



# MEMORANDUM

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**DATE:** November 23, 2016

**TO:** Mayor and City Council

**FROM:** Mark Perkins, City Administrator  
Daniel Smith, Director of Finance

**SUBJECT:** Feasibility of Moving to DB Plan for Current DC Employees and New Hires

Over the past year, the City Council and staff have been considering the feasibility of returning to a Defined Benefit (DB) Pension Plan for current employees covered under the City's Defined Contribution (DC) Plan and new hires. A number of city departments have expressed concerns about their ability to attract and retain employees when competing against other cities offering a DB Plan. This concern has been particularly acute in the Police Department, where several resigning employees over the last year have cited the lack of a defined benefit pension plan as a principle reason for leaving.

## **Missouri Local Government Employees Retirement System (LAGERS)**

Staff believes that if the City desires to return to a DB Pension Plan, LAGERS provides the best option. The past performance, structure, history and other factors are the reasons for this recommendation.

LAGERS offers a variety of benefit levels for the member cities to choose from. If the City enters LAGERS, staff would recommend the L-12 level, or 1.75% for each year of service. This is very similar to the city's current DB Plan which provides 1.7% for each year of service. In addition, staff would recommend a benefit basis of 5-year final average salary, and a 4% employee contribution. Employees would be eligible for retirement at age 55 for uniform and age 60 for non-uniform. Unlike the City pension plan, the LAGERS benefit also provides for an annual cost of living increase. A further explanation of how LAGERS benefits are calculated, including examples can be found [here](#) . An employee with 25 years of service with a final average salary of \$60,000 would receive \$26,280 annually in retirement. It should be noted that even if a decision is made to join LAGERS, employees will be encouraged to continue to contribute to the City's 457 deferred compensation plan to supplement their pension.

One initial stumbling block to considering LAGERS was their initial position that all employees, including those currently in the City's existing DB Plan must enter LAGERS. Recent changes in state legislation plus a change in interpretation of LAGERS-related Statutes have eliminated that issue. Therefore, the City would be able to enroll only those employees currently participating in the City's DC Plan and future employees.

## **Considerations**

In considering the decision to move from the current DC Plan to the LAGERS DB Plan there are a number of factors to be considered.

### **1. Cost**

The city's cost for LAGERS is projected to be 9.325% of salary (9.2% for general employees and 9.4% for police). It is estimated that the annual cost of the LAGERS Plan will be \$40,000 higher than the existing DC plan cost of \$310,000, assuming the LAGERS rate remains steady. By year 30, the cost is estimated to be \$112,555 higher than the DC plan, also assuming a consistent LAGERS rate.

If the City stays with its current DC plan, the cost for funding the DC plan is projected to rise from 8.25 % to 8.7% of salary for two reasons: 1) more employees are becoming eligible for the higher city contribution rate upon reaching 6 years of employment; and 2) the city has tentatively planned to increase the compensation base to include holiday pay and overtime, consistent with the salary base of other municipal DC plans as well as the compensation base offered by LAGERS.

### **2. Risk**

Risk is the most important financial consideration for the city. Under a DC Plan, investment risk is absorbed by the employee. In a DB Plan, the investment risk is absorbed by the city. Therefore, if LAGERS does not meet its investment assumption of 7.25%, the required employer contribution will go up. Also, as employees live longer a future change in mortality tables could increase the contribution rate.

The LAGERS rate could increase or decrease by as much 1% annually, based on an annual actuarial study. For example, a 1% change in employer contribution could cost the city an estimated additional \$187,500 annually in year 30. This should be given serious consideration

since there is much debate currently as to whether future investment returns will meet the 7.25% assumption.

LAGERS has historically been a very stable pension plan, based on the Statute requiring members to make their full contributions annually. Combined with the requirement that membership continues in perpetuity, LAGERS is able to amortize its unfunded liability over 30 years, resulting in relatively stable rates. LAGERS investment returns as of June 30, 2016 fiscal year:

- 5 Year – 7.57%
- 10 Year – 6.69%
- 20 Year – 7.8%

### **3. Recruitment and Employee Retention**

A number of department heads feel the current DC retirement Plan is not competitive against the majority of other cities offering a DB Plan. This could lead to added costs due to increased turnover and a general decline in the quality of employees being recruited by the City. This appears to be especially important in the Police Department due to the challenges that all police departments across the nation face in recruiting and retaining the best officers.

The vast majority of employees appear to favor DB Plans although no formal survey has been completed.

### **4. Finality of Decision**

Under Missouri State Statutes, the city would be bound to participate in LAGERS forever once a member. There would be no ability for the city to withdraw from LAGERS. However, the city would have the ability to move to a lower benefit level in order to reduce costs. During the economic downturn of the late 2000s, LAGERS staff has indicated that 5 of its 600 member entities elected to lower their benefit level in order to reduce costs.

### **Next Steps**

If the Council wishes to further consider LAGERS, it should be noted that a cost statement and 45 days of notice is required by State Statutes before plan changes can be adopted. Meetings with employees will

also be planned in advance of any adoption, to fully inform them of the LAGERS plan and to receive feedback.

City staff looks forward to discussing these issues in further detail at the November 28 Work Session, and Jeff Kempker of LAGERS will be in attendance to answer any questions. Council may wish to learn more about LAGERS via by visiting its website, <http://www.molagers.org>.