PUBLIC HEARING

ON

Bill 19-77 "Pension Protection and Sustainability Act of 2011"

BEFORE THE

Committee on Government Operations and the Environment
The Honorable Mary Cheh, Chairwoman

April 4, 2011, 1:00 p.m.
John A. Wilson Building, Council Chambers

Testimony of
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Good afternoon Chairwoman Cheh and the members of the Committee. I am Yesim Yilmaz, Director of Fiscal and Legislative Analysis at the D.C. Office of Revenue Analysis. I am happy to provide testimony on Bill 19-77, Pension Protection and Sustainability Act of 2011.

Provisions of the Bill

Bill 19-77, Pension Protection and Sustainability Act of 2011, proposes changes to the financial analysis requirements on District's pension plans for police officers, fire and emergency medical services (FEMS) personnel, and teachers. Bill 19-77 would also amend the benefits offered under these plans.

Bill 19-77 proposes the following three changes to the financial analysis requirements:

- First, for any proposed legislation that could potentially impose pension-related costs on the District, the **fiscal impact statement** would be required to include an estimate of these costs over the financial plan period as well as information on how this estimate was developed.

- Second, every three years, an enrolled actuary would conduct an **experience study**—a study on the validity of the actuarial assumptions that effect the calculations of actuarial assets (that is, current assets and future contributions to the plan) and liabilities (that is, current and future benefits paid to retirees) for the pension plans. Such assumptions include mortality, disability, separation, interest, and earnings rates.

The actuary then would be asked to recommend, if necessary, changes to these assumptions based on the findings of the experience study.

- Third, every four years, the District of Columbia Retirement Board (DCRB) would be required to conduct an **audit of the enrolled actuary**.

Bill 19-77 proposes the following four changes to the benefit structure of the pension plans:

- First, calculation of benefits would exclude any overtime earnings, vacation time, or bonus;

- Second, calculation of benefits and eligibility determination would exclude time spent on voluntary leave without pay (LWOP);[1]

- Third, for payments of benefits accrued by members after June 30, 2012, the annual cost-of-living adjustment (COLA) to retiree annuities would be limited to 50 percent of the area Consumer Price Index (CPI) published by the Bureau of Labor Statistics, so long as the COLA is not less than 1 percent or more than 3 percent;

- Fourth, effective January 1, 2012, employees and retirees participating in these retirement plans would no longer be eligible for COLA until they reach the Social Security full retirement age. Depending on the

[1] Current plan provisions allow up to 6 months of approved LWOP in any calendar or fiscal year to be credited toward both retirement eligibility and benefit accrual without contributions from the member.

participant's date of birth, the full retirement age varies between 65 and 67.[2]

Fiscal Implications

The proposed changes to the financial analysis requirements do not have a fiscal impact.

- The fiscal impact statements prepared by the Office of the Chief Financial Officer (OCFO) already consider pension implications of proposed collective bargaining agreements. The OCFO typically works with an actuary if the pensionable salary increase under a proposed collective bargaining agreement is significantly higher than the actuarial assumptions about salary increases.

- DCRB already regularly requests its actuary to conduct an experience study that meets the requirements of the proposed legislation. The last experience study was conducted in November 2007, and the next one would be done in the spring of 2011. The costs of these studies are paid out of the Retirement Trust Fund.

- DCRB already conducts a quadrennial actuarial audit. The last audit was done by Gabriel, Roeder, Smith and Company in June 2008, and the next one is planned for the summer of 2012. The costs of these studies are paid out of the Retirement Trust Fund.

[2] Police officers and FEMS personnel must retire by the age of 60, unless an exception is granted by the Mayor.

Three of the four proposed changes to benefits will reduce the actuarial liabilities of the retirement plan:

- Currently overtime, vacation time, and bonus earnings are excluded from benefit calculations. The proposal that requires these exclusions would codify current practice, but won't have a fiscal impact.

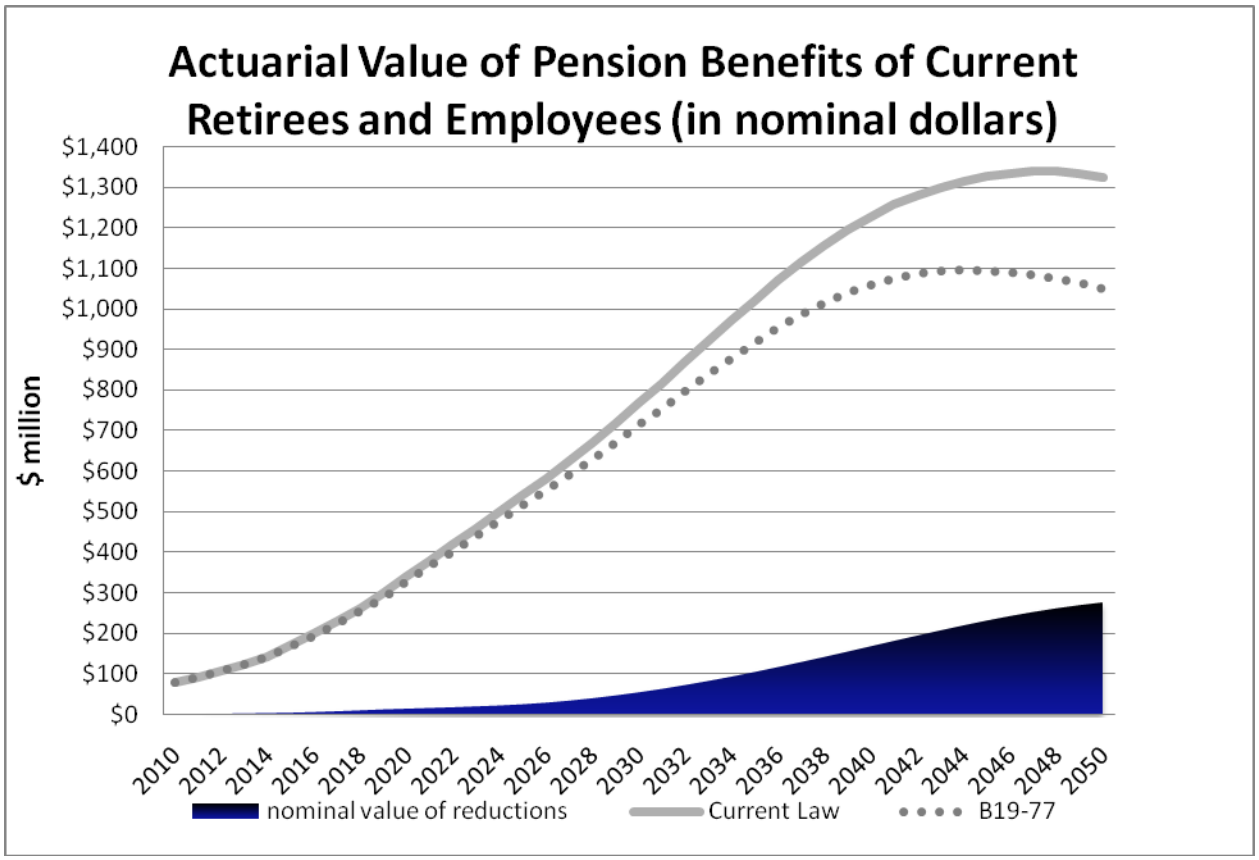
- The provision that limits the use of LWOP time towards benefits and eligibility calculations slightly reduces annual contribution requirements.

- The two provisions that limit COLA increases to half the area CPI and withhold these increases from those who retire before the Social Security full retirement age significantly reduce the required contributions.

The next chart shows the projected future benefit payments under current law and proposed law, and the difference between these two projections through 2050.

As you can see from this chart, the actuarial value of the pension benefits largely lies in the future. This is because the District's pension plans are relatively young—as a part of the federal Revitalization Act, the federal government took over the pension liabilities of the District through 1997. Any pensionable benefits earned before 1997 are the federal government's responsibility, even for District employees who retired or will retire after

1997, so long as they were hired before 1997. The District is responsible for the pensionable benefits earned since 1997.



Source: Analysis provided by Cavanaugh Macdonald Consulting LLC

CHART NOTE

- This chart represents benefits projected to be paid to current covered employees and retirees, only. It does not include any benefits that would be paid to personnel hired in the future.
- The chart reflects the assumptions used in the actuarial model.

Projected benefit payments are largely in the future, but our required contributions are forward looking: we contribute more than what is needed today to cover the benefits, so we can save for future benefits payments. Under the provisions of Bill 19-77, the value of the future benefits would decline; shifting down of the projected benefits curve in the chart. As a result,

the District won't have to save at its current rate, and District's required contributions would immediately go down.

The effects of these proposed changes on the District's required contributions are presented in the following table. It is important to emphasize that these are actuarial calculations done over long periods. This analysis, for example, covered 90 years. The valuations are deeply affected by changes in the economy and employee behavior, among other things.

Impact of Bill 19-77on the District's Required Contributions
FY 2012 – FY 2015 ($ millions)

	FY 2012	FY 2013	FY 2014	FY 2015	Four Year Total
Required Contributions Under:					
Current budget and financial plan	$116.70	$149.30	$179.70	$211.90	$657.60
Proposed LWOP provision	$115.90	$148.50	$177.20	$209.40	$651.00
Proposed COLA provision	$64.90	$94.00	$118.60	$141.60	$419.10
Proposed LWOP and COLA combined	$64.10	$93.10	$117.70	$140.70	$415.60
Impact on the Required Contributions	**($52.60)**	**($56.20)**	**($62.00)**	**($71.20)**	**($242.00)**
Positive impact on the Local General Fund	**$52.60**	**$56.20**	**$62.00**	**$71.20**	**$242.00**

Source: Actuarial Analysis conducted by Cavanaugh Macdonald Consulting LLC

TABLE NOTES

- Analysis uses the same payroll information and assumptions as those used in the December 10, 2010 report issued by Cavanaugh Macdonald Consulting, LLC.
- The model assumes that the full retirement age is 67.
- The LWOP calculation assumes that on average all individuals would have 1 month of LWOP service when they retired.
- The COLA calculations assume that the average COLA implemented under the proposed legislation would be 2 percent for all years going forward.
- The COLA calculations assume that withholding of COLA applies to all current retirees so long as they are younger than their full retirement age on January 1, 2012.

Implementation Costs

There are two sources of implementation costs not reflected in the above table:

- **Costs of reprogramming STAR.** District's retirement program is administered through the U.S. Treasury's System to Administer Retirement (STAR). The proposed legislation would require reprogramming of STAR because it would create a new tier of retirees for whom proper COLA triggers must be developed.
    - Additional clarifications to the proposed legislation are needed to correctly identify these triggers so we can obtain a reliable estimate of programming costs. We note these changes in the next section.
    - These programming costs cannot be paid out of the Retirement trust fund; they would be the District's responsibility.

- **Impact on PeopleSoft.** The provision that would exclude LWOP from the calculations of benefits and determination of eligibility may require programming of the District's PeopleSoft system to account for different LWOP categories might have to be accounted for as Bill 19-77 is implemented.
    - For example, under Uniformed Services Employment and Reemployment Rights Act (USERRA), members may count military leave as creditable service for both retirement eligibility and benefit accrual.

- It is not clear if the PeopleSoft system can distinguish between voluntary LWOP and the types of LWOP that are expressly counted towards retirement benefits such as LWOP under USERRA.

Comments and concerns

- The proposed legislation does not specify the agency that would conduct the experience study. Under current practice, DCRB conducts these studies.
- Additional clarification of the term "vacation time" would benefit our understanding of the fiscal impact. We interpret "vacation time" to mean accrued annual leave that is paid out at the time of separation.
- The bill must clarify the type of LWOP covered under the provisions of the bill.
- On COLA adjustments, further clarification is needed on whether the COLA limitations, cap, and floor would apply to survivors. Similarly it is not clear whether Social Security retirement age provision would apply to survivors' or only to plan members' age (alive or deceased).

This concludes my testimony. I will be happy to take any questions you might have on the fiscal implications of Bill 19-77.