CITY OF BATTLE CREEK
CITY MANAGER

Date: **April 19, 2019**

To: **Battle Creek City Commission**

From: **Rebecca L. Fleury, City Manager**

Subject: **Final Report and Recommendations of the Legacy Cost Committee**

In September 2015, I convened the Legacy Cost Committee to review the City's legacy costs consisting of all pension plans and retiree health plans; and recommend strategies to reduce annual operating costs and long-term liabilities associated with these legacy costs.

Members of the Committee included City Manager Fleury, Finance Director Linda Morrison, IAFF President Chris Love, Labor Relations Attorney Nancy Mullett, SEIU President Penny Hepler, Former SEIU President Eric Campbell, DPW Director Chris Dopp, Sergeant Todd Elliott, Commissioner Susan Baldwin, Former City Commissioner Andy Helmboldt, The Planning Group's Rick Tsoumas, former Treasurer Gail Budrow-Bradstreet, and former City Commissioner Mike Sherzer. Brandon Fournier of Shifman Fournier Law office served as a consultant to the Committee. Attorney Fournier is often called upon by the Michigan Municipal League in matters concerning municipal pensions and other post-employment benefits, thus his expertise was helpful to the Committee's work.

I never intended for this committee to convene for over three years, with substantial gaps between meeting dates. However, during this time, there were many legislative options regarding public pensions and other post-employment benefits discussed, debated and later implemented by the Legislature of the State of Michigan that would have a direct impact on the City of Battle Creek's legacy costs, and thus the parameters considered by the Legacy Cost Committee. Most notably PA202 of 2017.

The Legacy Costs Committee met on the following dates:

- September 8, 2015
- March 14, 2017
- April 20, 2017
- June 29, 2017
- September 25, 2017
- February 16, 2018
- September 14, 2018
- November 5, 2018
- December 3, 2018
- December 17, 2018
- February 13, 2019

The initial meetings included extensive overviews of the city's pension and retiree health care plans and their funding sources. Committee members were also provided white papers by MSU Extension, Bridge Magazine, Mackinaw Center, Boston College, other Michigan municipalities, Michigan Municipal League, and the Michigan Employees Retirement System. These resources were shared in an effort to educate and consider all options.

In February 2018 the Committee was briefed on PA 202 of 2017, the Protecting Local Government Retirement and Benefits Act. The City's required Form 5572 for PA 202 was shared with the Committee and discussions began to focus on the one plan that was considered underfunded by the new law. The City's MERS pension plan was below 60% funded, requiring the City to file a waiver form, and later a Corrective Action Plan (CAP) (as the waiver was denied by Treasury). I have incorporated the components of the CAP into the following recommendations by the Committee.

These Legacy Cost Committee recommendations are broken down into three areas:

- MERS Pension
- Police and Fire Pension
- Other Post-Employment Benefits (retiree health insurance)

After the recommendations are described, points of discussion of the Committee are documented for your review. These are topics for which the Committee did not actively make recommendations, but were covered in depth during discussions that included attorney Brandon Fournier, of Shifman Fournier Law.

The MERS Pension recommendation regarding the trend of increasing contributions from employees was part of the Public Act 202 Corrective Action Plan adopted by the City Commission with resolution number 40 on 12/18/18. The Commission has not yet considered all other recommendations.

MERS Pension

- Continue the trend of increasing employee contributions to the pension plan (subject to collective bargaining). Current rates and goals within 5 years are noted below and include the recognition that the closed groups have a higher pension benefit than the open groups:

MERS Pension Plan				
Division # and Name	Employee Contribution % @ 7/1/18	Target EE Contribution @ 7/1/23		Actives
01 - Non Union	5.00%	10.00%		62
02- AFSCME (closed)	2.75%	7.00%		52
03-Transit (closed)	2.50%	7.00%		11
12 - BCSA (closed)	5.16%	7.00%		22
14 - SEIU (closed)	3.50%	7.00%		41
15 - Commission Appointed	0.00%	5.00%		2
17 - Correction Officers	3.12%	5.00%		2
18 - AFCME (hired > 12/1/10)	2.50%	5.00%		64
19 - SEIU (hired after 7/1/11)	3.50%	5.00%		50
20 - BCSA (hired > 1/1/12)	2.50%	5.00%		3
HA - Transit (hired > 3/1/10)	0.00%	0.00%		22

As noted above, this recommendation was included in the Corrective Action Plan adopted by the City Commission in December 2018.

- Enact auto-enrollment for new hires in the City's 457 (ICMA-RC) defined contribution plan. This can ease the employee's reliance on the defined benefit pension in retirement.

- ❖ Eliminate the option to purchase service credit until the employee is within three years of retirement. Even though this actuarially determined cost is paid 100% by the employee at the time of purchase, it has the potential for additional employer costs if employees have the option to purchase at any time during their career with the City. Currently, many employees who make this service credit purchase are early in their career. Assumptions used for salary growth may be severely understated if the employee moves from an entry level position to a managerial level position during the course of their career.

- ❖ Implement Final Average Compensation (FAC) standards for non-represented employees that does not include longevity and education allowances in the calculation for anyone retiring after July 1, 2020.

Police & Fire Pension Recommendations

- ❖ Continue the trend of increasing employee contributions to the pension plan (subject to collective bargaining). Current rates and goals within 5 years are noted below:

Police & Fire Pension Plan				
Group (none of the below groups are covered by Social Security)	Employee Contribution % @ 7/1/18	Target EE Contribution @ 7/1/23		Actives
Police:				
Sergeants - POLC	11.72%	14.22%		15
Lieutenants	10.00%	12.50%		5
POLC - Non Supervisory	8.25%	10.75%		83
Non-Represented	10.00%	12.50%		6
Fire:				
OSP	11.00%	13.25%		4
IAFF	11.04%	13.54%		75
Non-Represented	10.00%	12.50%		1

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- ❖ Presently the Collective Bargaining Agreement with the firefighters provides for the inclusion of various special pays in order to calculate an employees' Final Average Compensation. It is our recommendation that these be eliminated or reduced in scope moving forward. This would have to be negotiated with both of the fire bargaining units.

- ❖ When Act345 participants are approved by the City Commission to purchase service credit, it is recommended the employer's portion be paid at the same time as the employee's portion. Currently the practice is to roll the employer portion into the actuarially calculated amortization payment, which increases the current liability and future required payments. This recommendation would be accomplished by including prior year military purchase employer costs in the new year millage rate calculation beginning with the rate effective July 1, 2020.

- Enact auto-enrollment for new hires in the City's 457 (ICMA-RC) defined contribution plan. This can ease the employee's reliance on the defined benefit pension in retirement.

Retiree Health Care Recommendations

- Establish a qualified medical trust for funding the non-police & fire pay-as-you-go stipends (Police and Fire currently have trusts created and held at MERS). This trust would be designated for non-police & fire retirement health system funding.

- Require retirees to use health plans of current employers if available, and spouses to utilize benefits from their employer, if available. Require an annual statement from City-plan participants that they do not have those plans/benefits available. This would be effective with the open enrollment for calendar year 2020.

- Examine the opportunity of the MERS Exchange (or other health care exchange) for retiree health care offerings to facilitate the elimination of the ability for retirees to purchase health insurance from the City.

- The only group for which new hires are eligible for a stipend towards retiree health insurance is the non-represented group. Eliminate this benefit for new hires on or after 7/1/19.

- Under the present Collective Bargaining Agreements, members of the fire union who were hired prior to May 14, 2007 and retire after July 1, 2004 are eligible for full retirement health care. The recommendation is for further conversations to address the plans that are offered to this group in retirement.

- Presently, there is a single group of firefighter retirees who are eligible to receive fully paid medical benefits. Under the terms of the Collective Bargaining Agreement with the firefighters Union, employees hired "on or before the date of the 2007 Act 312 Award (May 14, 2007) and who retired on or after July 1, 2004, with a pension benefit immediately payable, shall receive the same health insurance benefits as set forth in the collective bargaining agreement for current, active employees". This clause provides for the right of the City to provide the retirees with benefits equal to the active work force. As a result, the City should eliminate the CB PPO 2 plan based upon the high level of cost.

Points of Discussion (not recommendations by the Committee):

MERS PENSION

Consider moving from the current defined benefit plan for non-represented employees to a hybrid for new hires. This transition can eliminate/reduce liabilities related to new hires, and can provide a retirement plan that may be more suited to today's employees. There may be an option, depending on the funding requirements, to allow active non-represented employees to be given a one-time option to convert to this hybrid plan.

Alternately, consider a bridged benefit using a frozen final average compensation (FAC) for non-represented employees. Bridging benefits reduces the benefit multiplier for existing employees on a going-forward basis while leaving earned benefits unchanged. The multiplier for non-represented employees currently is 2.5%, and the recommended multiplier could range between 1.5% and 2.25%. Consider 2% as a mid-ground alternative with a frozen FAC date of 7/1/19.

Both of these points of discussion for MERS would require the current open plan to be closed. This will increase employer costs for this group.

Consider a sunset of the service credit purchase option. MERS allows municipalities to eliminate the option for employees to purchase additional service credit which could be implemented at a future date as determined by the City Commission.

Consider replacing the defined benefit pension plan for current and future employees with a defined contribution plan (subject to collective bargaining).

Consider elimination of the defined benefit pension plan for current and future employees (subject to collective bargaining).

POLICE & FIRE PENSION

The City should consider in engaging in negotiations with the respective labor unions to reduce the pension benefit multiplier from the current 3.0% to 2.75%, or another reduced amount. This can be accomplished through the utilization of a “bridge” multiplier. This could occur prior to the attainment of the twenty-fifth year of service. Under such a system, a pension is calculated under the old pension multiplier for the years of service that was in effect prior to the change and the reduced multiplier takes affect from the negotiated date.

The City has in place an 80%-75% maximum benefit of FAC. However, under this system as wages grow, the maximum also grows. The City could benefit from fixed dollar pension limitations which is generally referred to as a Hard Cap and example of $40,000 per year. This will allow the City greater control over the retirement system and improve the funding levels over time, while also allowing for wage growth (subject to collective bargaining).

Consider replacing the defined benefit pension plan for current and future employees with a defined contribution plan (subject to collective bargaining).

Consider elimination of the defined benefit pension plan for current and future employees (subject to collective bargaining).

RETIREE HEALTH CARE

The City should consider a phase out of health insurance stipends for all non-police & fire retirees. Effective January 1, 2020, consider reducing the $200 stipend to $150; effective January 1, 2021 reducing to $100; effective January 1, 2022 reducing to $50, with $0 stipend effective January 1, 2023.

Under the terms of the 401(h) program, police and fire retirees receive a subsidy for benefits received which are based upon age and retirement income eligibility. This program again offers employees the opportunity to purchase insurance through the City causing an unnecessary underwriting cost and increase in the City's OPEB liability. The City could offer to continue the subsidy program but direct retirees to purchase Medicare supplemental insurance in the market place.

Consider a buy-out program for participants in the 401(h) system by offering retirees a one-time payment for the value of their present and future healthcare benefit. This program may be considered an allowable expenditure for the use of ACT 345 revenue in this manner; however, the City should discuss this issue with the retirement system's attorney.

The City could also consider buying out non-Act-345 retirees who receive a subsidy from the City of Battle Creek, who are greater than age 65.

It is strongly recommended that the City consider the advantage of no longer offering employees the ability to buy insurance from the City and merely offer the contribution amounts. In addition to this consideration, the City could offer a cash buy-out program as to the continuing liability for providing defined amounts of retiree health care subsidy. A program such as this can be established in multiple ways and can include both retirees and active employees.

I will give the Commission time to digest this information and will plan an initial workshop in June/July. Financial information will be available just prior to the workshop or earlier if requested by Commissioners. All of the information shared with the Legacy Cost Committee are included in the City's website as part of the Finance Department page. I have provided links to this information below for ease of access.

Links to EXHIBITS:

Minutes/Agendas for Legacy Cost Committee meetings

http://www.battlecreekmi.gov/613/Legacy-Costs-Committee

City of Battle Creek PA 202 reporting

Form 5572 – 2018:

https://www.battlecreekmi.gov/DocumentCenter/View/5742/City-of-Battle-Creek-Form-5572-for-2018

Form 5572 – 2017:

http://www.battlecreekmi.gov/DocumentCenter/View/4717/PA-202-of-2017-Pension-and-OPEB-Report

Form 5598 – 2017 Corrective Action Plan:

https://www.battlecreekmi.gov/DocumentCenter/View/5741/City-of-Battle-Creek-Form-5598---Corrective-Action-Plan

Actuarial Reports

MERS 12/31/17:

http://www.battlecreekmi.gov/ArchiveCenter/ViewFile/Item/470

Police & Fire Pension 6/30/18:

http://www.battlecreekmi.gov/DocumentCenter/View/5606/2018-06-30-Police-and-Fire-Retirement-Fund-Actuarial-Valuation

OPEB Valuation 6/30/17:

https://www.battlecreekmi.gov/ArchiveCenter/ViewFile/Item/494