CITY COUNCIL AGENDA ITEM

DATE: May 10, 2011

TO: The Honorable Mayor and City Council Members

FROM: John Szerlag, City Manager
John M. Lamerato, Assistant City Manager/Finance & Administration
Peggy E. Sears, Human Resources Director

SUBJECT: **AGENDA ITEM** – Contract Ratification - Michigan Association of Police (MAP) 2010-2013 and Early Retirement Incentive Program

RECOMMENDATION

City management supports and recommends approval of the tentative agreement between the City of Troy and the Michigan Association of Police (MAP) for a three-year successor collective bargaining agreement that will replace the contract that expired June 30, 2010. City management further supports and recommends approval to offer the Early Retirement Incentive Program (ERIP) to MAP employees.

BACKGROUND

On May 5, 2011, the Michigan Association of Police (representing the City of Troy Clerical and Non-Sworn Police Personnel) ratified a tentative agreement between the City of Troy and MAP for a three-year successor collective bargaining agreement that will replace the contract that expired June 30, 2010. As directed by City Council, this agreement achieves a 10% savings calculated on payroll costs which include base pay, pension, workers compensation and FICA.

This tentative agreement incorporates cost-saving changes to health insurance, a pay reduction achieved through the loss of holiday time, a significant reduction in the City's cost of pension plans, elimination of longevity pay for all MAP members who had been previously eligible to receive it, and elimination of the tuition reimbursement program. This agreement provides for greater flexibility in the use of part-time staff thereby reducing overtime costs, and reduces training and overtime costs associated with shift selection in Communications.

The last component of the tentative agreement is the offering of an Early Retirement Incentive Program (ERIP). A description of the program recommended by city administration and the actuarial valuation are attached. The proposed program is consistent with the ERIP previously offered to the TFSOA and Classified and Exempt employees. Two options would be offered: a cash incentive of $1,000 per complete year of credited retirement service with the City of Troy, or the option to convert from a Defined Contribution Pension Plan to a Defined Benefit Pension Plan. This Early Retirement Incentive Program must be cost neutral. The DC to DB Program would be funded directly from the members' DC accounts. The cost associated with the cash incentive program will be covered by the department.

A summary of the tentative agreement and the resultant savings calculation are attached.

Attachments

PROPOSED AGREEMENT SUMMARY
City of Troy and MAP
2010-2013 Collective Bargaining Agreement

ISSUE	SOLUTION
Duration	Three year contract
Pay Reduction	Pay reduced 2.5% by the equivalent of a loss of 52 hours of holiday leave
Health Insurance	a. Blue Cross PPO replaced with Blue Cross Community Blue Plan 1 (Modified): 1. $10/$40 prescription drug rider (PDR) replaces $5/$10 PDR for generic/brand name drugs, including with mandatory generic, prior authorization, step therapy and 2X MOPD (co-pay for mail order prescription drugs increased to a two-month copay for a 3 month supply) 2. $30 office visit (OV) copay and $30 chiropractic office visit (COV) copay 3. $50 emergency room (ER) copay (waived if admitted) 4. $250/$500 basic deductible b. Current HMOs modified to include $10/$40 drug rider with mandatory generic, prior authorization, step therapy, 2X MOPD; $30 OV copay, $50 ER copay (waived if admitted) c. Employee co-pay for health insurance premium changed from flat amount to 3.0% of total premium cost d. Amount of cash-in-lieu payments for those opting out of city health insurance reduced for all employees to $200/month. (Previously equivalent to single premium rate for employees opting out prior to 10/13/04; $250 for employees opting out after 10/13/04.)
Retirement	a. For employees participating in the defined benefit pension plan, employee contribution increased by 3.0% b. For employees participating in the defined contribution pension plan, employer contribution decreased by 3.0%
Longevity	Eliminated
Tuition Reimbursement	Eliminated
Miscellaneous:	a. Job and shift selection process modified to reduce potential for overtime and training costs associated with maintaining trained and qualified personnel in Communications and Lock-up Sections b. Early Retirement incentive Plan (ERIP) to be offered to MAP members c. Obtained ability to supplement full-time workforce with part-time employees during periods of time the City provides dispatch or lock-up services to communities in addition to Troy and Clawson d. Modified conditions under which personal business time is approved to improve management of work schedules e. Streamlined layoff process and obtained ability to retain part-time positions in City Clerk's office during periods of layoffs in that department.

MAP NEGOTIATIONS - Contract Expiring 6/30/2010
PROPOSED SETTLEMENT SAVINGS
(As % of Payroll)

ISSUE	ANNUAL SAVINGS	
Equivalent of 2.5% Reduction in Pay and 3.0% Reduction in Employer Cost of Pension	$109,260	
Replace PPO Health Insur. w/Community Blue Plan I Modified	$130,246	
Eliminate All Remaining Longevity	$18,480	
Total Annual Savings	$257,986	
Savings as Percent of Base Pay + Rollups [Pension, Work. Comp., FICA] ($2,563,876)		10.06%
Savings as Percent of Base Pay Only ($2,071,626)		12.45%

EARLY RETIREMENT INCENTIVE PROGRAM 2011
MAP Employees

PROGRAM DESCRIPTION:

The City of Troy is implementing an Early Retirement Incentive Program (ERIP) in the form of two options, a cash incentive or a DC to DB conversion, in order to reduce personnel costs to accommodate budget constraints. The Program is being offered to eligible employees if the employee signs a Letter of Understanding with the City of Troy and, in the case of a union employee, that union agrees to the terms and conditions of the Program. Participation in the Program is entirely voluntary. Interested eligible employees in either the DB Pension Plan or the DC Pension Plan may elect to participate, but can only select one of the available options. Participating employees must retire on or before the date specified in the Plan.

INCENTIVE OPTIONS:

Cash Incentive
Eligible employees in either the Defined Benefit or Defined Contribution Pension Plan may elect to receive a cash incentive that is equal to $1,000 for each actual complete year of credited service with the City of Troy as of February 28, 2011. The cash incentive will be issued not later than three weeks after the employees' designated retirement date. The number of years for which the cash incentive is made shall not include years of service granted for prior government service from an employer other than the City of Troy.

For those employees participating in the Defined Benefit Pension Plan, the incentive will not be included in any computation of Final Average Compensation (FAC) under any provisions of the Retirement System. Both the City and the employee will make the required contributions to the plan.

For those employees participating in the Defined Contribution Pension Plan, the employee and the City of Troy will each contribute their appropriate percentage to the plan.

DC to DB Conversion
Eligible employees in the Defined Contribution Pension Plan may elect to transfer their total accumulated balance (including all employee contributions and interest thereon) to the City of Troy Employees Retirement System-Defined Benefit Plan. Their pension will be based solely on the value of their accumulated DC account balance at the date of transfer as determined by the Retirement System's actuary.

GENERAL CONDITIONS:

Employees who are eligible to participate in the Early Retirement Incentive Program will be sent notification following approval of the program by City Council. The notice will include the Early Retirement Incentive Program Voluntary Resignation Agreement and Release of Claims form, a Receipt form and a Waiver of Review Period form. Employees will have a minimum of 45 days in which to consider the Release in order to seek counsel regarding their rights. If the employee chooses to waive the 45-day review period, he/she must submit the signed Waiver. Employees who elect to participate in the Program must submit the signed Release not later than the end of the window period and will have seven (7) days after signing to revoke their decision. Retirement dates are subject to approval, and retirement must occur not later than August 12, 2011.

ELIGIBILITY REQUIREMENTS:

The Program will be available to MAP employees who meet the age and service requirements for normal or early retirement as of February 28, 2011, or are within five years of eligibility, as defined by the Employee Retirement System Ordinance or by the respective collective bargaining agreement. These eligibility requirements are as follows:

GROUP A
Regular Retirement

Age 50 with 27 years of service; or
Age 55 with 25 years of service; or
Age 60 with 10 years of service

Early Retirement
Age 55 with 10 years of service

GROUP B
Those within five (5) years of eligibility as stated above

EFFECTIVE DATES:

Window Period (45-days minimum):	May 17, 2011 through July 1, 2011
Revocation Period Ends (7 days):	July 8, 2011
Retirement Not Later Than:	August 12, 2011

GRS
Gabriel Roeder Smith & Company
Consultants & Actuaries
One Towne Square
Suite 800
Southfield, MI 48076-3723
248.799.9000 phone
248.799.9020 fax
www.gabrielroeder.com

January 21, 2011

CONFIDENTIAL

Mr. John Lamerato
Assistant City Manager - Finance
City of Troy
500 West Big Beaver Road
Troy, Michigan 48084

Re: A Supplemental Valuation of the Effect of a Proposed Early Retirement Incentive Plan (ERIP) for the City of Troy-MAP Union

This report presents the results of a supplemental valuation of the potential impact of a proposed Early Retirement Incentive Plan on the City of Troy Employees Retirement System (ERS) and Retiree Health Plan. A summary of the Early Retirement Incentive Plan provisions is shown on the following page.

Except where indicated, this valuation was based on the actuarial assumptions and methods used in the most recent ERS and Other Postemployment Benefits annual actuarial valuations.

Both of the undersigned are Members of the American Academy of Actuaries (MAAA) and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Sincerely,

Brad Armstrong, ASA, MAAA

Randall J. Dziubek, ASA, MAAA

BLA/RJD:lr
Enclosures

City of Troy Employees Retirement System (ERS)-MAP Union Early Retirement Incentive Plan (ERIP) Proposed Provisions

ERIP

Eligibility: Member is eligible or within five years of eligibility for regular or early retirement as of December 31, 2010. Members of both the ERS and the Defined Contribution Plan (DC) are eligible for the ERIP.

Benefits provided by the ERIP:

- ERS Members – Immediate commencement of unreduced retirement benefit based on accrued service as of December 31, 2010.
- ERS and DC Members - Immediate commencement of retiree health benefits based on accrued service as of December 31, 2010.
- ERS and DC Members – All eligible members as of December 31, 2010 will receive a lump sum payment of $1,000 for each complete year of service as of the same date. These lump sums will not be funded by the Retirement System. In the case of DC members, the eligibility for the lump sum is contingent on not converting their DC balance to a DB annuity under the Retirement System.

CITY OF TROY EMPLOYEES RETIREMENT SYSTEM (ERS)-MAP UNION EARLY RETIREMENT INCENTIVE PLAN (ERIP) PROPOSED PROVISIONS

DATA PROVIDED TO THE ACTUARY: The City provided a listing of all of the active members that are believed to be eligible for the ERIP. The listing was reviewed for reasonableness, but was not audited by the actuary. The listing contained credited service projected to December 31, 2010.

A summary of individuals deemed eligible for the ERIP and included in this report is shown below:

	Data as of December 31, 2010				
	Number	Total	Average	Average Service	
Group	Count	Annual Payroll	Age	Benefit	Eligibility
ERS					
NR Eligible	4	$ 190,439	60.4 yrs.	18.0 yrs.	18.0 yrs.
ER Eligible	1	62,293	58.3	22.3	22.3
Eligible within 5 yrs.	6	321,996	50.7	20.2	20.2
Total ERS	11	$ 574,728	54.9 yrs.	19.6 yrs.	19.6 yrs.
DC Plan					
NR Eligible	1	$ 43,846	48.3 yrs.	10.7 yrs.	10.7 yrs.
ER Eligible	2	94,723	53.5	19.8	19.8
Eligible within 5 yrs.	5	214,183	56.2	7.9	7.9
Total DC Plan	8	$ 352,752	54.5 yrs.	11.2 yrs.	11.2 yrs.

The estimated impact of the proposed ERIP as of December 31, 2010 is shown below, assuming 100% of eligible members retire. The “Retiree Health” results represent the impact of immediate retirement for both ERS and DC Plan members.

Annual contribution results shown below were determined by amortizing the increase in the present value of benefits over a five-year period as a level percent of pay. These contribution results are not the expected increases in the Annual Required Contributions (ARC) that will be determined in the actuarial valuations following the ERIP, but are a good representation of the expected overall costs of the ERIP if paid off over a five-year period.

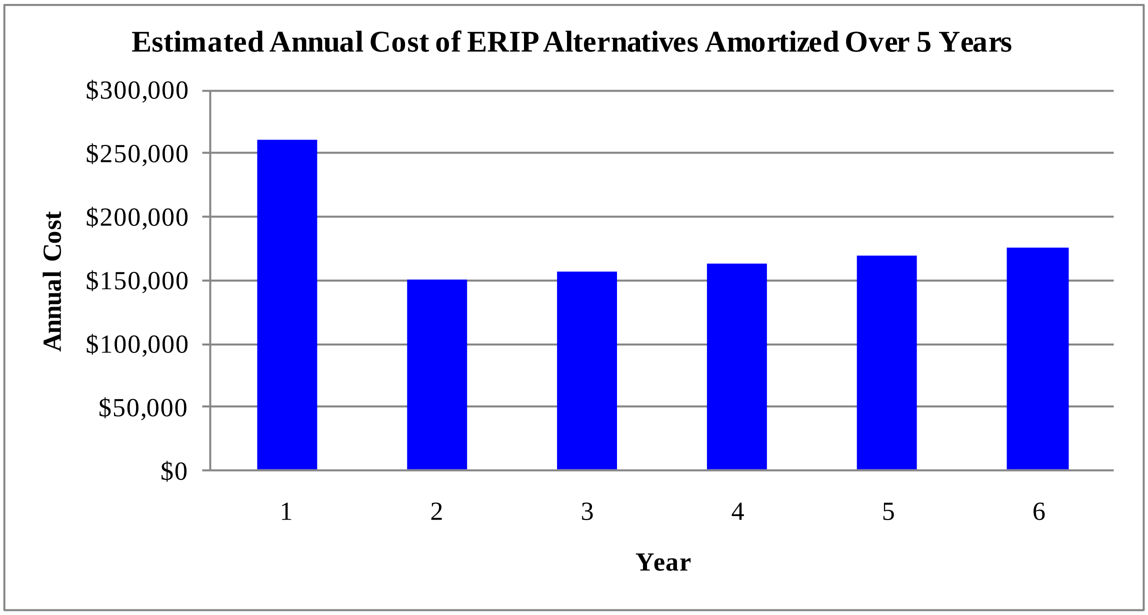
	Increase in Present Value (PV) of Projected Benefits	Annual Contribution Required to Amortize PV Increase Over 5 Years
Pension	$ 180,403	$ 39,386
Retiree Health	454,554	99,239
Sub-Total	$ 634,957	$ 138,625
$1,000 x Service *	261,500	NA
Total	$ 896,457	$ 138,625
Reduced Member DB Contributions	$ 53,105	$ 11,594
Increased Benefits Plus Reduced Member DB Contributions	$ 949,562	$ 150,219

* *The $1,000 x Service amounts shown above are based on accrued service as of December 31, 2010. These lump sum payments will not be funded by the Retirement System. The cost to amortize over 5 years is not shown since it is assumed these payments will be made immediately following the retirement of participating members.*

Increase in Annual Required Contribution (ARC) for Retiree Health Benefits

The Annual Required Contribution for retiree health benefits is currently based on the Entry-Age Normal (EAN) actuarial cost method. The expected increase in the actuarial accrued liability (AAL) under the EAN cost method due to the proposed ERIP is $903,017. Under current methods, 30-year amortization of the increase in the AAL under the EAN cost method will be included in the calculation of the ARC in the valuation following the ERIP.

The chart below illustrates the total expected cost of the additional pension and retiree health benefits provided under the ERIP alternatives if spread over a five year period. These results do not reflect the potential savings associated with the ERIP due to decreased payroll and fringe benefit costs and other factors. For an overall measure of the estimated cost/savings associated with the ERIP, the costs shown below should be combined with any expected savings due to decreased payroll and other factors. If the expected savings due to these factors over the next five years is equal to the costs shown below, the ERIP can be considered cost neutral to the City.



The estimated cost of the $1,000 x service benefit is shown in Year 1. The 5-year amortization of additional costs under the ERIP is shown in Years 2-6. Year 1 represents the fiscal year ending June 30, 2011. We assumed that 50% of the eligible DC Plan members will elect to convert their DC balance to a DB annuity under the Retirement System thereby forgoing any lump sum payment.

It is likely that less than 100% of eligible members will choose to retire under this ERIP. In the table below, we show the estimated increase in the present value of benefits and the 5-year amortization payment of these increases based on various election percentages (please refer to Comment 4 on page 6).

	Percentage of Eligible Members Assumed to Retire Under the Program			
	100%	**50%**	**20%**	**10%**
Number Assumed to Retire from ERS	11	6	2	1
Number Assumed to Retire from DC Plan	8	4	2	1
Increase in PV of Benefits Plus Reduced Member DB Contributions				
Pension	$ 180,403	$ 90,202	$ 36,081	$ 18,040
Retiree Health	454,554	227,277	90,911	45,455
$1,000 x Service	261,500	130,750	52,300	26,150
Reduced Member DB Contributions	53,105	26,553	10,621	5,311
Total	$ 949,562	$ 474,782	$ 189,913	$ 94,956
5-Year Amortization of Above (In addition to One-Time Cost of $1,000 x Service)				
Pension	$ 39,386	$ 19,693	$ 7,877	$ 3,939
Retiree Health	99,239	49,620	19,848	9,924
Reduced Member DB Contributions	11,594	5,797	2,319	1,159
Total	$ 150,219	$ 75,110	$ 30,044	$ 15,022

Please see the Comments on pages 6 and 7 for important information essential to understanding this report.

COMMENTS

Comment 1: This report is based on an assumption that individuals reported by the City as eligible for the ERIP, elect the ERIP and then retire on December 31, 2010. Data used for this report was based on the data provided by the City regarding eligible members, service as of December 31, 2010. Pay data provided for the December 31, 2009 annual actuarial valuation of the ERS was used to estimate pensionable earnings at retirement.

Comment 2: This report is based on the data and assumptions noted above and the proposed ERIP provisions shown on page 1. If you have reason to believe that the assumptions that were used are unreasonable, that the plan provisions are incorrectly described, that important and relevant plan provisions are not described, or that conditions have changed since the calculations were made, you should contact the author of this report prior to relying on information in the report.

Comment 3: This report shows the potential impact of the proposed ERIP on ERS pension and retiree health care costs as of December 31, 2010. The non-retirement costs/savings in other areas (payroll savings, fringe benefit savings, employer contributions to new hire defined contribution accounts, etc.) are not included in this report.

Comment 4: The cost of the proposed ERIP has been developed assuming that all of the individuals shown in this report are eligible for the ERIP and will elect to retire on December 31, 2010. Please be aware that the cost of the ERIP will vary for each individual member. For example, if half of the eligible employees elect to retire, and these employees are the ones who would benefit most from the incentive, the cost would be more than 50% of the maximum (100% retire) cost shown in this report. In other words, in the examples of 50%, 20%, and 10% election percentages on page 3, the cost would be increased if the employees electing to retire are the employees who would benefit most from the proposal.

Comment 5: The Government Finance Officers Association (GFOA) recommended practice for evaluating the use of early retirement incentives has been included in the Appendix of this report. The GFOA recommends the use of a short amortization period (such as 3-5 years) to finance the incremental cost of an early retirement incentive plan. Since savings are typically realized over a short period, the costs should also be recognized over a similar period. Regardless of the time period selected for funding, we recommend that policy makers carefully consider the 5 year results shown in this correspondence in the decision making process.

Comment 6: The calculations are based upon assumptions regarding future events, which may or may not materialize. They are also based upon present and proposed plan provisions that are outlined in the report. If you have reason to believe that the assumptions that were used are unreasonable, that the plan provisions are incorrectly described, that important plan provisions relevant to this proposal are not described, or that conditions have changed since the calculations were made, you should contact the authors of this report prior to relying on information in the report.

Comment 7: If you have reason to believe that the information provided in this report is inaccurate, or is in any way incomplete, or if you need further information in order to make an informed decision on the subject matter of this report, please contact the authors of the report prior to making such decision.

Comment 8: No statement in this report is intended to be interpreted as a recommendation in favor of the changes, or in opposition to them.

Comment 9: This report is intended to describe the financial effect of the proposed plan changes on the retirement system. Except as otherwise noted, potential effects on other benefit plans were not considered.

Comment 10: The reader of this report should keep in mind that actuarial calculations are mathematical estimates based on current data and assumptions about future events (which may or may not materialize). Please note that actuarial calculations can and do vary from one valuation year to the next, sometimes significantly if the group valued is very small (less than 30 lives). As a result, the cost impact of a benefit change may fluctuate over time, as the demographics of the group changes.

APPENDIX

GFOA Recommended Practice

Evaluating Use of Early Retirement Incentives - 2004

Background. Governments occasionally offer early retirement incentives (ERIs)[1] to employees as a strategy to reduce payroll costs or stimulate short-term turnover among staff. ERIs are temporary, offered during a window that usually covers a period of months. They increase the economic value of the standard retirement benefit. Historically, ERIs rarely have succeeded, since costs are often greater than initially anticipated by the government offering the incentive, and savings are lower than projected.

Recommendation. GFOA recommends that governments exercise extreme caution if considering ERIs. Governments should take several actions prior to the decision to offer an ERI in terms of (1) goal-setting, (2) cost/benefit analysis, and (3) budgetary analysis. Governments should also develop an implementation plan.

1. Goal-Setting for ERIs

Governments should be explicit in setting documented goals for the ERI. Goals can be financial in nature, such as realizing permanent efficiencies in staffing or achieving budgetary objectives. ERIs can also be designed to achieve human resource goals, such as creating vacancies that allow for additional promotion opportunities and allowing management to bring in new staff. Any ERI goals should not conflict with other retirement plan goals (e.g., features to reduce turnover or increase retention).

An explicit statement of goals is needed to judge the ultimate success of the initiative and to develop performance measures. Further, having a statement of goals promotes transparency. Inappropriate goals such as rewarding a select group of staff should be explicitly rejected. Potential conflicts of interest among decision-makers who design an ERI should be monitored closely, since any self-dealing is costly and could harm the long-term credibility of the government entity.

2. Cost/benefit analysis

In judging whether an ERI should be offered, governments should assess the potential costs and benefits of ERI proposals, and the cost/benefit analysis should be linked to the goals of the ERI. For example, if a government sets a financial goal of obtaining long-term staffing efficiencies, then an

[1] The scope of this recommended practice does not cover deferred retirement option plans (DROP) or partial lump-sum option plans (PLOP), which often promote employee retention. The CORBA Committee may address this issue separately.

independent cost/benefit analysis should determine whether the ERI will actually bring about such

staffing efficiencies. A cost/benefit analysis should be comprehensive. It should take into account direct and indirect impacts, such as the impact on the government for providing retiree health care and additional contractor costs. In addition, it should take into account the effect upon both the plan sponsor and the pension fund (if the pension fund is a separate organization). Governments should retain an actuary to assist in conducting a cost/benefit analysis.

Material changes to the ERI proposal during the legislative process should trigger adjustments to the cost/benefit and budgetary analyses.

Regarding financially-driven ERIs, a cost/benefit analysis should compare long-term benefits and costs against the "default" scenario of a hiring freeze. Most financially-driven ERIs project financial benefits based on payroll savings related to staff departures. However, any such savings should be discounted, because a hiring freeze also creates payroll savings (owing to the normal rate of staff departures). Thus, the ERI benefit is limited to the marginal increase in staff departures attributable to the ERI. Governments that attribute all staff departures to an ERI would over-state the ERI benefit, thus distorting the cost/benefit analysis.

Financially-driven ERIs may also obtain savings by replacing highly compensated staff with lower-paid staff. Analysis of such ERIs must take into account the fact that newly hired staff tend to experience faster salary increases than other employees.

If early retirement incentives are offered, they should be offered very infrequently and without a predictable schedule to avoid the expectation that another ERI will be offered. Such an expectation would distort normal employee retirement patterns.

The incremental costs of an ERI should be amortized over a short-term payback period, such as three to five years. This payback period should match the period in which the savings are realized. To calculate the incremental costs of an ERI, governments should conduct an actuarial analysis that discloses the present value of the liabilities associated with an ERI. Governments that have over-funded pension plans should avoid allocating any actuarial surplus to finance the incremental costs of the ERI.

3. Budgetary considerations

In order to develop accurate budgetary estimates for the ERI, it is necessary to estimate the incremental cost of the ERI, which will vary according to the level of employee participation. Any budgetary analysis should project multiple scenarios for employee participation levels.

A budgetary analysis should be comprehensive. It should take into account direct and indirect impacts, such as the impact on the government for providing retiree health care and additional contractor costs.

Because a collective bargaining agreement may affect potential ERI costs and benefits, it should be reviewed prior to developing budgetary estimates.

4. Implementation considerations

If implementing an ERI, at a minimum, governments should take into account the following points:

- A communication plan is desirable to help employees understand the ERI in the context of overall retirement planning;
- It may be necessary to gain input from collective bargaining units;
- Governments should consider the impact upon service delivery after employees retire, with identification of critical personnel whose services must be maintained;
- The duration of the window should take into account the ability of retirement staff to manage retirement application workloads, among other factors; and
- Performance measures should be used to ensure ERI goals are met. For financially-driven ERIs, governments should track and report direct and indirect costs and benefits to determine if goals are met, such as for vacancies and contract costs.

References:

A Primer on Early Retirement Incentives, GFOA, 2004.

Approved by the GFOA Executive Board, October 15, 2004.