

**CITY OF TEMPLE TERRACE, FLORIDA
MAYOR AND CITY COUNCIL
REPORT OF WORK SESSION**

**Tuesday, April 21, 2009
Council Chambers - City Hall
5:00 p.m.**

Having been duly advertised as required by law, the Mayor and City Council of the City of Temple Terrace, Florida, met in a work session with the Police and Fire Pension Boards, beginning at approximately 5:00 p.m., for an overview and status report of Fire and Police Pension Funds.

PRESENT WERE: Mayor Joe Affronti, Sr., Council Members Alison M. Fernandez, Ron A. Govin, Ken Halloway, and Mary Jane Neale, City Manager Kim Leinbach, City Attorney Mark Connolly, and City Clerk Lisa Burns. **ABSENT WAS:** Council Member Mark A. Knapp.

ALSO PRESENT WERE: Public Information Officer Michael Dunn, Code Compliance Director Joe Gross, Finance Director Diane Reichard, Police Chief Ken Albano, Fire Chief Keith Chapman, Deputy Fire Chief Ian Kemp, Deputy City Clerk Judith Read, Police Officer Mike Lowell, Police Officer Chris Morris, Firefighter Roger Chewning, Joe Bogdahn, Patrick Donlan, Jack Townsend, Steve Stack, and several other persons.

Mayor Affronti mentioned the purpose of the work session is to address City Council and citizen concerns regarding unfunded liability of the Police and Fire pension funds. He called on the City Manager to introduce the topic of the work session. The City Manager announced that Patrick Donlan of Foster & Foster, the Police and Fire Pension Fund Board of Trustees' actuarial consultant, will provide a presentation of how the pension systems work and the status of the City's pension funds. He asked the Chair of each Pension Board to stand and introduce their representatives that are present. Mike Lowell, Chairman of the Police Pension Board of Trustees, introduced Police Officer Trustee Chris Morris, Citizen Trustee Jack Townsend, Patrick Donlan of Foster and Foster, Steve Stack of ICC Capital Management, and Joe Bogdahn of the Bogdahn Group. Firefighters Pension Board of Trustees' Chairman Roger Chewning introduced himself.

Utilizing a PowerPoint presentation, a copy of which is part of the record, Patrick Donlan presented an overview of the Police and Fire pension funds. He briefly reviewed the Defined Benefit Program, which minimizes the expenses by "lumping" all the assets together in one pool; therefore, the investment management fees are very small. In addition, he said the Boards meet quarterly, at the same time, which cuts down on the consultant's expenses. He concluded that he believes both the Fire and Police Pension Boards have done a good job minimizing expenses.

Rather than the pay-as-you-go type of plan, Mr. Donlan remarked the City's pension plans are set up to contribute in advance for all projected, future benefit payments, which allows for investment earnings and not simply City, member, and State contributions. He briefly reviewed the percentages of fund contributions made by the members, City, State, and investment earnings over the past 14 years, noting that 42% of the Police pension fund contributions and 41% of the Fire pension fund contributions were from investment earnings.

Stating that the City's pension program is a Defined Benefit Program, Mr. Donlan explained the actuary has to determine proper funding from year-to-year in order to have enough money to pay benefits when they come due. He pointed out the various assumptions used: an 8% investment return; the entry-age normal funding method of cost allocation; liabilities are amortized over 10, 20, or 30 year periods, based on the length of time prior to the recipient's retirement; and "asset smoothing."

Mr. Donlan briefly described “asset smoothing” as using an actuarial value of assets, rather than the market value of assets. Mr. Donlan explained that there is a present value of all future benefits, and if all that money was in the fund right now, there would be no required contributions; however, in reality, there is not the full value of all those future pension benefits. He continued the smoothing technique is used so there is an actuarial value of assets, which is slightly different than the market value of the assets. He explained the entry-age normal cost method is where a level contribution is made from the time someone is hired until the time they retire and all the assumptions are met; then there will be enough money to pay their full benefits at retirement. He clarified that the City is behind in the unfunded actuarial accrued liability - the total present value of benefits minus the future normal costs to be incurred and the present assets. He further clarified that the unfunded actuarial accrued liability indicates how much the fund is behind in order to keep up with the projected benefits.

Referring to market volatility, Mr. Donlan stated that the Defined Benefit Pension Program is more able to handle the market fluctuations; the market may go up and down, but it doesn't matter, because the benefits are not going to be paid for a long time. He added that smoothing is done on a four-year rolling average return, which smoothes out the peaks and valleys of the market and provides more stability for the City's funding requirements.

Addressing a question from the last City Council meeting of how well-funded the programs are, Mr. Donlan reviewed several methods of comparison for funding ratios using the Police pension fund as an example; assets vs. all future benefits – 52.9% funded, actuarial accrued liability vs. assets – 58.3% funded, and assets vs. accrued benefits- 64.9% funded. He noted that the Fire pension funding ratio is a little better. Responding to another question from the last Council meeting of how the City will make up the unfunded actuarial liability, he said the City will make increased, short-term contributions, until the assets turn around, and hopefully, the unfunded actuarial accrued liability will begin to go down. He noted that it is no reason to panic, since every year the City receives a valuation report and adjusts its contributions appropriately; by the time everyone retires, there will be enough to fund all those retirement benefits.

Mayor Affronti asked for the dollar amount of increased contributions rather than percentage amounts. Mr. Donlan calculated the percentages and responded that the required Police fund contribution would increase by approximately \$150,000 a year, because of the devastating 2008 market, and the required Fire pension fund contribution would increase by approximately \$100,000. Mayor Affronti reviewed the total of the two would roughly be a \$250,000 increase.

Council Member Fernandez clarified that would be an increase over the current year contribution. Mr. Dolan concurred, clarifying that the requirements he is reviewing will be for Fiscal Year 2009-10. Council Member Govin interjected the comparison is between this year and the coming year; therefore, between the two funds the City will need to come up with an additional \$250,000 contribution. Mr. Donlan recalculated the Fire pension fund and stated the actual amount of increase would be about \$75,000, which is a total increase of approximately \$225,000.

Responding to a question by Council Member Govin regarding the estimated percentage of return on investment, Mr. Donlan reiterated that the assumption is an 8% return on investments; however, in 2008 the funds did not make that, which contributed to the unfunded actuarial accrued liability.

Council Member Govin inquired about the amount of earnings on the funds in 2008. Mr. Donlan responded that the Fire pension fund was a negative 11.4% and the Police pension fund was a negative 11.75%; compared to other pension plans in the State of Florida, they were very good returns. Mr. Bogdahn interjected it was in the top quartile of other plans.

Council Member Govin questioned how the City will come up with another \$225,000 when the budget is already reduced by approximately \$2 million. He noted that this year the market is still not correcting, and he questioned the 8% assumption. Reviewing a research article on conventional investment wisdom, Mr. Bogdahn explained there are cycles, and the portfolio is viewed as a long-term proposition; they are looking for long-term assumptions to come up with the funding mechanism for this plan. He continued that Mr. Donlan's assumptions include investments, long-term turnover in the departments, and salary increases. He briefly reviewed the calculations of the historical returns used to come up with the 8% return. Since ICC has been managing the plan funds for a long time, Mr. Bogdahn called on Mr. Stack to provide information on returns for the City.

Mr. Stack, of ICC Capital Management, remarked that ICC has been managing the funds since mid 1987, and from that time to the Fiscal Year End in September 2009, the City has averaged approximately 8.2% for the Fire fund and approximately 8.4% for the Police fund.

Mr. Bogdahn interjected that period included several down-turns, and the long-term averages are still above 8%. He continued that they are not looking at what is happening in the market today, tomorrow, or yesterday to determine the long-term funding applications. He noted that State Statutes require with every valuation that the Board declare what they expect the long-term rate to be in the next year, the next several years, or the long-term. Mr. Bogdahn said they are focusing on the long-term and are comfortable with an 8% return.

Mr. Bogdahn commented that the unfortunate thing for the City, as a plan sponsor, is that the State Statutes and standards treat the actuary as a day-trading fund, using a one-year snapshot, which sets off the funding requirement and allows smoothing over a 4-year period. He noted that if they could smooth over a 20-year period, the earnings would be 8.2% and the funding level would be smooth; however, the State makes them look at a shorter window rather than a longer-term smoothing average.

Mr. Bogdahn distributed a 2-page handout, a copy of which is part of the record, with the first page reflecting fluctuations of the market since 1808, and the second page reflecting historical market crises, since the Great Depression, and their subsequent recoveries. He noted that there are a number of indicators which give confidence in what the markets are going to look like going forward, such as unemployment spikes of one-half percent or greater, low consumer confidence, commercial real estate as the lagging indicator, and corporate bonds as a leading indicator. Considering all of those indicators, he said he is unsure of the return amount for this fiscal year; however, going forward, he believes the next fiscal year is going to look pretty "rosy." He mentioned that due to the smoothing, the loss is amortized over a period of time. While the City will not have to write a check for all of the loss this year, he said it follows the City; therefore, the City needs a couple of years of stellar returns to get to the point of reducing the City's contributions.

Council Member Halloway noted that the market fluctuation handout looks remarkably like the business cycle. He said in the past, even though it hit bottom, the fact that it would come back up was relied upon. He continued that he hopes what Mr. Bogdahn says will come true; however, he is concerned about the future of the free market in this country. Mr. Bogdahn mentioned that even the bearish people in his firm have started putting money back in the stock market.

Council Member Govin mentioned he is not sure that this unstable market situation is comparable to anything experienced in the past. He remarked that he does not know how the City will come up with the money for this, adding that it also discourages the addition of people to the forces, because every addition adds a multiplier to the fund. He expressed concern for where the City will find itself if the predictions do not come true.

Council Member Govin commented that he is aware that some of this is mandated by the State of Florida, without funding, and he asked whether the State of Florida is considering doing anything or if they are going to continue the 7%. Mr. Bogdahn briefly reviewed the State Legislature has clarified the use of the premium tax dollars that are collected from all citizens. The City of Temple Terrace's Boards have gotten the State to allow them to have the actuary re-price the cost of the benefit, so if it increased, additional State money could be used for the City to offset those costs; subsequently, the State has said that cannot be done. He expressed his belief that the State needs to look at its interpretation of that requirement, suggesting it should be a percentage of payroll, because payroll does change. He mentioned that the City's Boards have pro-actively gone that way, and made adjustments to help that.

Relative to the Fire pension, Mr. Donlan briefly explained the frozen State money; the actual State money received in 2008 was \$197,000; however, the frozen amount was \$117,000, so the City could only use \$117,000, and the other \$79,000 stays in the plan for a future benefit improvement. He noted that the State has a proposed bill to lift the restrictions on the frozen amount for the next two years, and if that is done, the City would be able to use the entire \$197,000; thereby, saving the City \$80,000 per year for two years. He remarked that the State is trying to accommodate this very volatile situation. Council Member Govin asked whether there is a bill attached to that, to which Mr. Donlan responded affirmatively. The Finance Director mentioned she has been tracking that bill. Council Member Govin asked that the information be provided to the City Manager for lobbying purposes.

Referring back to the Police Defined Benefit Plan, Mr. Donlan said that the City is allowed to do amortizations and smoothing so the City does not have significant yearly changes. He continued that the unfunded accrued liability exists, and at some point, the City must make up the \$1,789,000. Council Member Govin commented that the market created a larger liability, to which Mr. Donlan concurred.

Council Member Govin asked how much the City contributes for each plan. Mr. Donlan responded for the current year, before the increases, the City contributes \$675,000 for the Police plan and \$407,000 for the Fire plan. Council Member Govin noted that for the upcoming year, the total would be \$825,000 just for the Police plan.

Noting that the City's general employees have been converted to a Defined Contribution plan, Council Member Fernandez asked for clarification on the State mandates with regard to the Police and Fire plans, and what changes, if any, the City could possibly make in the pension plan.

Mr. Donlan responded that in order to receive State money, the plans must be Defined Benefit Pension Plans; if the City was to try to switch to a Defined Contribution Plan, the State would request their money back. Council Member Fernandez questioned whether that would still be true if the City converted the plan for new hires only, to which Mr. Donlan responded he is unsure; the City would need to contact the State regarding that question. Mr. Bogdahn interjected there would be discrimination issues. Council Member Fernandez surmised that it would be prohibitive to do any conversion, if it required giving back all of the State money.

Council Member Fernandez asked the most conservative way for the City to have a funding plan in place that could protect the City from the more drastic changes. Mr. Donlan responded that in recent meetings a funding floor, such as 25% of payroll, was discussed. He explained when times were good and the City was required to contribute very little, if they had contributed that same 25% of payroll yearly, it would have dampened the effect of bad years, and it would dampen the volatility in the future.

Council Member Fernandez questioned how often the assumptions are reviewed, to which Mr. Donlan said each Board sets the assumptions, and due to the volatile situation of 2008, both Boards approved an experience study with the 2009 valuation, to look at the past experience with Temple Terrace to see how it relates to the turnover, salary increases, and investment returns; however, they wanted to let the volatile situation settle down before that was done.

Council Member Fernandez questioned the accuracy of the life expectancy tables. Mr. Donlan responded the 1983 group annuity mortality table is currently used; however, changing to the 2000 mortality table will probably be recommended with the assumption changes and would increase the funding requirements by approximately 1.5% of payroll.

Council Member Fernandez suggested that the funding requirements seem artificially low, and expressed her concern as to whether the true cost is being reflected. Mr. Donlan remarked he does not believe the assumptions are unrealistic in either plans. Council Member Fernandez noted that she believes it would be conservative to have a percentage of payroll in place for funding, when the percentage of payroll is higher than the City's required funding.

Mayor Affronti commented that the City does not have a lot of options, but this session has provided more understanding of the City's position.

Pension Board Citizen Member Jack Townsend expressed concern for the unfunded liability, which will be growing continually and financed for years to come, and although, actuarially sound and allowed, the negative amortization of it is a concern. He continued that he would like the City to pay at least the assumed rate of return, 8%, although it would make this year's payment ridiculously high, and given the finances of the City, that can't happen; however, the idea of a payment floor has great merit, particularly with a long-range vision, which he hopes will be collectively developed.

Stating this is a real concern, Council Member Govin questioned where the City goes from here. He noted that the City paid \$1,082,000 and will pay an additional \$225,000 this year; the City must find a way do something with that. In addition, he said the City should never be "upside down" on the funding percentages and suggested the City set a funding level goal, for example within 3 to 5 years, or whatever makes sense, and make a payment of a set amount to keep the funds at perhaps 75%, as a funding level.

Council Member Govin questioned whether the Council may need another workshop, now that they understand the situation better, to determine how to fund the plans or put a plan together to fund the plans.

Mayor Affronti suggested making this part of the budget workshop discussions. He agreed with Mr. Townsend that the City needs to take care of whatever additional liability there is, instead of carrying it on for another 15 to 20 years; they just have to figure out how to do that.

The City Manager commented that is a challenge in a time when everything else is in the red, adding that they can at least set goals and do as much as they can to work toward those goals. He concurred this should be part of the budget workshop, which will be set up in the very near future.

Mayor Affronti said he believes Council now has a better understanding and thanked the consultants.

The work session ended at 6:05 p.m.

Submitted by,

Melissa E. Burns, MMC
City Clerk