Resetting the Contribution Rate

Presentation to
Government and Finance Committee
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In order to maintain its actuarial soundness, a pension plan needs to do three things:

- Carefully manage its liabilities
- Earn its actuarially assumed rate of return
- Receive in-full the calculated total Actuarially Required Contribution (ARC)

Liability Management: DERP, the City Administration, and City Council have been exceptionally prudent here:

- No provision for automatic COLAs
- No discretionary lifetime COLAs granted in the last 10 years
- No health insurance benefit increases granted in the last 10 years
- Allowing purchase of service only at full actuarial cost
- Reducing benefits for new hires when appropriate:
  - 2004 – Benefit multiplier moved from 2% down to 1.5%
  - 2010 – Exclusion of PTO cash-out from average salary
  - 2011 – Full slate of new-hire changes enacted:
    - Increased Avg. Monthly Salary calculation period from 3 years to 5 years
    - Instituted Rule of 85/60 minimum, replacing Rule of 75/55 minimum
    - Increased minimum early retirement age from 55 to 60
    - Reduced early retirement benefits
    - Eliminated the Social Security Make-up Benefit
    - Required full 5-year vesting rather than automatic at age 65

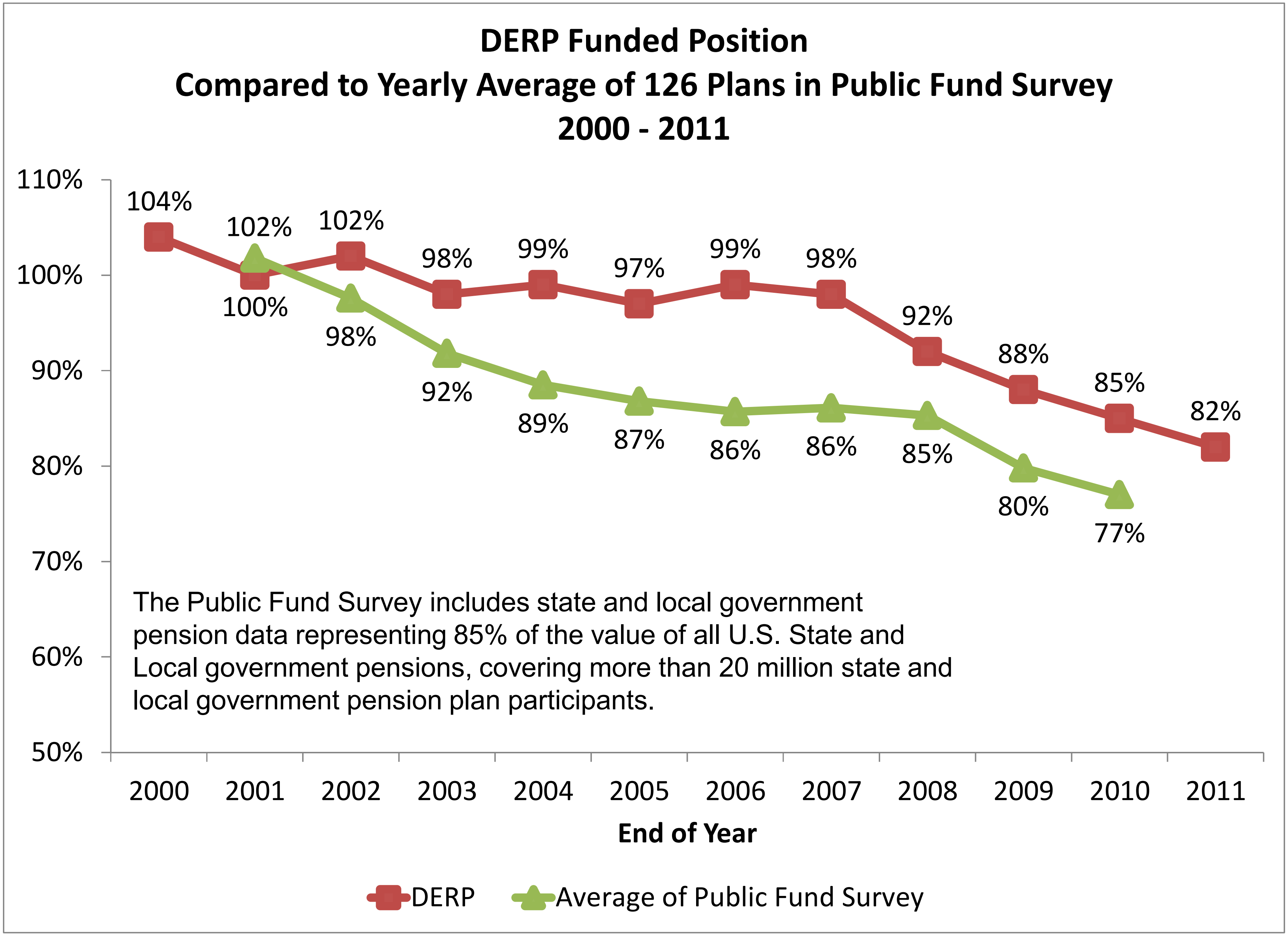
Earnings: Although the earnings target has been achieved over the long-term, DERP is still recovering from the 2008 market crisis

- Average annual return for 25 years ended 12/31/11 = 8.16% (after fees).
- At the end of 2007, funded status was 98%. Although that was excellent compared to others, there was no cushion to absorb the significant investment losses incurred in 2008.
- Since 2008, DERP's investment returns were strong in 2009 and 2010 (13.7% and 14.4% after fees, respectively) but slipped to basically 0% in 2011.
- Impact of investment shortfalls:
  - DERP only has two sources of inflows: investment returns and contributions. When investment returns in the short term are lower than assumed, the actuarial contribution model calls for contributions to be increased slowly over time, which gives markets a chance to recover.

Receiving the Actuarially Required Contribution (ARC) : The total ARC is calculated each year by the independent Actuary, as the amount of dollars, expressed in terms of "percentage of payroll," that is Required to be Contributed to pay for the separate elements of a pension fund's liabilities:

1) the "Normal Cost" of one more year of service credit for all current employees, and
2) the amount needed to pay down (or "amortize") the cumulative unfunded liability, if any, for already-earned benefits

The City, along with employees since 2003, has a 40+ year history of contributing the calculated ARC.

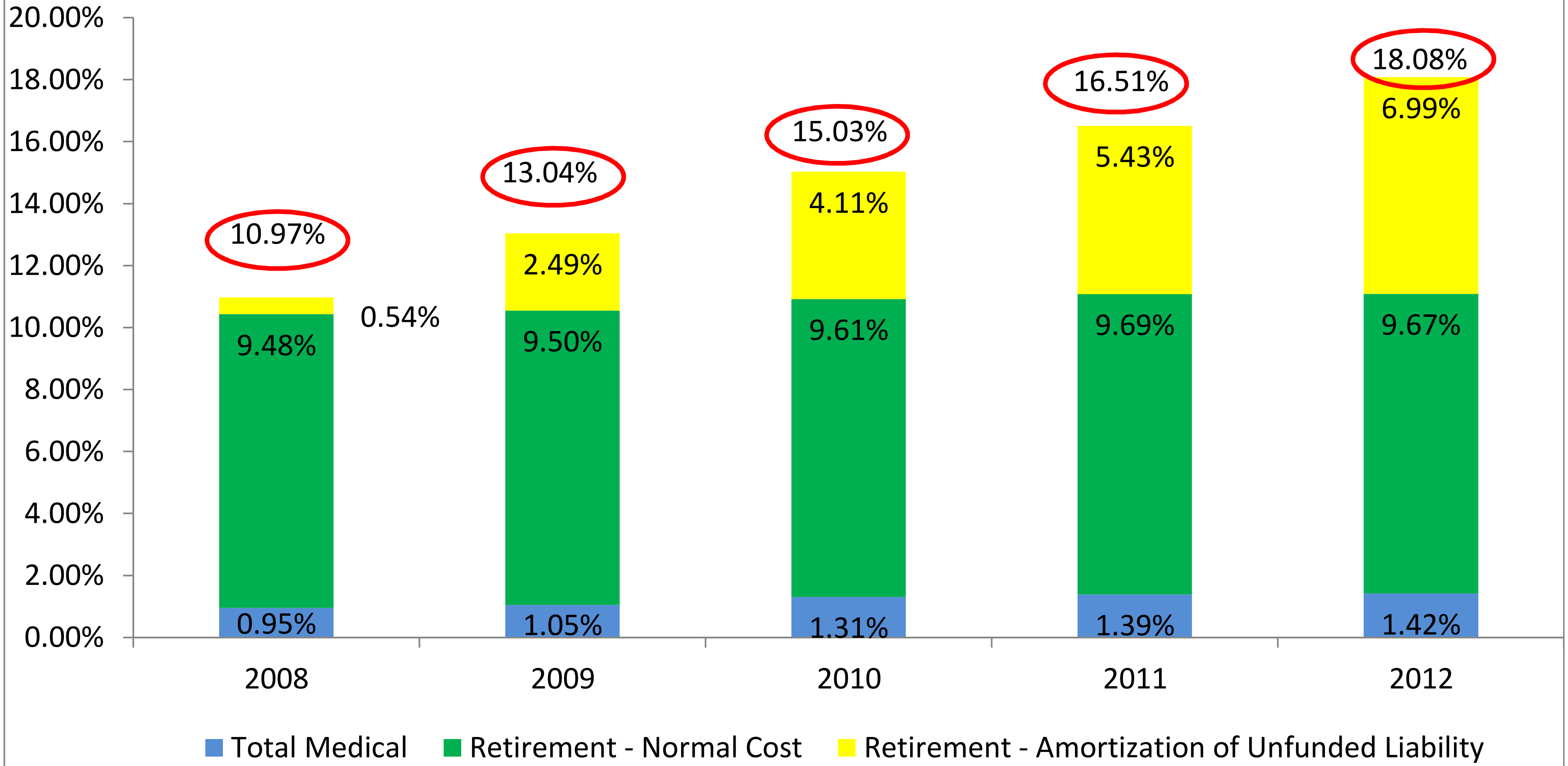

DERP Funded Position
Compared to Yearly Average of 126 Plans in Public Fund Survey
2000 - 2011
110%
100%
90%
80%
70%
60%
50%
104%
102%
102%
98%
99%
97%
99%
98%
92%
88%
85%
82%
100%
98%
92%
89%
87%
86%
86%
85%
80%
77%
The Public Fund Survey includes state and local government pension data representing 85% of the value of all U.S. State and Local government pensions, covering more than 20 million state and local government pension plan participants.
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
End of Year
DERP
Average of Public Fund Survey

Actuarial Findings and Recommendation by the Retirement Board

- DERP's independent actuary completed their January 1, 2012 Actuarial Valuation and reported that the total required contribution (ARC) as a percent of payroll increased to 18.08%.
- In accordance with the findings of the independent actuary, the Retirement Board has recommended that the total contribution rate be increased from 16.5% to 18.0%.

DENVER EMPLOYEES RETIREMENT PLAN
COMPONENTS OF THE TOTAL ACTUARIALLY REQUIRED CONTRIBUTION (ARC)
2008 - 2012

This chart shows the components of the total ARC: Retiree Medical, Retirement Normal Cost, and Amortization of the Retirement Unfunded Liabiltiy. The high level of amortization is a function our 82% funded position. We need a sustained period of strong investment returns to improve the funded status which will result in lower contributions in future years.



Recommendation by City Administration Regarding Cost-Sharing of Increased Contribution to DERP

- As noted in the Mayor’s 2013 Budget Transmittal Letter, the Administration has prepared the Budget with an assumption and recommendation that the 1.5% increase in the ARC will be split evenly between the City and the employees.
- This means an increase of 0.75% for each:
  - City share will go from 10.25% to 11.0%
  - Employee share will go from 6.25% to 7.0%
- Effective first full pay period after January 1, 2013