



MEMORANDUM

To: Councilmember Tim Burgess, Chair
Councilmember Lisa Herbold, Vice Chair
Councilmember Rob Johnson, Member
Affordable Housing, Neighborhoods, and Finance Committee

From: Erik Sund, Council Central Staff

Date: July 20, 2016

Subject: Legislation establishing a new benefit tier within the Seattle City Employees' Retirement System (SCERS)

Background

The Seattle City Employees' Retirement System (SCERS) was established in 1929 in response to a Charter amendment approved by City voters in 1927. SCERS provides a pension plan for most benefit-eligible City employees. Exceptions to membership include exempt employees who choose not to join and employees enrolled in the state-administered Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF).

The system is funded by member and employer payroll contributions and the returns on investments made with those contributions. A member "vests" in (becomes eligible for) a benefit by earning a minimum of 5 full years of service credit in covered employment. A member's benefit is calculated in one of two ways.

The formula based benefit provides a base annual allowance equal to up to 60% of the member's highest average salary over a 24-month period ("Final Average Salary or FAS"). For a member retiring with fewer than 30 years of service, the benefit is reduced to reflect the shorter service and for each year, if any, that the member is retiring before reaching age 65.

The alternate or "minimum" benefit provides an annuity that is actuarially equivalent to twice the member's accumulated SCERS contributions plus interest. This benefit is commonly referred to as "two times match". At the time that a member applies to retire, the Retirement Office calculates the member's retirement allowance using both methods and the member receives a benefit equal to the greater of the two results. This starting amount may be reduced based on other options that a member may select at the time of retirement, such as the provision of a survivor benefit.

Although the provisions of SCERS have been modified numerous times in the decades since the system was established, the basic structure has not been changed. SCERS currently has unfunded accrued actuarial liabilities of approximately \$1.2 billion, meaning that the value of benefits earned by all members to date exceeds the actuarial value of plan assets by that amount. This does not present a current risk to members' benefit payments; however, the funding status of the plan has led to an increase in contribution rates. Currently, the total contribution rate is equal to 25.26% of pay,

with members contributing 10.03% and the City covering 15.23%. In 2008, the total contribution rate was 16.06% of pay.

In 2010, the City Council issued a Statement of Legislative Intent that called for an interdepartmental team to explore options for the creation of a different pension benefit for new City employees. This effort continued for several years, resulting in the approval of a new SCERS Plan 2 benefit for new employees in collective bargaining agreements ratified in late 2015 and approved by the City Council earlier this year.

The Proposed Legislation

This legislation would establish the new SCERS Plan 2 (SCERS 2 or Plan 2) for members joining after December 31, 2016, consistent with the terms of the recently approved collective bargaining agreements. The new Plan 2 shares many characteristics of the current SCERS plan. Both are defined benefit plans with a 5 year vesting requirement. The primary changes in the new plan are summarized in the table below. Note that not all plan features are described in the table.

	SCERS 1	SCERS 2
Vesting requirement	5 years of service	No change
Normal retirement criteria	Age 65 or 30 years of service	Age 65 or 35 years of service
Period used to calculate Final Average Salary (FAS)	24 consecutive months	60 consecutive months
Multiplier for formula based benefit	Up to 2% of FAS per year of service	Up to 1.75% of FAS per year of service
Maximum formula based benefit	60% of FAS	No cap
Alternative or "minimum" benefit	"2x Match" annuity	None
Retiree Cost-of-Living Adjustment	Fixed 1.5%/year increase with 65% purchasing power floor	No change
Employee contribution	10.03% of pay	7.0% of pay
Interest rate on employee contributions	Established annually – policy target = 30 year Treasuries	No change
Expected Normal Cost	15.8%	11.9%
City contribution <u>to Normal Cost</u>	5.76% (total 2017 rate expected to be 15.29%)	4.9% (total 2017 rate expected to be 15.29%)

Generally speaking, the new Plan 2 is less costly and less generous to employees than Plan 1. Much of this is due to the lower benefit multiplier (1.75% per year rather than 2%) and the reduced provisions for early retirement. For members retiring after long service, however, Plan 2 could be more generous as the 60% cap on the standard pension benefit is eliminated. This means that long term employees may receive a benefit that is greater than 60% of their final average salary if they have more than 34.3 years of eligible service. The new plan also reduces employee (from 10.03% to 7.00%) and employer (from 5.76% to 4.90%) contribution rates for the "normal cost" (the expected long run cost) of the benefit. For now, the total City contribution rate will be the same for both plans. The City

continues to be responsible for covering unfunded liability in Plan 1 and ensuring that retirement benefits will be paid for all SCERS members.

In addition, the legislation also makes a number of clarifications to the language of the City code that do not have material fiscal impacts on the system or the benefits members receive. The labor unions have all reviewed this proposed ordinance and are comfortable with it.

Next Steps

The next scheduled meeting of the AHNFC is on Wednesday, August 3rd. If the Committee is prepared to vote on this legislation on that date, it will be available for consideration in Full Council on Monday, August 8th.

cc: Kirstan Arestad, CS Executive Director
Dan Eder, CS Deputy Director