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The U.S. Conference of Mayors is the official nonpartisan organization of cities with populations of 30,000 or more. There are 1,295 such cities in the country today, each represented in the Conference by its chief elected official, the Mayor.

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## FUTURE PENSION REPORTING

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INTRODUCTION

Background

Over the past year, public pension issues continued as a staple of news media coverage of state and local governments across the nation as growing numbers of governors, mayors, and other officials engaged in efforts to reform unsustainable pension systems. An annual survey released in May by the Center for State and Local Government Excellence found that 44 percent of state and local governments had made pension plan changes over a recent 12-month period, up from 37 percent in the previous 12 months. The survey found that, as a result of the changes, 29 percent of current employees and 34 percent of new hires saw increases in contribution requirements as a result of pension plan changes. Increased retirement age and service requirements were imposed for new hires by more than one in four of the governments surveyed.

In January, during The U.S. Conference of Mayors Winter Meeting in Washington, Louisville Mayor Greg Fischer, Chair of the Conference’s Standing Committee on Metro Economies, released a brief report on the severity of public pension problems being confronted in America’s cities today – problems exacerbated just a few years earlier by a recession that had dramatically reduced investment values and revenues and left cities with significantly larger shortfalls in pension funds (2009 shortfalls totaling $99 billion across 61 cities, according to one Pew Charitable Trust study).

The January report was based on a survey to which well over 100 mayors responded. Not surprisingly, that survey found:

- the vast majority of cities today are continuing to wrestle with problems in meeting public pension obligations that most consider to be significant, despite the efforts already made to resolve them, and
- while most cities recognized pension problems prior to the recession, and most were working at that time to resolve them, the recession made existing pension problems worse in more than three out of four cases, and created new problems in many more.

The survey report was part of a continuing effort by the Conference of Mayors to call attention to the difficulties faced by local governments in meeting pension obligations to their workers – past, current, and future – and to encourage discussion of cities’ efforts to reform existing, unsustainable pension programs.

The effort continues with this report, the fourth in the Conference’s series on city pension systems, which describes efforts undertaken in 19 cities of all sizes to reform unsustainable pension plans in which they are participants or which they administer for themselves. It builds on the report published by the Conference of Mayors in June 2012 which described responses being made to pension problems in 16 cities. Across the cities in that report, actions taken on pension problems included:
• increasing annual pension contributions for both cities and employees;
• eliminating benefit increases for current employees and offering fewer benefits for new employees;
• offering new employees defined contribution, not defined benefit, programs;
• lowering or deferring cost of living adjustments for both current employees and retirees;
• lowering benefit multipliers and benefit accrual rates;
• increasing retirement age and service requirements;
• increasing years of service used to determine final average salary for benefit determination; and
• modifying medical options and benefits offered.

The cities in this year’s report, as a group, describe approaches to pension problems that apply, in various ways, these same cost-cutting reforms.

All of this year’s cities were included in the survey conducted for the Conference’s January meeting, and four that were included in the Conference’s June 2012 report have updated their descriptions of their pension reform experience for inclusion in this year’s report.

**Approaches to Reform**

Across the 19 cities in this report, many of the descriptions of reform initiatives share common elements – such as retaining modified, less costly defined benefit plans, and achieving better balance of city and employee contributions to plans – but all are unique in their emphases, which include:

• **Allentown, PA** – use of a concession lease of the sewer and water system to generate the revenue needed to completely eliminate the City’s $200 million unfunded pension liability.

• **Arlington, TX** – working with the state-wide municipal pension system to change the actuarial cost method in use and reduce benefits to put the City on a path to increasing funded ratios – currently at more than 85 percent.

• **Barrington, IL** – working with other Illinois cities through a state-wide council of governments to support January 2011 reforms to the State’s municipal pension system that reduce benefit costs for police, firefighters, and other municipal employees.

• **Chula Vista, CA** – involving City administrators, the Police Chief, and the Fire Chief in negotiations that produced an agreement that all City employees would pay the full share of their pension contributions – initially saving the City $6 million.

• **Fort Worth, TX** – working through negotiations and legal challenges to maintain the existing defined benefit plan while reducing benefits for future earnings; accrued benefits of current employees will remain on the original pension plan, while future benefits earned will be on a new plan.
• **Jacksonville, FL** – seeking adoption of a police and fire benefit package that increases employee contributions, caps annual benefits, increases the retirement age, reduces the benefit accrual rate, and lowers COLAs; first year savings under the package would total $45 million.

• **Kentwood, MI** – modifying the City’s self-administered plan to retain the existing defined benefit option for current employees and add a defined contribution option for new hires, with increases in defined benefits covered by employee contributions.

• **Long Beach, CA** – reaching agreement with police, firefighters, and other City employees for new, less costly pension tiers for new hires and full employee pick-up of retirement contributions.

• **Louisville/Jefferson County, KY** – lobbying for State pension reform (enacted in March) that will limit Kentucky cities’ pension costs; new employees will be enrolled in a hybrid cash-balance plan and COLAs will be paid only if fully funded.

• **Milwaukee, WI** – adopting a stable employer contribution policy under which the actuary establishes a stable percent of payroll for five years to facilitate budget planning and avoid large-scale year-to-year volatility.

• **Murfreesboro, TN** – following a two-year review, retaining a defined benefit plan for current employees and adding a defined contribution plan for new hires; this saves $3 million over 10 years and adds no new unfunded liabilities.

• **Newport Beach, CA** – implementing a total compensation philosophy with a goal of having the City and its employees share equally in total retirement costs; results of labor negotiations include significant increases in retirement contributions by current employees and lower benefits for future employees.

• **North Miami Beach, FL** – beginning reform of the City’s three pension plans with changes in actuarial valuations that dramatically reduce City pension contributions and dramatically increase funding levels.

• **Pembroke Pines, FL** – freezing the defined benefit plan for current employees, not offering it to new hires, cutting pension costs to the City across the board, and giving employees the option of transferring accrued retirement benefits to a separate account on a deferred basis.

• **Phoenix, AZ** – implementing reforms to the City’s defined benefit plan developed by a broad-based task force and approved by voters in March; limited pension benefits for new hires are projected to cut the City contribution rate by half and save $596 million over 20 years.
• **Redmond, WA** – working to overcome problems related to the State-run retirement system, specifically: year-to-year fluctuations in cities’ required contributions, lack of involvement in pension plan decisions, and a “one size fits all” approach that does not allow for differences among participating cities.

• **San Jose, CA** – implementing voter-approved reforms in which existing employees are given the option of paying more to keep their current plan or move to a lower-cost plan for future years of service, and new employees are in a new, lower-cost plan.

• **Springfield, IL** – working within the limitations of the State pension system to mitigate growing pension obligations; three-prong approach includes making additional pension payments when possible, lowering personnel costs, and pressing the legislature for further reform.

• **Westland, MI** – offsetting costs of the Actuarially Required Contribution through pension cost cuts such as 5 percent pre-tax contributions to pensions imposed on, or negotiated with, nearly half of all City employees to date.

In the majority of these cities, some or all public employees are enrolled in state-administered pension plans, and their reports reflect the fact that, while their ability to motivate and shape reform within these plans may be limited, they have been actively engaged in efforts to do just that.

The individual city reports which follow were drafted by officials in the cities submitting them to the Conference of Mayors. They were edited for internal report consistency only; content and tone of the individual reports were not altered in this process.

Following at the end of this report are brief summaries of the new public pension financial reporting standards developed by the Governmental Accounting Standards Board, and the new Moody’s Investor Service approach to adjusting public pension assets and liabilities for use in the firm’s independent credit analysis.
REFORM EFFORTS IN 19 CITIES

ALLENTOWN, PENNSYLVANIA
Mayor Ed Pawlowski

Allentown employees are split between two pension systems: the Pennsylvania Municipal Retirement System (PMRS) for all but a very small minority of non-uniformed staff, and the City’s single-employer plan, which covers police, fire, and the handful of non-uniformed personnel in the Officers and Employees category.

Allentown’s pension landscape is totally lopsided: For the 510 employees in PMRS, the City’s 2013 contribution – its Minimum Municipal Obligation (MMO) – is $1.6 million. The 2013 MMO for the 319 employees in the City’s plan, $16.3 million, is 10 times higher. Added to this is $2.3 million in pension obligation debt service payments on bonds issued in 1996. The City’s retirement plan has more than 500 retirees but only about 280 contributing members.

City officials knew they were confronting an absurd and unsustainable situation that would only get worse with time. The unfunded liability represented a $200 million-plus legally binding full faith and credit general obligation debt of the City. The projected growth of this unfunded liability put the MMO on a trajectory that would quickly drain over 30 percent of the General Fund budget. It was understood that if action was not taken, Allentown’s finances would soon be crippled for decades to come. It was also understood that the problem was too big for the City to tax, save, borrow, or invest its way to a solution. For example, it would require a nearly 100 percent real estate tax increase to simply keep pace with the growing MMO payments, and Allentown already had the highest tax rate in the region. According to Mayor Pawlowski, taking this approach would constitute “irresponsible fiscal mismanagement and lead to insidious consequences.”

Following much research and evaluation, officials determined that the most prudent, cost-effective financing tool capable of generating the nearly $200 million needed to wipe out Allentown’s debilitating unfunded pension liability would be a concession lease, and it was decided to capitalize on the equity Allentown had built up in its water and sewer operations. Recruiting the best talent available from across the country, the City began a 15-month transparent process of qualifying, evaluating, and negotiating to create a bid document – the actual concession lease agreement – that pre-qualified bidders would competitively bid on.

In late April, the City received what it considered to be three very strong bids and, on May 2, the Mayor signed a 50-year concession lease agreement with the Lehigh County Authority (LCA) which allowed LCA to operate Allentown’s water and sewer system in exchange for a $220 million upfront payment, plus a $500,000 annual payment beginning in year four of the lease. The upfront payment allows the City to immediately fully fund its pension plan, eliminate certain debt and, most importantly, put Allentown on a firm financial footing well into the future.
On the day the lease agreement was signed, the lead story in Moody’s *U.S. Public Finance Weekly Credit Outlook* was titled “Long-Term Lease of Water and Sewer Enterprise Is a Credit Positive for Allentown, PA.”

Mayor Pawlowski believes that using the concession lease as a financing tool was a bold but necessary move, with the very survival of the City at stake. “The concession lease agreement that was developed over the past 15 months provides for strong protection to the City and the system’s ratepayers while also allowing LCA to do what it does best: provide clean, safe drinking water and environmentally compliant sewer services to the residents of the Lehigh Valley and now Allentown. I couldn’t ask for anything more.”

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ARLINGTON, TEXAS  
Mayor Robert Cluck  

The City of Arlington provides retirement benefits for its employees through the Texas Municipal Retirement System (TMRS), a cash balance type of defined benefit plan that serves approximately 850 Texas cities. Cities choose from a menu of plan design options, including member deposit rate, city matching ratio, and optional features, such as Updated Service Credit (USC), a defined benefit-like feature that supplements the cash balance base, and cost-of-living adjustments (COLAs), on either an ad hoc or annually repeating basis. Each city pays the percentage of member compensation needed to fund its Actuarially Required Contribution (ARC). Assets and liabilities of the cities are separately accounted for, but TMRS pools the assets of all cities for investment purposes. Arlington is the second largest city in TMRS.

In the mid-2000s, Arlington and several other cities that had adopted annually repeating benefits noticed a trend in the actuarial status of their plans: Contribution rates rose each year, while the cities’ funded ratio declined. At that point, Arlington successfully sought the Governor’s appointment of a staff member to join the system’s Board of Trustees, and a member of Arlington’s Police Department and its Fire Department were appointed to the system’s Advisory Board.

In 2007, TMRS and its consulting actuaries determined that the Unit Credit method – the actuarial cost method used by the system – was not providing full advance-funding of annually repeating USCs and COLAs. Working with an advisory body that included member associations, city management, retirees, and elected officials, the Board undertook a series of actions to reduce the volatility of city contribution rates and ensure sound future funding. Over the next two years, TMRS:

- changed the actuarial cost method to Projected Unit Credit, which provided full pre-funding of annually repeating benefits;
- changed the amortization schedule from an open period to a more conservative 30-year closed period (25-year closed, for some cities);
- successfully sought legislation, with the help of both member and City groups, that guaranteed annual member interest at 5 percent, allowed the crediting of unrealized income to city accounts, allowed city interest to be credited at a different rate from member interest, and facilitated investment diversification; and
- formalized the Advisory Committee as a standing body. Arlington has police and firefighter and representatives on this committee.

The actuarial changes caused an immediate increase in cities’ required contribution rates due to the liability associated with advance-funding repeating benefits. Arlington’s contribution rate grew from 14.66 percent of payroll for calendar year 2008, to 20.58 percent for calendar year 2009. Because of these significant rate increases, TMRS allowed cities to pay a “phase-in” rate over an eight year period. Arlington’s phase-in rate for 2009 was 15.33 percent. The liabilities, amortized under the new cost method, also caused a reduction in many cities’ funded ratios. System-wide, the funded ratio declined from 82.1 percent in 2006 to 73.7 percent in 2007.
During this time, TMRS also began diversifying its investment portfolio. Historically, TMRS invested almost 100 percent of its assets in bonds. In 2008, the Trustees, working with professional advisors, began diversifying investments following a total return strategy, which is similar to the way most other pension systems invest. TMRS began investment diversification immediately before the 2008 downturn in the markets. Since diversification had barely begun, TMRS was still primarily invested in bonds, and the System’s return for 2008 was -1.3 percent, which was one of the highest returns that year for any major public fund. TMRS has a conservative 7 percent investment income assumption and has averaged approximately 7.1 percent over the past three years.

With the increase in the cost of retirement benefits, a number of cities, including Arlington, examined the benefits they provide under TMRS and made adjustments, including either “turning off” or reducing the annually-repeating COLA. In 2010, Arlington reduced the percentage of its COLA CPI from 70 percent to 50 percent, which caused the City’s full contribution rate to decline from 19.42 percent to 16.98 percent for the year beginning January 1, 2011.

During 2010, the TMRS Trustees worked closely with their consulting actuary and Advisory Committee to devise another major change. TMRS’s internal accounts were divided into three separate funds: employee contributions, city contributions, and the fund from which retiree benefits were paid. The actuaries recommended a merger of the three accounts into a single Benefit Accumulation Fund. This fund restructuring became law in 2011, once again with the help of both City and member groups.

Restructuring allowed cities to receive higher interest credits over a longer period, further stabilized city contribution rates, and, for many cities, including Arlington, reduced the full contribution rate, effectively eliminating the remaining phase-in period. Arlington’s rate, after its 2010 COLA reduction and restructuring, was 16.63 percent of payroll. Overall, after the 2008 changes reduced the system’s funded ratio to 73.7 percent, actuarial experience, benefit reductions by cities, and restructuring have increased the funded ratio to 85.1 percent, and an additional increase is likely in 2013.

Arlington officials say factors contributing to TMRS’s successful changes today, and to its potential in the future, include the active attention of city officials to plan funding, expert analysis by actuaries and other professionals, cooperation among many diverse parties, diligence on the part of the Board of Trustees, and legislative support.

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BARRINGTON, ILLINOIS
Village President Karen Darch

Because the pension crisis faced by the Village of Barrington is shared in various ways by municipalities throughout Illinois, President Karen Darch has been working since 2006 on a solution through the Northwest Municipal Conference (NWMC), a council of governments representing 43 municipalities in the north suburbs of Chicago, and the Illinois Municipal League (IML). In her view, police and firefighter pensions are at the heart of the crisis: Unlike other municipal employees, who are enrolled in the Illinois Municipal Retirement Fund (a nationally-recognized example of a well-funded pension system), Barrington’s public safety workers are enrolled in one of the State’s 646 police and fire pension funds – one for each department, with assets ranging from under $1 million to over $100 million – that are spiraling downward.

As President Darch explains it, prior to the imposition of benefit enhancements in the early 2000s, the average fire pension fund for NWMC members was 100 percent funded while the police pensions were 89 percent funded. Thanks to the new benefits, these funds had dropped to 76 percent funded for fire and 70 percent funded for police by pre-recession 2007. The recession further dropped funds to their current 55 percent funded level. During this period, taxpayer contributions to these pension funds doubled, tripled and, in some communities, more than quadrupled, but failed to stem the growing unfunded liabilities.

Benefits levels are assigned a significant portion of the blame. Illinois municipalities have no authority to determine pension benefits for police and firefighters. The Illinois system allows a public safety employee to retire as young as age 50 and receive a pension at 75 percent of their final pay, with a 3 percent COLA compounded annually and very generous survivor benefits. Under this system, it is possible for a retiree (and their surviving spouse) to collect ever-increasing pension benefits for far longer than they served their communities. Employees contribute less than 10 percent of salary toward their pensions.

NWMC and IML, along with the Metropolitan Mayors Caucus, other councils of government, municipalities, and interest groups, formed the Pension Fairness for Illinois Communities Coalition (PFIC) in 2010 to pursue reasonable pension reforms that were strongly opposed by labor. PFIC was able to combine the resources of its partners to pursue a public relations strategy, part of which included educating legislators as to the extent of the public safety pension problem and educating the public through various means, including non-binding local referenda on pension reforms.

PFIC’s efforts produced results during the General Assembly’s fall veto session that year, when “Tier II” pension benefits were approved for new public safety employees, effective January 2011. Among Tier II changes were an increase in normal retirement age from 50 with 20 years of service to 55 with 10 years; a requirement that the 75 percent maximum salary benefit be based on 96-month salary averaging, rather than no averaging; a shift from a fixed 3 percent COLA to the lesser of 3 percent or one-half of the Consumer Price Index; and a reduction in the free Joint and Survivor Annuity from 100 percent to 66.7 percent. While this legislation was
considered a move in the right direction, it was viewed as failing to address the primary cause of declining funding levels: benefits for current employees.

President Darch says the most significant impediment to resolving the cities’ public safety pension crisis is the State’s own crisis: With Illinois facing $100 billion in unfunded liabilities across its five pension systems, the conflict between addressing this crisis versus strict pension protection provisions incorporated in the Illinois Constitution has left legislators with limited and difficult options. Without a solution to the State’s problems, pension reform for public safety pensions appears to be a distant prospect. Absent a legislative remedy, Barrington faces ever-increasing actuarially-required pension contributions, contributions that continuously take taxpayer dollars away from other services and priorities.

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CHULA VISTA, CALIFORNIA
Mayor Cheryl Cox

Chula Vista is the 76th largest city in the U.S., with a growing population of just under 250,000. When the economic downturn began in earnest in the fall of 2008, Chula Vista had already begun wrestling with the impact of an extraordinary number of new home foreclosures and a downturn in home values and property tax revenues. Sales taxes declined precipitously as joblessness rose. Almost 25 percent of the City’s employees left, most through early retirements or layoffs. Over the years, previous City Councils had offered increases in the City’s contribution to employee pensions when the City could not afford salary increases. The result: the City was paying 100 percent of employee pension contributions – a situation that could not be maintained – and pension reform became a must.

The key players in the negotiations leading to pension reform included Chula Vista’s City Manager, Assistant City Manager, Human Resources/Information Technology Director, Finance Director, Police Chief, and Fire Chief. As a result of the negotiations, beginning in January 2011, the City’s elected officials and executive/administrative staff and unrepresented employees voluntarily began paying their full share of their pension contribution. This meant an immediate savings of $850,000.

 Shortly after, all bargaining groups agreed to pick up 100 percent of their pension share. Some were phased in between January 2011 and January 2013. Today, all City employees pay the full share of their pension contributions. Three negotiating groups did not receive salary increases at that time (and have not received them since). However, police and fire bargaining units demanded their previously-negotiated raises in exchange for paying their full contributions. They elected to take pay raises ranging from 1 percent to 1.5 percent, understanding that the ensuing budget would be offset by their agreeing to layoffs within their ranks.

Chula Vista officials say the keys to success in their pension reform effort were: 1) having the right people at the table (with the City being well-served by its in-house counsel); 2) a high level of trust between employee groups and several members of the negotiating team; and 3) immediate and unanimous agreement by all elected and top staff.

Mayor Cox says that, when looking at the City’s immediate savings of $6 million, it is important to consider that the adopted pension reform measures meant hard hits to all employees who did not exchange salary increases for pension reform. Paychecks were reduced by $254 per month for the least well-compensated employees and up to $1,500 per month for top administrative staff, amounts that the Mayor describes as “real money, used to pay for childcare, college tuition, and mortgages.”

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FORT WORTH, TEXAS
Mayor Betsy Price

Historically, Fort Worth’s public employee pension has been a huge liability for taxpayers, and some changes had been made over the years in an effort to improve the fund’s health. Between fiscal years 2007 and 2012, taxpayers’ contributions to the pension fund nearly doubled; in 2012 alone, $78 million was paid to the fund. But despite additional revenues being pumped into the system, the funded status of the pension fund continued to fall.

In late 2012, the Fort Worth City Council acted decisively to further reduce the future liability of the pension fund. The changes did not take away benefits already earned by City employees, nor did they freeze or abolish the pension (as did many organizations across the country dealing with pensions). The City Council maintained the existing defined benefit plan while reducing benefits for future earnings: Accrued benefits of current employees will remain on the old pension plan, while future benefits earned will be on the new plan.

Some major benefits for new police and General Employees have been reduced, as have future service benefits for current police and General Employees. Among these:

- Pension earnings will be based on the five highest salary years, rather than three.
- The multiplier that determines the percentage of pay a retiree receives was adjusted to 2.5 percent from 3 percent.
- Overtime will not be included in pension calculations.
- For employees who have selected to have an ad hoc cost of living adjustment (COLA) in retirement, the COLA will revert to 2 percent for future service accrual, with an option to revert to a guaranteed 2 percent for past accrued service.

The Fort Worth Police Officer’s Association (POA) has Meet and Confer rights, and the City was able to make the changes for police officers without the POA’s consent. In its most recent contract, however, the POA did negotiate a reopener on the pension issue if the City reached a different deal with its firefighters. The City is negotiating with the firefighters union, which has collective bargaining rights, but is at serious risk of reaching an impasse on this issue.

Following the City Council’s most recent decision to reduce future benefits, the Fort Worth Retirement Fund Board, which controls actuarial assumptions, reduced the fund’s return assumption from 8.25 percent to 8 percent. This was another positive step, although the City maintains that a more realistic assumed rate of return would be 7.5 percent. Reducing the actuarial assumption will increase the unfunded liability in the short term, but officials believe the new rate is more realistic. Also, while moving from the ad hoc COLA to the guaranteed COLA will add this liability to the books, the guarantee is seen as more transparent and more predictable. As retirees roll off of the higher benefit plans, the health of the pension fund is projected to improve, and the fund's reported unfunded liability of $1.1 billion as of January 2013 could be reduced pending an agreement with the firefighter's union.

Fort Worth officials believe keys to their progress in resolving the City’s pension problems include: a City Council that was collectively committed to resolving the challenges while retaining a defined benefit plan; a supportive business community and supportive citizens;
limited union power for police; and a significant educational campaign among employees, with a message of “Sustainability. Affordability. Security. Long-term Fiscal Accountability.”

Fort Worth is currently in litigation with the Employee Retirement Fund seeking declaratory judgment regarding the constitutionality of the City Council’s prospective benefit changes, and the City has been sued by the current and former presidents of the Fort Worth POA regarding federal constitutional issues.

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Mayor Alvin Brown took office on July 1, 2011 with retirement reform as one of his top priorities. Less than two years later, on May 8, 2013, he announced a historic reform of pension benefits for Jacksonville’s public safety employees.

The City of Jacksonville, which is consolidated with Duval County, has approximately 825,000 residents and nearly 2,800 police and fire employees. It is also one of only two counties in the State with its own police and fire pension plan: Of Florida’s 67 counties, 65 enroll their police and fire employees in the Florida Retirement System.

In recent years, the City has faced serious financial challenges with its public safety retirement fund. Over the last decade, the City’s annual contribution to the fund has grown a staggering 1,125 percent, from approximately $10 million in FY 2003 to nearly $122 million in FY 2013. The plan’s unfunded liability grew from $400 million in 2003 to nearly $1.4 billion in 2011. As a result, it was only 38 percent funded as of October 2011, according to the plan’s investment advisers.

Mayor Brown’s retirement reform agreement has three main provisions:

- New employees hired on or after October 1, 2013 will start work under a new pension benefit package that includes an increased employee contribution. The new retirement structure caps annual benefits, increases the retirement age, reduces the benefit accrual rate, lowers the cost of living adjustment (COLA), and abolishes the Deferred Retirement Option Program (DROP).
- Current police and fire members of the Jacksonville Police and Fire Pension Fund will retain their benefits but will contribute additional funds to their pension plan.
- The agreement establishes new governance guidelines to promote accountability and transparency of the fund.

If approved by the Jacksonville City Council, the reform is projected to save taxpayers $1.2 billion over 30 years, including $45 million in FY 2014. To put these numbers in perspective, the first year’s savings represent the amount of money needed to pay approximately 800 City employees. These savings equal the combined budgets of the City’s public libraries and planning department.

Less than two weeks after unveiling the tentative police and fire pension agreement, Mayor Brown announced tentative retirement reform agreements for General Employees in the American Federation of State, County and Municipal Employees (AFSCME), which represents about 2,000 employees serving in clerical, technical, and administrative positions, and the Jacksonville Supervisors Association (JSA), which represents approximately 460 employees serving in supervisory positions.

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KENTWOOD, MICHIGAN
Mayor Richard Clanton

The City of Kentwood provides retirement benefits through two self-administered single-employer pension plans: a closed (no new participants) defined benefit plan and an active defined contribution plan. At the start of 2013, the DB plan provides benefits for 56 of the City’s 200 eligible employees (including 32 police and 17 fire union employees). At that time, the DB plan had a funded ratio of 86.2 percent and an accrued benefit funded ratio of 121 percent.

Through the early 1990s and into the early 2000s, the City was experiencing unpredictable pension costs; frequent negotiated retroactive DB plan benefit changes that resulted in added unfunded liabilities, each amortized over 25 years, which effectively added “mortgage on top of mortgage;” constant pressure to increase DB plan benefits during each successive round of collective bargaining, affected by changes made in comparable communities used for PA 312 mandatory binding arbitration; and significant pension cost increases. Between 1991 and 1996, City contributions went from $318,500 to $750,000, with increases ranging from 10.83 percent to 37.85 percent per year.

Current problems, going back to the 2008 market decline, include investment earnings not meeting actuarial assumptions and resulting in higher City contributions (since 2012, more than $1.6 million per year); having to assure adequate funding of a closed DB plan with a lump sum option; the projected weakening condition of the City’s General Fund, with expenditures rising faster than revenues; and continuing collective bargaining pressure to improve benefits.

Among the initial steps taken by Kentwood officials:
- To make pension costs predictable, negotiating for a DC plan option with the City’s firefighters (gained through a PA 312 mandatory binding arbitration award);
- With the firefighters’ DC plan decided, negotiating with other employee groups for the same; this was achieved by granting earlier normal retirement age to police patrol officer participants and establishing long-term disability insurance for all employees, to continue similar benefits for the two groups with disability pension;
- Establishing a DC plan for all new hires after June 30, 2000;
- Offering three options: Stay in DB plan, take lump sum from DB plan and move to DC plan, or freeze benefit earned in DB plan with future contributions to DC plan; and
- Negotiating for higher DB plan participant mandatory contributions to partially offset cost of benefit changes.

More recent additional solutions employed include:
- Changing the DB plan earnings rate assumption from 8 percent to 7.5 percent in 2006 and from 7.5 percent to 6.5 percent in 2012;
- Shortening the DB plan amortization periods used for unfunded pension liabilities to match average remaining work life of applicable group; and
- Insisting at the bargaining table that the cost of any DB plan benefit improvements is covered by participant contributions.
In the negotiations on changes to the pension system were members of the City administration and City Commission, including the Mayor, Human Resources Director, Deputy Administrator, Finance Director, and City Commissioners; members of the union leadership; and an arbitrator in PA 312 mandatory binding arbitration with the City’s firefighters. Kentwood officials focused on the need to hold firm to a plan for controlling benefit levels and resulting costs, especially now that benefits provided are at levels comparable to other area governmental units.

The City historically made DB plan contributions at the actuarially-calculated mid-range amount. Since 2001, Kentwood has contributed the maximum amount annually, which has allowed the City to stay current with funding requirements – something strongly supported by the City Commission – and which is especially important with a closed plan. Officials believe the City has been able to meet its pension contribution responsibilities, even in the face of investment market uncertainty, by continuing to make adequate pension funding a high priority – a policy that keeps the City from passing the costs on to future taxpayers.

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LONG BEACH, CALIFORNIA
Mayor Bob Foster

The City of Long Beach’s 22 departments employ approximately 5,000 full- and part-time employees. Personnel costs account for over 80 percent of the General Fund budget, and the City’s pension costs in FY 12 for all funds was $77 million. Long Beach faces a $700 million unfunded liability, and current pension levels are unsustainable. The City, primarily offering a defined benefit plan, is the largest in the CalPERS pension system. Retirement benefits are determined by multiplying the number of years of service by a factor of 2, 2.5, 2.7, or 3 percent, depending on the bargaining unit, to get a percent of salary to be paid in retirement.

The level of benefits negotiated in 2000 has created the most serious problem in relation to the City’s pension obligations, coupled with the fact that safety employees are retiring with full benefits at age 50 and non-safety employees are retiring at 55, and those employees and their spouses are living longer lives.

The City’s goal has been to work with employees to produce a sustainable, yet responsible, pension formula for all groups. As leaders of the pension reform effort, Mayor Foster and members of the Council personally pay the full 8 percent share of their employee pension cost. Through negotiations with employee groups, many of whom had closed contracts at the time and were under no obligation to negotiate, they made significant progress toward pension reform. The Police Officers Association, in particular, played a key role in implementing reforms and setting an example for other associations by agreeing to use contractually-obligated raises to make contributions to their pension, and to implement a reduced benefit formula for new employees.

City officials believe that Long Beach’s pension reform, achieved over several years, was a result of both disciplined budgeting and strong political leadership. Mayor Foster maintained a strong political position, which included the threat of a ballot measure, and opposed the business-as-usual approach to budgeting in which continuing growth in police and firefighting costs came at the expense of other City services. As reform efforts were getting underway, projections were showing police and firefighting costs on track to consume nearly the entire City budget by 2020. Without reforms, police pensions were projected to consume 45 percent of all Police Department spending.

Supporting the City Manager-instituted “proportionate share” budget, the Mayor and Council consistently voted to force departments to make cuts that accounted for cost growth within the fiscal year. In the Police Department, in particular, this very clearly demonstrated that layoffs and other service reductions would be needed to pay the bill for the growing pension costs. Mayor Foster instituted, and the Council supported, a policy prohibiting the use of one-time revenue funds to pay for ongoing (largely personnel) expenses. This made the budget much more transparent and took from policy makers and management the ability to “kick the can down the road” to another budget cycle, forcing them to reckon with current fiscal year costs.

It has been estimated that the police and firefighter agreements will save a total of more than $100 million over the next 10 years. These savings are realized through current employees
paying more for their pension benefits and through agreements on lower pension formulas for new employees. The City recently completed negotiations with the last large union, the International Association of Machinists (IAM), on a plan using a similar structure. The IAM savings equate to $11.8 million in the first full year of implementation – $3.7 million in the General Fund. All told, the City’s pension reform efforts have resulted in an estimated $231 million in savings through FY 2023 – $144 million in the General Fund.

Examples of negotiation successes in Long Beach include the following agreements:

- Police Officers Association, Firefighters Association – a new pension tier of 2 percent at age 50, three-year average final compensation for all new police officers, and full employee pick-up of retirement contributions for all employees.
- Long Beach Managers Association, Confidential Association, City Attorneys Association, City Prosecutors Association, Unrepresented Management Miscellaneous Employees, Unrepresented Non-Management Employees – a new pension tier for new employees with a formula of 2 percent at age 60, three-year average final compensation, and full employee pick-up of contributions.
- City Auditor, City Attorney, City Prosecutor, City Clerk – agreement to pick up an additional 1.8 percent toward their employee contribution rate.
- City Auditor – agreement by unrepresented management employees in Office to pick up an additional 2 percent toward their employee contribution rate.
- International Association of Machinists – agreement to full pick-up of contributions for all current employees.

With the exception of the IAM agreement, all of these reforms were achieved prior to State passage of AB 340, California’s pension reform bill which now has implemented new formulas for Safety employees of 2.7 percent at age 57 and for Miscellaneous members of 2 percent at age 62.

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LOUISVILLE/JEFFERSON COUNTY, KENTUCKY
Mayor Greg Fischer

The Louisville/Jefferson County Metro Government participates in the Kentucky Retirement County Employee Retirement System (CERS), a defined benefit plan which is funded through: employee contributions deducted from an employee’s creditable compensation, employer contributions paid by each county agency participating in the Kentucky Retirement Systems (KRS), and return on investments.

Louisville/Jefferson County’s annual contribution to CERS is approximately $75 million. The CERS statute requires employees in non-hazardous positions to contribute 5 percent of their creditable compensation; employees in hazardous jobs contribute 8 percent.

Pension costs represent approximately 15 percent of the Metro Government’s total General Fund expenditures. Seven years ago, those costs were 6 percent of expenditures. The KRS’s total unfunded pension liability is $18 billion.

The most serious problems facing the retirement system fall into familiar categories, including:

- effects of major economic recessions, which have driven investment returns below assumed rates of return;
- costs of health insurance benefits, with medical inflation rates exceeding estimated rates;
- the number of years required for full retirement;
- higher than anticipated retirement rates due to early retirement incentive windows during the 1990s and early 2000s;
- annual cost of living (COLA) increases for retirees; and
- increased expenditures for unfunded retiree COLAs.

Mayor Fischer has joined other local leaders concerned about unsustainable public pension obligations in Kentucky, appealing to the General Assembly to reform the State’s pension system in a way that would bring an end to cities’ and counties’ spiraling pension costs; a major press conference on this was held in January. The Mayor’s arguments for reform are based on the belief that local payments to the State pension system have reached the point that local government’s ability to provide services to citizens is being seriously compromised.

A Metropolitan Alliance for Growth, made up of mayors and county judges from the State’s metro areas (including Louisville, Lexington, Bowling Green, and Northern Kentucky), launched a public education campaign on the need for pension reform and a local tax option for infrastructure projects. The Alliance, led by Mayor Fischer and Lexington Mayor Jim Gray, lobbied their agenda in the State legislature.

It is now expected that reforms contained in new legislation enacted in March by the Kentucky House and Senate will have a positive effect on limiting the future growth in pension expenses. Among these are reforms:
• mandating that the General Assembly pay 100 percent of the Actuarially Required Contribution rate to the Kentucky Employee Retirement System and State Police Retirement System plans;
• providing an annual COLA only in the event that the plans are more than 100 percent funded, or the General Assembly appropriates sufficient funds to pre-fund the COLA;
• creating a hybrid cash balance plan for new employees hired on or after January 1, 2014 – a plan that will provide a pension benefit based upon the accumulated balance of funds in their retirement accounts; and
• creating a Public Pension Oversight Board to review all laws and regulations and make recommendations to the General Assembly.

Louisville/Jefferson County officials anticipate that this approach to pension funding will allow the State’s local governments to better plan for their annual contributions to CERS.

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The City of Milwaukee operates a home rule retirement plan, the Employees Retirement System (CMERS) which, with about $4.3 billion in assets, has been one of the best-funded public employee retirement systems in the United States. No employer contributions were required between 1996 and 2009, but following the 2008 financial crisis, the system’s funded status fell from 131 percent to 99 percent on an actuarial basis. An employer contribution of $49 million was made in 2010; the City made voluntary contributions to an employer reserve for pensions in 2011 and 2012; and the City made a $61.3 million required contribution in 2013.

The primary issue for the City has been the move from no employer contribution to $60 million-plus within a property tax levy of $250 million per year, and with declining State aid. The secondary issue has been potential year-to-year volatility in the City’s required contribution.

On April 30, the Council adopted a stable employer contribution policy, under which the actuary establishes a stable percent of payroll for five years, thus facilitating budget planning and avoiding year-to-year volatility. As a result, the budget for employer pension contributions is essentially stable for five years, thus eliminating potential volatility of between $10 million and $20 million a year. The new policy also eliminates the “full funding limit,” which means the City will now continue to make employer contributions after the system’s funded status returns to 100 percent.

Modifications to the plan design for new General Employees hired on or after January 1, 2014 were adopted on May 15. Under the modifications, which are projected to save the City $93 million over 20 years, the plan design remains defined benefit, but at a lower normal cost than the pre-existing design.

Key players in Milwaukee’s deliberations to resolve its pension issues have been the Mayor, the City’s Budget and Management Division, the Common Council, the CMERS actuary, and the CMERS Executive Director. Keys to successful negotiations are seen as disciplined budget planning, including development of the pension reserve balance; cooperative work with the system actuary; and Mayor and Council cooperation.

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MURFREESBORO, TENNESSEE
Mayor Tommy Bragg

Murfreesboro is a city of 110,000 residents served by 800 full-time employees. Three years ago, following a two-year review, the City changed its employee pension from a defined benefit plan to a defined contribution plan which will limit the City's obligation to approximately 9 percent of covered payroll in future years; the current plan has been creeping toward a 12 percent contribution. A five-year blended return average is used to make actuarial assumptions. The current assets of the plan (with approximately 110 covered retirees in addition to the current employees) total $104 million.

In the City’s existing defined benefit plan, the normal retirement age is 65, or age 55 with 30 years of service. A monthly payment, made beginning at the normal retirement age, is calculated on 2 percent of average earnings times years of service, with a 30-year maximum. The City currently contributes 11.89 percent of salary to the pension fund.

Since FY 1991, the City’s plan has averaged an 8.9 percent cost increase on an annual basis. By FY 2009, the pension cost had reached over $5.1 million.

The study of an alternative pension plan was launched in April 2007. A review of 32 different plan designs resulted in the selection of two defined benefit and two defined contribution options for more intense study. The process involved meetings and workshops with the City’s Pension Committee, the City Council, department heads, and employees.

In October 2008, the Pension Committee recommended adoption of a defined contribution plan for new employees hired after July 1, 2010, and maintenance of the existing defined benefit program for all current employees. The recommendation reflected a trend in substituting DC plans for DB plans in an effort to avoid market volatility and comply with new accounting rules.

In the new DC plan, both employee contributions and City contributions of 3 percent are mandatory; employees may contribute an additional 1 to 5 percent on a voluntary basis; and the City must match the employee’s voluntary contribution. This provides a minimum benefit of 6 percent of salary for all affected employees and a maximum potential benefit of 16 percent.

A Council workshop on reform of the City’s pension plan was held in December 2008; individual meetings of staff and Council members were held in the following months. In May, meetings were held with City employees and, in July, the plan was approved by the City Council. A Request for Proposals was issued and, in January and February 2010, three pension organizations were interviewed and one was selected.

Murfreesboro officials believe that the pension plan it has adopted benefits the City in several ways: The City’s maximum contribution is known; there are substantial savings to the City over time ($3 million over first 10 years); there are no new unfunded liabilities using the DC model (the current unfunded liability is $15 million, which will take 33 years to pay off); and the City is a more attractive employer as it competes with private sector employers offering DC plans.
For City employees, they say, the plan offers several advantages: It is portable, easy to understand, and provides an opportunity to save more and to exert individual control and responsibility.

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NEWPORT BEACH, CALIFORNIA
Mayor Keith Curry

The City of Newport Beach, with 735 full-time employees, is a member of the California Public Employees Retirement System (CalPERS). Along with many other government member agencies, the City has been faced with what it characterizes as a previously inconceivable problem. A sudden and dramatic rise in CalPERS employee pension costs meant the City’s accrued pension liabilities began, and continue, to exceed the assets set aside to fund the projected benefit obligations. The combined effect of market volatility and changes in the State system’s actuarial assumptions have caused Newport Beach’s unfunded pension liability to increase from less than $2 million in 2007 to $226 million in 2013.

Because immediate changes were needed to stem the imbalance and protect the City’s financial future, the past couple of years have seen significant reform of Newport Beach’s retirement pension program. The process began with organizational restructuring, slowly reducing the staff and evolving into a smarter, faster, smaller local government. Since 2009, the City’s full-time positions have been reduced from 832 to 752. The proposed FY 2014 balanced budget includes a net reduction of an additional 16 full-time positions and 14 full-time equivalent (FTE) part-time positions. Many of these recent staff reductions occurred via a Voluntary Separation Incentive Plan (VSIP) in which 21 employees participated. The VSIP provides a six-month lump sum for health insurance contributions and the equivalent of up to 10 weeks of salary. While the one-time cash outlay for the VSIP will cost the City approximately $700,000, the ongoing salary and benefit savings will amount to $1.4 million annually.

Next, the Newport Beach City Council adopted a total compensation philosophy with a goal of having the City and its employees share equally in total retirement costs. Labor negotiations in 2011 and 2012 resulted in lower benefits for future employees and required current employees to significantly increase their contributions toward their retirement benefits. Through this State-mandated negotiations process, miscellaneous employees in non-safety departments agreed to an increase of 1.45 percent per year for three years, which will amount to paying 12.35 percent toward their pension costs by July 2015 – almost 50 percent of the total pension cost. By the conclusion of FY 2014, all safety employees (police, firefighters, and lifeguards) will contribute a minimum of 9 percent of pensionable earnings to CalPERS. Police employees will contribute an additional 3.1 percent toward retirement, for a total of 12.1 percent, or almost 26 percent of the total current pension obligation.

In addition, the City negotiated elimination of the Employer Paid Member Contribution (EPMC) benefit for all units; this is a CalPERS optional benefit that calculates pension rates on 109 percent of payroll. Further, the bargaining units agreed to implement second tier (lower) retirement benefit formulas for future employees, and changed the single highest year pay calculation for determining the actual pension benefit amount to the highest three years. Though reducing the benefit formula for new employees will not result in an immediate reduction of pension costs, the pension obligation is anticipated to decrease over time as more employees enroll in the lower-tier benefit.
In April, the City Council faced the pension obligation head-on when it voted to accelerate payments toward the unfunded liability – paying it over a fixed, shorter, time period and avoiding the potential for $100 million of interest expense over the next 30 years. In a separate action, CalPERS adopted changes to its rate-smoothing policies which are expected to improve the financial stability of the plans over time, achieving fully funded status in 30 years.

City officials point to an agreed-upon strategy, support from the City Council, cooperation among employees, and thoughtful, collaborative negotiation and downsizing efforts as keys to Newport Beach’s progress in pension reform. Combined, these elements have enabled the City to achieve cost savings which will provide long-term fiscal sustainability and a retirement program that will remain available for both current and future staff.

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NORTH MIAMI BEACH, FLORIDA  
Mayor George Vallejo

North Miami Beach is a city of 41,523 with an operating budget of $38 million. All of its approximately 400 full-time employees are provided retirement benefits through one of three defined benefit pension plans – Police and Fire, General Employees, and Management – depending on their employment classification.

The greatest financial challenge facing the City is not related to the recession; it is related, instead, to the actuarial valuations of the three pension plans. The Mayor and Council have embarked on an aggressive campaign to reform all three pension plans, with reform of the Management plan being completed early this year.

A comparison of the valuation reports for FY 2013 and 2014 illustrate the dramatic impact that changes in actuarial valuations for the Management plan will have on City finances:

- In FY 2013, before the plan was modified, the pensionable payroll of active employees will be $2,361,127. For FY 2014, the pensionable payroll will be $1,860,605.
- The City contribution in FY 2013 will be $1,202,994, or about 51 percent of payroll. For FY 2014, it drops to $418,835, or 22.5 percent of payroll.
- In FY 2013, the Unfunded Actuarial Accrued Liability will be $5,264,904, which reflects a 69 percent funding level. For FY 2014, the UAAL drops to $3,937,092, which raises the funding level to 83 percent.

One significant barrier to the reform of the General Employee and the Police and Fire plans is that plan documents for both contain provisions requiring all pension amendments to be approved in a vote by a two-thirds majority of the plan participants. The City, however, believes it has the legal grounds to remove the vote and continue forward with its pension reform plans.

The financial impact of the unreformed General Employee pension plans in FY 2014 is as follows:

- Pensionable payroll of active employees – $10,612,185
- City contribution – $4,281,589, or 40.3 percent of payroll
- Unfunded Actuarial Accrued Liability – $36,175,064, a 62.6 percent funding level

The impact of the unreformed Police and Fire plan is:

- Pensionable payroll of active employees – $5,976,571
- City contribution – $5,946,688, or 99.5 percent of payroll
- Unfunded Actuarial Accrued Liability – $49,446,474, a 60.2 percent funding level

The City’s greatest concern is the proportion of the pension contribution for the Police and Fire plan – nearly the total payroll for all active pension participants in the plan, and well above that required for the General Employee plan. The City, which declared impasse with both unions during the collective bargaining process, proposed the following changes to the plans, which include deletion of the Deferred Retirement Option Program (DROP) through which employees may defer receipt of retirement benefits while continuing employment with the City.
For General Employees

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<th>Service Years</th>
<th>Multiplier</th>
<th>COLA</th>
<th>Pensionable Earnings</th>
<th>DROP</th>
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<td>3</td>
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For Police and Fire

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<th>Service Years</th>
<th>Multiplier</th>
<th>COLA</th>
<th>Pensionable Earnings</th>
<th>DROP</th>
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</tbody>
</table>

With these proposed changes to the pension plans, the City projects total savings of approximately $3.5 million annually. The proposals are subject to change, however, as negotiations with the unions continue.

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The City of Pembroke Pines undertook pension reforms in February 2010 when, as a result of negotiations with its employee unions, the defined benefit pension for the City’s General Employees became unavailable for new hires, retiree life insurance was no longer offered, and the annual pension COLA was decreased from 3 percent to 2 percent.

On July 1, 2010 the General Employees’ defined benefit plan was frozen, meaning that no additional benefits shall be accrued, for the approximately 268 current bargaining members, and base wages were reduced by 4 percent. Eliminated were longevity payments, annual COLA adjustments for bargaining members that retire after July 1, 2010, and the annual pensionable payout of excess unused sick time. All bargaining members that retire on or after that date have to pay the insurance equivalent (blended rate) to be covered under the retiree health insurance program. Sick time accruals cannot exceed a maximum of 120 hours and will not be paid out at termination.

The police pension was reformed by decreasing the benefit multiplier from 4 percent to 3.5 percent for any current member’s service time accrued after April 30, 2010. As of that date: the benefit multiplier for new hires decreased to 3 percent; the pension COLA changed from 3 percent to 2 percent per year, and for new hires the COLA was set at 1.5 percent; only accrued time earned before that date is included in the pension calculations, up to a maximum of 1,000 hours; the longevity pay percentage was frozen for current members; and a maximum of 300 hours of overtime may be included in pension calculations. Employees hired after October 1, 2006 have to pay the insurance equivalent (blended rate) to be covered under the retiree health insurance program.

The City’s Deferred Retirement Option Plan (DROP) enables employees to transfer accrued retirement benefits to a separate account on a deferred basis while remaining in the active employment of the City. Basically, employees’ credited service, accrued benefit, and average monthly earnings will be calculated as if employees had actually retired from service. For current police members, DROP funds will earn a minimum of 5 percent and up to 8 percent based on the pension fund gross rate of return, and new hires receive the actual market rate of return on DROP funds.

Under firefighter pension reforms, the pension COLA for current employees as of April 30, 2010 changed from 3 percent to 2 percent. The benefit multiplier changed as follows:

- For employees hired prior to June 18, 2003, service time accrued as of April 30, 2010 is calculated at 4 percent per year and for subsequent years it is calculated at 3.5 percent. Employees may remain active until such time that their creditable service would equal a multiplier of 80 percent.
- For employees hired on or after June 18, 2003, service time accrued as of April 30, 2010 is calculated at 4 percent per year and for subsequent years it is calculated at 3.5 percent.
- Employees are eligible to remain active until such time as the accumulated total multiplier under the new plan would equal the amount he/she would have received under the terms of the plan in effect on April 30, 2010.
Only accrued time earned as of April 30, 2010 is included in the pension calculations, up to a maximum of 1,000 hours. DROP funds earn a minimum of 5 percent and a maximum of 8 percent based on the pension fund gross annual rate of return.

For employees hired after April 30, 2010, the benefit multiplier is calculated at 3 percent for each year of service. No payment of accrued leave hours may be calculated towards the member’s pension. Members may elect to retire or enter DROP no earlier than completion of 20 years of service or attainment of age 50 with 10 years of service, and no later than attainment of 80 percent of their average monthly earnings of their highest two years regardless of age. A member’s eligibility to participate in DROP for the total of five years is reduced for any time served after reaching 80 percent. Participants receive only the actual market rate of return on DROP funds. The pension COLA is fixed at 1.5 percent. Longevity pay is frozen for any current member receiving it as of April 30, 2010, and no additional longevity pay is paid beyond that date.

Contact: René González, Finance Director, (954) 435-6515, rgonzalez@ppines.com
The City of Phoenix has a population of 1,445,632 served by approximately 15,000 City employees – 10.4 employees per 1,000 in population. As of June 30, 2011, 8,569 employees were members of the City of Phoenix Employees’ Retirement System (COPERS), a defined benefit plan with assets of $1.82 billion. Other City employees are covered by the Public Safety Personnel Retirement System (PSPRS) or the Elected Officials Retirement Program (EORP). PSPRS and EORP are administered by the State of Arizona.

Defined benefit pensions are commonly used in the public sector to help recruit and retain employees, with 23 or the 25 largest cities surveyed using them. Plans are typically financed as a partnership between employer and employee. Phoenix residents voted to establish such a pension system in the City Charter in 1947, and over the years voters have amended it 25 times. The Charter fixes a specific employee contribution rate at 5 percent, and the City must pay the remaining portion of the Actuarially Required Contribution (ARC). While the City is legally required to pay, and has always paid, the full amount required, the cost of doing so has risen significantly, from just under 7 percent of salary in Fiscal Year 2003 to more than 20 percent in Fiscal Year 2013. With pension costs increasingly competing with the costs of providing public services, one of the City’s goals was to reduce the impact of COPERS on the budget. Other goals included establishing a 50/50 partnership with employees through equal contributions, increasing the retirement age, and maintaining competitiveness in attracting and retaining high-performing employees.

The City of Phoenix Pension Reform Task Force, appointed by the Mayor and City Council in January 2011, worked with management, outside consultants, and other stakeholders to review the COPERS plan and recommend changes. 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. The Task Force held 13 meetings, all open to the public and offering public comment opportunities, between February and its sunset on December 31, 2011.

An actuarial consultant worked with the Task Force to evaluate the financial impact of possible changes to plan provisions and alternative strategies for COPERS, and to assess the financial impact of changes by the State Legislature to the elected officials and public safety plans. The Task Force completed a comprehensive review of information on the COPERS system as well as private sector retirement plans, and directed the consultant team to prepare a survey of 10 similarly sized and geographically diverse pension plans. Among many other considerations, the Task Force focused on limiting growth in the City's liability, sharing more of the plan risk with employees, and examining eligibility for, and the level of, retirement benefits. Following a goal-setting process facilitated by the actuarial consultant, the Task Force requested and reviewed 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. The Task Force also examined the impact of freezing the plan to new entrants and implementing a defined contribution plan for new employees.
A legal consultant was retained by the City to advise the Task Force, Mayor, and Council on the legal issues related to the pension system and potential reforms. Major legal considerations include a provision in the Arizona constitution relating to public pension programs and provisions in the City Charter relating to COPERS.

On December 6, 2011, the Task Force concluded its work on recommendations pertaining to new hires as well as existing employees – recommendations that included maintaining a defined benefit pension plan with reforms such as increasing the retirement age, establishing a 50/50 split of pension costs between the City and the employee, and others that make the system competitive with the Arizona State Retirement System (ASRS). The Task Force recommended against moving to a defined contribution plan. On February 14, 2012, following a thorough review of the plan and actuarial and legal analysis, Task Force recommendations were presented to the City Council.

In May 2012, the resolution of a Maricopa County Superior Court judgment against the State of Arizona for changing contribution rates for existing employees made clear that the reforms recommended by the Task Force, if applied to current employees, might not be sustainable legally. On June 9, staff returned to the Council with an update and potential options for pension reform. On June 19, the Council adopted a pension reform timeline and directed staff to conduct an actuarial analysis of three reform models which apply only to new employees.

Residents were invited to attend and offer feedback on the COPERS pension reform process at two community meetings held in September 2012. Feedback submitted electronically was also recorded and provided to the Mayor and Council.

On September 25, staff presented the City Council with the actuarial analysis of proposed pension reform alternatives for COPERS it had requested. At that time, staff requested Council direction to draft proposed revisions to the City Charter pension language for referral to the March 2013 ballot. Staff recommended reforming the pension system for new hires only as follows:

- Change Rule of 80 provision to Rule of 87. Rule of 80 is an age-plus-service retirement eligibility trigger (i.e., employees age 55 with 25 years of service can retire). Normal retirement ages are 60 with 10 or more years of service and 62 with five or more years of service. Average retirement age is around 58.
- Change the pension multiplier to a graduated multiplier based on years of service, matching the Arizona State Retirement System (ASRS) schedule.
- Increase time of service requirements and eliminate minimum pensions as recommended by the Pension Reform Task Force.
- Base employee contribution rate on 50/50 split of actuarially determined rate.
- Allow new City hires with service on account with ASRS prior to July 1, 2011 to join COPERS under current provisions.

With these changes, the City’s contribution rate was projected to decrease by 51 percent; it was estimated that this would yield approximately $596 million in cumulative savings by 2037. The highest employee contribution rate under this scenario was projected to be 13.6 percent of salary.
Staff also noted at the time that the Governmental Accounting Standards Board (GASB) had recently approved new accounting and reporting standards for pensions provided through state and local governments, many of which will become effective for plan fiscal years beginning after June 15, 2013. The new standards make significant changes to pension accounting and reporting, and the impacts of the new GASB changes have not yet been determined.

The COPERS Board also recommended that two additional Charter revisions be referred to the ballot: The first involved removing some investment limitations from the Charter in order to provide the opportunity to maximize investment returns for the Plan. The second involved putting into the Charter certain IRS-required operational and documentation provisions that are current practice, but should be placed into Charter, since the COPERS operates as a tax-qualified retirement plan.

Finally, at the time, the City Charter required the City to contribute the full Actuarially Required Contribution (ARC) each year, to ensure the financial integrity and stability of COPERS. Because the Charter did not allow for the City to contribute more than the ARC each year – an option that could be fiscally advantageous to the City in some years – staff recommended including language in the Charter that would allow for this.

The City Council approved referral to the ballot of these items, and they were approved overwhelmingly by the voters on March 12. They will be implemented in July.

The Phoenix pension reform agendas, minutes, reports, and consultant analyses are available to the public at phoenix.gov/pensionreform.

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REDMOND, WASHINGTON
Mayor John Marchione

All but three cities in Washington participate in the State’s Department of Retirement System’s plans. Officials believe the state-wide public pension systems in Washington follow best practices for public pensions with relatively strong funding ratios. The employees have a high degree of confidence that the plans will pay them the promised benefits, and the plans have evolved ahead of national trends.

The current plan, known as Plan 3, is a hybrid defined benefit and contribution based plan. The State has done a good job of keeping the plans current from a design standpoint, officials say, and largely has not pursued the various fads that have created problems for pension systems in other parts of the country. As a result of contemporary design and fiscal support, Washington’s plans have been funded in the 90-plus percent range, with some funded at or above 100 percent.

Despite their assessment of State plans as being generally well managed, Redmond officials say that, as a participant, the City has encountered problems.

- **Fluctuations in funding strategy based on the State’s financial condition.** In Washington’s combined plan, the contribution rates are the same for both State and local governments. When the State is having financial difficulties, it may lower the funding contribution commitment made to the plans, and this creates a temporary windfall for the local governments that participate. But when the State is in a position to increase contributions and restore past funding shortfalls, contribution rates for cities are pushed up as well. This was especially challenging in the 2006-2007 period. Cities’ financial recovery lagged that of the State and so cities were unprepared to increase their contributions to keep pace with State. The situation placed significant and arbitrary budget pressures on city governments.

- **Lack of involvement in pension plan decisions.** The Department of Retirement Systems often makes decisions without consulting or considering the implications for local government employers. These may be administrative or funding decisions, or involve day-to-day management of the many business issues that are involved in this large and complicated enterprise, but they often pit the cities against an administrator within the State agency. An example is seen in the method the State created to manage pension system “credits” for employees. The reporting requirements were onerous and inconsistent with best practices within city governments. As cities struggled with compliance, however, the DRS response was to levy fines rather than work to align State and city systems and needs.

- **Inconsistencies in the State’s plan design and cities’ practical needs.** The “one size fits all” approach of the state-wide system has many benefits, but one of the drawbacks is that its laws and regulations do not allow for differences among the participating cities. For example, Redmond has an “Other Post Employment Benefit” liability but a surplus in its pre-state pension system, which dates back to workers hired prior to 1971. This surplus is growing, as it has a dedicated revenue source set by statute, but due to limitations in
State law, the City is unable to use it to meet the OPEB obligations. The concern is that, when this law comes up for discussion, the natural tendency will be for potential beneficiaries to want to claim the surplus rather than allowing the City to apply it to the unfunded OPEB.

Redmond and other Washington cities have worked with both State administrators and legislators to resolve these issues. These efforts are often challenged by labor unions – a strong presence in Washington – which view many of the reform proposals advanced by cities as threats to gains that have been made on behalf of workers. As a result, the gains that have been made are generally in areas that don’t directly affect benefits – for example, investment oversight and the leveraging of existing resources in one area to fill gaps in another – or relate to benefits that apply only to future employees, such as new hybrid plans.

City efforts to counter labor’s strong resistance to their pension reform strategies have taken the form of an education campaign targeting organized labor, the State’s legislators, and the public in general.

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SAN JOSE, CALIFORNIA
Mayor Chuck Reed

Starting in FY 2001-02, the City of San Jose experienced 10 straight years of budget deficits, which forced City leaders to dramatically reduce all services, including public safety, and eliminate 2,000 positions from its workforce. The main driver of these deficits was skyrocketing employee retirement costs, which grew from $73 million in FY 2001-02 to $245 million in FY 2011-12. Retirement contributions now cost more than 50 percent of payroll and consume more than 20 percent of the City’s General Fund. San Jose’s two independent retirement systems report close to $3 billion in unfunded liabilities for pension and retiree healthcare benefits.

In 2011, Mayor Reed and the City Council began pursuing a set of retirement reforms and spent more than eight months in negotiations with City employee unions. No agreement was reached, but a number of changes to the proposed reforms were made in the process. The City Council ultimately placed its revised pension reform proposal on the June 2012 ballot, where it was approved with nearly 70 percent of the vote. As a result of these reforms:

- New employees are being placed in a new, lower-cost pension plan.
  - New employees pay 50 percent of the total cost (normal cost and unfunded liability).
  - Normal retirement age is 60 for public safety, 65 for all others.
  - Accrual rate is 2 percent of salary per year of service, with a 65 percent maximum benefit.
  - Benefit is based on the highest average salary over a three-year period.
  - COLA is based on CPI, capped at 1.5 percent per year.
  - Optional defined contribution plan offers no City match at this time.

- Existing employees will be given the option to either pay more to keep their current plan or move to a lower-cost plan for their future years of service.
  - Under Option 1, employees contribute an additional 4 percent of their salary per year until they are paying for one-half of the cost of the plan’s unfunded liabilities or reach a cap of 16 percent.
  - Under Option 2, employees switch to a lower-cost plan for their remaining years on the job.
    - Retirement age is 57 for public safety, 62 for all others, phased in over 14 years.
    - Accrual rate is 2 percent of salary per year for future years of service.
    - Benefit is based on the highest average salary over a three-year period.
    - COLA is based on CPI, capped at 1.5 percent per year.

- The City Council can temporarily suspend retiree COLAs during a fiscal emergency.
• The retirement systems can no longer issue supplemental pension payments (‘13th check’) to retirees when investment returns exceed assumptions.
• Retirement benefits cannot be enhanced in the future without voter approval.

While the City has begun the process of implementing these reforms, the City’s employee unions have filed a number of lawsuits seeking to block the reforms. A trial is scheduled for July 2013.

San Jose has also applied for an Internal Revenue Service ruling on its provision that allows current employees to choose a lower-cost plan in lieu of higher pension contributions. The IRS has not issued private letter rulings on optional plans since 2006; San Jose is seeking support from other cities and states to encourage the IRS to issue guidance on providing employees a lower-cost pension option.

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SPRINGFIELD, ILLINOIS
Mayor J. Michael Houston

Springfield finds it increasingly difficult to meet the financial demands of its three separate pension plans – in particular, the two covering police and fire employees – and it has little control over the needed reform of these plans. Through the Illinois Pension Code, the Illinois legislature maintains oversight of public pensions within the State, including those at the municipal level, and any true reform with regard to benefits, contributions, retirement age, or other elements must come from the legislature.

According to the most recent actuarial examinations, Springfield’s fire and police pensions are funded at only 45.8 percent and 54 percent, respectively. The combination of past pension sweeteners, lower than expected returns, and other forces have resulted in exponential growth in the City’s required pension contributions. Police and fire contributions have gone from approximately $6 million in fiscal 2002 to roughly $18 million in the current fiscal year. The current budget shows the City contributing over 61 percent of the firefighter payroll and approximately 46 percent of the police officer payroll to their respective pension funds, which have combined assets of approximately $210 million.

Recognizing that pensions were becoming a heavy burden for both State and local governments, the legislature enacted pension reform in the midst of the “Great Recession,” creating a “Tier II” system for new employees which went into effect on January 1, 2011. Under this new system, police and fire employees hired after this date are enrolled in plans having higher retirement ages, less generous COLAs, payments of 75 percent of salary based on a 96-month average salary rather than final salary, a smaller Joint and Survivor Annuity benefit, and other features designed to lower pension costs. Tier II plans for other municipal employees require, for example, more years to vest and higher normal retirement and early retirement ages. Mayor Houston recognizes that while the legislature is responsible for producing this pension reform, it’s also responsible for contributing to the problem in the first place by adding generous “pension sweeteners” over many years.

The Mayor says his administration has taken a proactive approach in working within the limitations of the State system to mitigate the growing budgetary demand of pension obligations. The City’s three-prong approach includes making additional pension payments when possible, lowering personnel costs, and working with the Illinois Municipal League and other Illinois mayors to press the legislature for further reform.

The City has succeeded in cutting costs and generating multi-million-dollar surpluses over the past few years. At the end of the most recent fiscal year, the Mayor requested and received authority from the City Council to use $1 million of available surplus to make an extra $500,000 payment to each of the City’s police and fire pension funds. The intent is to ramp up funding whenever possible in order to take advantage of potential returns from recovering market conditions.

Because governmental pension obligations increase with every dollar paid out in salaries, Springfield is reducing headcount wherever and whenever possible. Since taking office, the
Mayor has removed over 100 positions from City government and continues to look for opportunities for more reductions. When a worker leaves City employment, a thorough examination is conducted to determine whether maintaining the vacated job is absolutely necessary. Cutting positions results in lower future pension obligations while freeing up dollars that can be used to meet existing contribution obligations.

Another avenue being pursued in Springfield involves salary enhancements reached in the collective bargaining process. For the City’s 23 separate collective bargaining contracts, it has become common practice to aggressively pursue raises that are in line with, rather than above, the Consumer Price Index. The effort has been successful and is showing immediate results. Contracts that previously had 3 percent to 4 percent annual raises are receiving a 2.1 percent increase in the current fiscal year because they are tied to the CPI. The City also has been working to reduce and/or remove end-of-career pension boosters from union contracts. As with employee reductions, this results in lower future pension obligations as well as dollars to relieve current pension payment pressures.

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WESTLAND, MICHIGAN
Mayor William Wild

The City of Westland has undertaken several efforts to better manage its financial obligations in providing retirement benefits to its 280-plus employees who are enrolled in State or local pension plans with pension multipliers ranging from 2.25 percent to 2.8 percent. Pension reform in Westland has included employee cost-sharing, less generous benefit plans for new hires, and the elimination of certain allowances from the retirement benefit calculation.

Westland’s central problem includes financing its current Actuarially Required Contribution (ARC) and meeting, on the longer term, continued increases in pension costs produced by a decline in investment earnings and an increase in the number of retirees drawing a pension. This situation has resulted in the pension plans receiving less funding than in the past and has necessitated a corresponding increase in the ARC. The City’s police and fire retirement plan is funded through a property tax millage assessment; meeting the plan’s annual costs required City officials to increase this tax levy.

City officials including the Mayor, Finance Director, Budget Director, and Personnel Director have worked closely with union negotiators to address the pension challenges. Most recently, 5 percent pre-tax contributions toward pensions were imposed on the Mayor, all Mayoral appointees, and other non-union staff – approximately 30 employees. The City also negotiated a similar 5 percent pre-tax contribution to the pensions of the 59 employees in its AFSCME unit. Including the 40 new hires in the police and fire ranks since 2007, the City now has nearly half of its full-time employees contributing 5 percent toward their pensions – and offsetting the City’s ARC.

In some employee groups, new hires will be placed in defined benefit plans with lower multipliers (1.5 percent) or defined contribution plans to which the City will contribute 10 percent. In the police and fire units, a number of allowances that were previously included in the Final Average Compensation (FAC) calculation are no longer included, thus reducing the FAC amount on which pension payments are based.

The City continues to seek similar cost-sharing among the remaining employee groups, including police and fire employees hired prior to 2007, and among its supervisory and union court employees, and less costly retirement plans for new hires to these bargaining groups.

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FUTURE PENSION REPORTING

Governmental Accounting Standards Board

Future reporting on public employee pension plan finances by both local and state governments will be shaped by two new standards approved in June 2012 by the Governmental Accounting Standards Board (GASB). The guidance contained in these Statements, the organization says, “will change how governments calculate and report the costs and obligations associated with pensions in important ways. It is designed to improve the decision-usefulness of reported pension information and to increase the transparency, consistency, and comparability of pension information across governments.”

As described by GASB:

- Statement 67 is effective for financial statements for periods beginning after June 15, 2013. The Statement revises and establishes new financial reporting requirements for most governments that provide their employees with pension benefits. It builds upon the existing framework for financial reports of defined benefit pension plans, which includes a statement of fiduciary net position (the amount held in a trust for paying retirement benefits) and a statement of changes in fiduciary net position. It enhances note disclosures and Required Supplementary Information (RSI) for both defined benefit and defined contribution pension plans and also requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in 10-year RSI schedules.
- Statement 68 is effective for fiscal years beginning after June 15, 2014. The Statement relates to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. It requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and RSI.

Moody’s Investor Service

In April, Moody’s published a report describing its new approach to adjusting pension assets and liabilities reported by states and local governments for the purpose of its independent credit analysis. The organization says that the new adjustments are part of its “ongoing efforts to bring greater transparency and consistency to the analysis of pension liabilities, which have increased in size across the public sector in the past decade and driven credit rating downgrades and outlook changes for a number of states and local governments in recent years.”

Four principal adjustments to as-reported pension plan data will be made:

- Multiple-employer cost-sharing plan liabilities will be allocated to specific government employers based on proportionate shares of total plan contributions.
• Accrued actuarial liabilities will be adjusted based on a high-grade long-term taxable bond index discount rate as of the date of valuation.
• Asset smoothing will be replaced with reported market or fair value as of the actuarial reporting date.
• The resulting adjusted net pension liability (i.e., adjusted liabilities less assets) will be amortized over 20 years using a level-dollar method to create a measure of annual burden related to the net pension liability.

Moody’s says that, with the implementation of this methodology, “less than 2 percent of the total population of general obligation (GO) and equivalent and related ratings will be placed under review for possible downgrade. As pensions are just one of many factors we consider in a rating, any downgrades resulting from the subsequent reviews are likely to be limited to two notches.”

The company will publish adjusted pension statistics for individual state governments and the largest local governments on an annual basis. For individual local governments, adjusted statistics will be incorporated in specific reports on such issuers, “typically at the time of a new bond sale, rating or outlook change, or other occasion prompting a specific issuer report.”

Moody’s estimates that, based on its new adjustments, total state pension liability in FY 2011 would be $1.91 trillion – a significant increase over the $1.45 trillion that had been reported. Applied to state and local pension systems, large increases in liability would translate into much lower funding ratios and, it follows, much greater pressure on governments to increase contributions.

When Moody’s adjustments to pension liabilities were originally proposed last year, the Government Finance Officers Association (GFOA) said it had no choice but to oppose them on several grounds. The organization urged Moody’s to “wait until the GASB changes have been implemented before developing yet another methodology for measuring pension liabilities and expenses.” The National Association of State Auditors, Comptrollers and Treasurers also opposed Moody’s plan, their primary concern being the confusion it would produce, “especially given the recent passage of the two new pension standards released in June” by GASB.

The adjustments announced in April indicate that, following a comment period on Moody’s proposed adjustments, which ended last September, few changes were made to the original proposal.