The federal government reimburses the District government for the pension benefits paid to federal personnel who retire under the District's police officer and fire fighters' plan. Their benefits do not affect the plan's unfunded liability.

Background

The Congress instituted defined benefit pension plans[1] for the District's police officers and fire fighters in 1916, for teachers in 1920, and for judges in 1970.[2] Benefits provided by the three plans were basically provided by the federal government on a pay-as-you-go basis; that is, federal payments each year were sufficient only to cover that year's benefit payments. No money was accumulated to pay for the benefits that employees were currently earning and would receive after they retired.

In 1979, the Congress passed the District of Columbia Retirement Reform Act (P.L. 96-122). The act stated that the retirement benefits—which Congress had authorized for the police officers, fire fighters, teachers, and judges of the District of Columbia—had not been financed on an actuarially sound basis. Neither federal payments to the District nor District payments for pensions had taken into account the long-term financial requirements of the District's retirement plans. Consequently, the act established, for the first time, separate retirement funds for (1) police officers and fire fighters, (2) teachers, and (3) judges. The act also established a retirement board to manage the funds, required that the funds be managed on an actuarially sound basis, and provided federal contributions to these funds to partially finance the liability for retirement benefits incurred before January 2, 1975.

The act authorizes the funds to receive money from employee contributions, federal contributions totaling about $52.1 million annually authorized by the act through fiscal year 2004, and a variable District contribution.

Employers in the private sector who sponsor defined benefit pension plans are required by federal law to contribute annually to the plan an

[1]Defined benefit plans pay specific retirement benefits generally based on years of service, earnings, or both.

[2]Other District employees hired before October 1, 1987, are covered under the Federal Civil Service Retirement System. The District's remaining employees are covered under Social Security. After 1 year of service, permanent full-time employees hired after October 1, 1987, are also covered by a defined contribution plan and an employee deferred compensation plan.

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Before the act's passage, comparative public employee retirement data showed that the District's pension plan provisions, which allowed police officers and fire fighters to retire after serving 20 years and based retirement annuities on the average of the retiree's highest 12 consecutive months' pay, were more generous than those of most other cities. To lower pension costs, the act tightened these requirements for personnel hired after February 15, 1980. The act amended the retirement requirements to serving 25 years and attaining age 50, and based retirement annuities on the highest 36 consecutive months' pay.

Certain members of the U.S. Secret Service and the U.S. Park Police hired before January 1, 1984, participate in the District's pension plan for police officers and fire fighters.

Scope and Methodology

To obtain the information presented in this report, we met with D.C. government officials, D.C. Retirement Board members and staff, and the actuaries who prepared the most recent actuarial report for the Board. We reviewed the legislative history of Public Law 96-122, pertinent sections of the D.C. Code, and studies that examined the District's liability for funding the pension plans. In addition, we analyzed actuarial reports prepared for the Board.

To compare the benefits of the District plans with those provided to public employees elsewhere, we relied on the results of a survey of state and local government employee retirement systems conducted by the Public Pension Coordinating Council between May and August 1991. We judgmentally selected pension plans from this data base to compare with each of the three District plans. Details of our selection procedure are discussed in appendix I.

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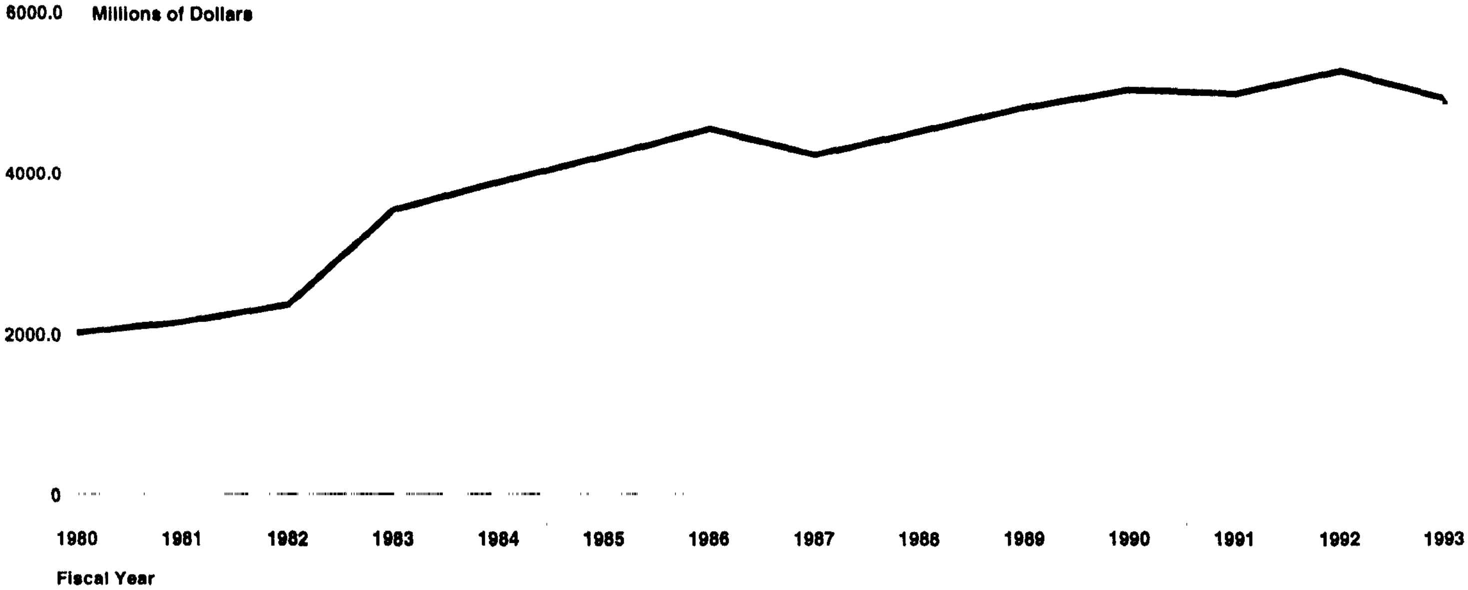
Figure 1: Unfunded Liability of D.C. Pension Plans (FY 1980-93)



The Commission on Budget and Financial Priorities of the District of Columbia (the Rivlin Commission) concluded that this growing unfunded liability jeopardizes both the future financial security of thousands of District employees and the long-term solvency of the District government.

The fiscal year 1993 unfunded liability is estimated to be about $4.9 billion, almost 2-1/2 times the Treasury's fiscal year 1980 estimate. Most of this amount, about $3.7 billion, results from the original $2.0 billion unfunded liability increased by interest. Increases in benefits to retirees have resulted in an increase of $79 million in liability. Actuarial loss factors make up the remaining $1.1 billion of the unfunded liability: pay increases and interest rates differed from actuarial estimates, and budgeted District contributions differed from actual pay-as-you-go costs. The relative sizes of these components of the unfunded liability are shown in figure 2.

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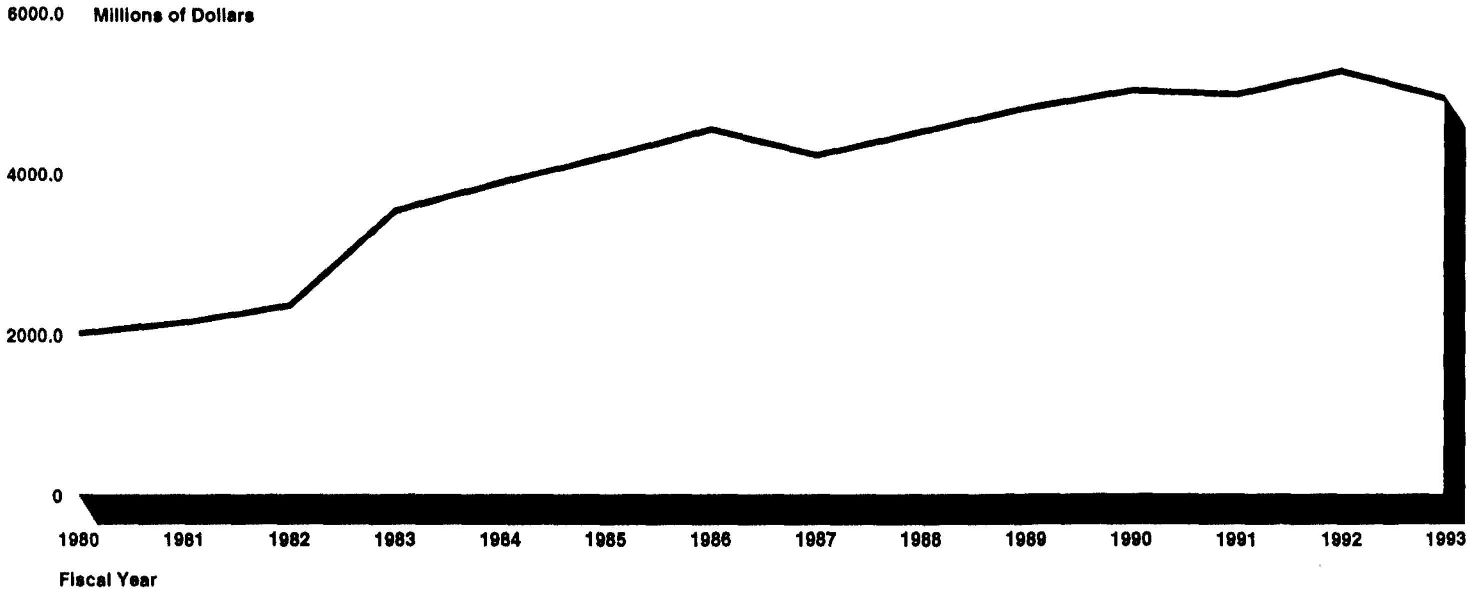

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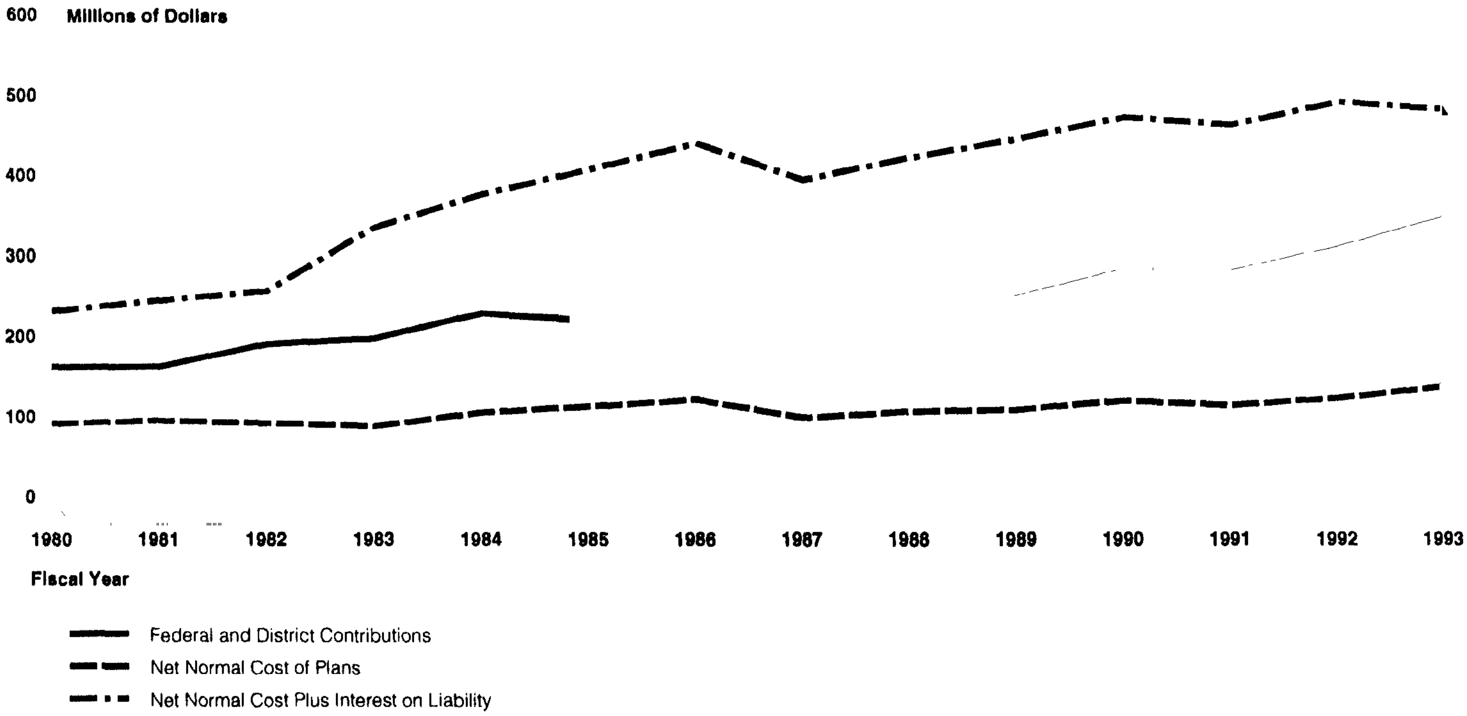

As a result, the District is, in effect, paying for benefits earned by current employees. The old liability is increasing, however, because contributions do not fully compensate for lost earnings on the unfunded portion.

If federal and District contributions continue to be less than the net normal cost plus interest on the unfunded liability, the unfunded liability will continue to grow until 2004; the following year, the act requires the District contribution to equal the net normal cost plus the interest on the unfunded liability, currently estimated by the board's actuary to be $7.7 billion. Assuming that the net normal cost increases 5 percent per year, and that the unfunded liability will increase as projected by the Board's actuary, the District contribution for 2005 will be about $806 million. If District revenues (not including federal payments and grants) increase by 5 percent per year, this 2005 payment would represent about 15 percent of revenues. By comparison, the 1991 payment represented about 8 percent of revenues.

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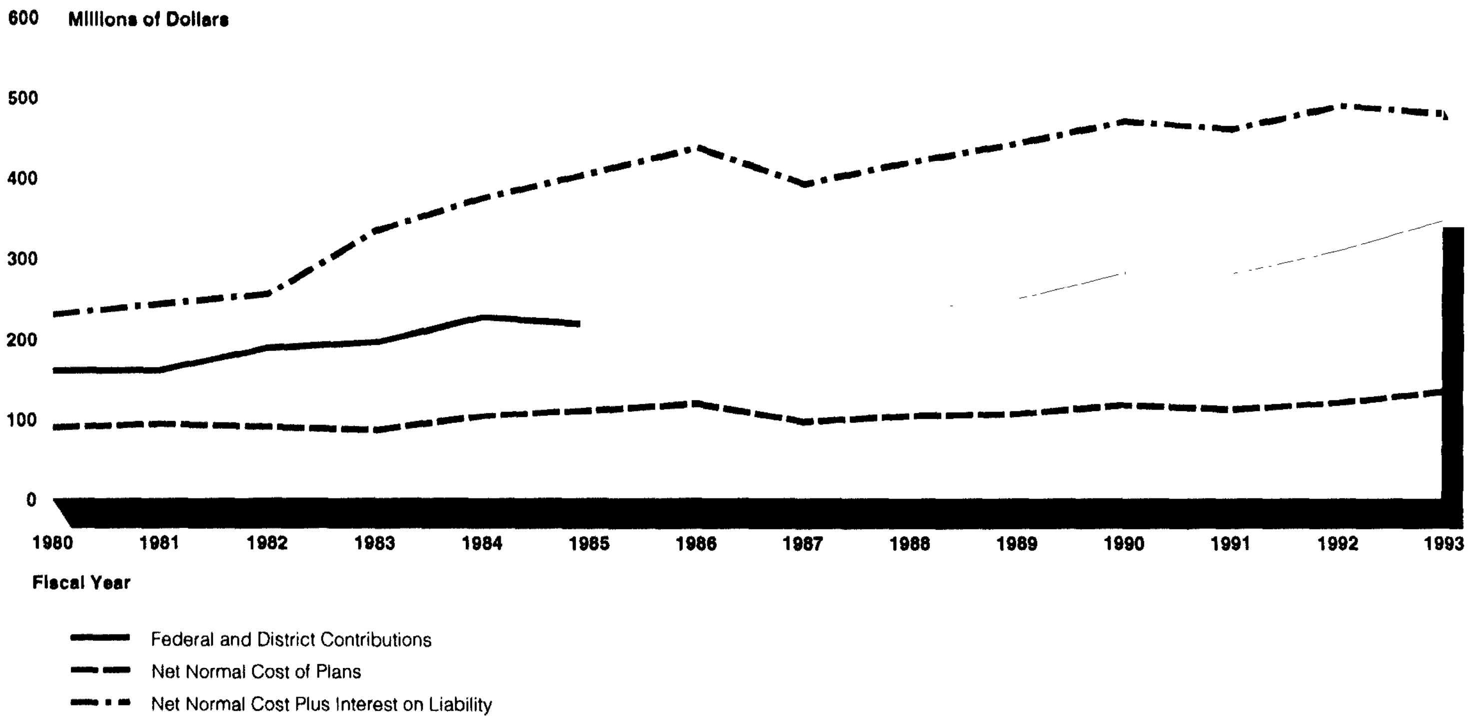

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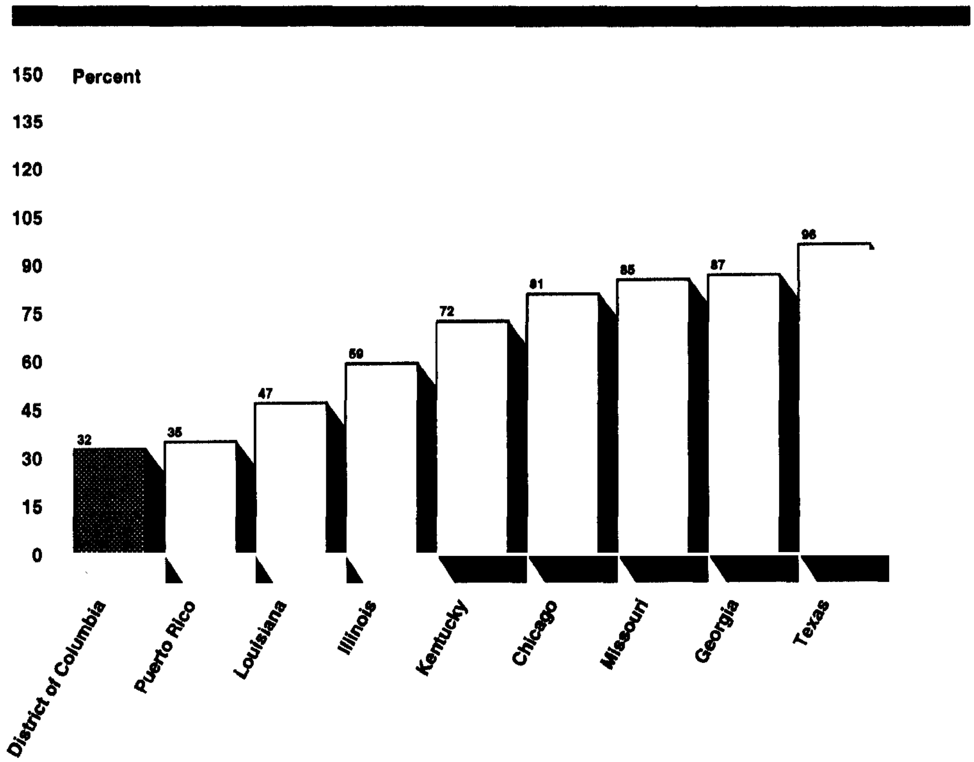

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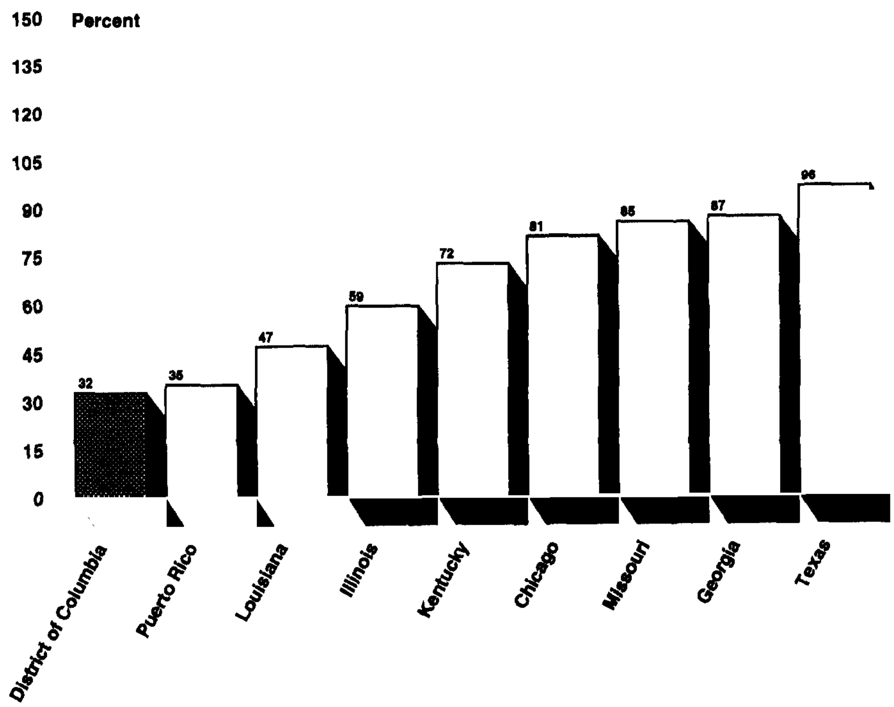

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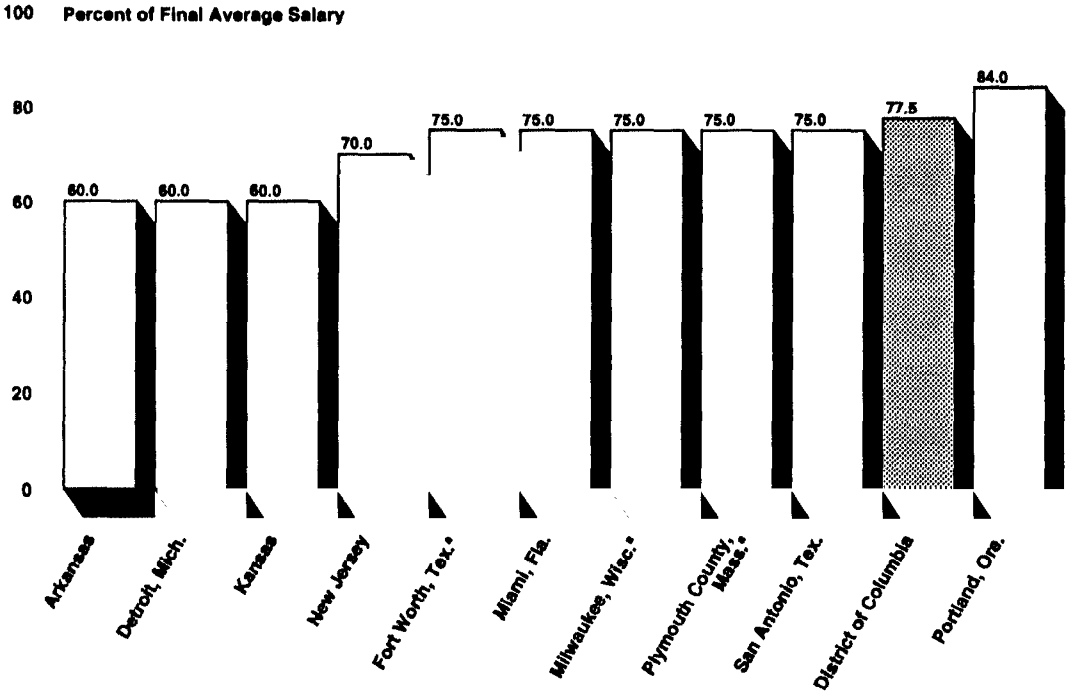

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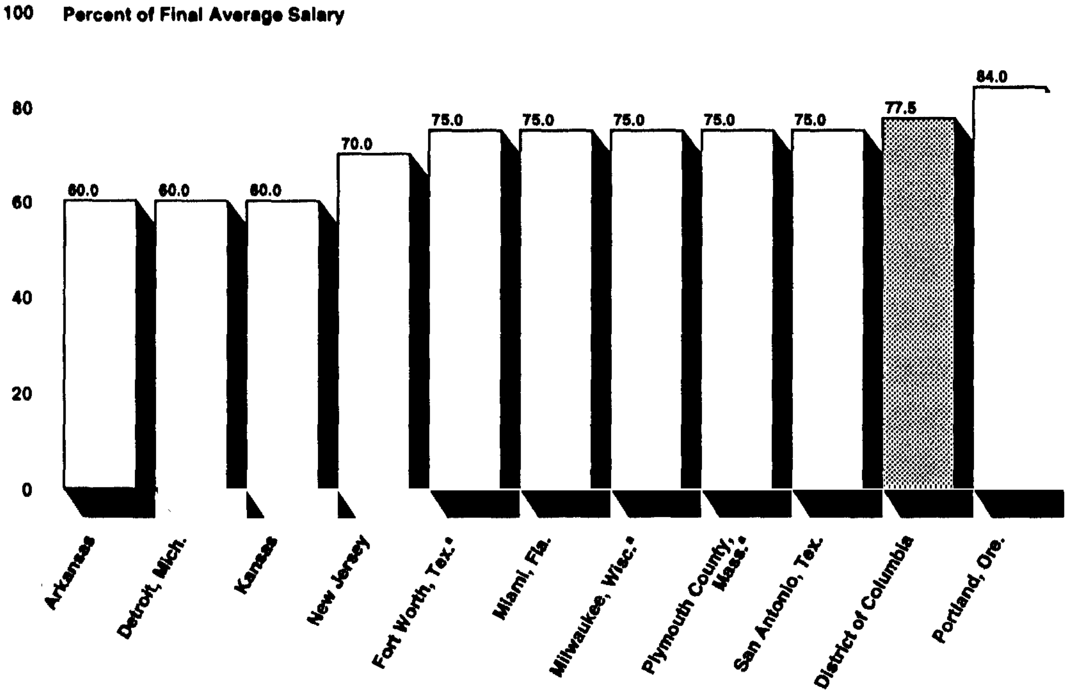

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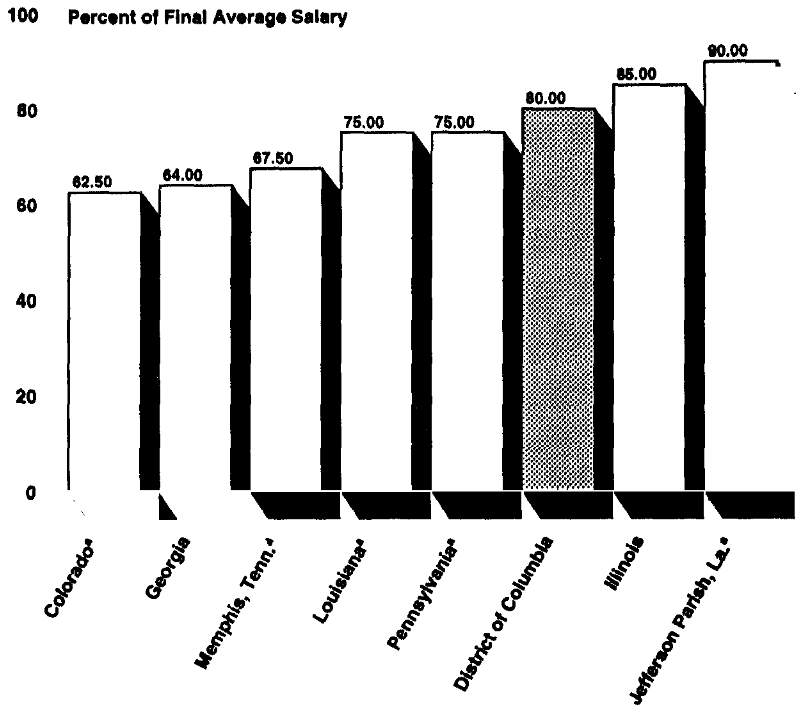

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Unfunded Liability Unaffected by Federal Employees' Participation in the District's Police Officer and Fire Fighter Plan

The federal government reimburses the District, on a pay-as-you-go basis, for pension payments for members of the U.S. Secret Service and U.S. Park Police who participate in the District's retirement plan for police officers and firefighters. In fiscal year 1991, these payments totaled about $40.6 million. In calculating the assets and liabilities for the District plan, pension obligations for federal personnel are not considered. Consequently, these obligations have no impact on the District's unfunded liability.

Agency Comments

On November 5, 1992, the Chief Financial Officer of the District of Columbia provided comments on a draft of this report (see app. III). She stated that our report rightly pointed out that the Congress passed on to the District a $2.0 billion unfunded pension liability in 1979, that the formula mandated by Congress in 1979 does not fund the plans on an

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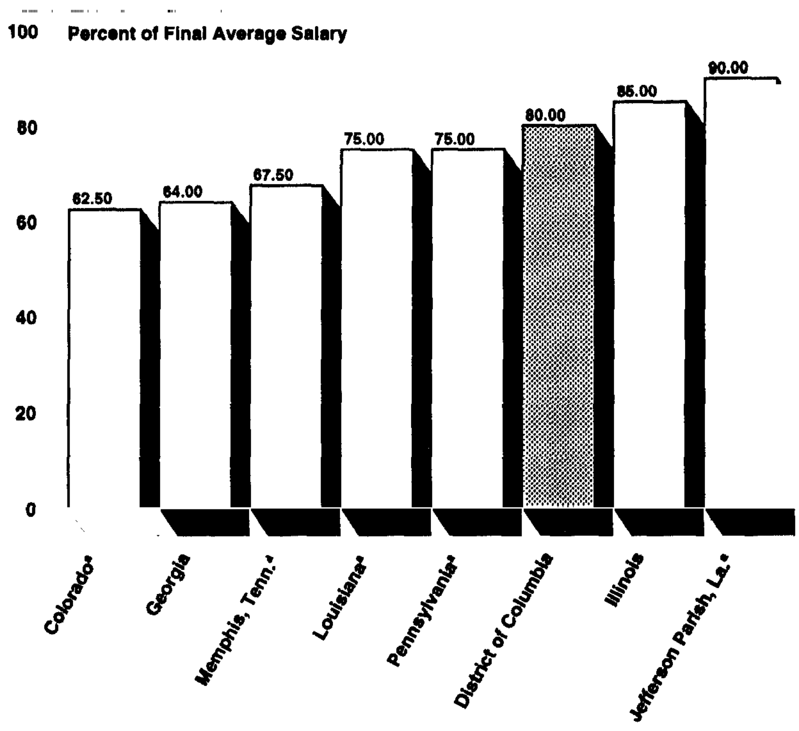

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From the survey response data base, we selected three groups of plans for comparison. We limited our selection to plans that reported benefits for employees not covered by Social Security,[1] since employees under the three District plans are not covered. These were:

- 10 plans with more than 1,000 active participants that covered both police officers and fire fighters employed by local governments;[2]
- 9 plans whose participants included elementary and high school teachers; and
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Comparison of District Retirement Plans With Selected Public Plans

Table II.1: Comparison of Police Officer and Firefighters' Pension Plan Benefits

	District of Columbia Police & Fire Retirement Plan	Detroit Police and Fire Retirement System	Plymouth County, MA, Retirement System
Age and service requirements for normal retirement			
Years of service			
5	55	NA	NA
10	55	40	55
15	55	40	55
20	55	40	0
25	50	40	0
30	50	40	0
Final salary computed as average of	Highest 36 months	Other	Highest 36 months
Annual benefit formula			
First 10 years	2.50%	2.00%	2.50%
Next 10 years	2.50%	2.00%	2.50%
Next 10 years	2.75%[a]	2.00%	2.50%
Accumulated benefit earned at normal retirement			
Years of service			
30	77.50%	60.00%	75.00%
20	50.00%	40.00%	50.00%
10	25.00%	20.00%	25.00%
5	12.50%	10.00%	0.00%
Does plan provide cost-of-living adjustments?	Yes	No	Yes
Most recent year provided	1991	-	1988
Average annual increases			
Last year	4.2%[b]	-	NA
Last 5 years	4.4%[b]	-	3.00%
Last 10 years	4.0%[b]	-	5.00%
Vesting requirements	5 years	8 Years	10 years
Employee contribution rate	7.00%	3.40%	8.00%

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15	55	40	55
20	55	40	0
25	50	40	0
30	50	40	0
Final salary computed as average of	Highest 36 months	Other	Highest 36 months
Annual benefit formula			
First 10 years	2.50%	2.00%	2.50%
Next 10 years	2.50%	2.00%	2.50%
Next 10 years	2.75%[a]	2.00%	2.50%
Accumulated benefit earned at normal retirement			
Years of service			
30	77.50%	60.00%	75.00%
20	50.00%	40.00%	50.00%
10	25.00%	20.00%	25.00%
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Table II.2: Comparison of Teachers' Pension Plan Benefits

	District of Columbia Teachers Plan	Teachers' Retirement System of Louisiana	Connecticut Teachers' Retirement System
Age and service requirements for normal retirement			
Years of service			
5	62	NA	NA
10	62	60	60
15	62	60	60
20	60	60	60
25	60	55	60
30	55	0	60
Final salary computed as average of	High 3 years	Highest 36 months	Highest 36 months
Annual benefit formula			
First 10 years	1.63%[a]	2.00%	2.00%
Next 10 years	2.00%	2.00%	2.00%
Next 10 years	2.00%	2.50%	2.00%
Accumulated benefit earned at normal retirement			
Years of service			
30	56.25%	70.00%	60.00%
20	36.25%	40.00%	40.00%
10	16.25%	20.00%	20.00%
5	7.50%	10.00%	0.00%
Does plan provide cost-of-living adjustments?	Yes	No	Yes
Most recent year provided	1991	-	1991
Average annual increases			
Last year	4.2%[b]	-	4.30%
Last 5 years	4.4%[b]	-	4.00%
Last 10 years	4.0%[b]	-	4.00%
Vesting requirements	5 years	10 years	10 years
Employee contribution rate	7.00%	8.00%	5.00%

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Years of service			
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10	62	60	60
15	62	60	60
20	60	60	60
25	60	55	60
30	55	0	60
Final salary computed as average of	High 3 years	Highest 36 months	Highest 36 months
Annual benefit formula			
First 10 years	1.63%[a]	2.00%	2.00%
Next 10 years	2.00%	2.00%	2.00%
Next 10 years	2.00%	2.50%	2.00%
Accumulated benefit earned at normal retirement			
Years of service			
30	56.25%	70.00%	60.00%
20	36.25%	40.00%	40.00%
10	16.25%	20.00%	20.00%
5	7.50%	10.00%	0.00%
Does plan provide cost-of-living adjustments?	Yes	No	Yes
Most recent year provided	1991	-	1991
Average annual increases			
Last year	4.2%[b]	-	4.30%
Last 5 years	4.4%[b]	-	4.00%
Last 10 years	4.0%[b]	-	4.00%
Vesting requirements	5 years	10 years	10 years
Employee contribution rate	7.00%	8.00%	5.00%

Table II.3: Comparison of Judges' Pension Benefits

	District of Columbia Judges' Retirement Plan	Illinois Judges' Retirement System	Jefferson Parish Employees' Retirement Plan	Employees' Retirement System of Georgia - Trial Judges	Louisiana State Employees' Retirement System	Public Employees' Retirement System of Colorado	City of Memphis Retirement Plan
Age and service requirements for normal retirement							
Years of service							
5	70	NA	NA	NA	NR	65	NA
10	60	60	60	60	60	65	65
15	60	60	60	NR	NR	65	65
20	50	60	60	NR	NR	60	65
25	50	60	50	NR	55	60	62
30	50	60	0	NR	0	55	60
Final salary computed as average of	At retirement	Last year's salary	Highest 36 months	Last 24 months	Highest 36 months	Highest 36 months	Highest 36 months
Annual benefit formula							
First 10 years	3.33%	3.50%	3.00%	4.00%	2.50%	2.50%	2.50%
Next 10 years	3.33%	5.00%	3.00%	4.00%	2.50%	2.50%	2.50%
Next 10 years	3.33%	5.00%	3.00%	4.00%	2.50%	1.25%	1.75%
Accumulated benefit earned at normal retirement							
Years of service							
30	80.00%	85.00%	90.00%	64.00%	75.00%	62.50%	67.50%
20	66.67%	85.00%	60.00%	64.00%	50.00%	50.00%	50.00%
10	33.33%	35.00%	30.00%	40.00%	25.00%	25.00%	22.50%
5	16.67%	NA	0.00%	0.00%	0.00%	12.50%	12.50%
Does plan provide cost-of-living adjustments?	Yes	Yes	No	No	No	Yes	No
Most recent year provided	1991	1991	-	-	-	1990	-
Average annual increases							
Last year	4.2%[a]	3.00%	-	-	-	5.40%	-
Last five years	4.4%[a]	3.00%	-	-	-	4.00%	-
Last 10 years	4.0%[a]	3.00%	-	-	-	5.40%	-
Vesting requirements	10 years	10 years	10 years	10 years	NR	5 years	10 years
Employee contribution	3.50%	11.00%	0.48%	7.50%	7.50%	8.00%	8.00%

Note: "NA" means not applicable. "NR" means that plan did not provide the information.

[a]Increase is based on consumer price index (CPI). Numbers are historical increase in CPI, not actual increases paid.

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	District of Columbia Judges' Retirement Plan	Illinois Judges' Retirement System	Jefferson Parish Employees' Retirement Plan	Employees' Retirement System of Georgia - Trial Judges	Louisiana State Employees' Retirement System	Public Employees' Retirement System of Colorado	City of Memphis Retirement Plan
Age and service requirements for normal retirement							
Years of service							
5	70	NA	NA	NA	NR	65	NA
10	60	60	60	60	60	65	65
15	60	60	60	NR	NR	65	65
20	50	60	60	NR	NR	60	65
25	50	60	50	NR	55	60	62
30	50	60	0	NR	0	55	60
Final salary computed as average of	At retirement	Last year's salary	Highest 36 months	Last 24 months	Highest 36 months	Highest 36 months	Highest 36 months
Annual benefit formula							
First 10 years	3.33%	3.50%	3.00%	4.00%	2.50%	2.50%	2.50%
Next 10 years	3.33%	5.00%	3.00%	4.00%	2.50%	2.50%	2.50%
Next 10 years	3.33%	5.00%	3.00%	4.00%	2.50%	1.25%	1.75%
Accumulated benefit earned at normal retirement							
Years of service							
30	80.00%	85.00%	90.00%	64.00%	75.00%	62.50%	67.50%
20	66.67%	85.00%	60.00%	64.00%	50.00%	50.00%	50.00%
10	33.33%	35.00%	30.00%	40.00%	25.00%	25.00%	22.50%
5	16.67%	NA	0.00%	0.00%	0.00%	12.50%	12.50%
Does plan provide cost-of-living adjustments?	Yes	Yes	No	No	No	Yes	No
Most recent year provided	1991	1991	-	-	-	1990	-
Average annual increases							
Last year	4.2%[a]	3.00%	-	-	-	5.40%	-
Last five years	4.4%[a]	3.00%	-	-	-	4.00%	-
Last 10 years	4.0%[a]	3.00%	-	-	-	5.40%	-
Vesting requirements	10 years	10 years	10 years	10 years	NR	5 years	10 years
Employee contribution	3.50%	11.00%	0.48%	7.50%	7.50%	8.00%	8.00%

Note: "NA" means not applicable. "NR" means that plan did not provide the information.

[a]Increase is based on consumer price index (CPI). Numbers are historical increase in CPI, not actual increases paid.

<u>Page 2; Appendix II. District Plan Benefits Compared to Other Plans</u>

The "accumulated benefit earned at normal retirement" measures only the beginning value of the annual retirement payment to beneficiaries. Annual increases, such as cost of living adjustments, can change the comparative level of benefits substantially thereafter. A more comprehensive survey of benefits would be needed to compare the effects of the District's twice-per-year, uncapped cost of living adjustment with the annual increases of other plans.

Should you have any questions about these comments, we would be happy to discuss them with you.

Sincerely,

Ellen M. O'Connor
Chief Financial Officer

Enclosure

<u>Page 2: Appendix II. District Plan Benefits Compared to Other Plans</u>

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Enclosure

Comments From the District of Columbia Retirement Board

D.C. RETIREMENT BOARD
1400 L Street, N.W.
Suite 300
Washington, D.C. 20005
(202) 535-1271
FAX (202) 535-1414

November 13, 1992

DELIVERY BY HAND

Mr. Joseph F. Delfico
Director, Income Security Issues
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Delfico:

This is in response to your request for review and comment on the draft report entitled District Pensions: Billions of Dollars in Liability Not Funded issued by your organization.

Subsequent to your request, your representative Mr. Robert D. Sampson, Evaluator-in-Charge, meet with the Board's enrolled actuary, Mr. Gene Kalwarski, and the Board's Acting Manager/Assistant Executive Director for Benefits, Mr. Jorge Morales to discuss the report. The report was reviewed by these individuals as well as the Board's General Counsel.

The report is principally an analysis of the Board's actuarial valuations since its inception. It primarily focuses on reporting historical events. The comments we have on the report are minimal. Our comments are as follows:

- The Board's current actuary has informed us that the actual initial 1979 unfunded liability is $2.6 billion rather than the $2.0 billion figure referenced in the report.

- The Board's current actuary has opined that the conclusions reached in the report are reasonable.

- The Board's current actuary has opined that the report's analysis of what portion of today's unfunded liability is attributable to interest since 1979 versus actual losses is correct.

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Major Contributors to This Report

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Robert D. Sampson, Senior Evaluator

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