Burlington Retirement Committee
Q&A with David Driscoll, Buck Consultants, City of Burlington Actuary
March 10, 2014

From: Driscoll, David [mailto:David.Driscoll@buckconsultants.com]
Sent: Monday, March 10, 2014 4:20 PM
To: Bob Rusten
Subject: RE: a few questions

Hi, Bob:

I now have some answers to your questions. I have typed them in below in crimson font. Please contact me if you need additional information.

Talk to you Friday, if not before!

David

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From: Bob Rusten [mailto:brusten@burlingtonvt.gov]
Sent: Wednesday, March 05, 2014 7:23 AM
To: Driscoll, David
Subject: a few questions

Good morning David.

I hope you are well.

A few questions have come up in the pension committee that I am hoping you can give us some direction on.

I am not looking for actual numbers, but your opinion.

Here goes:

1. As you know, employees have multiple options to choose from regarding what pension benefit they wish to receive. Two employees, both the same class, start the same day, earn the same wage, retire the same day, have the same family situation, and both pass away on the same day. The two employees have chosen a different benefits package. Is it likely, with the criteria identified above, that each would receive exactly the same amount of money out of the system, very similar amount of money from the system, or it could be some significant difference due to the option they choose?
    a. If more criteria are needed to make this an apples to apples comparison, please let me know. Essentially we are trying to look at if there is some difference in payout, purely based on the benefits package one chooses, then that opens the question as to whether there should be some differential in contribution.

    For the two employees in your hypothetical example, there would be differences in the payouts based on the option elections each one made, but benefits are adjusted when participants make their elections so that they have the same actuarial present value. For example, if one of the participants in your example chose a benefit payable over his or her life only, while the other participant chose a form involving continuation to a surviving spouse after his or her death, the benefit payable to the latter participant would be reduced to reflect the added cost of the survivorship coverage. The factors used for this conversion may in some cases need to be updated to make them consistent with the actuarial assumptions used in the valuation currently, but the practice of the system has always been to adjust participants' benefits to reflect the differing cost of options available to them.

2. Second question is if we had gone this year to a closed 30 year amortization system, and changed from the projected unit credit method, would that likely have changed this year's unfunded liability amount? If yes, likely would it have increased or decreased it? And, would it have also likely increased, decreased or not have impact the recommended contribution amount?

    I take this question to mean that you are interested in what the impact would be of amortizing each year's addition to the unfunded liability over a period that would end in a common future year (FY 2044) instead of amortizing each year's gain or loss over a new 30-year closed period. Making this change by itself this year would not have had any impact on the unfunded liability, but it would have resulted in a higher recommended City contribution for FY 2015, as at least some components of the unfunded liability would have to have been amortized over a shorter period of years in determining that contribution.

    If the funding method had been changed as well, that would definitely change the unfunded liability as well as the recommended FY 2015 city contribution, but the magnitude and direction of the change would have depended on the specific new funding method chosen. If the answer were the entry age normal method, that would likely have led to an increase in contributions, as the method funds the benefits of active members as a level percentage of pay over their careers, while the projected unit credit does not do that.

3. Since your recommended contribution, and the unfunded liability, is based on actuarial assumptions, is it likely or not likely, that the number of our benefits options makes your assumptions more difficult and therefore more problematic in determining the unfunded liability and the recommended contribution? In other words, if we had fewer options for people to choose would that make your projections easier to compute and therefore might change your projections?

   In general, having so many different categories of participants with different benefit provisions complicates our work in two ways. One is that it is makes it harder to verify that each person is slotted appropriately in the valuation. The other is that these differing provisions affect the behavior of participants, but because there are relatively small number of people in each benefit group it is hard to establish credible experience statistics for these different populations,

4. Understanding the caveats that surround an open-group valuation method, I am still wondering whether Buck can give a broad stroke indication of whether that type of method can capture some of the benefits that will result from the lower benefit tiers instituted in 2006 and 2009. Part of the concern I have is that the newer employees (of which 6 new firefighters just started) will have a positive effect that remains out of reach with the current method. I believe you used the term "responsible" application of that valuation method may be part of a plan forward. Again if we were to institute an open system, perhaps basing it on numbers of new employees we know we will have in just the next two years, might the impact on the unfunded liability and the contribution would be insignificant or perhaps significant?

   This is an idea that is worth considering. What I would want to do is stress-test a stable contribution percentage that would result from application of an open-group method to ensure that even if there is adverse experience over the course of the next few years the stable contribution percentage would contain sufficient margin to ensure the health of the system was not compromised. Proper application of this method can produce a gradual amortization of the unfunded liability as well as city contributions that are less volatile. This is something we can discuss in more detail.

I hope you feel comfortable giving us some generalized answers to these as that will help us to decide if we want to pursue any of these ideas, or not.

The next meeting of the committee is Tuesday the 11th, so if you can respond to this by Monday that would be a great help.

Thanks.

Bob Rusten
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