PENSION MANAGEMENT OVERSIGHT COMMISSION

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MEETING MINUTES[1]

Meeting Date:	September 12, 2003
Meeting Time:	10:30 A.M.
Meeting Place:	State House, 200 W. Washington St., Room 130
Meeting City:	Indianapolis, Indiana
Meeting Number:	1

Members Present: Sen. Joseph Harrison, Chairperson; Sen. Allie Craycraft; Sen. Larry Lutz; Rep. Thomas Kromkowski; Rep. Ron Liggett; Rep. Larry Buell; Rep. Richard Mangus; Steve Meno; Kip White.

Members Absent: Sen. Thomas Weatherwax; William Gettings, Jr.; Connie Lux.

Senator Joseph Harrison, chair of the Pension Management Oversight Commission (PMOC), called the meeting to order at 10:35 a.m. He introduced the members of the Commission and the staff. Senator Harrison then called on Mary Beth Braitman of Ice Miller to present the first topic assigned to the Commission.

I. Funding Status for Police and Firefighter Pension Funds

Ms. Braitman introduced the topic by distributing a summary of the municipal police and fire pension funding history (Exhibit 1). Ms. Braitman briefly reviewed the actions taken by the General Assembly, beginning in 1977, to help control the growth of property taxes levied by municipalities for pre-1977 fund police officer and firefighter pension liabilities mandated under state statutes.

In 1977, the Pension Relief Fund (Relief Fund) was created along with the 1977 Police Officers' and Firefighters' Pension and Disability Fund (1977 Fund) to assist cities and towns with the burden of paying police and fire pensions from the pre-1977 pension funds. Cigarette tax and

[1] Exhibits and other materials referenced in these minutes can be inspected and copied in the Legislative Information Center in Room 230 of the State House in Indianapolis, Indiana. Requests for copies may be mailed to the Legislative Information Center, Legislative Services Agency, 200 West Washington Street, Indianapolis, IN 46204-2789. A fee of $0.15 per page and mailing costs will be charged for copies. These minutes are also available on the Internet at the General Assembly homepage. The URL address of the General Assembly homepage is http://www.ai.org/legislative/. No fee is charged for viewing, downloading, or printing minutes from the Internet.

alcohol tax revenues were dedicated to the Relief Fund. The revenues were distributed under the "k" formula. The 1977 Fund also offered police officers and firefighters who were hired before May 1, 1977, a one-time opportunity to "convert" their membership from a pre-1977 fund to the 1977 Fund. (The Relief Fund distributions are determined using a complicated formula that was developed to calculate the amount of relief to be distributed to municipalities each year. The "k" factor in the formula is the amount by which the total pre-1977 pension funds' benefits are allowed to increase each year. The concept behind the "k" distribution is to build the Relief Fund until increases in the total pension outlays under the pre-1977 pension funds have peaked, and to have the Relief Fund distribute its last dollar just as the outlays peak.)

In 1981, the General Assembly provided additional relief under a supplemental formula called the "m" formula. (The supplemental distribution formula was designed to supplement the "k" distribution formula. The "m" factor in the supplemental distribution formula was developed to take into account increases in outlays required to fund actuarially the 1977 Fund: 21% of payroll for 1977 Fund members.)

In 1989, $10,000,000 annually in lottery revenues was dedicated to funding the Relief Fund distributions using the "k" formula. In 1996 and 1997, an additional $100,000,000 was appropriated to the Relief Fund from the state general fund.

On October 1, 1998, the General Assembly shifted from municipalities to the 1977 Fund the responsibility for paying the benefits for "converted" members who were retired or disabled before July 1 1998, removing approximately $250,000,000 in unfunded liability from the pre-1977 plans.

In 1999, an additional $20,000,000 annually from lottery revenues was dedicated to the "m" formula.

In 2001, the General Assembly enacted certain changes to the Relief Fund structure. First, inequities in the state pension relief formulas were corrected to ensure that the Relief Fund contributed to each city and town a minimum of 50% of the pre-1977 pension fund payments made through December 31, 2007, as long as the city or town maintains its 1998 level of payments according to a maintenance of effort test. Secondly, the funding cycle for Relief Fund payments was advanced to provide current funding of state relief for local pension costs. Finally, municipalities were authorized to leave funds on deposit in the Relief Fund in order to receive a greater return on investments than was available otherwise. Municipalities may withdraw these funds once each year.

Also in 2001, the General Assembly authorized the transfer of interest earnings from the Public Deposit Insurance Fund to the Pension Distribution Fund. Each year from 2001 through 2011, municipalities receive a distribution from the Pension Distribution Fund to help them meet benefit payment obligations under the pre-1977 pension funds. The distribution is allocated proportionally based on each municipality's share of the total benefits paid from pre-1997 pension funds each year.

In 2002, a deferred retirement option plan (DROP) was authorized for police and firefighter pension funds. Municipalities were provided a levy limit exception for the non-reimbursed portion of DROP lump sum payments.

Doug Todd of McCready & Keene, actuaries for the police and fire pension funds, discussed a chart that he had prepared showing the Relief Fund's share and the municipalities' share of the projected distribution of benefit payments under the current statutes for Indiana municipal police and fire pension plans whose members were hired before May 1, 1977 (Exhibit 2). Mr. Todd discussed the upward trend of the distributions until 2025 when the distributions would start to decline. He noted that the Relief Fund includes income from invested funds as well as cigarette tax, alcohol tax, and lottery revenues. He called the Commission members' attention to four points of interest shown on Exhibit 2:

(1) There is a dip in the distribution in 1999, because the responsibility for benefits paid to nonactive "converted" members was shifted to the 1977 Fund.

(2) Municipalities did not fund any of the 2001 distribution, because the state made: (a) a double distribution to establish current year funding for state relief; and (2) a make-up distribution to ensure that the Relief Fund paid at least 50% of each municipality's pension liability for 1998 through 2000.

(3) In 2008, the cities' share of the distribution will increase, because the state 50% funding relief provision expires December 31, 2007.

(4) The "Gray Area" of Exhibit 2 shows a shortfall of $ 103.6 million (present value as of January 1, 2003), because of the exhaustion of the Relief Fund. The shortfall will occur because there will not be enough money to fund fully the "m" formula. Without any changes, the shortfall will become the municipalities' responsibility. Exhibit 2 assumes 5% salary increases each year. If the increases are less, the shortfall amount will be smaller.

In response to a question from Mr. Meno, Mr. Todd stated that, in the past, the Relief Fund assumed an investment return of 7%, but the rate may be lower today.

Matt Brase of the Indiana Association of Cities and Towns (IACT) expressed the appreciation of IACT members for the legislators' past support. He indicated that IACT members continue to regard this as an important issue and illustrated the point by recalling a telephone call placed at 3 a.m. by the then IACT president Fred Armstrong from Singapore to Senator Garton on the Senate floor to discuss pension legislation.

Kokomo Mayor Jim Trobaugh, current IACT president, delivered written remarks (Exhibit 3) applauding the General Assembly's more than 20 year approach of addressing the pre-1977 unfunded police and fire pension liabilities before there is a disaster. He urged that the Relief Fund continue to receive its share of the cigarette, alcohol, and lottery dollars, or more, in order to not fall behind in the progress made towards fulfilling the promised benefits to pre-1977 Fund pensioners. Mayor Trobaugh declared that "we must stay the course" because cities and towns will have difficulty meeting their pension obligations as soon as 2007 when the 50% relief mechanism expires.

Tom Miller representing the Indiana Association of Firefighters stated his appreciation that PMOC reconsiders the pension funding issue every couple of years. He stated that he has worked on the issue for twenty-five years, but the job is not yet finished.

Leo Blackwell representing the Fraternal Order of Police testified that he has spent ten to twelve years working on this issue. He stated that he will share with his members the General Assembly's funding history presented to PMOC today. Mr. Blackwell added that, despite past hard work, the funding problems are not solved.

II. Review of the State's Deferred Compensation Program

Senator Harrison called on Jeffrey Heinzmann, Deputy Auditor of Policy and Legal Counsel, Auditor of State's Office, to discuss PMOC's second assigned topic: the Indiana Deferred Compensation Plan (the Plan). Mr. Heinzmann identified himself as the Secretary of the Deferred Compensation Committee (the Committee) and the Auditor of State's appointment to the Committee.

Mr. Heinzmann reported that as of August 31, 2003, the Plan's total assets were $555,444,736. On December 31, 2002, the total assets were $504,396,072.

The Committee is in the process of negotiating a contract with Buck Consultants LLC for investment consulting services to accomplish three separate tasks: (1) an evaluation and quarterly reports to the Committee concerning the performance and management of the investment options available under the Plan; (2) assistance to the Committee in the drafting of an Investment Policy Statement; and (3) assistance to the Committee in the replacement of the Plan's investment options should that be advisable.

Mr. Heinzmann explained that Plan participants remain heavily invested in conservative options. As of August 31, 2003, 62.12% of the Plan's assets were invested in the Indiana Stable Value Fund (ISVF). On an ongoing basis, the ISVF receives nearly half of the monthly contributions to the Plan.

Mr. Heinzmann testified that the Auditor of State is responsible for the Plan's administration and, since February 1, 2001, has contracted with ING for third party administrator services.

Mr. Heinzmann distributed a packet containing the following additional information about the Plan (Exhibit 4), including:

(1) As required by IC 5-10-1.1-4(h), the Committee's annual report to the State Board of Finance on the status of and any changes to the Plan.
(2) The August 31, 2003, Plan balances, broken down by investment option.
(3) The August 2003 Plan contributions, broken down by investment option.
(4) A performance update on the Plan's investment options for the year through August 31, 2003.

Senator Harrison asked whether the Auditor of State or the Committee are seeking legislative changes to the Plan. Mr. Heinzmann responded that he did not know of any. He stated that, after investigation, the Committee believes that the Plan currently is state of the art.

III. Judges' Retirement Fund Issues

(A) Cost of living adjustment (COLA) for members of the 1985 Judges' Retirement Fund

Senator Harrison recognized Judge Nancy Vaidik, President of the Indiana Judges Association, and a judge on the Indiana Court of Appeals. Judge Vaidik requested that the Commission again consider recommending legislation establishing a COLA for the 1985 Fund. She testified that the earlier judges' plan does have a COLA.

(B) The addition of full-time magistrates to the 1985 Judges' Retirement Fund

Ken Abbott, Clark County magistrate, requested that the Commission consider recommending legislation to add full-time magistrates to the 1985 Judges' Retirement Fund. Magistrate Abbott described his duties as the only magistrate in Clark County. Each year he handles about 2500 small claims cases, hears about 500 requests for protective orders, presides at traffic court, conducts initial hearings, and serves as a pro tem when the Clark County judges are on vacation. In short, in most respects, he is performing the same duties as a judge. In addition, Magistrate Abbott related that he left a successful law practice to become a full-time magistrate and since then has been funding his retirement plan out of his own pocket. He believes that fairness requires that magistrates receive the same treatment as judges.

In response to a question from Representative Buell, Magistrate Abbott stated that, as a magistrate, he is eligible to participate in the public employees' retirement fund (PERF).

Senator Harrison closed the meeting by announcing that he expects to set a date in two to three weeks to hold the next PMOC meeting. He is not setting a meeting date today in order to give those preparing proposals for PMOC's consideration enough time to do so.

Senator Harrison adjourned the meeting at 11:10 a.m.