

Municipal Policemen's or Firemen's Pension and Relief Fund  
Deferred Retirement Option Plan (DROP)  
Components

At the May 23, 2013 meeting of the Municipal Pensions Oversight Board, Board members requested staff to prepare a set of criteria a local municipal policemen's or firemen's pension and relief fund should consider when developing proposed DROP plans. Below are items each pension board as well as each municipality should consider when determining whether to propose DROP plans to the Municipal Pensions Oversight Board.

The first section is a list of requirements (not all-inclusive) stated in WV Code §8-22-25a.

- A member must be eligible for regular retirement after July 1, 2011. A member is eligible for regular retirement after attaining age 50 and completing at least 20 years of service. A member is eligible for the DROP six months after becoming eligible for regular retirement.
- An eligible member who makes the election to participate in the DROP will:
  - Receive a retirement benefit based on service and final average salary as of the DROP participation date.
  - During the DROP period the member's benefit are accumulated in the DROP account.
  - The DROP period may span from one year to five years provided that the member's age is less than 65.
  - Benefits in the DROP account may be credited with interest at a rate not to exceed 3.5% per year
- If a member voluntarily terminates employment and consequently DROP participation before the end of the elected DROP period, benefits within the DROP account will accumulate with zero interest. If a member is terminated by the employer, then member benefits accrue with interest within the DROP account. If the member is terminated for cause then member benefits do not accrue interest within the DROP account.
- If a member becomes disabled during the DROP period, then member benefits do not accrue interest within the DROP account.
- If a member dies during the DROP period, the beneficiary receives the accumulated DROP account with interest.
- DROP members will be considered retired members for purposes of the state premium tax allocation.
- The DROP plan must be revenue neutral before it can be approved by the MPOB

The following items will need to be contemplated by the local pension plan and municipality and an answer determined for each before submitting a plan to the MPOB for its actuary to review.

- Please provide the DROP interest credit policy, which is subject to an annual limit of 3.5%.
  - Saint Albans Firemen's Pension DROP plan stipulates that all interest earned on the individual DROP accounts will go back to the credit of the existing pension

plan, not the individual DROP members. Benefits in the DROP account will not be credited with interest per the pension board's decision. This applies to (1) members who terminate employment before the end of the elected DROP period, (2) members who become disabled during the DROP period, or, (3) if any of the members die during the DROP period, their beneficiary's accumulation account. THIS IS ONE OF THE PRIMARY REASONS THE SAINT ALBAN'S FIREMEN'S PENSION DROP PLAN SHOWED A NET GAIN TO PLAN ASSETS AND IS NOT PROJECTED TO HAVE A NET LOSS TO ASSETS.

- Please provide any changes to the sponsor's funding policy. For example, if your municipality is currently funding benefits under the (Standard Funding policy or Alternative Funding policy), is the municipality considering another policy such as the actuarially sound Optional Funding policy or the Conservation Funding policy?
- Please provide details on when COLA (supplemental benefits) for members that have elected to participate in the DROP plan will begin, i.e. the July 1<sup>st</sup> after two consecutive retirement anniversaries have occurred or the July 1<sup>st</sup> after the DROP period ends and the member is no longer working.
- Are member contributions "picked up" by the plan sponsor (the city) as defined in IRS rules 414(h)(2)?
- Will the DROP members continue to pay a percentage of their salary into the retirement system – a percentage that the DROP member will not receive credit for at the end of the DROP.
  - THIS IS ONE OF THE PRIMARY REASONS THE SAINT ALBAN'S FIREMEN'S PENSION DROP PLAN SHOWED A NET GAIN TO PLAN ASSETS AND IS NOT PROJECTED TO HAVE A NET LOSS TO ASSETS. Members of this DROP plan will pay 9.5% of their salary to the Pension Plan and not ever receive any credit for these payments to their plan.
- How will a members accumulated vacation hours be used in the member's calculation of benefits prior to DROP election?
- How will a members accumulated sick leave hours be used in the member's calculation of benefits prior to DROP election?
- Your pension fund must follow WV Code §8-22-16d to define salary when calculating retirement pensions.

The following items will need to be gathered by the Pension Secretary and the Municipal Treasurer and sent to the MPOB when the application is filed by the municipality for the DROP plan. This data is used by the MPOB's actuary within their DROP plan models to determine whether the DROP plan is actuarially revenue neutral. The actuary's model must show that the proposed DROP plan design is not expected to cause an increase in the unfunded actuarial liability.

- Please provide the following data for each member that is eligible to participate in the DROP.
  - Pensionable history salary information ending with the most recently ended calendar year, shown month by month.
  - Base salary, ending with the most recently ended calendar year, (exclusive of all overtime and other non-base pay) used to determine the average adjusted salary

- Expected pension salary and base salary for 12 month period ending with current calendar year.
- Service as of end of last calendar year, including any prior or current military service which may be included in the determination of pension benefits
- The number of active members eligible to participate in the DROP.

The remaining text is actual information from the City of Saint Albans DROP application review by Gabriel Roeder Smith & Co (“GRS”). It is being presented here as an example of components used by the City of Saint Albans to request a DROP plan for its Fire Department.

GRS’s DROP evaluation model is based on the assumption that the member will select the DROP and in the period that maximizes the member’s DROP account value and present value of future retirement benefits.

GRS has assumed the DROP design requires that the member DROP election include the DROP election period, i.e. one to five years participation in the DROP.

GRS cost estimates for the City of Saint Albans Firemen’s Pension Fund DROP design are based on the following data and assumptions:

- The City of Saint Albans provided census information for the five eligible members, including salary history through December 31, 2012. The projected salaries have been adjusted to estimate the impact of accumulated vacation time.
- Member’s accumulated DROP benefits will not earn interest during the DROP period.
- Present values are based on an interest rate factor of 5.0%.
- Eligible members are assumed to either retire or select a five-year DROP, at the end of the calendar year, in which they are first eligible to retire.
- Premium tax allocation for 2013 of \$7,167 per active member and \$2,072 per retired member.  
After 2013, the premium tax allocation increases based on the assumptions used for the July 1, 2011, valuation.
- An eligible member who makes the election to participate in the DROP will:
  - Receive a retirement benefit based on service and final average salary as of the DROP participation date.
  - During the DROP period the member’s benefit are accumulated in the DROP account.
  - The DROP period may span from one year to five years provided that the member’s age is less than 65.
- Benefits in the DROP account will not be credited with interest per the pension board’s decision. This applies to (1) members who terminate employment before the end of the elected DROP period, (2) members who become disabled during the DROP period, or, (3) if any of the members die during the DROP period, their beneficiary’s accumulation account.
- Although not required by statute, the City of St. Alban’s DROP design will require that DROP members contribute 9.5% of compensation during the DROP period.

A summary of the costs for the City of Saint Albans Firemen’s Fund DROP design is shown below for the five eligible DROP members:

Impact of Proposed DROP Design (Gain)/Loss	Present Value 12/31/2012
Accelerated Retirement	\$ 237,572
DROP Member Contributions	\$ (159,271)
DROP Interest Credit	\$ 0
Premium Tax Allocation	\$ 147,324
Delay of New Hires that Replace DROP Eligible Retirees	\$ (250,876)
Net (Gain)/Loss	\$ (25,251)

A net gain was generated under the proposed design and assumptions, methods, and data outlined above. The results are based on the actuary’s “best estimate” assumptions. It is possible that another equally plausible scenario, based on another set of reasonable assumptions, could produce materially different results. Also, it is possible that other emerging experience due to actual salary or retirement experience could produce materially different results.

Please note that the preceding results apply to the DROP design and data specific to the City of Saint Albans Firemen’s Fund. The results and conclusions could be materially different for another fund.