
CITY COUNCIL REPORT

POLICY AGENDA

TO: David Cavazos
City Manager

AGENDA DATE: February 14, 2012

FROM: Rick Naimark
Deputy City Manager

ITEM:5

SUBJECT: PENSION REFORM TASK FORCE RECOMMENDATIONS

This report transmits the recommendations of the Pension Reform Task Force to the Mayor and City Council.

THE ISSUE

The Pension Reform Task Force was appointed by the Mayor and City Council in January of 2011 to work with management, outside consultants, and other stakeholders to review and recommend changes to the City of Phoenix Employees' Retirement System (COPERS). The 16-member Task Force included public members of the City Manager's Innovation and Efficiency Task Force, additional members of the public, and members representing employees, retirees, and the COPERS' Board. Independent actuarial and legal consultants provided support to the Task Force. The Task Force met 13 times between February and December of 2011 to complete its review, and sunset on December 31, 2011. This report reviews the Task Force's process and presents its recommendations.

OTHER INFORMATION

COPERS is a defined benefit plan established in the City Charter by a vote of the residents of Phoenix in 1947 and revised in 1953. Since that time various changes to COPERS have been approved by voters. COPERS includes classified civil service employees and full-time appointed employees, except public safety employees and elected officials who are enrolled in retirement systems administered by the State of Arizona. COPERS membership is comprised of 8,569 active members, 680 inactive members, and 5,191 retirees. The average annual pension as of June 30, 2010, was \$28,042. The City Charter requires the City to contribute an actuarially determined amount each year, which ensures the financial solvency of COPERS.

The Task Force recommended, and the City Council approved, the issuance of a Request for Qualifications (RFQ) for pension consulting services to study COPERS, conduct actuarial analyses, and evaluate alternative plan options. On May 5, 2011, a selection committee comprised of City staff and several members of the Task Force recommended The Segal Company to serve as the pension consultant for the Task Force. On June 1, 2011, the City Council authorized the City Manager to enter into a contract with The Segal Company for this purpose.

The Law Department procured legal consulting services for the Task Force from an existing Qualified Vendors List (QVL). A panel comprised of City staff and Task Force members interviewed selected respondents from the QVL and chose the firm Littler Mendelson, P.C. to advise the City on the legal issues related to the pension system and its potential reform. Littler Mendelson will continue to advise the Mayor and Council throughout the potential reform process.

The Task Force reviewed comprehensive information on the pension system including:

- prior studies and audits of COPERS,
- City Charter investment restrictions,
- annual financial reports,
- the 2010 Actuarial Valuation report,
- a history of changes to the City Charter pertaining to COPERS,
- examples of sick leave and vacation leave impact on pension benefits,
- a benefit formula overview,
- retirement eligibility and subsidies,
- annual benefit payments,
- Arizona constitutional provisions pertaining to public pension systems,
- benefit provisions of the Arizona State Retirement System and the Public Safety Personnel Retirement System, and
- recent changes to public pension systems from across the country.

After considering the most populous cities in the U.S., several Fortune 500 companies headquartered in Phoenix, as well as the top employers in Phoenix, the Task Force asked the consultant team to prepare a pension systems survey. The survey compared:

- demographics of the membership,
- actuarial methods and assumptions,
- retirement eligibility criteria,
- benefits and benefit calculation formulas,
- post-retirement benefit increases,
- funded percentage (i.e., ratio of actuarial assets to actuarial liabilities), and
- employer and employee contributions.

The public pension plans included in the survey were Los Angeles, Houston, Philadelphia, Phoenix, San Antonio, San Diego, Tucson, San Jose, Jacksonville, and the Arizona State Retirement System. These cities include three of the top five largest cities, plus the next five largest cities that follow Phoenix to create a balance between geographic diversity and cities comparable in size to Phoenix.

The Task Force also reviewed comprehensive information on private sector retirement plans, including information published by the U.S. Department of Labor Employee Benefits Security Administration and Bureau of Labor Statistics, the S&P 500, Morgan Stanley, Towers Watson, the Employee Benefit Research Institute, the Center for State & Local Government Excellence, the Center for Retirement Research at Boston College, and Kiplinger's Personal Finance.

Following a goal setting process facilitated by the actuarial consultant, The Segal Company, the Task Force conducted a comprehensive review of COPERS components and numerous actuarial projections of possible plan changes for future and existing employees. The analysis modeled the impact of possible changes on the estimated City contribution rate and plan funded percentage. Pension Reform Task Force agendas, minutes, reports, and consultant analyses are available to the public at phoenix.gov/pensionreform.

RECOMMENDATION

On December 6, 2011, the Pension Reform Task Force recommended that the City Council adopt the following changes to COPERS:

New Hires Only:

1. Modify retirement eligibility:
 - Eliminate Rule of 80 and other current age/time worked retirement provisions
 - Establish Normal Retirement Age of 63 with a minimum of 10 years of service
 - Establish an Early Retirement Age of at least 55 with 10 years of service (Early Retirement benefit amount would be actuarially reduced from Age 63)
2. Change the pension multiplier to a graduated multiplier based on years of service. These are cumulative multipliers applying to all prior years of service.
 - Up to 14.99 years of service: 1.85%
 - 15-19.99 years of service: 1.90%
 - 20-24.99 years of service: 1.95%
 - 25-29.99 years of service: 2.00%
 - 30 or more years of service: 2.10%
3. Vacation and Sick payments made at retirement cannot be used in Final Average Compensation for pension calculations.
4. Final Average Compensation for pension calculation purposes will exclude travel, communications, and technical allowances.
5. Time of service calculations shall reflect actual service time with 20 days of service required before a month of service is credited and 240 days of service required before a year of service is credited.
6. Minimum Pension: Terminate any existing minimum pension requirements.

New Hires and Existing Employees:

Institute a floating contribution rate for all new and existing employees with no grandfathered group. The actuarially determined rate shall be split evenly between employees and the City as determined officially each year. The City/employee rate will vary as the determined rate varies, but will be split evenly. The new rate would be implemented immediately for new employees, and would be phased-in for existing employees beginning with the effective date, with the employee rate rising no more than 2 percent of salary per year until it reaches the equal split amount.

The Pension Reform Task Force recommended implementation of its recommendations on July 1, 2012, or the earliest legal effective date. Based on an analysis conducted by The Segal Company, if implemented on July 1, 2012, the recommendations proposed by the Task Force would result in an estimated cumulative savings in City contribution

amounts of approximately \$140 million by 2016 and by slightly more than \$1 billion by 2031. The City's estimated contribution rate would decrease to approximately 12 percent of employee payroll by 2016 and to approximately 8 percent by 2031. Without any changes to COPERS, the City's estimated contribution rate would be approximately 19 percent in 2016 and approximately 14 percent in 2031. Segal's analysis was based upon the results of the 2010 actuarial valuation. The proposed recommendations do not significantly impact the COPERS estimated funded percentage, which is projected to increase to approximately 80 percent by 2030. Currently, COPERS members contribute 5 percent of salary into the system. Under the recommendations of the Pension Reform Task Force, by 2016 City employees are projected to contribute just under 12 percent of salary and by 2031 approximately 9 percent of salary.

On February 1, 2012, a ruling was issued in the Maricopa County Superior Court finding that increasing current employee retirement contribution rates violates the Arizona State Constitution. In order to comply with this ruling, if the City moves forward with the Task Force recommendations without applying them to current employees, the cumulative savings in City Contribution by 2016 would be just over \$33 million and just under \$600 million by 2031. Any changes to COPERS tied to the City Charter must be referred to the ballot for approval by Phoenix voters.

This item is for information and discussion.