



MEMORANDUM

Date: May 9, 2017

To: The Honorable Chair and Members
Pima County Board of Supervisors

From: C.H. Huckelberry
County Administrator 

Re: **Public Safety Personnel Retirement System Contribution Rates**

I asked the Finance Director to provide a comprehensive report regarding how our Public Safety Personnel Retirement System (PSPRS) liability is calculated. The total current total liability and the total required employer contribution report is attached for your information.

Pima County has 454 active employees in the PSPRS. As of June 30, 2016, the unfunded pension liability for the County for this PSPRS is \$207 million. Employees within PSPRS had earned \$355 million in pension benefits and accumulated \$148 million in the PSPRS in assets. Hence, the \$207 million in unfunded liability.

Our contribution for Fiscal Year 2017/18 will be \$21 million, an increase of \$4.5 million over the previous year. The contribution as a percent of salary now stands at 63.07 percent. This means that for every dollar of income earned by a public safety employee, the County pays an additional 63 cents in retirement benefits.

The attached memorandum includes a spreadsheet comparison of 13 employer plans in the system with more than 300 employees. (There are 230 total employer plans in the PSPRS.) As can be seen from the spreadsheet, our employer contribution rate is not the highest, but it is among the higher amounts paid into this retirement system.

CHH/anc

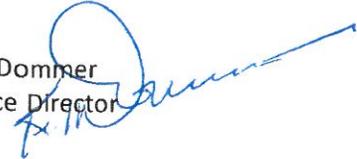
Attachment

c: Tom Burke, Deputy County Administrator for Administration
Keith Dommer, Director, Finance and Risk Management
Robert Johnson, Budget Manager, Finance and Risk Management

Date: April 27, 2017

To: C.H. Huckelberry
County Administrator

From: Keith Dommer
Finance Director



Re: **PSPRS Pension Contribution Rates**

Arizona Public Safety Personnel Retirement System (System) contribution rates for the Pima County Sheriff's Department (Department) are based on the System pension benefits that have been earned by both active and retired employees of the Department that participate in the System. Below is an overview of the earned pension liability calculation and how the System determines required contribution rates using that pension liability.

The required contribution rates have two components – a component for benefits that employees earned during the current year (the normal cost) and a component for unfunded benefits earned in prior years (the financing of unfunded pension liability). Beginning July 1, 2017, new employees participating in the System will earn fewer pension benefits. We can lower our normal cost rate over time by taking steps to increase the proportion of new hires within the Department. In addition, we can lower our rate to finance the unfunded pension liability by contributing more than the minimum to the System. The applicable subsections below discuss both options. Neither one is particularly attractive.

Calculating the Pension Liability

Annually the System uses a three-step process to estimate a pension liability amount for the System's benefits owed to participants. The System's actuaries calculate estimates separately for each employer plan in the System. The Department has its own pension liability calculation.

The first step in calculating the pension liability for the Department is estimating the dollar amount of future pension benefits that the System will pay to or on behalf of participating employees. The System's actuaries use both demographic data about a plan's participating employees and the benefits provided by the System to calculate the pension liability. Demographic data about a plan's participating employees includes age, years of service, compensation, average retirement age, and mortality. Benefits

provided by the System include normal pension, disability, and survivor benefits as well as cost of living adjustments.

The second step is applying a discount rate to estimate the present value of the future benefits. The System used 7.5 percent as the discount rate, which matched the System's long-term expected rate of return on its investments.

The third step is determining the portion of the present value of the future benefits earned by participating employees. Employees earn the portion of their estimated future benefits that corresponds to their progress towards their expected retirement age. Employees that have worked two-thirds of the way to their expected retirement age will have earned two-thirds of their estimated future benefits and two-thirds of the present value of their future benefits will be included as part of the pension liability.

Using this three-step process, the Department's pension liability at June 30, 2016 was \$355 million. The corresponding value of assets held by the System for the Department was \$148 million. The Department's was only 42 percent funded. Pima County's financial statements will report the remaining unfunded portion of \$207 million as a component of the County's pension liability.

Determining the Required Contribution Rates

At June 30, 2016, the System included 224 employer plans with active members. The System's actuaries calculate required contribution rates separately for each of these employer plans. The System designs these contribution rates to achieve several funding objectives including: maintaining adequate assets to pay benefits, providing stability of required contribution rates, demonstrating accountability and transparency, and promoting of intergenerational equity. The required contribution rate consists of two parts: the normal cost of pension benefits and financing for the unfunded pension liability. The normal cost covers the pension benefits earned by participating employees during the current year. The Department's normal cost calculated at June 30, 2016 was 16.9 percent of payroll for its employees in the System. The financing for the unfunded pension liability amortizes the Department's pension liability over a period of 20 years. The Department's financing of its unfunded pension liability calculated at June 30, 2016 was 46.2 percent of payroll for its employees in the system. Financing the unfunded pension liability is the larger component of the Department's total required contribution rate of 63.1 percent.

Normal Cost Component – The required contribution for the normal cost for these plans averaged 15.2 percent with 95 percent of employer plans within 2 percent of the average. See the normal cost chart below. These rates are similar across all plans because the prime drivers of the normal cost rate component are demographic

information and the System's benefits. These drivers are consistent for most employees. As such, the Department has very little immediate control over many of the factors that influence the normal cost rate component. However, the Department could encourage eligible employees to retire when first eligible before they earn larger System benefits and replace those employees with new hires who earn less costly System benefits each year. A newer workforce may decrease current payroll costs as well as pension costs. The City of Tucson is currently implementing such a program. See the attached news story.

Normal Cost Rate - Estimated Retirement Benefits Earned in the Current Year by Current Employees



Financing the Unfunded Pension Liability Component – The required contribution for financing the unfunded pension liability for these plans averaged 22.6 percent with greater variation among employer plans than the normal cost. Some plans have rates above 100 percent and other plans have nearly 0 percent rates or even negative rates for this component. Two of the main drivers of the rate to finance the unfunded pension liability are the size of the unfunded pension liability and the number of active employees. The larger the unfunded liability, the larger the required contribution rate needs to be to fully fund the liability. The more active employees, the smaller the required contribution rate because the System can allocate the financing to a larger number of active employees. The System plans to finance unfunded pension liabilities over a 20-year period.

The System's actuaries calculated the Department's June 30, 2016 unfunded pension liability at \$207 million. The Department's employees had earned \$355 million in pension benefits and the Department had accumulated \$148 million in System assets. The Department's plan had 454 active employees. This results in an unfunded pension liability of \$456 thousand for each of the Department's active employees. Of the System's 205 employer plans that have an unfunded pension liability, the Department has the 30th highest unfunded pension liability per active employee. The Department's required contribution to finance the unfunded pension liability of 42.6 percent is the 31st highest. The chart below shows the Department's position relative to the other employer plans.

Financing Unfunded Pension Liabilities



Similar to the normal cost component, the Department has limited control over the System's 20-year financing plan or other factors in the calculation of the rate to finance the unfunded pension liability such as mortality rates or the investment rate of return. However, the Department can have a significant impact on the rate to finance the unfunded pension liability by contributing more than the minimum required amount. The System's reports appear to encourage this by stating in their June 30, 2016 report on the Department's plan that "It is most important that this Plan receive contributions at least equal to the rates shown in this report." The emphasis is in the System's report. The report also includes a table "Impact of Extra Contributions" showing that the

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Department's contribution rate could be reduced by 2.5 percent if the Department contributed an additional \$10 million to the System. A 2.5 percent reduction in the Department's contribution rate would save the Department an estimated \$900 thousand per year.

If the Department had monies to contribute more to the System than the minimum requirement, one disadvantage is that that state law currently considers additional System contributions to be spending that is subject to the County's spending limit. Because the County is at or just below its spending limit, this would likely mean that the County would have to borrow money to make the additional contributions to the System. Although several Arizona governments have borrowed money for this purpose, the cost of borrowing makes this a financially risky option.

Comparable Information

Attached is a table of relevant data about each of the 13 employer plans in the System with more than 300 employees. Information about all 230 employer plans in the System can be found in the System's June 30, 2016 Consolidated Report available on the System's website.

Note: This memo only discusses the pension portion of the System. The health care portion is less than 1 percent of the Pima County Sheriff's Department plan, the related June 30, 2016 contribution rate was 0.44 percent, and the health care portion is fully funded.

Source: Information in this memo is from the System's June 30, 2016 reports on the consolidated system and on the Department's plan.

KD/tp

Attachments

c: Tom Burke, Deputy County Administrator

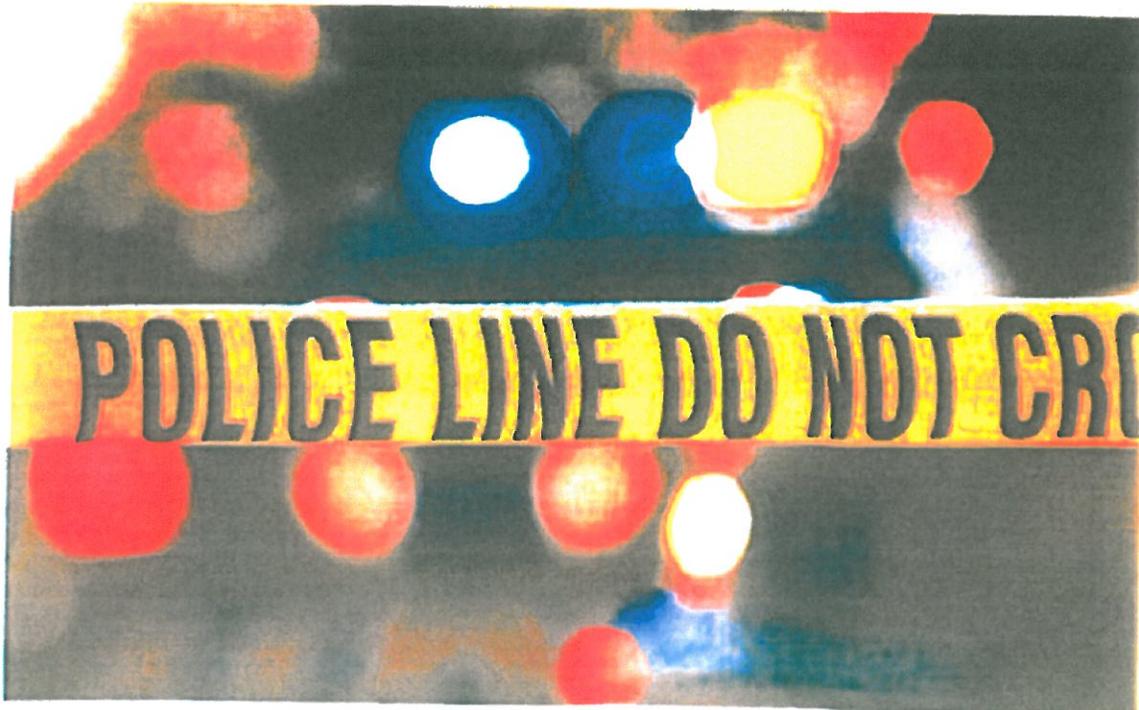
Arizona Public Safety Personnel Retirement System
 Consolidated Report
 June 30, 2015
 Employer Plans with More than 300 Employees

Employer Name	Active Members	Active Member Payroll	Payroll Per Active Member	Retired Members	Annual Retiree Benefits	Average Annual Retiree Benefit	Pension Liability Earned by Members	Pension System Assets	Funded Percent	Unfunded Pension Liability	Unfunded Pension Liability per Active Member	Required Contribution Rates			
												Current Year Normal Cost	Financing for Unfunded Pension Liability	Total Required Employer Contribution	Retired Members to Active Members
DEPT. OF PUBLIC SAFETY	1,030	68,966,183	66,957	1,314	66,702,286	50,763	1,090,807,162	355,281,332	32.60%	735,525,830	714,103	16.90%	70.07%	86.97%	56%
TUCSON POLICE	842	59,290,594	70,416	923	46,455,894	50,331	818,357,817	290,020,070	35.40%	528,337,747	627,480	16.85%	59.04%	75.89%	52%
TUCSON FIRE	582	42,306,370	72,691	581	30,332,996	52,208	512,224,147	165,899,664	32.40%	346,324,483	595,059	16.43%	53.65%	70.12%	50%
PHOENIX POLICE DEPT.	2,486	225,235,566	90,602	2,195	130,412,524	59,413	2,949,524,806	1,270,780,865	43.10%	1,678,743,941	675,279	17.52%	49.78%	67.30%	47%
PIMA COUNTY SHERIFF'S DEPT.	454	29,789,829	65,616	384	18,008,285	46,897	355,422,768	148,572,160	41.80%	206,850,608	455,618	16.89%	46.18%	63.07%	46%
PHOENIX FIRE DEPT.	1,390	124,321,697	89,440	1,052	68,043,600	64,680	1,558,107,788	704,251,445	45.20%	853,856,343	614,285	16.78%	45.91%	62.69%	43%
TEMPE POLICE DEPT.	320	28,069,771	87,718	241	13,121,326	54,445	285,510,601	115,675,700	40.50%	169,834,901	530,734	15.11%	40.56%	55.67%	43%
MESA POLICE DEPT.	715	61,210,877	85,610	513	27,389,482	53,391	642,638,088	308,505,416	48.00%	334,132,672	467,318	16.91%	36.78%	53.69%	42%
MARICOPA COUNTY SHERIFF	676	52,596,336	77,805	463	22,165,578	47,874	489,813,043	217,091,528	43.40%	282,721,515	418,227	16.98%	35.81%	52.79%	41%
MESA FIRE DEPT.	392	32,453,269	82,789	235	14,211,053	60,473	347,179,542	175,860,147	50.70%	171,319,395	437,039	16.39%	35.50%	51.89%	37%
SCOTTSDALE POLICE DEPT.	376	32,445,266	86,291	225	12,225,560	54,336	303,912,464	158,332,002	52.10%	145,580,462	387,182	16.84%	30.42%	47.26%	37%
GLENDALE POLICE DEPT.	388	34,196,185	88,134	186	9,694,712	52,122	282,015,577	132,768,053	47.10%	149,247,524	384,659	15.40%	29.42%	44.82%	32%
CHANDLER POLICE DEPT.	314	27,682,071	88,159	132	7,241,176	54,857	228,609,248	120,918,515	52.90%	107,690,733	342,964	15.16%	26.45%	41.61%	30%

http://tucson.com/news/local/watchdog/city-offering-tucson-police-fire-employees-hefty-retirement-bonus/article_1be8e327-bc00-5d86-af92-970c6c247a84.html

City offering Tucson police, fire employees hefty retirement bonus

By Caitlin Schmidt Arizona Daily Star Apr 20, 2017 Updated 18 hrs ago



Tucson Police Department

Up to 35 Tucson police and fire employees could receive a \$50,000 cash bonus if they decide to take the city up on an early retirement offer.

The incentive package, which was discussed by Mayor Jonathan Rothschild and the Tucson City Council during a Wednesday study session, also includes sick-leave payout for 100 percent of the employee's accrued hours and an optional medical subsidy to pay for health insurance premiums for up to three years.

The package is designed to “streamline operations and modify the work-force composition” in the Tucson Police and Fire departments, City Manager Mike Ortega wrote in a memo.

For the Police Department, the incentive will only be available to sergeants, lieutenants, captains and assistant chiefs and will be capped at 10 sergeants and 13 commanders, the memo said.

In the Fire Department, captains, battalion chiefs, deputy chiefs and assistant chiefs are eligible for the incentive package, which will be capped at 10 captains and two chiefs.

The anticipated cost for sick-leave payout plus the \$50,000 bonus would be about \$65,083 per police employee and \$82,498 per fire employee, according to the memo.

The medical subsidy would cost \$28,800 per employee.

Based on the assumption that 12 employees would retire from each department, the total cost of the package would be about \$2.5 million, Ortega wrote in the memo.

The anticipated savings from creating vacancies depends on the action taken by each department, Ortega said. The plan is for the Fire Department to use the savings to convert commissioned positions to civilian positions, according to the memo.

The plan within the Police Department would be to add 12 entry-level police officers in place of the vacated positions, saving the department a projected \$645,000 in the first year, Ortega wrote in the memo.

"Vacancies give us opportunities from a management perspective to look at how we do business," he said. "What I've challenged both police and fire to do is to really look hard at the basis for us providing those services, whatever those services are. Because of some of the constraints we've had we obviously can't afford to do it exactly the way we've always done it."

After the first year, the total savings between both departments would be about \$1.1 million.

The incentive will be available during a limited window, and eligible employees will be given a 10-day sign-up period and need to declare their intent to retire by July 1.

"One of the reasons that I understated the potential savings ... is because I don't have high confidence that we're going to have huge participation in this," Ortega said, adding that if not enough people sign up, he'll have to go back to the budget to find a way to make up the savings.

The council asked Ortega to provide an update on how the reorganization of vacant positions will work after the sign-up period has ended.

Tucson Police Officers Association President Roland Gutierrez said the union has not taken a position on the incentive plan.

"It is not my intent to convert every single vacancy into a civilian position," Ortega said during the study session. "This is consistent with what we've talked about for about a year and a half, to really challenge vacancies across the board and particularly in the public safety ranks, where there may be opportunity to look at civilians providing services that are currently provided by commissioned personnel."

No savings are projected during the first year, but Ortega described the action as "an investment in future year savings."

Councilwoman Karin Uhlich said there had been previous discussion of fire safety inspectors being converted to civilian positions and asked Ortega if this was part of the incentive plan.

"The conversation is broader than just the inspectors," Ortega said. "If we agree that the station staffing, which is of paramount importance, is basically what we want to focus on in terms of response time ... what I really challenge the department to do is we hold that harmless and everything else becomes ... part of the conversation."

Ortega stressed there are no immediate plans to convert any commissioned fire or police department positions to civilian posts, adding that the restructuring depends entirely on how many employees take the city up on its offer.