer their existing retirement account balance to the proposed DB plan in exchange for credit for their service under the DC plan. Of the responding firefighters and police officers, over 80% indicated they would transfer their DC account balance to the DB plan.

On June 24, 2003, Council adopted the proposed DB pension plan in concept, and authorized the City Manager:

1. To proceed with the development of a detailed plan and conversion process,
2. To obtain final binding decisions from the firefighters and police officers who wish to convert and who agree to transfer their DC account balance into the new DB plan,
3. To give employees, as mandated by the current DC plan, 60 days to comment on any changes to the existing plan including commenting on new plan documents, and
4. If appropriate, to present the plan to Council for final adoption.

Documents: Since June, the City has obtained outside pension legal counsel, who have developed *The City of Alexandria Firefighters and Police Officers Pension Plan (Plan)* (Attachment 3). Copies of the Plan along with a draft *Retirement Income Plan for Firefighters and Police Officers Handbook* (Attachment 4) were distributed to the firefighters and police officers. The handbook contains a series of questions and answers designed to be easier for the participant to understand than the formal pension Plan. As mandated by the current DC plan, participants in the current DC plan were given notice of the proposed new DB plan.

Past Service Election: Even though years of Credited Service under the proposed DB Plan are normally based on post-2003 service as a City firefighter or police officer, the provisions of the proposed DB Plan provide that the City is to give firefighters and police officers a one-time opportunity to "exchange" the City funded portion of their account under the current DC Plan for pre-2004 years of Credited Service under the proposed DB Plan. This opportunity to exchange the City funded portion of their retirement income account for pre-2004 years of Credited Service under the proposed DB Plan is referred to as the "Past Service Election."

On December 5, 2003, we distributed three documents to all firefighters and police officers: a Disclosure Statement, an election form and a confirmation form not to elect the past service offer. The 28 page Disclosure Statement gave participants an overview of the past service election, the terms and conditions of the past service election opportunity and factors to consider in deciding whether or not to make the past service election. The election form and the confirmation form not to elect the past service offer were the formal written acceptance or rejection of the City's offer. The forms were to be returned to the City's Pension Administrator in January.

The Pension Administrator received replies from 137 firefighters and 248 police officers. This represents 89% of the firefighters and 86% of the police for a total of 87% of the eligible participants. If a participant did not submit either form, it was assumed under the Plan provisions that the participant had decided not to exchange his/her City funded retirement income account for pre-2004 Credited Service. To ensure the documents were received by employees, staff attempted to contact all the firefighters and police officers who did not respond. Of those contacted, eight stated that they intentionally were not going to respond.

Of the firefighters who submitted a response, 123 or 90% indicated they would exchange their DC account balance for past service in the proposed DB plan; of the responding police officers, 226 or 91% indicated they would make this exchange. Only 10% of responding firefighters and 9% of responding police officers directly stated that they would not exchange their DC account balance. Of the total eligible participants (when the non-responding participants are taken into account), 79% took the opportunity to exchange their DC account balance for past service in the DB plan and 21% did not. It should be noted that while this 21% will retain their DC account balances and not be credited for past service, going forward they will be DB participants.

Based on the past service election, Segal Company, the City's pension actuarial consultants, determined that the proposed DB plan is financially feasible.

Employees: While most employees are in favor of the new plan, it should be noted that some employees have asked that the City maintain two plans: (a) a new DB plan for employees who wish to exchange their DC account balances for past service in the proposed DB Plan; and (b) a DC plan for employees who do not wish to make such an exchange and, instead, wish to remain in the current DC plan. Unfortunately, for a DB plan of the nature that has been proposed to be financially feasible, all employees must move to the new plan if it is established, including those who elect not to exchange their DC account balance for pre-2004 Credited Service. The finances of the DB plan leave no room for employees to remain, in the future, in the DC plan. The reasons for this all-or-nothing requirement are the following:

1. The proposed DB plan would not be fiscally feasible if the plan's normal cost and past service cost are not distributed as a percentage of the entire payroll. If individuals were able to opt out entirely from the DB plan and not make the employee contribution, the DB plan's annual cost would need to increase to a level that would render the plan unaffordable. The proposed DB plan works because everyone shares the cost.
2. There would be significantly higher administrative costs for maintaining two types of pension plans for the same employee group. The City would be required to maintain two types of investment monitoring systems, two types of employee pension files and reporting requirements, and two separate annual actuarial calculations and financial reports covering the same employee group.

CONCLUSION: As a long-term policy, we believe that, instead of having the public safety employees bear 100% of the investment risk for their entire pension, it is more appropriate for the City to assume the risk. The City is far better able to handle fluctuations in the equity and bond markets and in earnings over time than individual employees. An employee near retirement is especially less able

to handle such fluctuations. Moreover, the City now takes this same type of risk under the retirement programs that cover most other City employees (through VRS and other pension programs). It is reasonable for the City to take a similar risk for sworn police and fire employees.

The proposed DB program ensures that a definite retirement income not-affected-by-investment-returns will be available throughout the retirement years of a firefighter and police officer. For some, this might be less than they would have been able to receive under the DC plan. For others, this will be more than what the DC plan would have delivered. But for all there will be no investment risk. We believe it is desirable that public safety employees receive similar retirement benefits for similar service to the City, regardless of their investment acumen or the state of the economy, particularly in their later years of service.

FISCAL IMPACT: The City has been and is currently paying 20% of payroll into the firefighters and police officers DC plan. This percentage does not change over the years as the investment market changes. If the City adopts a DB pension plan, initially the cost to the City will be 20% of payroll. However, the City's 20% cost could increase if the market value of the pension plan assets and investment earnings decrease or if plan retirement cost experience is higher than projected. Conversely, the City's 20% cost could decrease if the market value of the pension plan assets and investment earnings increase beyond projected returns or if plan retirement costs are lower than projected.

ATTACHMENTS:

Attachment 1. Ordinance

Attachment 2. Proposed Defined Benefit Pension Plan Summary

Attachment 3. The City of Alexandria Firefighters and Police Officers Pension Plan

Attachment 4. City of Alexandria Retirement Income Plan for Firefighters and Police Officers Handbook

STAFF:

Daniel A. Neckel, Director of Finance

Michele Evans, Assistant City Manager

Mark Jinks, Assistant City Manager

Henry Howard, Personnel Services Director

Caterina Tarver, Pension Administrator

Myla Riggs, Division Chief, Personnel Services

Attachments were provided at the February 10, 2004 meeting.

ORDINANCE NO. 4336

AN ORDINANCE to amend and reordain Section 2-5-51 (RETIREMENT PLAN – ADOPTED FOR POLICE, FIRE DEPARTMENT AND SHERIFF PERSONNEL; EFFECTIVE DATE; SIGNING OF CONTRACTS, ETC.), and Section 2-2-65 (ALTERATION, AMENDMENT OR REPEAL OF PLANS), of Article D (RETIREMENT AND INSURANCE), Chapter 5 (OFFICERS AND EMPLOYEES), Title 2 (GENERAL GOVERNMENT) of The Code of the City of Alexandria, Virginia, 1981, as amended.

THE CITY COUNCIL OF ALEXANDRIA HEREBY ORDAINS:

Section 1. That Section 2-5-51 of The Code of the City of Alexandria, Virginia, 1981, as amended, be, and the same is, amended and reordained to read as follows:

Sec. 2-5-51 Retirement plan--adopted for police, fire department and sheriff personnel; effective date; signing of contracts, etc.

- (a) The “defined benefit” retirement and disability income plan known as the “City of Alexandria Pension Plan for Firefighters and Police Officers,” as the same may be adopted and amended from time to time by resolution of the city council, is hereby adopted for the personnel of the police and fire departments of the city covered by such plan and first employed before February 13, 1979, unless prior to May 30, 1979, an employee covered under such plan has elected to convert to a "defined contribution" plan as provided for such employees prior to January 1, 2004.
- (b) The “defined contribution” retirement plan known as the “City of Alexandria Retirement Income Plan for Firefighters and Police Officers,” as the same may be adopted and amended from time to time by resolution of the city council, for the personnel of the police and fire departments of the city first employed on and after February 13, 1979, and covered by such plan, is hereby converted from a defined contribution plan to a combined defined contribution plan and defined benefit plan effective January 1, 2004, subject to the provisions of Section 2-5-65 of this code, and shall be known as the “City of Alexandria Firefighters and Police Officers Pension Plan.” On and after February 21, 2004, all benefits shall accrue under the defined benefit portion of such plan.
- (c) The “defined contribution” retirement plan known as the “City of Alexandria Retirement Income Plan for Deputy Sheriffs and Emergency Rescue Technicians,” as the same may be adopted and amended from time to time by resolution of the city council, is hereby adopted for the personnel of the fire department and sheriff covered by such plan.
- (d) The “defined benefit” disability income plan known as the “City of Alexandria Firefighters and Police Officers Disability Income Plan,” as the same may have been adopted and amended from time to time by resolution of the city council, for

