**Goal Development**

**City of Burlington Retirement Committee**

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**Goal: Benefit Complexity**

**Discussion**

By their nature, DB plans are complex. Unlike defined contribution plans, which focus solely on a simple input—the contribution—DB plans focus on a complicated output: a benefit to be paid years in the future, with a specific value, over a time period that is unknowable. Maintaining a DB plan is akin to hitting a moving target. Determining the amount necessary to contribute each year, in order to appropriately fund a DB plan benefit, involves considerable effort and complexity.

DB plan complexity manifests itself in several areas, including:

* plan administration
* determining the plan’s liabilities and costs
* managing assets for a large group of individuals across the age spectrum, some who are paying in to the plan and others who are receiving a benefit
* communicating the value and benefit of the plan to workers
* communicating the benefit of the plan to other stakeholders, such as taxpayers
* aligning the plan design with the objectives of plan stakeholders

Because DC plans are relatively simple, and because they are the prevailing retirement plan outside the public sector, they tend to be better understood by the general public and the media. Their simplicity and familiarity also make DC plans more prone to simple—and sometimes simplistic—appeals and explanations of their functionality and benefits.

By contrast, the inherent complexity of DB plans makes them more difficult to explain and defend to the uninitiated observer. A key risk of a DB plan is that its complexity can increase the likelihood of plan malfunction. Such malfunction could take any of multiple forms, such as miscalculation of costs or liabilities. This, in turn, could result in a misallocation of costs among generations.

A pension plan is designed to operate on a long-term basis, which is the timeframe needed for a plan to realize its full actuarial experience. Frequent changes made to the design of a pension plan conflict with the plan’s long-term nature and can disrupt its actuarial balance.

Ironically, tinkering with a pension plan’s design can encourage additional revision, in two ways: first, to offset or respond to the effects of previous tinkering; and also, because plan revisions foster an environment in which tinkering is perceived to be a normal event.

Complexity of plan design, however, is just one factor for policymakers to consider in evaluating a retirement benefit. As mentioned previously, a DC plan may be simple, but it also is an unreliable vehicle for delivering retirement income. The goal in designing and maintaining a retirement benefit should be not solely to simplify the plan, but also to strike a balance between these key objectives: simplicity, adequacy of benefits, cost stability, and affordability. The Burlington ERP appears to fall short in three of these areas.

Key features of the City of Burlington’s retirement plan appear to have been amended on multiple occasions. These amendments appear to have been intended either to reduce employer plan costs or as part of labor negotiations.

Complexity of retirement plan design can diminish public support for a retirement benefit. Members of the public who see a plan a) whose benefits or funding structure are difficult to understand; b) that is or seems to be frequently adjusted; or c) that appears to favor certain groups over others due to workers’ affiliation or political influence, may perceive the system tilted in favor of certain groups, whether or not such a perception is justified.

**The city may wish to consider the following goals related to the complexity of the plan:**

* Resolve to establish and maintain a retirement plan design that is a) simple; b) comprehensible to casual observers; and c) that aligns the benefit with the employer’s key objectives: to attract and to retain qualified workers, and to enable those workers to retire in a predictable and orderly manner. Perhaps the city’s goal could be to describe the plan design on a single side of a 3 x 5 index card.
* Resolve that the city’s retirement benefit plan design shall be changed only under pre-defined conditions (for example, attainment of a specified funding level or a UAL equal to a designated percentage of city payroll), and that such changes shall also be pre-defined (for example, adjustments in employee or employer contribution rates).

**Appendix: Summary of Class A retirement benefit provisions**

* Fire employees hired before 1/1/07: 2.75% plus 0.5% for years between 25 and 35
* Police employees hired before 7/1/06: 2.75% plus 0.5% for years between 25 and 35
* Police employees hired after 1/10/11: 2.5% plus 0.5% for years between 20 and 25
* All others: 2.65% plus 0.5% for years between 25 and 35
* Hired before 7/1/06: may choose 3.25% plus 0.5% for years between 25 and 35, and a one-half COLA, or 3.8% for all service before 6/30/06 for first 25 years; 3.6% for service since 7/1/06 up to 25 years, plus 0.5% for years between 25 and 35
* Fire employees hired after 12/31/06: full COLA only
* Police employees hired after 6/30/06: full COLA only
* Police employees hired after 1/10/11: retirement benefit reduced actuarially for retirement before age 50
* Fire employees hired after 10/7/11: retirement benefit reduced actuarially for retirement before age 50
* Fire employees hired before 10/8/11 who retire after 6/30/13: retirement benefit is reduced actuarially until age 48 for period by which retirement precedes age 55
* All others, prior to age 55, benefit is reduced actuarially for period by which retirement precedes the earlier of 25 years of service and age 55.
* For employees who terminate with 20 to 25 years of service, benefit is reduced by 1.82% for each year that service is less than 25
* For all Class A workers: 1.07 years of credit for each year in which employee worked prior to 7/1/96 and 1.17 years thereafter, in a position regularly assigned a workweek consisting on average of 53+ hours of work per week.

**Summary of Class B retirement benefit provisions**

* Employees hired prior to 7/1/06: age 65+, greater of 1.6% for years to 25 plus 0.5% for years above 25, or the actuarial equivalent of benefit determined at age 65
* Employees hired after 6/30/06: age 65+, greater of 1.4% for first 25 years of service plus 0.5% at age 65 for years above 25, or actuarial equivalent of benefit determined at age 65
* Or, member may choose 1.9% for service up to 6/30/06 for first 25 years, 1.8% for years since 7/1/06 for first 25 years, plus 0.5% for service above 25 years, and half COLA, or 2.2% for all service before 7/1/06 for first 25 years, 2.0% for service beginning 7/1/06 for first 25 years plus 0.5% for service above 25 years, and no COLA
* With certain exceptions, benefits identified above are reduced by 2% for each year retirement precedes age 65.
* For IBEW workers hired before 5/1/08 who elect a contribution rate of 4%, early reduction is 2% each year retirement precedes age 65
* For IBEW workers hired before 5/1/08 who elect a contribution rate of 3%, benefit is reduced by a factor that varies with age.
* For IBEW workers hired after 5/1/08, benefit is reduced by a factor that varies by age.
* For AFSCME Local 1343 workers hired before 1/1/06 that meet Rule of 82 by 12/7/11 but retire thereafter, reduction is 4% per year at ages 55 to 59 for each year under age 65, and the standard 2% per year reduction for ages 60 to 65.
* For other AFSCME Local 1343 employees retiring after 12/7/11, full actuarial reduction from ages 55 to 59 and standard 2% per year reduction for ages 60 to 65