

INITIAL DRAFT

Local Government Retirement Package Options

July 17, 2009

It is the intent that each package will sufficiently address the anticipated \$140 million to \$150 million shortfall that is anticipated by state and local government for the 2011 fiscal year. Each package addresses the problem differently, with the same end-goal in mind. In creating these options we have been cognizant of the guiding principles that were established, but each package weighs these guiding principles differently.

It is also assumed that the retire/rehire issue will be addressed regardless of which package is chosen, so I have omitted that option from each package presuming it will be an addendum to each.

PACKAGE 1: The Contributory Options with Smoothing

This option would not reduce any pension benefit for any retirement sub-system. It would allow the state and local government employers to cap the employer contribution rate at the 2010 rate, and require that participating employees contribute the remaining portion of the required, actuarially adjusted contribution rate. This option would allow for all employee contributions to be exempt from vesting requirements, thus increasing employee portability from URS. With the establishment of the employer contribution rate, it is anticipated that the employee contribution amount will float from year to year based on actuarial assumptions that will be made by the URS.

This option would limit the amount of employee contribution to not allow an increase of over 2.5% year over year (smoothing), thus limiting employee exposure. This option would also require that the employer make a 401K or 457 payments to the employee if the actuarial assumptions require less contribution than what has been established as the capped employer rate, which would be based on the 2010 rate. This option would not preclude the employer from "picking up" the employee's required contribution as a part of an employee compensation package.

Fiscal Implication: This option would eliminate the need for additional state and local government appropriations for the 2011 fiscal year, but would require the employee to either take a salary reduction commensurate to the employee contribution match or payment of the additional contribution could be negotiated with the employer as a part of the municipal or state compensation arrangement.

Guiding Principles Evaluation:

- The following principles are adhered to:
 - Fiscal responsibility of the state and local government should be considered
 - Enhanced risk sharing between employees and employers
 - Look for long-term sustainable system
 - Legislative action should have a correlation to the market and dynamic with market conditions
 - Preserve and protect current benefits
- The following principles are less prevalent in this proposal:
 - Possible HR concerns if a salary reduction is required
 - Disparity in impact between young and older employees

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PACKAGE 2: Hybrid Option

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This option would allow the state and local government employers to partially cap the employer contribution rate at the 2010 rate, and then require that participating employees share equally with the employer any increase in the contribution rate over the 2010 rate. This option would also allow for any employee contribution to be exempt from vesting requirements, thus allowing for portability from the system. With the establishment of the employer contribution rate, it is anticipated that the employee contribution amount will float from year to year based on actuarial assumptions that will be made by the URS. This option would limit the amount of employee contribution to not allow an increase of over 1.5% year over year (smoothing), thus limiting employee exposure.

In addition, this option would also require that the employer only make a 401K or 457 payments equal to half of the rate decrease if the rate fell below the partially-capped rate that is based on the 2010 rate. An example of this concept would be if the rate were capped at 14.5% and the actuarial adjustment only requires a 12% contribution, the employer would make the 12% contribution and also provide a 1.25% 401K contribution $[(14.5-12) \times 0.5]=1.25$

Because this option only partially reduces the financial exposure of public employers, this option would also include the following benefit reductions.

- Redirect the current 1.5% 401K contribution to the current URS system
- Members pay the full actuarial cost of retiring prior to age 65 if they have less than 30 years of service (Rather than the 3% currently applied)
- Change the minimum retirement age for all non-public safety/firefighter employees to age 57.

Fiscal Implication: This option would have to be evaluated to see if the benefit reductions are sufficient to make up the difference in a reduced employee match requirement. Based on the current list of URS assumptions it should be close, if applying a discounted additive methodology assumption would be approximately 1.2%-1.5% cumulative rate impact. That coupled with the reduction in employer match requirements should be sufficient to make up the \$140M-\$150M gap in funding.

Guiding Principles Evaluation:

- The following principles are adhered to:
 - Fiscal responsibility of the state and local government should be considered
 - Enhanced risk sharing between employees and employers.
 - Look for long-term sustainable system.
 - Legislative action should have a correlation to the market and be dynamic with market conditions.
- The following principles are less prevalent in this proposal:
 - Preserve and protect current benefits – This proposal would not diminish benefits already earned, but would have an impact on future benefits and change some deadlines and thresholds for attaining benefits.
 - Possible HR concerns if a salary reduction is required.

Package 3: Benefit reduction package:

This package solely uses benefit reductions to address the financial exposure of the state and local government. This package also addresses the anticipated \$140M-\$150M funding gap. This package includes options that were evaluated by the local government retirement working group and includes those changes in order from “most acceptable changes” to least acceptable changes” The following benefit reductions would likely be necessary to address the funding issues of state and local government:

- Redirect the 1.5% 401K contribution to the URS (only addresses the state funding issues, and not the local government funding issues -- 1.5% for state, 0.0% for local gov.)
- Members pay the full actuarial cost of retiring prior to age 65 if they have less than 30 years of service (0.30%)
- Change the minimum retirement age to 60 for all non public-safety/firefighter employees (0.30%)
- Change the final average salary calculator from the highest 3 years of salary to the highest 4 years of salary (0.6%)
- Defer the COLA to the 3rd anniversary of retirement or 1st anniversary after turning age 65 (0.70%)

Fiscal Implication: This option would have to be evaluated to see if the benefit reductions are sufficient to make up the difference in a reduced employee match requirement. Based on the current list of URS assumptions it should be close for the state system, and relatively close for the other systems.

Guiding Principles Evaluation:

- The following principles are adhered to:
 - Fiscal responsibility of the state and local government should be considered.
 - Enhanced risk sharing between employees and employers.
- The following principles are less prevalent in this proposal:
 - Preserve and protect current benefits – This proposal would not diminish benefits already earned, but would have an impact on future benefits and change some deadlines and thresholds for attaining benefits.
 - Look for long-term sustainable system.
 - HR implications for older employees who may leave the system to avoid impact.
 - Does not respond to changes in the market.