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TO: Shirley V. Lightsey, President
Detroit Retired City Employees Association

FROM: Irvin Corley, Jr., Fiscal Analysis Director

DATE: May 5, 2005

RE: 2005-2006 Budget Analysis

Attached is our analysis regarding your budget request for the upcoming 2004-05 Fiscal Year.

Your Budget Hearing before Council is scheduled for Friday, May 6, 2005, at 2:00 P.M.

Please contact us if you have any questions regarding our analysis.

Thank you for your cooperation in this matter.

IC:cyb

Attachment

cc: Councilmembers
Council Divisions
Auditor General's Office
Roger Short, Budget Department Director
Renee Short, Budget Department
Walter Stampor, Retirement System Manager
Kandia Milton, Mayor's Office

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Detroit Retired City Employees Association

FY 2005-2006 Budget Analysis by the Fiscal Analysis Division

Council's changes to the 2004-2005 Budget for Retirees

The 2004-05 budget as recommended by the Mayor and adopted by City Council did not include any increases for already retired employees.

In November of 2004, the City Council passed two resolutions requesting the administration to initiate the appropriation of a portion of the casino wagering tax revenue increase (as a result of state initiated wagering tax increase) for the purpose of increasing benefits for already retired employees. To this point in time the administration has not responded to the Council request. The two benefit increases requested to be funded included an increase in the minimum pension calculation and extension of the supplemental health insurance co-pay assistance program to the next two-year group of retirees.

The supplemental health insurance premium co-pay assistance program increases the City's portion of the health insurance premium cost-sharing program begun in the mid 1980's. During labor negotiations in the early 1980's it was agreed that the City and retirees (who retired after July 1, 1984) would share all future health insurance premium increases over a base rate on a 50/50 basis. This is the same agreement and calculation that active employees agreed to and continues currently. The supplemental health insurance premium co-pay assistance program requires the City to pay an additional amount equal to one-half of the retiree's originally agreed to 50/50 split.

Detroit Retired City Employees Association (DRCEA) 2005-2006 Improvement Proposal and Costs

In the DRCEA's letter to the City Council dated February 9, 2005 the association requested funding be provided for two retiree benefit improvements. The same two proposals requested but not included in the budget last year, and that were requested to be implement by Council in resolutions to the Mayor in November 2004. The February 2005 letter included updated cost estimates.

1. A New Minimum Pension Formula - $691,600 estimated cost

2. Reduced Medical Insurance Co-pay for Retirees (July 1994 – June 1996) - $693,300 estimated cost

The DRCEA may limit their request to only the improvement to the minimum pension formula. The DRCEA understands the financial challenges facing the City of Detroit at this time and withdraw the request to reduce the medical insurance co-pay for retirees who retired between July 1994 thru June 1996, a two-year period.

New Minimum Pension Formula – Currently the formula to calculate the minimum pension is: "in no case shall the total of the annual Straight Life Pension be less than three hundred sixty dollars ($360.00) times each of the first ten years of service at retirement plus one hundred twenty dollars ($120) for each year of service in excess of ten years." The request is to increase the second factor in the formula by $60 to $180 for each year of service in excess of ten years.

Years of Service at Retirement	Current Minimum Pension	New Minimum	Increase
10	$3,600	$3,600	$ -0-
15	4,200	4,500	300
20	4,800	5,400	600
25	5,400	6,300	900
30	6,000	7,200	1,200

The first year cost is estimated to be $881,700 for all funds and $691,600 for the general fund and DOT fund. The total cost over 15 years is estimated at $7.7 million for all funds and $9.0 million. The last two figures represent the increase in unfunded accrued actuarial liability (UAAL) as a result of increasing the benefits for retirees.

This above retirement benefit increase is an example of one of the items that must be considered when pension obligation bonds are issued by a municipality. There is a perception that the UAAL goes away when funded by the pension obligation bonds. This is true only at that point in time. Retirement improvements after the sale of the bonds will create additional or new UAAL. And the City will find itself in the position of paying off the debt plus having to fund the additional UAAL created by retirement benefit increases. The UAAL may also increase if the assumed investment earnings or other assumptions do not match actual results over time.

Reduced Medical Insurance Co-pay for Retirees – This request is to continue the expansion of the supplemental medical insurance co-pay program and cover another two year period of retirees, July 1, 1994 to June 30, 1996. The explanation of the plan is covered above in the discussion of the improvement being implemented during the current budget. Based on certain assumptions the first year cost for this request is $1.0 million for all funds and $.8 million for the general fund. Also as discussed above, the recommended budget includes an estimated **$12.0 million** to fund this benefit for those retirees and beneficiaries already covered by the program. In essence, increasing the number of retirees covered will add nearly $1.0 million to this figure for a number of years. In fact, the amount will be increasing each year as the medical insurance premiums continue to increase yearly.

Since this is a benefit for retirees, not an actual retirement plan payment increase, this is funded on a current basis, rather than on an actuarial basis like the pension itself. In the near future, accounting standards may require that the City begin to fund retirement benefits on an actuarial basis rather than a cash basis. In effect, this will create a UAAL for retirement benefits, just like the basic pension benefit.

Considering the financial challenges facing the City Council in the review of the 2004-05 Budget, including 377 layoff, removal of vacant positions, the refinancing of the risk management fund and $80 million of pension obligation bonds, it will be very difficult for the City to find funds for pension benefits improvements. In addition, by the time the 2004-05 is adopted, the City will have issued $61 million of fiscal stabilization bonds and completely depleted the Budget Stabilization Fund to address the June 30, 2003 shortfall. It would be ill advised to continue to award new and costly benefit increases to any group.

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